

PRUDENTIAL FINANCIAL INC  
Form 10-Q  
May 01, 2008  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-Q**

x **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended March 31, 2008

OR

.. **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the Transition Period from            to

Commission File Number 001-16707

# Prudential Financial, Inc.

(Exact Name of Registrant as Specified in its Charter)

**New Jersey**  
(State or Other Jurisdiction of  
Incorporation or Organization)

**22-3703799**  
(I.R.S. Employer  
Identification Number)

**751 Broad Street**  
**Newark, New Jersey 07102**  
**(973) 802-6000**

(Address and Telephone Number of Registrant's Principal Executive Offices)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes  No

As of April 30, 2008, 434 million shares of the registrant's Common Stock (par value \$0.01) were outstanding. In addition, 2 million shares of the registrant's Class B Stock, for which there is no established public trading market, were outstanding.



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**FORWARD-LOOKING STATEMENTS**

Certain of the statements included in this Quarterly Report on Form 10-Q, including but not limited to those in Management's Discussion and Analysis of Financial Condition and Results of Operations, constitute forward-looking statements within the meaning of the U.S. Private Securities Litigation Reform Act of 1995. Words such as expects, believes, anticipates, includes, plans, assumes, estimates, projects, should, will, shall or variations of such words are generally part of forward-looking statements. Forward-looking statements are made based on management's current expectations and beliefs concerning future developments and their potential effects upon Prudential Financial, Inc. and its subsidiaries. There can be no assurance that future developments affecting Prudential Financial, Inc. and its subsidiaries will be those anticipated by management. These forward-looking statements are not a guarantee of future performance and involve risks and uncertainties, and there are certain important factors that could cause actual results to differ, possibly materially, from expectations or estimates reflected in such forward-looking statements, including, among others: (1) general economic, market and political conditions, including the performance and fluctuations of fixed income, equity, real estate and other financial markets; (2) interest rate fluctuations; (3) reestimates of our reserves for future policy benefits and claims; (4) differences between actual experience regarding mortality, morbidity, persistency, surrender experience, interest rates or market returns and the assumptions we use in pricing our products, establishing liabilities and reserves or for other purposes; (5) changes in our assumptions related to deferred policy acquisition costs, valuation of business acquired or goodwill; (6) changes in our claims-paying or credit ratings; (7) investment losses and defaults; (8) competition in our product lines and for personnel; (9) changes in tax law; (10) economic, political, currency and other risks relating to our international operations; (11) fluctuations in foreign currency exchange rates and foreign securities markets; (12) regulatory or legislative changes; (13) adverse determinations in litigation or regulatory matters and our exposure to contingent liabilities, including in connection with our divestiture or winding down of businesses; (14) domestic or international military actions, natural or man-made disasters including terrorist activities or pandemic disease, or other events resulting in catastrophic loss of life; (15) ineffectiveness of risk management policies and procedures in identifying, monitoring and managing risks; (16) effects of acquisitions, divestitures and restructurings, including possible difficulties in integrating and realizing the projected results of acquisitions; (17) changes in statutory or U.S. GAAP accounting principles, practices or policies; (18) changes in assumptions for retirement expense; (19) Prudential Financial, Inc.'s primary reliance, as a holding company, on dividends or distributions from its subsidiaries to meet debt payment obligations and continue share repurchases, and the applicable regulatory restrictions on the ability of the subsidiaries to pay such dividends or distributions; and (20) risks due to the lack of legal separation between our Financial Services Businesses and our Closed Block Business. Prudential Financial, Inc. does not intend, and is under no obligation, to update any particular forward-looking statement included in this document. See Risk Factors included in the Annual Report on Form 10-K for the year ended December 31, 2007 for discussion of certain risks relating to our businesses and investment in our securities.

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Throughout this Quarterly Report on Form 10-Q, Prudential Financial and the Registrant refer to Prudential Financial, Inc., the ultimate holding company for all of our companies. Prudential Insurance refers to The Prudential Insurance Company of America, before and after its demutualization on December 18, 2001. Prudential, the Company, we and our refer to our consolidated operations before and after demutualization.

**PART I FINANCIAL INFORMATION****ITEM 1. Financial Statements****PRUDENTIAL FINANCIAL, INC.****Unaudited Interim Consolidated Statements of Financial Position**

March 31, 2008 and December 31, 2007 (in millions, except share amounts)

|   | March 31,<br>2008 | December 31,<br>2007 |
|---|-------------------|----------------------|
| <b>ASSETS</b>   |                   |                      |
| Fixed maturities:   |                   |                      |
| Available for sale, at fair value (amortized cost: 2008 \$164,676; 2007 \$160,137)      | \$ 164,472        | \$ 162,162           |
| Held to maturity, at amortized cost (fair value: 2008 \$3,741; 2007 \$3,543)            | 3,735             | 3,548                |
| Trading account assets supporting insurance liabilities, at fair value                  | 14,644            | 14,473               |
| Other trading account assets, at fair value   | 2,833             | 3,613                |
| Equity securities, available for sale, at fair value (cost: 2008 \$8,115; 2007 \$7,895) | 8,129             | 8,580                |
| Commercial loans (includes \$657 measured at fair value at March 31, 2008)              | 31,938            | 30,047               |
| Policy loans  | 9,538             | 9,337                |
| Securities purchased under agreements to resell   | 178               | 129                  |
| Other long-term investments   | 6,405             | 6,431                |
| Short-term investments  | 5,731             | 5,237                |
| <b>Total investments</b>  | <b>247,603</b>    | <b>243,557</b>       |
| Cash and cash equivalents   | 9,760             | 11,060               |
| Accrued investment income   | 2,266             | 2,174                |
| Reinsurance recoverables  | 1,975             | 2,119                |
| Deferred policy acquisition costs   | 12,828            | 12,339               |
| Other assets  | 21,986            | 18,982               |
| Separate account assets   | 181,902           | 195,583              |
| <b>TOTAL ASSETS</b>   | <b>\$ 478,320</b> | <b>\$ 485,814</b>    |
| <b>LIABILITIES AND STOCKHOLDERS EQUITY</b>  |                   |                      |
| <b>LIABILITIES</b>  |                   |                      |
| Future policy benefits  | \$ 114,863        | \$ 111,468           |
| Policyholders' account balances   | 90,380            | 84,154               |
| Policyholders' dividends  | 2,458             | 3,661                |
| Reinsurance payables  | 1,396             | 1,552                |
| Securities sold under agreements to repurchase  | 8,799             | 11,441               |
| Cash collateral for loaned securities   | 4,958             | 6,312                |
| Income taxes  | 3,575             | 3,553                |
| Short-term debt   | 16,224            | 15,657               |

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|   |                   |                   |
|---|-------------------|-------------------|
| Long-term debt  | 15,052            | 14,101            |
| Other liabilities   | 16,016            | 14,875            |
| Separate account liabilities  | 181,902           | 195,583           |
| Total liabilities   | 455,623           | 462,357           |
| <b>COMMITMENTS AND CONTINGENT LIABILITIES (See Note 11)</b>   |                   |                   |
| <b>STOCKHOLDERS EQUITY</b>  |                   |                   |
| Preferred Stock (\$.01 par value; 10,000,000 shares authorized; none issued)  |                   |                   |
| Common Stock (\$.01 par value; 1,500,000,000 shares authorized; 604,901,800 and 604,901,479 shares issued as of March 31, 2008 and December 31, 2007, respectively) | 6                 | 6                 |
| Class B Stock (\$.01 par value; 10,000,000 shares authorized; 2,000,000 shares issued and outstanding as of March 31, 2008 and December 31, 2007, respectively)     |                   |                   |
| Additional paid-in capital  | 21,802            | 20,856            |
| Common Stock held in treasury, at cost (167,455,593 and 157,534,628 shares as of March 31, 2008 and December 31, 2007, respectively)                                | (10,476)          | (9,693)           |
| Accumulated other comprehensive income (loss)   | (539)             | 447               |
| Retained earnings   | 11,904            | 11,841            |
| Total stockholders equity   | 22,697            | 23,457            |
| <b>TOTAL LIABILITIES AND STOCKHOLDERS EQUITY</b>  | <b>\$ 478,320</b> | <b>\$ 485,814</b> |

*See Notes to Unaudited Interim Consolidated Financial Statements*

**Table of Contents****PRUDENTIAL FINANCIAL, INC.****Unaudited Interim Consolidated Statements of Operations****Three Months Ended March 31, 2008 and 2007 (in millions, except per share amounts)**

|   | <b>Three Months Ended<br/>March 31,</b> |                 |
|---|---|-----------------|
|   | <b>2008</b>                             | <b>2007</b>     |
| <b>REVENUES</b>   |   |                 |
| Premiums  | \$ 3,958                                | \$ 3,559        |
| Policy charges and fee income   | 825                                     | 785             |
| Net investment income   | 3,027                                   | 2,935           |
| Realized investment gains (losses), net   | (912)                                   | 420             |
| Asset management fees and other income  | 666                                     | 1,076           |
| <b>Total revenues</b>   | <b>7,564</b>                            | <b>8,775</b>    |
| <b>BENEFITS AND EXPENSES</b>  |   |                 |
| Policyholders' benefits   | 4,035                                   | 3,685           |
| Interest credited to policyholders' account balances  | 637                                     | 843             |
| Dividends to policyholders  | 559                                     | 711             |
| General and administrative expenses   | 2,279                                   | 2,109           |
| <b>Total benefits and expenses</b>  | <b>7,510</b>                            | <b>7,348</b>    |
| <b>INCOME FROM CONTINUING OPERATIONS BEFORE INCOME TAXES AND EQUITY IN EARNINGS OF OPERATING JOINT VENTURES</b> | <b>54</b>                               | <b>1,427</b>    |
| Income tax expense  | 29                                      | 423             |
| <b>INCOME FROM CONTINUING OPERATIONS BEFORE EQUITY IN EARNINGS OF OPERATING JOINT VENTURES</b>                  | <b>25</b>                               | <b>1,004</b>    |
| Equity in earnings of operating joint ventures, net of taxes  | 43                                      | 77              |
| <b>INCOME FROM CONTINUING OPERATIONS</b>  | <b>68</b>                               | <b>1,081</b>    |
| Income from discontinued operations, net of taxes   | 1                                       | 39              |
| <b>NET INCOME</b>   | <b>\$ 69</b>                            | <b>\$ 1,120</b> |
| <b>EARNINGS PER SHARE (See Note 6)</b>  |   |                 |
| <b>Financial Services Businesses</b>  |   |                 |
| <b>Basic:</b>   |   |                 |
| Income from continuing operations per share of Common Stock   | \$ 0.20                                 | \$ 2.14         |
| Income from discontinued operations, net of taxes   |   | 0.08            |
| Net income per share of Common Stock  | \$ 0.20                                 | \$ 2.22         |
| <b>Diluted:</b>   |   |                 |
| Income from continuing operations per share of Common Stock   | \$ 0.20                                 | \$ 2.10         |
| Income from discontinued operations, net of taxes   |   | 0.08            |



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|                                      |         |         |
|--------------------------------------|---------|---------|
| Net income per share of Common Stock | \$ 0.20 | \$ 2.18 |
|--------------------------------------|---------|---------|

**Closed Block Business**

**Basic and Diluted:**

|   |            |          |
|---|------------|----------|
| Income (loss) from continuing operations per share of Class B Stock | \$ (10.00) | \$ 39.00 |
| Income from discontinued operations, net of taxes                   |            | 1.00     |
| Net income (loss) per share of Class B Stock                        | \$ (10.00) | \$ 40.00 |

*See Notes to Unaudited Interim Consolidated Financial Statements*

**Table of Contents****PRUDENTIAL FINANCIAL, INC.****Unaudited Interim Consolidated Statement of Stockholders Equity****Three Months Ended March 31, 2008 (in millions)**

|  | Common<br>Stock | Class B<br>Stock | Additional<br>Paid-in<br>Capital | Retained<br>Earnings | Common<br>Stock<br>Held In<br>Treasury | Accumulated<br>Other<br>Comprehensive<br>Income<br>(Loss) | Total<br>Stockholders<br>Equity |
|--|-----------------|------------------|----------------------------------|----------------------|--|---|---------------------------------|
| <b>Balance, December 31, 2007</b>  | \$ 6            | \$               | \$ 20,856                        | \$ 11,841            | \$ (9,693)                             | \$ 447  | \$ 23,457                       |
| Common Stock acquired  |                 |                  |                                  |                      | (869)                                  |   | (869)                           |
| Stock-based compensation programs  |                 |                  | (31)                             | (9)                  | 86                                     |   | 46                              |
| Impact on Company's investment in Wachovia Securities due to addition of A.G. Edwards business, net of tax |                 |                  | 977                              |                      |  |   | 977                             |
| Cumulative effect of changes in accounting principles, net of taxes  |                 |                  |                                  | 3                    |  |   | 3                               |
| Comprehensive income:  |                 |                  |                                  |                      |  |   |                                 |
| Net income   |                 |                  |                                  | 69                   |  |   | 69                              |
| Other comprehensive loss, net of taxes   |                 |                  |                                  |                      |  | (986)   | (986)                           |
| <b>Total comprehensive income (loss)</b>   |                 |                  |                                  |                      |  |   | (917)                           |
| <b>Balance, March 31, 2008</b>   | \$ 6            | \$               | \$ 21,802                        | \$ 11,904            | \$ (10,476)                            | \$ (539)  | \$ 22,697                       |

*See Notes to Unaudited Interim Consolidated Financial Statements*

**Table of Contents****PRUDENTIAL FINANCIAL, INC.****Unaudited Interim Consolidated Statements of Cash Flows****Three Months Ended March 31, 2008 and 2007 (in millions)**

|  | <b>2008</b>    | <b>2007</b>  |
|--|----------------|--------------|
| <b>CASH FLOWS FROM OPERATING ACTIVITIES</b>  |                |              |
| Net income   | \$ 69          | \$ 1,120     |
| Adjustments to reconcile net income to net cash provided by operating activities:                      |                |              |
| Realized investment (gains) losses, net  | 912            | (420)        |
| Policy charges and fee income  | (277)          | (248)        |
| Interest credited to policyholders' account balances   | 637            | 843          |
| Depreciation and amortization  | 91             | 62           |
| Change in:   |                |              |
| Deferred policy acquisition costs  | (254)          | (247)        |
| Future policy benefits and other insurance liabilities   | 1,057          | 712          |
| Trading account assets supporting insurance liabilities and other trading account assets               | (87)           | (52)         |
| Income taxes   | (402)          | (22)         |
| Other, net   | (392)          | (1,057)      |
| <b>Cash flows from operating activities</b>  | <b>1,354</b>   | <b>691</b>   |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES</b>  |                |              |
| Proceeds from the sale/maturity/prepayment of:   |                |              |
| Fixed maturities, available for sale   | 23,856         | 22,802       |
| Fixed maturities, held to maturity   | 49             | 76           |
| Trading account assets supporting insurance liabilities and other trading account assets               | 5,813          |              |
| Equity securities, available for sale  | 869            | 1,650        |
| Commercial loans   | 535            | 1,372        |
| Policy loans   | 380            | 324          |
| Other long-term investments  | 302            | 293          |
| Short-term investments   | 9,569          | 2,451        |
| Payments for the purchase/origination of:  |                |              |
| Fixed maturities, available for sale   | (25,643)       | (23,184)     |
| Fixed maturities, held to maturity   | (9)            | (59)         |
| Trading account assets supporting insurance liabilities and other trading account assets               | (5,982)        |              |
| Equity securities, available for sale  | (1,036)        | (1,620)      |
| Commercial loans   | (1,927)        | (1,213)      |
| Policy loans   | (361)          | (318)        |
| Other long-term investments  | (795)          | (582)        |
| Short-term investments   | (10,272)       | (2,619)      |
| Other, net   | 32             | 201          |
| <b>Cash flows used in investing activities</b>   | <b>(4,620)</b> | <b>(426)</b> |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES</b>  |                |              |
| Policyholders' account deposits  | 9,501          | 5,265        |
| Policyholders' account withdrawals   | (4,963)        | (5,646)      |
| Net change in securities sold under agreements to repurchase and cash collateral for loaned securities | (3,867)        | (2,812)      |
| Cash dividends paid on Common Stock  | (75)           | (72)         |
| Net change in financing arrangements (maturities 90 days or less)                                      | 760            | 990          |
| Common Stock acquired  | (869)          | (712)        |
| Common Stock reissued for exercise of stock options  | 29             | 83           |
| Proceeds from the issuance of debt (maturities longer than 90 days)                                    | 2,110          | 1,111        |
| Repayments of debt (maturities longer than 90 days)  | (1,010)        | (387)        |
| Excess tax benefits from share-based payment arrangements  | 12             | 60           |
| Other, net   | (41)           | 73           |

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|  |          |          |
|--|----------|----------|
| <b>Cash flows from (used in) financing activities</b>  | 1,587    | (2,047)  |
| Effect of foreign exchange rate changes on cash balances   | 379      | 1        |
| <b>NET DECREASE IN CASH AND CASH EQUIVALENTS</b>   | (1,300)  | (1,781)  |
| <b>CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR</b>  | 11,060   | 8,589    |
| <b>CASH AND CASH EQUIVALENTS, END OF PERIOD</b>  | \$ 9,760 | \$ 6,808 |
| <b>NON-CASH TRANSACTIONS DURING THE PERIOD</b>   |          |          |
| Impact on Company's investment in Wachovia Securities due to addition of A.G. Edwards business, net of tax | \$ 977   | \$       |
| Treasury Stock shares issued for stock-based compensation programs   | \$ 84    | \$ 87    |

*See Notes to Unaudited Interim Consolidated Financial Statements*

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**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements**

**1. BUSINESS AND BASIS OF PRESENTATION**

Prudential Financial, Inc. ( Prudential Financial ) and its subsidiaries (collectively, Prudential or the Company ) provide a wide range of insurance, investment management, and other financial products and services to both individual and institutional customers throughout the United States and in many other countries. Principal products and services provided include life insurance, annuities, mutual funds, pension and retirement-related services and administration, and investment management. In addition, the Company provides retail securities brokerage services indirectly through a minority ownership in a joint venture. The Company has organized its principal operations into the Financial Services Businesses and the Closed Block Business. The Financial Services Businesses operate through three operating divisions: Insurance, Investment, and International Insurance and Investments. The Company's real estate and relocation services business as well as businesses that are not sufficiently material to warrant separate disclosure and businesses to be divested are included in Corporate and Other operations within the Financial Services Businesses. The Closed Block Business, which includes the Closed Block (see Note 4), is managed separately from the Financial Services Businesses. The Closed Block Business was established on the date of demutualization and includes the Company's in force participating insurance and annuity products and assets that are used for the payment of benefits and policyholders' dividends on these products, as well as other assets and equity that support these products and related liabilities. In connection with the demutualization, the Company ceased offering these participating products.

***Basis of Presentation***

The Unaudited Interim Consolidated Financial Statements include the accounts of Prudential Financial, entities over which the Company exercises control, including majority-owned subsidiaries and minority-owned entities such as limited partnerships in which the Company is the general partner, and variable interest entities in which the Company is considered the primary beneficiary. The Unaudited Interim Consolidated Financial Statements have been prepared in accordance with accounting principles generally accepted in the United States of America ( U.S. GAAP ) on a basis consistent with reporting interim financial information in accordance with instructions to Form 10-Q and Article 10 of Regulation S-X of the Securities and Exchange Commission ( SEC ). Intercompany balances and transactions have been eliminated.

In the opinion of management, all adjustments necessary for a fair statement of the financial position and results of operations have been made. All such adjustments are of a normal, recurring nature. Interim results are not necessarily indicative of the results that may be expected for the full year. These financial statements should be read in conjunction with the Company's audited Consolidated Financial Statements included in the Company's Annual Report on Form 10-K for the year ended December 31, 2007.

***Use of Estimates***

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

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The most significant estimates include those used in determining deferred policy acquisition costs, goodwill, valuation of business acquired, valuation of investments including derivatives, future policy benefits including guarantees, pension and other postretirement benefits, provision for income taxes, reserves for contingent liabilities and reserves for losses in connection with unresolved legal matters.

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**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

***Reclassifications***

Certain amounts in prior periods have been reclassified to conform to the current period presentation.

**2. ACCOUNTING POLICIES AND PRONOUNCEMENTS**

***Share-Based Payments***

The Company issues employee share-based compensation awards, under a plan authorized by the Board of Directors, that are subject to specific vesting conditions; generally the awards vest ratably over a three-year period, the nominal vesting period, or at the date the employee retires (as defined by the plan), if earlier. For awards granted between January 1, 2003 and January 1, 2006 that specify an employee vests in the award upon retirement, the Company accounts for those awards using the nominal vesting period approach. Under this approach, the Company records compensation expense over the nominal vesting period. If the employee retires before the end of the nominal vesting period, any remaining unrecognized compensation cost is recognized at the date of retirement.

Upon the adoption of Statement of Financial Accounting Standards ( SFAS ) No. 123(R), Share-Based Payment on January 1, 2006, the Company revised its approach to the recognition of compensation costs for awards granted to retirement-eligible employees and awards that vest when an employee becomes retirement-eligible to apply the non-substantive vesting period approach to all new share-based compensation awards granted on or after January 1, 2006. Under this approach, all compensation cost is recognized on the date of grant for awards issued to retirement-eligible employees, or over the period from the grant date to the date retirement eligibility is achieved, if that is expected to occur during the nominal vesting period.

If the Company had accounted for all share-based compensation awards granted after January 1, 2003 under the non-substantive vesting period approach, net income of the Financial Services Businesses for the three months ended March 31, 2008 would have been increased by \$0.8 million, with no reportable impact to the earnings per share of Common Stock, on both a basic and diluted basis, and \$2.4 million, or \$0.01 per share of Common Stock, on both a basic and diluted basis for the three months ended March 31, 2007.

***Accounting Pronouncements Adopted***

In February 2007, the Financial Accounting Standards Board ( FASB ) issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities. This statement provides companies with an option to report selected financial assets and liabilities at fair value, with the

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associated changes in fair value reflected in the Consolidated Statements of Operations. The Company adopted this guidance effective January 1, 2008.

Upon the adoption of SFAS No. 159, the Company elected the fair value option for certain investments held within the commercial mortgage operations of the Asset Management segment. Specifically, the fair value option was elected for funded commercial loans held for sale originated beginning January 1, 2008. In addition, the Company elected the fair value option for fixed rate commercial loans held for investment that were held at December 31, 2007 and for such loans originated beginning January 1, 2008. The Company elected the fair value option for the loan programs mentioned above primarily to eliminate the need for hedge accounting under SFAS No. 133, while still achieving an offset in earnings from the associated interest rate derivative hedges.

Due to recent volatility in the credit markets, the Company experienced unexpected volatility in the fair value of the aforementioned fixed rate commercial loans held for investment that was not substantially offset by the associated interest rate derivative hedges during the quarter ended March 31, 2008. Therefore, the Company



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**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

will no longer elect the fair value option on loans held for investment that are originated after March 31, 2008, and will be pursuing hedge accounting under SFAS No. 133. See Note 9 for more information on SFAS No. 159.

The Company does not have material commercial loans held for sale outside of the commercial mortgage operations. The fair value option has not been elected for the Company's other fixed rate commercial loans held for investment (primarily held by the general account), as the underlying business drivers and economics are different for these loans in that they are part of a diverse portfolio backing insurance liabilities.

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements. This statement defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. This statement does not change which assets and liabilities are required to be recorded at fair value, but the application of this statement could change practices in determining fair value. The Company adopted this guidance effective January 1, 2008. See Note 9 for more information on SFAS No. 157.

In November 2007, the staff of the Securities and Exchange Commission (SEC) issued Staff Accounting Bulletin (SAB) No. 109, Written Loan Commitments Recorded at Fair Value Through Earnings. SAB 109 revises and rescinds portions of SAB 105, Application of Accounting Principles to Loan Commitments. Specifically, SAB 109 states that the expected net future cash flows related to the associated servicing of the loan should be included in the measurement of all written loan commitments that are accounted for at fair value through earnings. SAB 109 is effective for all written loan commitments recorded at fair value that are entered into, or substantially modified, in fiscal quarters beginning after December 15, 2007. The Company adopted SAB 109 effective January 1, 2008 for its loan commitments that are recorded at fair value through earnings. The Company's adoption of this guidance did not have a material effect on the Company's consolidated financial position or results of operations.

In April 2007, the FASB issued FASB Staff Position (FSP) FIN 39-1, Amendment of FASB Interpretation No. 39. FSP FIN 39-1 modifies FIN No. 39, Offsetting of Amounts Related to Certain Contracts, and permits companies to offset cash collateral receivables or payables with net derivative positions under certain circumstances. This FSP is effective for fiscal years beginning after November 15, 2007 and is required to be applied retrospectively to financial statements for all periods presented. The Company's adoption of this guidance effective January 1, 2008 did not have a material effect on the Company's consolidated financial position or results of operations.

In January 2008, the FASB issued Statement No. 133 Implementation Issue No. E23, Hedging General: Issues Involving the Application of the Shortcut Method under Paragraph 68. Implementation Issue No. E23 amends Statement No. 133, paragraph 68 with respect to the conditions that must be met in order to apply the shortcut method for assessing hedge effectiveness. This implementation guidance was effective for hedging relationships designated on or after January 1, 2008. The Company's adoption of this guidance effective January 1, 2008 did not have a material effect on the Company's consolidated financial position or results of operations.

***Recent Accounting Pronouncements***

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In March 2008, the FASB issued SFAS No. 161, Disclosures about Derivative Instruments and Hedging Activities – an amendment of FASB Statement No. 133. This statement amends and expands the disclosure requirements for derivative instruments and hedging activities by requiring companies to provide enhanced disclosures about (a) how and why an entity uses derivative instruments, (b) how derivative instruments and related hedged items are accounted for under Statement No. 133 and its related interpretations, and (c) how

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**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

derivative instruments and related hedged items affect an entity's financial position, financial performance, and cash flows. This statement is effective for fiscal years and interim periods beginning after November 15, 2008. The Company is currently assessing the impact of SFAS No. 161 on the notes to the consolidated financial statements.

In February 2008, the FASB issued FSP FAS 140-3, Accounting for Transfers of Financial Assets and Repurchase Financing Transactions. The FSP provides recognition and derecognition guidance for a repurchase financing transaction, which is a repurchase agreement that relates to a previously transferred financial asset between the same counterparties, that is entered into contemporaneously with or in contemplation of, the initial transfer. The FSP is effective for fiscal years beginning after November 15, 2008. The FSP is to be applied prospectively to new transactions entered into after the adoption date. The Company will adopt this guidance effective January 1, 2009. The Company is currently assessing the impact of this FSP on the Company's consolidated financial position and results of operations.

In February 2008, the FASB issued FSP FAS 157-2, Effective Date of FASB Statement No. 157. This FSP applies to nonfinancial assets and nonfinancial liabilities, except for items that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually). FSP FAS 157-2 delays the effective date of SFAS No. 157 for these items to fiscal years beginning after November 15, 2008, and interim periods within those fiscal years.

In December 2007, the FASB issued SFAS No. 141R, Business Combinations. This statement, which addresses the accounting for business acquisitions, is effective for fiscal years beginning on or after December 15, 2008, with early adoption prohibited, and generally applies to business acquisitions completed after December 31, 2008. Among other things, the new standard requires that all acquisition-related costs be expensed as incurred, and that all restructuring costs related to acquired operations be expensed as incurred. This new standard also addresses the current and subsequent accounting for assets and liabilities arising from contingencies acquired or assumed and, for acquisitions both prior and subsequent to December 31, 2008, requires the acquirer to recognize changes in the amount of its deferred tax benefits that are recognizable because of a business combination either in income from continuing operations in the period of the combination or directly in contributed capital, depending on the circumstances. The Company is currently assessing the impact of SFAS No. 141R on the Company's consolidated financial position and results of operations.

In December 2007, the FASB issued SFAS No. 160, Noncontrolling Interests in Consolidated Financial Statements. SFAS No. 160 will change the accounting for minority interests, which will be recharacterized as noncontrolling interests and classified by the parent company as a component of equity. This statement is effective for fiscal years beginning on or after December 15, 2008, with early adoption prohibited. Upon adoption, SFAS No. 160 requires retroactive adoption of the presentation and disclosure requirements for existing minority interests and prospective adoption for all other requirements. The Company is currently assessing the impact of SFAS No. 160 on the Company's consolidated financial position and results of operations.

In September 2006, the FASB issued SFAS No. 158, Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans—an amendment of FASB Statements No. 87, 88, 106 and 132(R). This statement requires an employer on a prospective basis to recognize the overfunded or underfunded status of its defined benefit pension and postretirement plans as an asset or liability in its statement of financial position and to recognize changes in that funded status in the year in which the changes occur through other comprehensive income. The Company adopted this requirement, along with the required disclosures, on December 31, 2006. SFAS No. 158 also requires an employer on a

prospective basis to measure the funded status of its plans as of its

**Table of Contents****PRUDENTIAL FINANCIAL, INC.****Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

fiscal year-end. This requirement is effective for fiscal years ending after December 15, 2008. The Company will adopt this guidance on December 31, 2008 and anticipates that the impact of changing from a September 30 measurement date to a December 31 measurement date will not have a material effect on the Company's consolidated financial position.

**3. ACQUISITIONS AND DISPOSITIONS*****Acquisition of Hyundai Investment and Securities Co., Ltd.***

In 2004, the Company acquired an 80 percent interest in Hyundai Investment and Securities Co., Ltd., a Korean asset management firm, from an agency of the Korean government, for \$301 million in cash, including \$210 million used to repay debt assumed. Subsequent to the acquisition, the company was renamed Prudential Investment & Securities Co., Ltd. On January 25, 2008, the Company acquired the remaining 20 percent for \$90 million.

***Additional Investment in UBI Pramerica***

On January 18, 2008, the Company made an additional investment of \$154 million in its UBI Pramerica operating joint venture in Italy, which is accounted for under the equity method. This additional investment was necessary to maintain the Company's ownership interest at 35% and was a result of the merger of the Company's joint venture partner with another Italian bank, and their subsequent consolidation of their asset management companies into the UBI Pramerica joint venture.

***Discontinued Operations***

Income (loss) from discontinued businesses, including charges upon disposition, are as follows:

|   | <b>Three Months Ended<br/>March 31,</b> |             |
|---|---|-------------|
|   | <b>2008</b>                             | <b>2007</b> |
|   | <b>(in millions)</b>                    |             |
| Equity sales, trading and research operations | \$ (1)                                  | \$ 2        |
| Real estate investments sold or held for sale | 1                                       | 18          |
| International securities operations           | 1                                       | (3)         |

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|   |      |       |
|---|------|-------|
| Healthcare operations                                   |      | 5     |
| Income from discontinued operations before income taxes | 1    | 22    |
| Income tax expense (benefit)                            |      | (17)  |
| Income from discontinued operations, net of taxes       | \$ 1 | \$ 39 |

The three months ended March 31, 2007 includes a \$26 million tax benefit associated with a discontinued international business. Real estate investments sold or held for sale reflects the income from discontinued real estate investments.

The Company's Unaudited Interim Consolidated Statements of Financial Position include total assets and total liabilities related to discontinued businesses of \$215 million and \$54 million, respectively, as of March 31, 2008 and \$242 million and \$98 million, respectively, as of December 31, 2007. Charges recorded in connection with the disposals of businesses include estimates that are subject to subsequent adjustment. It is possible that such adjustments might be material to future net results of operations of a particular quarterly or annual period.

**Table of Contents****PRUDENTIAL FINANCIAL, INC.****Notes to Unaudited Interim Consolidated Financial Statements (Continued)****4. CLOSED BLOCK**

On the date of demutualization, Prudential Insurance established a Closed Block for certain individual life insurance policies and annuities issued by Prudential Insurance in the U.S. The recorded assets and liabilities were allocated to the Closed Block at their historical carrying amounts. The Closed Block forms the principal component of the Closed Block Business.

The policies included in the Closed Block are specified individual life insurance policies and individual annuity contracts that were in force on the effective date of the Plan of Reorganization and for which Prudential Insurance is currently paying or expects to pay experience-based policy dividends. Assets have been allocated to the Closed Block in an amount that has been determined to produce cash flows which, together with revenues from policies included in the Closed Block, are expected to be sufficient to support obligations and liabilities relating to these policies, including provision for payment of benefits, certain expenses, and taxes and to provide for continuation of the policyholder dividend scales in effect in 2000, assuming experience underlying such scales continues. To the extent that, over time, cash flows from the assets allocated to the Closed Block and claims and other experience related to the Closed Block are, in the aggregate, more or less favorable than what was assumed when the Closed Block was established, total dividends paid to Closed Block policyholders in the future may be greater than or less than the total dividends that would have been paid to these policyholders if the policyholder dividend scales in effect in 2000 had been continued. Any cash flows in excess of amounts assumed will be available for distribution over time to Closed Block policyholders and will not be available to stockholders. If the Closed Block has insufficient funds to make guaranteed policy benefit payments, such payments will be made from assets outside of the Closed Block. The Closed Block will continue in effect as long as any policy in the Closed Block remains in force unless, with the consent of the New Jersey insurance regulator, it is terminated earlier.

The excess of Closed Block Liabilities over Closed Block Assets at the date of the demutualization (adjusted to eliminate the impact of related amounts in Accumulated other comprehensive income (loss) ) represented the estimated maximum future earnings at that date from the Closed Block expected to result from operations attributed to the Closed Block after income taxes. In establishing the Closed Block, the Company developed an actuarial calculation of the timing of such maximum future earnings. If actual cumulative earnings of the Closed Block from inception through the end of any given period are greater than the expected cumulative earnings, only the expected earnings will be recognized in income. Any excess of actual cumulative earnings over expected cumulative earnings will represent undistributed accumulated earnings attributable to policyholders, which are recorded as a policyholder dividend obligation. The policyholder dividend obligation represents amounts to be paid to Closed Block policyholders as an additional policyholder dividend unless otherwise offset by future Closed Block performance that is less favorable than originally expected. If the actual cumulative earnings of the Closed Block from its inception through the end of any given period are less than the expected cumulative earnings of the Closed Block, the Company will recognize only the actual earnings in income. However, the Company may reduce policyholder dividend scales in the future, which would be intended to increase future actual earnings until the actual cumulative earnings equaled the expected cumulative earnings. The Company recognized a policyholder dividend obligation of \$579 million and \$732 million as of March 31, 2008 and December 31, 2007, respectively, to Closed Block policyholders for the excess of actual cumulative earnings over the expected cumulative earnings. Additionally, net unrealized investment gains (losses) that have arisen subsequent to the establishment of the Closed Block were reflected as an adjustment to the policyholder dividend obligation of \$(128) million and \$1.047 billion as of March 31, 2008 and December 31, 2007, respectively, with an offsetting amount reported in Accumulated other comprehensive income (loss). See the table below for changes in the components of the policyholder dividend obligation for the three months ended March 31, 2008.

**Table of Contents****PRUDENTIAL FINANCIAL, INC.****Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

Closed Block Liabilities and Assets designated to the Closed Block, as well as maximum future earnings to be recognized from Closed Block Liabilities and Closed Block Assets, are as follows:

|   | March 31,<br>2008 | December 31,<br>2007 |
|---|-------------------|----------------------|
|   | (in millions)     |                      |
| <b>Closed Block Liabilities</b>   |                   |                      |
| Future policy benefits  | \$ 51,271         | \$ 51,208            |
| Policyholders' dividends payable  | 1,268             | 1,212                |
| Policyholder dividend obligation  | 451               | 1,779                |
| Policyholders' account balances   | 5,568             | 5,555                |
| Other Closed Block liabilities  | 9,789             | 10,649               |
| <b>Total Closed Block Liabilities</b>   | <b>68,347</b>     | <b>70,403</b>        |
| <b>Closed Block Assets</b>  |                   |                      |
| Fixed maturities, available for sale, at fair value   | 42,676            | 45,459               |
| Other trading account assets, at fair value   | 149               | 142                  |
| Equity securities, available for sale, at fair value  | 3,503             | 3,858                |
| Commercial loans  | 7,895             | 7,353                |
| Policy loans  | 5,391             | 5,395                |
| Other long-term investments   | 1,208             | 1,311                |
| Short-term investments  | 1,492             | 1,326                |
| <b>Total investments</b>  | <b>62,314</b>     | <b>64,844</b>        |
| Cash and cash equivalents   | 1,483             | 1,310                |
| Accrued investment income   | 673               | 630                  |
| Other Closed Block assets   | 832               | 581                  |
| <b>Total Closed Block Assets</b>  | <b>65,302</b>     | <b>67,365</b>        |
| <b>Excess of reported Closed Block Liabilities over Closed Block Assets</b>                   | <b>3,045</b>      | <b>3,038</b>         |
| Portion of above representing accumulated other comprehensive income:                         |                   |                      |
| Net unrealized investment gains (losses)  | (168)             | 1,006                |
| Allocated to policyholder dividend obligation   | 128               | (1,047)              |
| <b>Future earnings to be recognized from Closed Block Assets and Closed Block Liabilities</b> | <b>\$ 3,005</b>   | <b>\$ 2,997</b>      |

Information regarding the policyholder dividend obligation is as follows:

**Three Months Ended  
March 31, 2008**



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|  | (in millions) |         |
|--|---------------|---------|
| Balance, January 1, 2008   | \$            | 1,779   |
| Impact on income before gains (losses) allocable to policyholder dividend obligation |               | (153)   |
| Change in net unrealized investment gains (losses)                                   |               | (1,175) |
| Balance, March 31, 2008  | \$            | 451     |

**Table of Contents****PRUDENTIAL FINANCIAL, INC.****Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

Closed Block revenues and benefits and expenses for the three months ended March 31, 2008 and 2007 were as follows:

|   | <b>Three Months Ended<br/>March 31,</b> |              |
|---|---|--------------|
|   | <b>2008</b>                             | <b>2007</b>  |
|   | <b>(in millions)</b>                    |              |
| <b>Revenues</b>   |   |              |
| Premiums  | \$ 856                                  | \$ 838       |
| Net investment income   | 841                                     | 859          |
| Realized investment gains (losses), net   | (95)                                    | 200          |
| Other income  | 19                                      | 13           |
| <b>Total Closed Block revenues</b>  | <b>1,621</b>                            | <b>1,910</b> |
| <b>Benefits and Expenses</b>  |   |              |
| Policyholders' benefits   | 972                                     | 949          |
| Interest credited to policyholders' account balances  | 35                                      | 36           |
| Dividends to policyholders  | 502                                     | 683          |
| General and administrative expenses   | 172                                     | 171          |
| <b>Total Closed Block benefits and expenses</b>   | <b>1,681</b>                            | <b>1,839</b> |
| Closed Block revenues, net of Closed Block benefits and expenses, before income taxes and discontinued operations | (60)                                    | 71           |
| Income tax expense (benefit)  | (52)                                    | 63           |
| Closed Block revenues, net of Closed Block benefits and expenses and income taxes, before discontinued operations | (8)                                     | 8            |
| Income from discontinued operations, net of taxes   |   | 2            |
| <b>Closed Block revenues, net of Closed Block benefits and expenses, income taxes and discontinued operations</b> | <b>\$ (8)</b>                           | <b>\$ 10</b> |

**5. STOCKHOLDERS' EQUITY**

The Company has outstanding two classes of common stock: the Common Stock and the Class B Stock. The changes in the number of shares issued, held in treasury and outstanding are as follows for the periods indicated:

**Common Stock**

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|                                      | Issued | Held In<br>Treasury | Outstanding<br>(in millions) | Class B<br>Stock<br>Issued and<br>Outstanding |
|--------------------------------------|--------|---------------------|------------------------------|---|
| <b>Balance, December 31, 2007</b>    | 604.9  | 157.5               | 447.4                        | 2.0   |
| Common Stock issued                  |        |                     |                              |   |
| Common Stock acquired                |        | 11.4                | (11.4)                       |   |
| Stock-based compensation programs(1) |        | (1.4)               | 1.4                          |   |
| <b>Balance, March 31, 2008</b>       | 604.9  | 167.5               | 437.4                        | 2.0   |

(1) Represents net shares issued from treasury pursuant to the Company's stock-based compensation programs.

**Table of Contents****PRUDENTIAL FINANCIAL, INC.****Notes to Unaudited Interim Consolidated Financial Statements (Continued)*****Common Stock Held in Treasury***

In November 2007, Prudential Financial's Board of Directors authorized the Company to repurchase up to \$3.5 billion of its outstanding Common Stock in calendar year 2008. The timing and amount of any repurchases under this authorization will be determined by management based upon market conditions and other considerations, and the repurchases may be effected in the open market, through derivative, accelerated repurchase and other negotiated transactions and through prearranged trading plans complying with Rule 10b5-1(c) of the Securities Exchange Act of 1934, as amended (the Exchange Act). The 2008 stock repurchase program supersedes all previous repurchase programs. During the three months ended March 31, 2008, the Company acquired 11.4 million shares of its Common Stock at a total cost of \$869 million.

***Comprehensive Income***

The components of comprehensive income are as follows:

|  | <b>Three Months Ended<br/>March 31</b> |             |
|--|--|-------------|
|  | <b>2008</b>                            | <b>2007</b> |
|  | <b>(in millions)</b>                   |             |
| Net income   | \$ 69                                  | \$ 1,120    |
| Other comprehensive income (loss), net of taxes:                       |  |             |
| Change in foreign currency translation adjustments                     | 253                                    | (40)        |
| Change in net unrealized investments gains (losses)(1)                 | (1,238)                                | 201         |
| Change in pension and postretirement unrecognized net periodic benefit | (1)                                    | 12          |
| Other comprehensive income (loss)(2)                                   | (986)                                  | 173         |
| Comprehensive income (loss)  | \$ (917)                               | \$ 1,293    |

(1) Includes cash flow hedges of \$(76) million and \$3 million for the three months ended March 31, 2008 and 2007, respectively.

(2) Amounts are net of tax expense (benefit) of \$(531) million and \$131 million for the three months March 31, 2008 and 2007, respectively.

The balance of and changes in each component of Accumulated other comprehensive income (loss) for the three months ended March 31, 2008 are as follows (net of taxes):

**Accumulated Other Comprehensive Income (Loss)**

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|                                   | Foreign<br>Currency<br>Translation<br>Adjustments | Net<br>Unrealized<br>Investment<br>Gains<br>(Losses)(1) | Pension and<br>Postretirement<br>Unrecognized<br>Net Periodic<br>Benefit<br>(Cost) | Total<br>Accumulated<br>Other<br>Comprehensive<br>Income<br>(Loss) |
|-----------------------------------|---|---|--|--|
|                                   |   |   | (in millions)  |  |
| Balance, December 31, 2007        | \$ 312  | \$ 400  | \$ (265)   | \$ 447   |
| Change in component during period | 253   | (1,238)   | (1)  | (986)  |
| Balance, March 31, 2008           | \$ 565  | \$ (838)  | \$ (266)   | \$ (539)   |

(1) Includes cash flow hedges of \$(249) million and \$(173) million as of March 31, 2008 and December 31, 2007, respectively.

**Table of Contents****PRUDENTIAL FINANCIAL, INC.****Notes to Unaudited Interim Consolidated Financial Statements (Continued)****6. EARNINGS PER SHARE**

The Company has outstanding two separate classes of common stock. The Common Stock reflects the performance of the Financial Services Businesses and the Class B Stock reflects the performance of the Closed Block Business. Accordingly, earnings per share is calculated separately for each of these two classes of common stock.

Net income for the Financial Services Businesses and the Closed Block Business is determined in accordance with U.S. GAAP and includes general and administrative expenses charged to each of the respective businesses based on the Company's methodology for the allocation of such expenses. Cash flows between the Financial Services Businesses and the Closed Block Business related to administrative expenses are determined by a policy servicing fee arrangement that is based upon insurance and policies in force and statutory cash premiums. To the extent reported administrative expenses vary from these cash flow amounts, the differences are recorded, on an after tax basis, as direct equity adjustments to the equity balances of the businesses.

The direct equity adjustments modify the earnings available to each of the classes of common stock for earnings per share purposes.

**Common Stock**

A reconciliation of the numerators and denominators of the basic and diluted per share computations is as follows:

|   | Three Months Ended March 31, |                               |                        |          |                               |                        |
|---|------------------------------|-------------------------------|------------------------|----------|-------------------------------|------------------------|
|   | 2008                         |                               | 2007                   |          |                               |                        |
|   | Income                       | Weighted<br>Average<br>Shares | Per<br>Share<br>Amount | Income   | Weighted<br>Average<br>Shares | Per<br>Share<br>Amount |
| (in millions, except per share amounts)   |                              |                               |                        |          |                               |                        |
| <b>Basic earnings per share</b>   |                              |                               |                        |          |                               |                        |
| Income from continuing operations attributable to the Financial Services Businesses   | \$ 76                        |                               |                        | \$ 988   |                               |                        |
| Direct equity adjustment  | 12                           |                               |                        | 15       |                               |                        |
| Income from continuing operations attributable to the Financial Services Businesses available to holders of Common Stock after direct equity adjustment | \$ 88                        | 442.1                         | \$ 0.20                | \$ 1,003 | 468.4                         | \$ 2.14                |
| <b>Effect of dilutive securities and compensation programs</b>  |                              |                               |                        |          |                               |                        |
| Stock options   |                              | 3.9                           |                        |          | 5.8                           |                        |

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|  |       |       |         |                        |
|--|-------|-------|---------|------------------------|
| Deferred and long-term compensation programs                                   |       | 2.6   |         | 3.0                    |
| <b>Diluted earnings per share</b>  |       |       |         |                        |
| Income from continuing operations attributable to the Financial Services       |       |       |         |                        |
| Businesses available to holders of Common Stock after direct equity adjustment | \$ 88 | 448.6 | \$ 0.20 | \$ 1,003 477.2 \$ 2.10 |

For the three months ended March 31, 2008 and 2007, 4.1 million and 1.2 million options, respectively, weighted for the portion of the period they were outstanding, with a weighted average exercise price of \$83.44 and \$91.36 per share, respectively, were excluded from the computation of diluted earnings per share because the options, based on application of the treasury stock method, were antidilutive.

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**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

*Convertible Senior Notes*

The Company's convertible senior notes provide for the Company to issue shares of its Common Stock as a component of the conversion of the notes. The \$2.0 billion November 2005 issuance was called for redemption in May 2007. These notes were not dilutive to earnings per share for the three months ended March 31, 2007, as the average market price of the Common Stock was below the initial conversion price of \$90.00. The \$2.0 billion December 2006 issuance will be dilutive to earnings per share if the average market price of the Common Stock for a particular period is above the initial conversion price of \$104.21. The \$3.0 billion December 2007 issuance will be dilutive to earnings per share if the average market price of the Common Stock for a particular period is above the initial conversion price of \$132.39.

*Class B Stock*

Income (loss) from continuing operations per share of Class B Stock was \$(10.00) and \$39.00 for the three months ended March 31, 2008 and 2007, respectively.

The income (loss) from continuing operations attributable to the Closed Block Business available to holders of Class B Stock after direct equity adjustment for the three months ended March 31, 2008 and 2007 amounted to \$(20) million and \$78 million, respectively. The direct equity adjustment resulted in a decrease in the income (loss) from continuing operations attributable to the Closed Block Business applicable to holders of Class B Stock for earnings per share purposes of \$12 million and \$15 million for the three months ended March 31, 2008 and 2007, respectively. For the three months ended March 31, 2008 and 2007, the weighted average number of shares of Class B Stock used in the calculation of earnings per share amounted to 2.0 million. There are no potentially dilutive shares associated with the Class B Stock.

**7. EMPLOYEE BENEFIT PLANS**

The Company has funded and non-funded contributory and non-contributory defined benefit pension plans, which cover substantially all of its employees. For some employees, benefits are based on final average earnings and length of service, while benefits for other employees are based on an account balance that takes into consideration age, service and earnings during their career.

The Company provides certain health care and life insurance benefits for its retired employees, their beneficiaries and covered dependents (other postretirement benefits). The health care plan is contributory; the life insurance plan is non-contributory. Substantially all of the Company's U.S. employees may become eligible to receive other postretirement benefits if they retire after age 55 with at least 10 years of service or under certain circumstances after age 50 with at least 20 years of continuous service.





**Table of Contents****PRUDENTIAL FINANCIAL, INC.****Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

Net periodic (benefit) cost included in General and administrative expenses includes the following components:

|  | Three Months Ended March 31, |         |                               |       |
|--|------------------------------|---------|-------------------------------|-------|
|  | Pension Benefits             |         | Other Postretirement Benefits |       |
|  | 2008                         | 2007    | 2008                          | 2007  |
|  | (in millions)                |         |                               |       |
| <b>Components of net periodic (benefit) cost</b> |                              |         |                               |       |
| Service cost                                     | \$ 39                        | \$ 42   | \$ 3                          | \$ 3  |
| Interest cost                                    | 117                          | 108     | 31                            | 34    |
| Expected return on plan assets                   | (180)                        | (192)   | (40)                          | (23)  |
| Amortization of prior service cost               | 11                           | 7       | (3)                           | (1)   |
| Amortization of actuarial (gain) loss, net       | 4                            | 7       |                               | 3     |
| Special termination benefits                     | 2                            |         |                               |       |
| Net periodic (benefit) cost                      | \$ (7)                       | \$ (28) | \$ (9)                        | \$ 16 |

**8. SEGMENT INFORMATION*****Segments***

The Company has organized its principal operations into the Financial Services Businesses and the Closed Block Business. Within the Financial Services Businesses, the Company operates through three divisions, which together encompass eight reportable segments. The Company's real estate and relocation services business as well as businesses that are not sufficiently material to warrant separate disclosure and businesses to be divested are included in Corporate and Other operations within the Financial Services Businesses. Collectively, the businesses that comprise the three operating divisions and Corporate and Other are referred to as the Financial Services Businesses.

In reporting results for the three months ended March 31, 2008, the Company has classified its commercial mortgage securitization operations as a divested business, reflecting its decision to exit this business. As a result of this decision, these operations, which involved the origination and purchase of commercial mortgage loans for sale into commercial mortgage-backed securitization transactions, together with related hedging activities, previously reported within the Asset Management segment, have been classified within divested businesses and are reflected in the Company's Corporate and Other operations. Accordingly, these results are excluded from adjusted operating income, with prior period results being adjusted to reflect such reclassification. These operations had a pre-tax loss of \$107 million for the first quarter of 2008. The Company will retain and continue the remainder of its commercial mortgage origination, servicing and other commercial mortgage related activities, which remain a part of the Asset Management segment.

*Adjusted Operating Income*

In managing the Financial Services Businesses, the Company analyzes the operating performance of each segment using adjusted operating income. Adjusted operating income does not equate to income from continuing operations before income taxes and equity in earnings of operating joint ventures or net income as determined in accordance with U.S. GAAP but is the measure of segment profit or loss used by the Company to evaluate segment performance and allocate resources, and, consistent with SFAS No. 131, Disclosures about Segments of an Enterprise and Related Information, is the measure of segment performance presented below.

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**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

Adjusted operating income is calculated by adjusting each segment's income from continuing operations before income taxes and equity in earnings of operating joint ventures for the following items, which are described in greater detail below:

realized investment gains (losses), net, and related charges and adjustments;

net investment gains and losses on trading account assets supporting insurance liabilities and changes in experience-rated contractholder liabilities due to asset value changes;

the contribution to income/loss of divested businesses that have been or will be sold or exited but that did not qualify for discontinued operations accounting treatment under U.S. GAAP; and

equity in earnings of operating joint ventures.

These items are important to an understanding of overall results of operations. Adjusted operating income is not a substitute for income determined in accordance with U.S. GAAP, and the Company's definition of adjusted operating income may differ from that used by other companies. However, the Company believes that the presentation of adjusted operating income as measured for management purposes enhances the understanding of results of operations by highlighting the results from ongoing operations and the underlying profitability factors of the Financial Services Businesses.

Effective with the first quarter of 2008, the Company has amended its definition of adjusted operating income as it relates to certain externally managed investments in the European market held within the general account portfolio. These investments are medium term notes that are collateralized by investment portfolios primarily consisting of investment grade European fixed income securities, including corporate bonds and asset-backed securities, and derivatives, as well as varying degrees of leverage. The notes have a stated coupon and provide a return based on the performance of the underlying portfolios and the level of leverage. The Company invests in these notes to earn a coupon through maturity, consistent with its investment purpose for other debt securities. The notes are accounted for under U.S. GAAP as available for sale fixed maturity securities with bifurcated embedded derivatives (total return swaps). Changes in the value of the fixed maturity securities are reported in Stockholders' Equity under the heading Accumulated Other Comprehensive Income and changes in the market value of the embedded total return swaps are included in current period earnings in Realized investment gains (losses), net. Historically, adjusted operating income included cumulative losses and recoveries of such losses on the embedded derivatives in the period they occurred, while cumulative net gains on the embedded derivatives were deferred and amortized into adjusted operating income over the remaining life of the notes.

Adjusted operating income under the amended definition excludes any amounts related to changes in the market value of the embedded derivatives. Adjusted operating income for all periods presented has been revised to conform with the amended definition. The Company views adjusted operating income under the amended definition as a more meaningful presentation of its results for purposes of analyzing the operating performance of, and allocating resources to, its business segments, as the amended definition presents the results of these investments on a basis generally consistent with similar investments held directly within the general account portfolio. The Company believes the mark to market losses discussed below, resulting primarily from unprecedented credit spread widening, are not representative of the fundamental value of the underlying investments over the long term. Adjusted operating income continues to include the coupon on these notes, which reflects the market

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based interest rate and spread of securities comparable to the underlying securities that existed at the time the Company entered into the investments. The accounting for these investments under U.S. GAAP has not changed.

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**Table of Contents****PRUDENTIAL FINANCIAL, INC.****Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

For the three months ended March 31, 2008 and 2007, the Company recorded a loss of \$208 million and a gain of \$8 million, respectively, within Realized investment gains (losses), net related to the change in value on the embedded derivatives associated with these investments, which are excluded from adjusted operating income under the amended definition. The loss of \$208 million for the three months ended March 31, 2008 is reflected within the U.S. GAAP results of the following segments: Individual Life \$12 million, Individual Annuities \$11 million, Group Insurance \$10 million, Retirement \$39 million, and International Insurance \$136 million. Adjusted operating income under the former definition included a \$1 million gain for the three months ended March 31, 2007, which represented the amortization of cumulative deferred gains.

*Realized investment gains (losses), net, and related charges and adjustments.* Adjusted operating income excludes realized investment gains (losses), net, except as indicated below. A significant element of realized investment gains and losses are impairments and credit-related and interest rate-related gains and losses. Impairments and losses from sales of credit-impaired securities, the timing of which depends largely on market credit cycles, can vary considerably across periods. The timing of other sales that would result in gains or losses, such as interest rate-related gains or losses, is largely subject to the Company's discretion and influenced by market opportunities, as well as the Company's tax profile. Trends in the underlying profitability of the Company's businesses can be more clearly identified without the fluctuating effects of these transactions.

Charges that relate to realized investment gains (losses), net, are also excluded from adjusted operating income. The related charges are associated with: policyholder dividends; amortization of deferred policy acquisition costs, valuation of business acquired (VOBA), unearned revenue reserves and deferred sales inducements; interest credited to policyholders' account balances; reserves for future policy benefits; payments associated with the market value adjustment features related to certain of the annuity products the Company sells; and minority interest in consolidated operating subsidiaries. The related charges associated with policyholder dividends include a percentage of the net increase in the fair value of specified assets included in Gibraltar Life's reorganization plan that is required to be paid as a special dividend to Gibraltar Life policyholders. Deferred policy acquisition costs, VOBA, unearned revenue reserves and deferred sales inducements for certain products are amortized based on estimated gross profits, which include net realized investment gains and losses on the underlying invested assets. The related charge for these items represent the portion of this amortization associated with net realized investment gains and losses. The related charges for interest credited to policyholders' account balances relate to certain group life policies that pass back certain realized investment gains and losses to the policyholder. The reserves for certain policies are adjusted when cash flows related to these policies are affected by net realized investment gains and losses, and the related charge for reserves for future policy benefits represents that adjustment. Certain of the Company's annuity products contain a market value adjustment feature that requires us to pay to the contractholder or entitles us to receive from the contractholder, upon surrender, a market value adjustment based on the crediting rates on the contract surrendered compared to crediting rates on newly issued contracts or based on an index rate at the time of purchase compared to an index rate at time of surrender, as applicable. These payments mitigate the net realized investment gains or losses incurred upon the disposition of the underlying invested assets. The related charge represents the payments or receipts associated with these market value adjustment features. Minority interest expense is recorded for the earnings of consolidated subsidiaries owed to minority investors. The related charge for minority interest in consolidated operating subsidiaries represents the portion of these earnings associated with net realized investment gains and losses.

Adjustments to Realized investment gains (losses), net, for purposes of calculating adjusted operating income, include the following:

Gains and losses pertaining to derivative contracts that do not qualify for hedge accounting treatment, other than derivatives used in the Company's capacity as a broker or dealer, are included in Realized investment gains



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**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

(losses), net. This includes mark-to-market adjustments of open contracts as well as periodic settlements. As discussed further below, adjusted operating income includes a portion of realized gains and losses pertaining to certain derivative contracts.

Adjusted operating income of the International Insurance segment and International Investments segment, excluding the global commodities group, reflect the impact of an intercompany arrangement with Corporate and Other operations pursuant to which the segments' non-U.S. dollar denominated earnings in all countries for a particular year, including its interim reporting periods, are translated at fixed currency exchange rates. The fixed rates are determined in connection with a currency hedging program designed to mitigate the risk that unfavorable rate changes will reduce the segments' U.S. dollar equivalent earnings. Pursuant to this program, the Company's Corporate and Other operations execute forward currency contracts with third parties to sell the hedged currency in exchange for U.S. dollars at a specified exchange rate. The maturities of these contracts correspond with the future periods in which the identified non-U.S. dollar denominated earnings are expected to be generated. These contracts do not qualify for hedge accounting under U.S. GAAP and, as noted above, all resulting profits or losses from such contracts are included in Realized investment gains (losses), net. When the contracts are terminated in the same period that the expected earnings emerge, the resulting positive or negative cash flow effect is included in adjusted operating income (net gains of \$1 million and \$21 million for the three months ended March 31, 2008 and 2007, respectively). As of March 31, 2008 and December 31, 2007, the fair value of open contracts used for this purpose was a net liability of \$128 million and a net asset of \$12 million, respectively.

The Company uses interest rate and currency swaps and other derivatives to manage interest and currency exchange rate exposures arising from mismatches between assets and liabilities, including duration mismatches. For the derivative contracts that do not qualify for hedge accounting treatment, mark-to-market adjustments of open contracts as well as periodic settlements are included in Realized investment gains (losses), net. However, the periodic swap settlements, as well as other derivative related yield adjustments, are included in adjusted operating income to reflect the after-hedge yield of the underlying instruments. Adjusted operating income includes net gains of \$12 million and \$23 million for the three months ended March 31, 2008 and 2007, respectively, due to periodic settlements and yield adjustments of such contracts.

Certain products the Company sells are accounted for as freestanding derivatives or contain embedded derivatives. Changes in the fair value of these derivatives, along with any fees received or payments made relating to the derivative, are recorded in Realized investment gains (losses), net. These Realized investment gains (losses), net are included in adjusted operating income in the period in which the gain or loss is recorded. In addition, the changes in fair value of any associated derivative portfolio that is part of an economic hedging program related to the risk of these products (but which do not qualify for hedge accounting treatment under U.S. GAAP) are also included in adjusted operating income in the period in which the gains or losses on the derivative portfolio are recorded. Adjusted operating income includes net losses of \$43 million and net gains of \$15 million for the three months ended March 31, 2008 and 2007, respectively, related to these products and any associated derivative portfolio.

Adjustments are also made for the purposes of calculating adjusted operating income for the following items:

The Company conducts certain activities for which Realized investment gains (losses), net are a principal source of earnings for its businesses and therefore included in adjusted operating income, particularly within the Company's Asset Management segment. For example, Asset Management's proprietary investing business makes investments for sale or syndication to other investors or for placement or co-investment in the Company's managed funds and structured products. The Realized investment gains (losses), net associated with the sale of





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**Table of Contents****PRUDENTIAL FINANCIAL, INC.****Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

these proprietary investments, including related derivative results, are a principal source of earnings for this business and included in adjusted operating income. In addition, the Realized investment gains (losses), net associated with loans originated by the Company's commercial mortgage operations, including related derivative results and retained mortgage servicing rights, are a principal source of earnings for this business and included in adjusted operating income. Net realized investment losses of \$39 million and gains of \$19 million related to these and other businesses were included in adjusted operating income for the three months ended March 31, 2008 and 2007, respectively.

The Company has certain investments supporting insurance liabilities in its general account portfolio that are classified as trading. These trading investments are carried at fair value and included in Other trading account assets, at fair value on the Company's statements of financial position. Realized and unrealized gains and losses for these investments are recorded in Asset management fees and other income, and interest and dividend income for these investments is recorded in Net investment income. Consistent with the exclusion of realized investment gains and losses with respect to other investments supporting insurance liabilities managed on a consistent basis the net gains or losses on these investments, which is recorded within Asset management fees and other income, is excluded from adjusted operating income and is reflected as an adjustment to Realized investment gains (losses), net. These adjustments were a net gain of \$3 million for the three months ended March 31, 2008. There was no adjustment for the three months ended March 31, 2007.

The Company has certain assets and liabilities for which, under GAAP, the change in value due to changes in foreign currency exchange rates during the period is recorded in Asset management fees and other income. To the extent the foreign currency exposure on these assets and liabilities is economically hedged, the change in value included in Asset management fees and other income is excluded from adjusted operating income and is reflected as an adjustment to Realized investment gains (losses), net. These adjustments were a net gain of \$65 million and \$12 million for the three months ended March 31, 2008 and 2007, respectively.

*Investment gains and losses on trading account assets supporting insurance liabilities and changes in experience-rated contractholder liabilities due to asset value changes.* Certain products included in the Retirement and International Insurance segments are experience-rated in that investment results associated with these products will ultimately accrue to contractholders. The investments supporting these experience-rated products, excluding commercial loans, are classified as trading and are carried at fair value. These trading investments are reflected on the statements of financial position as Trading account assets supporting insurance liabilities, at fair value. Realized and unrealized gains and losses for these investments are reported in Asset management fees and other income. Interest and dividend income for these investments is reported in Net investment income. Commercial loans that support these experience-rated products are carried at unpaid principal, net of unamortized discounts and an allowance for losses, and are reflected on the statements of financial position as Commercial loans.

Adjusted operating income excludes net investment gains and losses on trading account assets supporting insurance liabilities. This is consistent with the exclusion of realized investment gains and losses with respect to other investments supporting insurance liabilities managed on a consistent basis. In addition, to be consistent with the historical treatment of charges related to realized investment gains and losses on available for sale securities, adjusted operating income also excludes the change in contractholder liabilities due to asset value changes in the pool of investments (including commercial loans) supporting these experience-rated contracts, which are reflected in Interest credited to policyholders account balances. The result of this approach is that adjusted operating income for these products includes only net fee revenue and interest spread the Company earns on these experience-rated contracts, and excludes changes in fair value of the pool of investments, both realized and unrealized, that accrue to the contractholders.



**Table of Contents****PRUDENTIAL FINANCIAL, INC.****Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

*Divested businesses.* The contribution to income/loss of divested businesses that have been or will be sold or exited, but that did not qualify for discontinued operations accounting treatment under U.S. GAAP, are excluded from adjusted operating income as the results of divested businesses are not relevant to understanding the Company's ongoing operating results.

*Equity in earnings of operating joint ventures.* Equity in earnings of operating joint ventures, on a pre-tax basis, are included in adjusted operating income as these results are a principal source of earnings. These earnings are reflected on a GAAP basis on an after-tax basis as a separate line on the Company's Unaudited Interim Consolidated Statements of Operations.

The summary below reconciles adjusted operating income before income taxes for the Financial Services Businesses to income from continuing operations before income taxes and equity in earnings of operating joint ventures:

|  | <b>Three Months Ended<br/>March 31,</b> |              |
|--|---|--------------|
|  | <b>2008</b>                             | <b>2007</b>  |
|  | <b>(in millions)</b>                    |              |
| <b>Adjusted Operating Income before income taxes for Financial Services Businesses by Segment:</b> |   |              |
| Individual Life  | \$ 96                                   | \$ 101       |
| Individual Annuities   | 115                                     | 166          |
| Group Insurance  | 90                                      | 51           |
| <b>Total Insurance Division</b>  | <b>301</b>                              | <b>318</b>   |
| Asset Management   | 119                                     | 175          |
| Financial Advisory   | 44                                      | 97           |
| Retirement   | 124                                     | 148          |
| <b>Total Investment Division</b>   | <b>287</b>                              | <b>420</b>   |
| International Insurance  | 413                                     | 412          |
| International Investments  | 26                                      | 62           |
| <b>Total International Insurance and Investments Division</b>                                      | <b>439</b>                              | <b>474</b>   |
| Corporate Operations   | (12)                                    | 12           |
| Real Estate and Relocation Services  | (23)                                    | (3)          |
| <b>Total Corporate and Other</b>   | <b>(35)</b>                             | <b>9</b>     |
| <b>Adjusted Operating Income before income taxes for Financial Services Businesses</b>             | <b>992</b>                              | <b>1,221</b> |
| <b>Reconciling items:</b>  |   |              |
| Realized investment gains (losses), net, and related adjustments                                   | (665)                                   | 147          |

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|  |       |          |
|--|-------|----------|
| Charges related to realized investment gains (losses), net   | (13)  | (6)      |
| Investment gains (losses) on trading account assets supporting insurance liabilities, net  | (262) | 82       |
| Change in experience-rated contractholder liabilities due to asset value changes   | 200   | (62)     |
| Divested businesses  | (112) | 28       |
| Equity in earnings of operating joint ventures   | (60)  | (120)    |
| Income from continuing operations before income taxes and equity in earnings of operating joint ventures for Financial Services Businesses | 80    | 1,290    |
| Income (loss) from continuing operations before income taxes and equity in earnings of operating joint ventures for Closed Block Business  | (26)  | 137      |
| Income from continuing operations before income taxes and equity in earnings of operating joint ventures                                   | \$ 54 | \$ 1,427 |

**Table of Contents****PRUDENTIAL FINANCIAL, INC.****Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

The Insurance division results reflect deferred policy acquisition costs as if the individual annuity business and group insurance business were stand-alone operations. The elimination of intersegment costs capitalized in accordance with this policy is included in consolidating adjustments within Corporate and Other operations.

The summary below presents revenues for the Company's reportable segments:

|   | <b>Three Months Ended<br/>March 31,<br/>2008                      2007<br/>(in millions)</b> |              |
|---|--|--------------|
| <b>Financial Services Businesses:</b>   |  |              |
| Individual Life   | \$ 680   | \$ 631       |
| Individual Annuities  | 573  | 604          |
| Group Insurance   | 1,257  | 1,205        |
| <b>Total Insurance Division</b>   | <b>2,510</b>   | <b>2,440</b> |
| Asset Management  | 548  | 545          |
| Financial Advisory  | 51   | 111          |
| Retirement  | 1,267  | 1,163        |
| <b>Total Investment Division</b>  | <b>1,866</b>   | <b>1,819</b> |
| International Insurance   | 2,325  | 2,053        |
| International Investments   | 176  | 177          |
| <b>Total International Insurance and Investments Division</b>                             | <b>2,501</b>   | <b>2,230</b> |
| Corporate Operations  | 53   | 100          |
| Real Estate and Relocation Services   | 46   | 59           |
| <b>Total Corporate and Other</b>  | <b>99</b>  | <b>159</b>   |
| <b>Total</b>  | <b>6,976</b>   | <b>6,648</b> |
| <b>Reconciling items:</b>   |  |              |
| Realized investment gains (losses), net, and related adjustments                          | (665)  | 147          |
| Charges related to realized investment gains (losses), net                                | 1  | 1            |
| Investment gains (losses) on trading account assets supporting insurance liabilities, net | (262)  | 82           |
| Divested businesses   | (97)   | 26           |
| Equity in earnings of operating joint ventures  | (60)   | (120)        |
| <b>Total Financial Services Businesses</b>  | <b>5,893</b>   | <b>6,784</b> |

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|  |                 |                 |
|--|-----------------|-----------------|
| Closed Block Business  | 1,671           | 1,991           |
| <b>Total per Unaudited Interim Consolidated Financial Statements</b> | <b>\$ 7,564</b> | <b>\$ 8,775</b> |

The Asset Management segment revenues include intersegment revenues of \$93 million and \$91 million for the three months ended March 31, 2008 and 2007, respectively, primarily consisting of asset-based management and administration fees. Management has determined the intersegment revenues with reference to market rates. Intersegment revenues are eliminated in consolidation in Corporate and Other.

**Table of Contents****PRUDENTIAL FINANCIAL, INC.****Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

The summary below presents total assets for the Company's reportable segments as of the periods indicated:

|   | March 31,<br>2008 | December 31,<br>2007 |
|---|-------------------|----------------------|
|   | (in millions)     |                      |
| Individual Life   | \$ 35,214         | \$ 36,124            |
| Individual Annuities  | 73,018            | 76,685               |
| Group Insurance   | 32,020            | 32,913               |
| Total Insurance Division                                      | 140,252           | 145,722              |
| Asset Management  | 41,449            | 40,592               |
| Financial Advisory  | 2,887             | 1,294                |
| Retirement  | 127,764           | 132,614              |
| Total Investment Division                                     | 172,100           | 174,500              |
| International Insurance                                       | 69,718            | 65,387               |
| International Investments                                     | 8,855             | 7,711                |
| Total International Insurance and Investments Division        | 78,573            | 73,098               |
| Corporate Operations  | 14,365            | 17,430               |
| Real Estate and Relocation Services                           | 1,280             | 1,281                |
| Total Corporate and Other                                     | 15,645            | 18,711               |
| Total Financial Services Businesses                           | 406,570           | 412,031              |
| Closed Block Business   | 71,750            | 73,783               |
| Total per Unaudited Interim Consolidated Financial Statements | \$ 478,320        | \$ 485,814           |

**9. FAIR VALUE**

**Transition Impact** As discussed in Note 2, the Company adopted SFAS No. 157 and SFAS No. 159 effective January 1, 2008. As a result of adopting SFAS No. 157, the Company eliminated the deferral of gains at inception of certain derivatives contracts whose fair value was not evidenced by market-observable data. The elimination of the deferral of these gains resulted in a net after-tax increase to retained earnings of \$3 million.



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Also as discussed in Note 2, in conjunction with the adoption of SFAS No. 159, the Company elected the fair value option for fixed rate commercial loans held for investments that were held at December 31, 2007. This election resulted in \$399 million of commercial loans being reported at fair value, with no material impact on the Company's consolidated financial position. In addition, SFAS No. 159 requires entities to classify cash receipts and cash payments related to items measured at fair value according to their nature and purpose on the Statement of Cash Flows. As a result, cash flows related to trading account assets supporting insurance liabilities and certain other assets are classified as investing rather than operating as of the adoption date of this guidance.

**Fair Value Measurement** Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. SFAS No. 157 establishes a framework for measuring fair value that includes a hierarchy used to classify the inputs used in measuring fair value. The hierarchy prioritizes the inputs to valuation techniques used to measure fair value into three levels. The level in the fair value hierarchy within which the fair value measurement falls is determined based on the lowest level input that is significant to the fair value measurement. The levels of the fair value hierarchy are as follows:

Level 1 Fair value is based on unadjusted quoted prices in active markets that are accessible to the Company for identical assets or liabilities. These generally provide the most reliable evidence and are used to

**Table of Contents****PRUDENTIAL FINANCIAL, INC.****Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

measure fair value whenever available. The Company's Level 1 assets and liabilities primarily include equity securities and derivative contracts that are traded in an active exchange market. Valuations are obtained from readily available pricing sources for market transactions involving identical assets or liabilities.

Level 2 Fair value is based on significant inputs, other than Level 1 inputs, that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the asset or liability through corroboration with observable market data. Level 2 inputs include quoted market prices in active markets for similar assets and liabilities, quoted market prices in markets that are not active for identical or similar assets or liabilities and other observable inputs. The Company's Level 2 assets and liabilities include: fixed maturities (corporate public and private bonds, most government securities, certain asset-backed and mortgage-backed securities, etc.), certain equity securities, commercial loans, short-term investments and cash equivalents (primarily commercial paper and money market funds), and certain over-the-counter derivatives. Valuations are generally obtained from third party pricing services for identical or comparable assets or liabilities (and validated through backtesting to trade data or confirmation that the pricing service significant inputs are observable) or determined through use of valuation methodologies using observable market inputs.

Level 3 Fair value is based on significant unobservable inputs for the asset or liability. These inputs reflect the Company's or third party pricing service assumptions about the assumptions market participants would use in pricing the asset or liability. The Company's Level 3 assets and liabilities primarily include: certain private fixed maturities and equity securities, certain manually priced public equity securities and fixed maturities, (including certain asset-backed securities), certain highly structured over-the-counter derivative contracts, and embedded derivatives resulting from certain products with guaranteed benefits. Valuations are determined using valuation methodologies such as option pricing models, discounted cash flow models and other similar techniques.

The table below presents the balances of assets and liabilities measured at fair value on a recurring basis, as of March 31, 2008.

|   | Level 1       | Level 2    | Level 3   | Netting(2) | Total      |
|---|---------------|------------|-----------|------------|------------|
|   | (in millions) |            |           |            |            |
| Fixed maturities, available for sale                    | \$ 5          | \$ 161,368 | \$ 3,099  | \$         | \$ 164,472 |
| Trading Account Assets Supporting Insurance Liabilities | 601           | 13,850     | 193       |            | 14,644     |
| Other trading account assets                            | 428           | 5,211      | 626       | (3,432)    | 2,833      |
| Equity securities, available for sale                   | 5,372         | 2,570      | 187       |            | 8,129      |
| Commercial loans  |               | 657        |           |            | 657        |
| Other long-term investments                             | 308           | 336        | 877       |            | 1,521      |
| Short term investments                                  |               | 4,100      |           |            | 4,100      |
| Cash and cash equivalents                               | 115           | 7,393      |           |            | 7,508      |
| Other assets  | 88            | 2,696      |           |            | 2,784      |
| Sub-total excluding separate account assets             | 6,917         | 198,181    | 4,982     | (3,432)    | 206,648    |
| Separate account assets(1)                              | 82,027        | 77,767     | 22,108    |            | 181,902    |
| Total assets  | \$ 88,944     | \$ 275,948 | \$ 27,090 | \$ (3,432) | \$ 388,550 |

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|                        |       |          |        |            |  |          |
|------------------------|-------|----------|--------|------------|--|----------|
| Future policy benefits |       |          |        | 452        |  | 452      |
| Long-term debt         |       |          |        | 184        |  | 184      |
| Other liabilities      | 13    | 4,209    | 118    | (3,109)    |  | 1,231    |
| Total liabilities      | \$ 13 | \$ 4,209 | \$ 754 | \$ (3,109) |  | \$ 1,867 |

**Table of Contents****PRUDENTIAL FINANCIAL, INC.****Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

- (1) Separate account assets represent segregated funds that are invested for certain customers. Investment risks associated with market value changes are borne by the customers, except to the extent of minimum guarantees made by the Company with respect to certain accounts. Separate account assets classified as Level 3 consist primarily of real estate and real estate investment funds. Separate account liabilities are not included in the above table as they are reported at contract value and not fair value in the Company's consolidated Statement of Financial Position.
- (2) Netting amounts represent cash collateral and the impact of offsetting asset and liability positions held with the same counterparty as permitted by FASB Interpretation No. 39, *Offsetting of Amounts Related to Certain Contracts and FSP FIN 39-1, Amendment of FASB Interpretation No. 39*.

The following tables provide a summary of the changes in fair value of Level 3 assets and liabilities for the period January 1, 2008 to March 31, 2008, as well as the portion of gains or losses included in income attributable to unrealized gains or losses related to those assets and liabilities still held at March 31, 2008.

|  | Fixed<br>Maturities,<br>Available For<br>Sale | Trading<br>Account Assets<br>Supporting<br>Insurance<br>Liabilities | Other Trading<br>Account Assets | Equity<br>Securities,<br>Available for<br>Sale |
|--|---|---|---------------------------------|--|
|  | (in millions)                                 |   |                                 |  |
| Fair value, beginning of period                | \$ 2,890                                      | \$ 291  | \$ 497                          | \$ 190   |
| Total gains or (losses) (realized/unrealized): |   |   |                                 |  |
| Included in earnings:                          |   |   |                                 |  |
| Realized investment gains (losses), net        | (144)   |   | 99                              | (1)  |
| Asset management fees and other income         |   | 1   | (5)                             |  |
| Included in other comprehensive income (loss)  | (122)   |   |                                 | (12)   |
| Net investment income                          | 3   |   |                                 |  |
| Purchases, sales, issuances, and settlements   | (58)  | (9)   | 34                              | (2)  |
| Foreign currency translation                   |   |   | 1                               | 1  |
| Transfers into (out of) Level 3                | 530   | (90)  |                                 | 11   |
| Fair value, end of period                      | \$ 3,099                                      | \$ 193  | \$ 626                          | \$ 187   |

Unrealized gains (losses) for the period relating to those Level 3 assets that were still held by the Company at the end of the period(2):

|   |          |         |        |         |
|---|----------|---------|--------|---------|
| Included in earnings:                         |          |         |        |         |
| Realized investment gains (losses), net       | \$ (150) | \$      | \$ 99  | \$ (1)  |
| Asset management fees and other income        | \$       | \$ (10) | \$ (5) | \$      |
| Included in other comprehensive income (loss) | \$ (118) | \$      | \$     | \$ (12) |

**Table of Contents****PRUDENTIAL FINANCIAL, INC.****Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

|  | Other Long-term<br>Investments | Separate<br>Account<br>Assets(1) | Future<br>Policy<br>Benefits<br>(in millions) | Long-<br>Term Debt | Other<br>Liabilities |
|--|--------------------------------|----------------------------------|---|--------------------|----------------------|
| Fair value, beginning of period                      | \$ 824                         | \$ 21,815                        | \$ (168)                                      | \$ (152)           | \$ (77)              |
| Total gains or (losses) (realized/unrealized):       |                                |                                  |   |                    |                      |
| Included in earnings:                                |                                |                                  |   |                    |                      |
| Realized investment gains (losses), net              |                                |                                  | (265)   |                    | (41)                 |
| Asset management fees and other income               | 21                             |                                  |   | 1                  |                      |
| Interest credited to policyholders' account balances |                                | 169                              |   |                    |                      |
| Included in other comprehensive income               |                                |                                  |   |                    |                      |
| Net investment income                                | 2                              |                                  |   | (33)               |                      |
| Purchases, sales, issuances, and settlements         | 30                             | 162                              | (19)  |                    |                      |
| Transfers into (out of) Level 3                      |                                | (38)                             |   |                    |                      |
| Fair value, end of period                            | \$ 877                         | \$ 22,108                        | \$ (452)                                      | \$ (184)           | \$ (118)             |

Unrealized gains (losses) for the period relating to those Level 3 assets and liabilities that were still held by the Company at the end of the period(2):

| Included in earnings:                                |         |        |          |      |         |
|--|---------|--------|----------|------|---------|
| Realized investment gains (losses), net              |         | \$     | \$ (267) | \$   | \$ (41) |
| Asset management fees and other income               | \$ (13) | \$     | \$       | \$ 1 | \$      |
| Interest credited to policyholders' account balances | \$      | \$ 170 | \$       | \$   | \$      |

- (1) Separate account assets represent segregated funds that are invested for certain customers. Investment risks associated with market value changes are borne by the customers, except to the extent of minimum guarantees made by the Company with respect to certain accounts. Separate account liabilities are not included in the above table as they are reported at contract value and not fair value in the Company's consolidated Statement of Financial Position.
- (2) Unrealized gains or losses related to assets still held at the end of the period do not include amortization or accretion of premiums and discounts.

Certain assets and liabilities are measured at fair value on a nonrecurring basis. During the first quarter of 2008, the Company recorded a loss of \$23 million as a result of writing down certain commercial loans that are carried at the lower of cost or market. These loans have a carrying value of \$331 million as of March 31, 2008. These fair value adjustments were classified as Level 2 in the valuation hierarchy. In addition, the Company recorded a loss of \$2 million related to impairments of equity method investments. These fair value adjustments were classified as Level 3 in the valuation hierarchy.

**Table of Contents****PRUDENTIAL FINANCIAL, INC.****Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

**Fair Value Option** As discussed above, SFAS No. 159 provides a fair value option election that allows the Company to irrevocably elect fair value as the measurement attribute for certain financial assets and liabilities. The following table presents information regarding changes in fair values recorded in earnings, including gains or losses on sales, for commercial loans where the fair value option has been elected.

|  | <b>Three Months<br/>Ended March 31,<br/>2008<br/>Reported in<br/>Realized Investment<br/>Gain (Losses),<br/>net<br/>(in millions)</b> |
|--|---|
| <b>Assets:</b>                             |   |
| <b>Commercial Loans:</b>                   |   |
| Changes in instrument-specific credit risk | \$ (19)   |
| Other changes in fair value                | \$ 14   |

Changes in fair value due to instrument-specific credit risk are estimated based on changes in credit spreads and quality ratings for the period reported.

The fair values and aggregate contractual principal amounts of commercial loans, for which the fair value option has been elected, were \$657 million as of March 31, 2008.

None of the loans where the fair value option has been selected are more than 90 days past due or in non-accrual status. Interest income on commercial loans is included in net investment income. For the quarter ended March 31, 2008, the Company recorded \$11 million of interest income on these loans. Interest income on these loans is recorded based on the effective interest rates as determined at the closing of the loan.

**10. INVESTMENT IN WACHOVIA SECURITIES**

On July 1, 2003, the Company combined its retail securities brokerage and clearing operations with those of Wachovia Corporation ( Wachovia ) and formed Wachovia Securities Financial Holdings, LLC ( Wachovia Securities ), a joint venture headquartered in St. Louis, Missouri. As of December 31, 2007, the Company had a 38% ownership interest in the joint venture with Wachovia owning the remaining 62%. The transaction included certain assets and liabilities of the Company's securities brokerage operations; however, the Company retained certain assets and liabilities related to the contributed businesses, including liabilities for certain litigation and regulatory matters. The Company and Wachovia have each agreed to indemnify the other for certain losses, including losses resulting from litigation and regulatory matters relating to certain events arising from the operations of their respective contributed businesses prior to March 31, 2004.

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On October 1, 2007, Wachovia completed the acquisition of A.G. Edwards, Inc. ( A.G. Edwards ) for \$6.8 billion and on January 1, 2008 combined the retail securities brokerage business of A.G. Edwards with Wachovia Securities.

The Company has elected the lookback option under the terms of the agreements relating to the joint venture. The lookback option permits the Company to delay for two years following the combination of the A.G. Edwards business with Wachovia Securities the Company's decision to make or not to make payments to avoid or limit dilution of its ownership interest in the joint venture. During this lookback period, the Company's share in the earnings of the joint venture and one-time costs associated with the combination of the A.G. Edwards business with Wachovia Securities is based on the Company's diluted ownership level, which is in

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**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

the process of being determined. Any payments at the end of the lookback period to restore all or part of the Company's ownership interest in the joint venture will be based on the appraised or agreed value of the joint venture excluding the A.G. Edwards business as well as the A.G. Edwards business. In such event, the Company would also need to make a true-up payment of one-time costs incurred during the lookback period associated with the combination to reflect the incremental increase in its ownership interest in the joint venture. Alternatively, at the end of the lookback period, the Company may put its joint venture interests to Wachovia based on the appraised value of the joint venture, excluding the A.G. Edwards business, as of January 1, 2008, the date of the combination of the A.G. Edwards business with Wachovia Securities.

The Company also retains its separate right to put its joint venture interests to Wachovia at any time after July 1, 2008 based on the appraised value of the joint venture, including the A.G. Edwards business, determined as if it were a public company and including a control premium such as would apply in the case of a sale of 100% of its common equity. However, if in connection with the lookback option the Company elects at the end of the lookback period to make payments to avoid or limit dilution, the Company may not exercise this put option prior to the first anniversary of the end of the lookback period. The agreement between Prudential Financial and Wachovia also gives the Company put rights, and Wachovia call rights, in certain other specified circumstances, at prices determined in accordance with the agreement.

The Company and Wachovia are currently negotiating possible modifications to the terms of the existing agreements relating to the joint venture. Based upon the existing agreements and our estimates of the values of the A.G. Edwards business and the joint venture excluding the A.G. Edwards business, the Company adjusted the carrying value of its ownership interest in the joint venture effective as of January 1, 2008 to reflect the addition of that business and the dilution of its 38% ownership level and to record the value of the above described rights under the lookback option. As a result, effective January 1, 2008, the Company recognized an increase to Additional paid-in capital of \$977 million, net of tax. The Company's recorded share of pre-tax earnings from the joint venture of \$51 million for the three months ended March 31, 2008 reflects its estimated diluted ownership level based upon the existing agreements and its estimates of the values of the A.G. Edwards business and the joint venture excluding the A.G. Edwards business. As noted above, the Company and Wachovia are negotiating possible modifications to the terms of the existing agreements relating to the joint venture. Such modifications, if agreed to, as well as the establishment of definitive agreed or appraised values for the A.G. Edwards business and the joint venture excluding the A.G. Edwards business, will result in an adjustment to the credit to equity and a true-up to the earnings from the joint venture for any difference between the diluted ownership percentage used to record earnings for the three months ended March 31, 2008 and the finally determined diluted ownership percentage. The Company does not anticipate any such adjustment to have a material effect on its reported results of operations.

**11. CONTINGENT LIABILITIES AND LITIGATION AND REGULATORY MATTERS**

***Contingent Liabilities***

On an ongoing basis, the Company's internal supervisory and control functions review the quality of sales, marketing and other customer interface procedures and practices and may recommend modifications or enhancements. From time to time, this review process results in the discovery of product administration, servicing or other errors, including errors relating to the timing or amount of payments or contract values due to customers. In certain cases, if appropriate, the Company may offer customers remediation and may incur charges, including the cost of such remediation, administrative costs and regulatory fines.



*Litigation and Regulatory Matters*

The Company is subject to legal and regulatory actions in the ordinary course of its businesses. Pending legal and regulatory actions include proceedings relating to aspects of the Company's businesses and operations that are specific to it and proceedings that are typical of the businesses in which it operates, including in both

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**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

cases businesses that have either been divested or placed in wind-down status. Some of these proceedings have been brought on behalf of various alleged classes of complainants. In certain of these matters, the plaintiffs are seeking large and/or indeterminate amounts, including punitive or exemplary damages. The outcome of a litigation or regulatory matter, and the amount or range of potential loss at any particular time, is often inherently uncertain.

**Insurance and Annuities**

From November 2002 to March 2005, eleven separate complaints were filed against the Company and the law firm of Leeds Morelli & Brown in New Jersey state court. The cases were consolidated for pre-trial proceedings in New Jersey Superior Court, Essex County and captioned *Lederman v. Prudential Financial, Inc., et al.* The complaints allege that an alternative dispute resolution agreement entered into among Prudential Insurance, over 350 claimants who are current and former Prudential Insurance employees, and Leeds Morelli & Brown (the law firm representing the claimants) was illegal and that Prudential Insurance conspired with Leeds Morelli & Brown to commit fraud, malpractice, breach of contract, and violate racketeering laws by advancing legal fees to the law firm with the purpose of limiting Prudential's liability to the claimants. In 2004, the Superior Court sealed these lawsuits and compelled them to arbitration. In May 2006, the Appellate Division reversed the trial court's decisions, held that the cases were improperly sealed, and should be heard in court rather than arbitrated. In November 2006, plaintiffs filed a motion seeking to permit over 200 individuals to join the cases as additional plaintiffs, to authorize a joint trial on liability issues for all plaintiffs, and to add a claim under the New Jersey discrimination law. In March 2007, the court granted plaintiffs' motion to amend the complaint to add over 200 additional plaintiffs and a claim under the New Jersey discrimination law but denied without prejudice plaintiffs' motion for a joint trial on liability issues. In June 2007, Prudential Financial and Prudential Insurance moved to dismiss the complaint. In November 2007, the court granted the motion, in part, and dismissed the commercial bribery and conspiracy to commit malpractice claims and denied the motion with respect to other claims. In December 2007, the Prudential defendants answered the complaints and asserted counterclaims against each plaintiff for breach of contract and cross-claims against Leeds Morelli & Brown for breach of contract and the covenant of good faith and fair dealing, fraudulent inducement, indemnification and contribution. In January 2008, plaintiffs filed a demand pursuant to New Jersey law stating that they were seeking damages in the amount of \$6.5 billion.

The Company, along with a number of other insurance companies, received formal requests for information from the State of New York Attorney General's Office ( NYAG ), the Securities and Exchange Commission ( SEC ), the Connecticut Attorney General's Office, the Massachusetts Office of the Attorney General, the Department of Labor, the United States Attorney for the Southern District of California, the District Attorney of the County of San Diego, and various state insurance departments relating to payments to insurance intermediaries and certain other practices that may be viewed as anti-competitive. The Company may receive additional requests from these and other regulators and governmental authorities concerning these and related subjects. The Company is cooperating with these inquiries and has had discussions with certain authorities in an effort to resolve the inquiries into this matter. In December 2006, Prudential Insurance reached a resolution of the NYAG investigation. Under the terms of the settlement, Prudential Insurance paid a \$2.5 million penalty and established a \$16.5 million fund for policyholders, adopted business reforms and agreed, among other things, to continue to cooperate with the NYAG in any litigation, ongoing investigations or other proceedings. Prudential Insurance also settled the litigation brought by the California Department of Insurance and agreed to business reforms and disclosures as to group insurance contracts insuring customers or residents in California and to pay certain costs of investigation. In addition, in April 2008, Prudential Insurance reached a settlement of proceedings regarding these matters with the District Attorneys of San Diego, Los Angeles and Alameda

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**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

counties. Pursuant to this settlement, Prudential Insurance paid \$350,000 in penalties and costs. These matters are also the subject of litigation brought by private plaintiffs, including purported class actions that have been consolidated in the multidistrict litigation in the United States District Court for the District of New Jersey, *In re Employee Benefit Insurance Brokerage Antitrust Litigation*. In August and September 2007, the court dismissed the anti-trust and RICO claims. In January 2008, the court dismissed the ERISA claims with prejudice. In February 2008, the court dismissed the state law claims without prejudice. Plaintiffs have filed a notice of appeal to the Third Circuit Court of Appeals. The above settlements may adversely affect the existing litigation or cause additional litigation and result in adverse publicity and other potentially adverse impacts to the Company's business.

In April 2005, the Company voluntarily commenced a review of the accounting for its reinsurance arrangements to confirm that it complied with applicable accounting rules. This review included an inventory and examination of current and past arrangements, including those relating to the Company's wind down and divested businesses and discontinued operations. Subsequent to commencing this voluntary review, the Company received a formal request from the Connecticut Attorney General for information regarding its participation in reinsurance transactions generally and a formal request from the SEC for information regarding certain reinsurance contracts entered into with a single counterparty since 1997 as well as specific contracts entered into with that counterparty in the years 1997 through 2002 relating to the Company's property and casualty insurance operations that were sold in 2003. It is possible that the Company may receive additional requests from regulators relating to reinsurance arrangements. The Company intends to cooperate with all such requests.

The Company's subsidiary, Prudential Annuities Life Assurance Corporation (formerly known as American Skandia Life Assurance Corporation), is in the final stages of its remediation program to correct errors in the administration of approximately 11,000 annuity contracts issued by that company. The owners of these contracts did not receive notification that the contracts were approaching or past their designated annuitization date or default annuitization date (both dates referred to as the contractual annuity date) and the contracts were not annuitized at their contractual annuity dates. Some of these contracts also were affected by data integrity errors resulting in incorrect contractual annuity dates. The lack of notice and data integrity errors, as reflected on the annuities administrative system, all occurred before the acquisition of the American Skandia entities by the Company. The remediation and administrative costs of the remediation program are subject to the indemnification provisions of the acquisition agreement pursuant to which the Company purchased the American Skandia entities in May 2003 from Skandia.

**Securities**

Prudential Securities has been named as a defendant in a number of industry-wide purported class actions in the United States District Court for the Southern District of New York relating to its former securities underwriting business. Plaintiffs in one consolidated proceeding, captioned *In re: Initial Public Offering Securities Litigation*, allege, among other things, that the underwriters engaged in a scheme involving tying agreements, undisclosed compensation arrangements and research analyst conflicts to manipulate and inflate the prices of shares sold in initial public offerings in violation of the federal securities laws. Certain issuers of these securities and their current and former officers and directors have also been named as defendants. In October 2004, the district court granted plaintiffs' motion for class certification in six focus cases. In December 2006, the United States Court of Appeals for the Second Circuit vacated that decision and remanded the case to the district court for further proceedings. In August 2000, Prudential Securities was named as a defendant, along with other underwriters, in a purported class action, captioned *CHS Electronics Inc. v. Credit Suisse First Boston Corp. et al.*, which alleges on behalf of issuers of securities in initial public offerings that the defendants conspired to fix at 7% the discount that underwriting syndicates receive from issuers in violation of federal



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**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

antitrust laws. Plaintiffs moved for class certification in September 2004 and for partial summary judgment in November 2005. The summary judgment motion has been deferred pending disposition of the class certification motion. In April 2006, the district court denied class certification. In September 2007, the Second Circuit Court of Appeals reversed the district court's decision denying class certification and remanded the case to the district court for further proceedings. In a related action, captioned *Gillet v. Goldman Sachs et al.*, plaintiffs allege substantially the same antitrust claims on behalf of investors, though only injunctive relief is currently being sought.

**Other Matters**

*Mutual Fund Market Timing Practices*

In August 2006, Prudential Equity Group, LLC (PEG), a wholly owned subsidiary of the Company, reached a resolution of the previously disclosed regulatory and criminal investigations into deceptive market related activities involving PEG's former Prudential Securities operations. The settlements relate to conduct that generally occurred between 1999 and 2003 involving certain former Prudential Securities brokers in Boston and certain other branch offices in the U.S., their supervisors, and other members of the Prudential Securities control structure with responsibilities that related to the market timing activities, including certain former members of Prudential Securities senior management. The Prudential Securities operations were contributed to a joint venture with Wachovia Corporation in July 2003, but PEG retained liability for the market timing related activities. In connection with the resolution of the investigations, PEG entered into separate settlements with each of the United States Attorney for the District of Massachusetts (USAO), the Secretary of the Commonwealth of Massachusetts, Securities Division, SEC, the National Association of Securities Dealers, the New York Stock Exchange, the New Jersey Bureau of Securities and the New York Attorney General's Office. These settlements resolve the investigations by the above named authorities into these matters as to all Prudential entities without further regulatory proceedings or filing of charges so long as the terms of the settlement are followed and provided, in the case of the settlement agreement reached with the USAO, that the USAO has reserved the right to prosecute PEG if there is a material breach by PEG of that agreement during its five year term and in certain other specified events. Under the terms of the settlements, PEG paid \$270 million into a Fair Fund administered by the SEC to compensate those harmed by the market timing activities. In addition, \$330 million was paid in fines and penalties. Pursuant to the settlements, PEG retained, at PEG's ongoing cost and expense, the services of an Independent Distribution Consultant acceptable to certain of the authorities to develop a proposed distribution plan for the distribution of Fair Fund amounts according to a methodology developed in consultation with and acceptable to certain of the authorities. In addition, as part of the settlements, PEG has agreed, among other things, to continue to cooperate with the above named authorities in any litigation, ongoing investigations or other proceedings relating to or arising from their investigations into these matters. In connection with the settlements, the Company has agreed with the USAO, among other things, to cooperate with the USAO and to maintain and periodically report on the effectiveness of its compliance procedures. The settlement documents include findings and admissions that may adversely affect existing litigation or cause additional litigation and result in adverse publicity and other potentially adverse impacts to the Company's businesses.

In addition to the regulatory proceedings described above that were settled in 2006, in October 2004, the Company and Prudential Securities were named as defendants in several class actions brought on behalf of purchasers and holders of shares in a number of mutual fund complexes. The actions are consolidated as part of a multi-district proceeding, *In re: Mutual Fund Investment Litigation*, pending in the United States District Court for the District of Maryland. The complaints allege that the purchasers and holders were harmed by dilution of the funds' values and excessive fees, caused by market timing and late trading, and seek unspecified damages. In August 2005, the Company was dismissed from several of the actions, without prejudice to repleading the state



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**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

claims, but remains a defendant in other actions in the consolidated proceeding. In July 2006, in one of the consolidated mutual fund actions, *Saunders v. Putnam American Government Income Fund, et al.*, the United States District Court for the District of Maryland granted plaintiffs leave to refile their federal securities law claims against Prudential Securities. In August 2006, the second amended complaint was filed alleging federal securities law claims on behalf of a purported nationwide class of mutual fund investors seeking compensatory and punitive damages in unspecified amounts. Discovery is ongoing. Motions to dismiss the other actions are pending.

Commencing in 2003, the Company received formal requests for information from the SEC and NYAG relating to market timing in variable annuities by certain Prudential Annuities entities. In connection with these investigations, with the approval of Skandia Insurance Company Ltd. (publ) ( Skandia ), an offer was made by Prudential Annuities to the authorities investigating its companies, the SEC and NYAG, to settle these matters by paying restitution and a civil penalty of \$95 million in the aggregate. While not assured, the Company believes these discussions are likely to lead to settlements with these authorities. Any regulatory settlement involving a Prudential Annuities entity would be subject to the indemnification provisions of the acquisition agreement pursuant to which the Company purchased the Prudential Annuities entities in May 2003 from Skandia. If achieved, settlement of the matters relating to Prudential Annuities also could involve continuing monitoring, changes to and/or supervision of business practices, findings that may adversely affect existing or cause additional litigation, adverse publicity and other adverse impacts to the Company's businesses.

*Other*

In October 2007, Prudential Retirement Insurance and Annuity Co. ( PRIAC ) filed an action in the United States District Court for the Southern District of New York, *Prudential Retirement Insurance & Annuity Co. v. State Street Global Advisors*, in PRIAC's fiduciary capacity and on behalf of certain defined benefit and defined contribution plan clients of PRIAC, against an unaffiliated asset manager, State Street Global Advisors ( SSgA ) and SSgA's affiliate, State Street Bank and Trust Company ( State Street ). This action seeks, among other relief, restitution of certain losses attributable to certain investment funds sold by SSgA as to which PRIAC believes SSgA employed investment strategies and practices that were misrepresented by SSgA and failed to exercise the standard of care of a prudent investment manager. PRIAC also intends to vigorously pursue any other available remedies against SSgA and State Street in respect of this matter. Given the unusual circumstances surrounding the management of these SSgA funds and in order to protect the interests of the affected plans and their participants while PRIAC pursues these remedies, PRIAC implemented a process under which affected plan clients that authorized PRIAC to proceed on their behalf have received payments from funds provided by PRIAC for the losses referred to above. The Company's consolidated financial statements, and the results of the Retirement segment included in the Company's Investment Division, for the year ended December 31, 2007 include a pre-tax charge of \$82 million, reflecting these payments to plan clients and certain related costs.

In September and October 2005, five purported class action lawsuits were filed against the Company, Prudential Securities and PEG claiming that stockbrokers were improperly classified as exempt employees under state and federal wage and hour laws, were improperly denied overtime pay and that improper deductions were made from the stockbrokers' wages. Two of the stockbrokers' complaints, *Janowsky v. Wachovia Securities, LLC and Prudential Securities Incorporated* and *Goldstein v. Prudential Financial, Inc.*, were filed in the United States District Court for the Southern District of New York. The *Goldstein* complaint purports to have been filed on behalf of a nationwide class. The *Janowsky* complaint alleges a class of New York brokers. Motions to dismiss and compel arbitration were filed in the *Janowsky* and *Goldstein* matters, which have been consolidated for pre-trial purposes. The three stockbrokers complaints filed in California Superior Court, *Dewane v. Prudential Equity Group, Prudential Securities Incorporated, and Wachovia Securities LLC; DiLustro v.*





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**Table of Contents****PRUDENTIAL FINANCIAL, INC.****Notes to Unaudited Interim Consolidated Financial Statements (Continued)**

*Prudential Securities Incorporated, Prudential Equity Group Inc. and Wachovia Securities; and Carayanis v. Prudential Equity Group LLC and Prudential Securities Inc.*, purport to have been brought on behalf of classes of California brokers. The *Carayanis* complaint was subsequently withdrawn without prejudice in May 2006. In June 2006, a purported New York state class action complaint was filed in the United States District Court for the Eastern District of New York, *Panesenko v. Wachovia Securities, et al.*, alleging that the Company failed to pay overtime to stockbrokers in violation of state and federal law and that improper deductions were made from the stockbrokers' wages in violation of state law. In September 2006, Prudential Securities was sued in *Badain v. Wachovia Securities, et al.*, a purported nationwide class action filed in the United States District Court for the Western District of New York. The complaint alleges that Prudential Securities failed to pay overtime to stockbrokers in violation of state and federal law and that improper deductions were made from the stockbrokers' wages in violation of state law. In December 2006, these cases were transferred to the United States District Court for the Central District of California by the Judicial Panel on Multidistrict Litigation for coordinated or consolidated pre-trial proceedings. The complaints seek back overtime pay and statutory damages, recovery of improper deductions, interest, and attorneys' fees. In December 2007 plaintiffs moved to certify the class. The motion is pending. In October 2006, a purported class action lawsuit, *Bouder v. Prudential Financial, Inc. and Prudential Insurance Company of America*, was filed in the United States District Court for the District of New Jersey, claiming that the Company failed to pay overtime to insurance agents who were registered representatives in violation of federal and state law, and that improper deductions were made from these agents' wages in violation of state law. In March 2008, the court granted plaintiffs' motion to conditionally certify a nationwide class.

**Summary**

The Company's litigation and regulatory matters are subject to many uncertainties, and given its complexity and scope, their outcome cannot be predicted. It is possible that results of operations or cash flow of the Company in a particular quarterly or annual period could be materially affected by an ultimate unfavorable resolution of pending litigation and regulatory matters depending, in part, upon the results of operations or cash flow for such period. In light of the unpredictability of the Company's litigation and regulatory matters, it is also possible that in certain cases an ultimate unfavorable resolution of one or more pending litigation or regulatory matters could have a material adverse effect on the Company's financial position. Management believes, however, that, based on information currently known to it, the ultimate outcome of all pending litigation and regulatory matters, after consideration of applicable reserves and rights to indemnification, is not likely to have a material adverse effect on the Company's financial position.

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March 31, 2008 and December 31, 2007 (in millions)

|  | March 31, 2008                      |                             |                   | December 31, 2007                   |                             |                   |
|--|-------------------------------------|-----------------------------|-------------------|-------------------------------------|-----------------------------|-------------------|
|  | Financial<br>Services<br>Businesses | Closed<br>Block<br>Business | Consolidated      | Financial<br>Services<br>Businesses | Closed<br>Block<br>Business | Consolidated      |
| <b>ASSETS</b>  |                                     |                             |                   |                                     |                             |                   |
| Fixed maturities:  |                                     |                             |                   |                                     |                             |                   |
| Available for sale, at fair value                                      | \$ 117,914                          | \$ 46,558                   | \$ 164,472        | \$ 112,748                          | \$ 49,414                   | \$ 162,162        |
| Held to maturity, at amortized cost                                    | 3,735                               |                             | 3,735             | 3,548                               |                             | 3,548             |
| Trading account assets supporting insurance liabilities, at fair value | 14,644                              |                             | 14,644            | 14,473                              |                             | 14,473            |
| Other trading account assets, at fair value                            | 2,684                               | 149                         | 2,833             | 3,471                               | 142                         | 3,613             |
| Equity securities, available for sale, at fair value                   | 4,551                               | 3,578                       | 8,129             | 4,640                               | 3,940                       | 8,580             |
| Commercial loans   | 23,444                              | 8,494                       | 31,938            | 22,093                              | 7,954                       | 30,047            |
| Policy loans   | 4,147                               | 5,391                       | 9,538             | 3,942                               | 5,395                       | 9,337             |
| Securities purchased under agreements to resell                        | 178                                 |                             | 178               | 129                                 |                             | 129               |
| Other long-term investments  | 5,266                               | 1,139                       | 6,405             | 5,163                               | 1,268                       | 6,431             |
| Short-term investments   | 4,176                               | 1,555                       | 5,731             | 3,852                               | 1,385                       | 5,237             |
| Total investments  | 180,739                             | 66,864                      | 247,603           | 174,059                             | 69,498                      | 243,557           |
| Cash and cash equivalents  | 8,133                               | 1,627                       | 9,760             | 9,624                               | 1,436                       | 11,060            |
| Accrued investment income  | 1,540                               | 726                         | 2,266             | 1,496                               | 678                         | 2,174             |
| Reinsurance recoverables   | 1,975                               |                             | 1,975             | 2,119                               |                             | 2,119             |
| Deferred policy acquisition costs                                      | 11,924                              | 904                         | 12,828            | 11,396                              | 943                         | 12,339            |
| Other assets   | 20,357                              | 1,629                       | 21,986            | 17,754                              | 1,228                       | 18,982            |
| Separate account assets  | 181,902                             |                             | 181,902           | 195,583                             |                             | 195,583           |
| <b>TOTAL ASSETS</b>  | <b>\$ 406,570</b>                   | <b>\$ 71,750</b>            | <b>\$ 478,320</b> | <b>\$ 412,031</b>                   | <b>\$ 73,783</b>            | <b>\$ 485,814</b> |
| <b>LIABILITIES AND ATTRIBUTED EQUITY</b>                               |                                     |                             |                   |                                     |                             |                   |
| <b>LIABILITIES</b>   |                                     |                             |                   |                                     |                             |                   |
| Future policy benefits   | \$ 63,590                           | \$ 51,273                   | \$ 114,863        | \$ 60,259                           | \$ 51,209                   | \$ 111,468        |
| Policyholders' account balances  | 84,812                              | 5,568                       | 90,380            | 78,599                              | 5,555                       | 84,154            |
| Policyholders' dividends   | 739                                 | 1,719                       | 2,458             | 670                                 | 2,991                       | 3,661             |
| Reinsurance payables   | 1,396                               |                             | 1,396             | 1,552                               |                             | 1,552             |
| Securities sold under agreements to repurchase                         | 3,727                               | 5,072                       | 8,799             | 5,281                               | 6,160                       | 11,441            |
| Cash collateral for loaned securities                                  | 2,761                               | 2,197                       | 4,958             | 3,041                               | 3,271                       | 6,312             |
| Income taxes   | 3,575                               |                             | 3,575             | 3,402                               | 151                         | 3,553             |
| Short-term debt  | 13,788                              | 2,436                       | 16,224            | 14,514                              | 1,143                       | 15,657            |
| Long-term debt   | 13,302                              | 1,750                       | 15,052            | 12,351                              | 1,750                       | 14,101            |
| Other liabilities  | 15,494                              | 522                         | 16,016            | 14,609                              | 266                         | 14,875            |
| Separate account liabilities   | 181,902                             |                             | 181,902           | 195,583                             |                             | 195,583           |
| Total liabilities  | 385,086                             | 70,537                      | 455,623           | 389,861                             | 72,496                      | 462,357           |
| <b>COMMITMENTS AND CONTINGENT LIABILITIES</b>                          |                                     |                             |                   |                                     |                             |                   |
| <b>ATTRIBUTED EQUITY</b>   |                                     |                             |                   |                                     |                             |                   |
| Accumulated other comprehensive income (loss)                          | (473)                               | (66)                        | (539)             | 459                                 | (12)                        | 447               |

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|  |                   |                  |                   |                   |                  |                   |
|--|-------------------|------------------|-------------------|-------------------|------------------|-------------------|
| Other attributed equity                        | 21,957            | 1,279            | 23,236            | 21,711            | 1,299            | 23,010            |
| Total attributed equity                        | 21,484            | 1,213            | 22,697            | 22,170            | 1,287            | 23,457            |
| <b>TOTAL LIABILITIES AND ATTRIBUTED EQUITY</b> | <b>\$ 406,570</b> | <b>\$ 71,750</b> | <b>\$ 478,320</b> | <b>\$ 412,031</b> | <b>\$ 73,783</b> | <b>\$ 485,814</b> |

*See Notes to Unaudited Interim Supplemental Combining Financial Information*

**Table of Contents****PRUDENTIAL FINANCIAL, INC.****Unaudited Interim Supplemental Combining Statements of Operations****Three Months Ended March 31, 2008 and 2007 (in millions)**

|  | Three Months Ended March 31,        |                                     |              |                                     |                                     |                 |
|--|-------------------------------------|-------------------------------------|--------------|-------------------------------------|-------------------------------------|-----------------|
|  | Financial<br>Services<br>Businesses | 2008<br>Closed<br>Block<br>Business | Consolidated | Financial<br>Services<br>Businesses | 2007<br>Closed<br>Block<br>Business | Consolidated    |
| <b>REVENUES</b>  |                                     |                                     |              |                                     |                                     |                 |
| Premiums   | \$ 3,102                            | \$ 856                              | \$ 3,958     | \$ 2,721                            | \$ 838                              | \$ 3,559        |
| Policy charges and fee income  | 825                                 |                                     | 825          | 785                                 |                                     | 785             |
| Net investment income  | 2,121                               | 906                                 | 3,027        | 2,002                               | 933                                 | 2,935           |
| Realized investment gains (losses), net  | (802)                               | (110)                               | (912)        | 213                                 | 207                                 | 420             |
| Asset management fees and other income   | 647                                 | 19                                  | 666          | 1,063                               | 13                                  | 1,076           |
| <b>Total revenues</b>  | <b>5,893</b>                        | <b>1,671</b>                        | <b>7,564</b> | <b>6,784</b>                        | <b>1,991</b>                        | <b>8,775</b>    |
| <b>BENEFITS AND EXPENSES</b>   |                                     |                                     |              |                                     |                                     |                 |
| Policyholders' benefits  | 3,063                               | 972                                 | 4,035        | 2,736                               | 949                                 | 3,685           |
| Interest credited to policyholders' account balances   | 602                                 | 35                                  | 637          | 807                                 | 36                                  | 843             |
| Dividends to policyholders   | 57                                  | 502                                 | 559          | 28                                  | 683                                 | 711             |
| General and administrative expenses  | 2,091                               | 188                                 | 2,279        | 1,923                               | 186                                 | 2,109           |
| <b>Total benefits and expenses</b>   | <b>5,813</b>                        | <b>1,697</b>                        | <b>7,510</b> | <b>5,494</b>                        | <b>1,854</b>                        | <b>7,348</b>    |
| <b>INCOME (LOSS) FROM CONTINUING OPERATIONS BEFORE INCOME TAXES AND EQUITY IN EARNINGS OF OPERATING JOINT VENTURES</b> |                                     |                                     |              |                                     |                                     |                 |
|  | 80                                  | (26)                                | 54           | 1,290                               | 137                                 | 1,427           |
| Income tax expense (benefit)   | 47                                  | (18)                                | 29           | 379                                 | 44                                  | 423             |
| <b>INCOME (LOSS) FROM CONTINUING OPERATIONS BEFORE EQUITY IN EARNINGS OF OPERATING JOINT VENTURES</b>                  |                                     |                                     |              |                                     |                                     |                 |
|  | 33                                  | (8)                                 | 25           | 911                                 | 93                                  | 1,004           |
| Equity in earnings of operating joint ventures, net of taxes   | 43                                  |                                     | 43           | 77                                  |                                     | 77              |
| <b>INCOME (LOSS) FROM CONTINUING OPERATIONS</b>  |                                     |                                     |              |                                     |                                     |                 |
|  | 76                                  | (8)                                 | 68           | 988                                 | 93                                  | 1,081           |
| Income from discontinued operations, net of taxes  | 1                                   |                                     | 1            | 37                                  | 2                                   | 39              |
| <b>NET INCOME (LOSS)</b>   | <b>\$ 77</b>                        | <b>\$ (8)</b>                       | <b>\$ 69</b> | <b>\$ 1,025</b>                     | <b>\$ 95</b>                        | <b>\$ 1,120</b> |

See Notes to Unaudited Interim Supplemental Combining Financial Information



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**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Supplemental Combining Financial Information**

**1. BASIS OF PRESENTATION**

The supplemental combining financial information presents the consolidated financial position and results of operations for Prudential Financial, Inc. and its subsidiaries (together, the Company), separately reporting the Financial Services Businesses and the Closed Block Business. The Financial Services Businesses and the Closed Block Business are both fully integrated operations of the Company and are not separate legal entities. The supplemental combining financial information presents the results of the Financial Services Businesses and the Closed Block Business as if they were separate reporting entities and should be read in conjunction with the Consolidated Financial Statements.

The Company has outstanding two classes of common stock. The Common Stock reflects the performance of the Financial Services Businesses and the Class B Stock reflects the performance of the Closed Block Business.

The Closed Block Business was established on the date of demutualization and includes the assets and liabilities of the Closed Block (see Note 4 to the Unaudited Interim Consolidated Financial Statements for a description of the Closed Block). It also includes assets held outside the Closed Block necessary to meet insurance regulatory capital requirements related to products included within the Closed Block; deferred policy acquisition costs related to the Closed Block policies; the principal amount of the IHC debt (as discussed in Note 2 below) and related unamortized debt issuance costs, as well as an interest rate swap related to the IHC debt; and certain other related assets and liabilities. The Financial Services Businesses consist of the Insurance, Investment, and International Insurance and Investments divisions and Corporate and Other operations.

**2. ALLOCATION OF RESULTS**

This supplemental combining financial information reflects the assets, liabilities, revenues and expenses directly attributable to the Financial Services Businesses and the Closed Block Business, as well as allocations deemed reasonable by management in order to fairly present the financial position and results of operations of the Financial Services Businesses and the Closed Block Business on a stand alone basis. While management considers the allocations utilized to be reasonable, management has the discretion to make operational and financial decisions that may affect the allocation methods and resulting assets, liabilities, revenues and expenses of each business. In addition, management has limited discretion over accounting policies and the appropriate allocation of earnings between the two businesses. The Company is subject to agreements which provide that, in most instances, the Company may not change the allocation methodology or accounting policies for the allocation of earnings between the Financial Services Businesses and Closed Block Business without the prior consent of the Class B Stock holders or IHC debt bond insurer.

The Financial Services Businesses and Closed Block Business participate in the Company's commingled internal short-term cash management facility, pursuant to which they invest cash from securities lending and repurchase activities as well as certain trading and operating activities. The net funds invested in the facility are generally held in investments that are short term, including mortgage- and asset-backed securities. As of March 31, 2008, the balance held in this facility was approximately \$15.9 billion. Historically, and as of March 31, 2008, a proportionate interest in each security held in the portfolio was allocated to the Financial Services Businesses and the Closed Block Business based upon their

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proportional cash contributions to the facility as of the balance sheet date. Participation in the facility by the Financial Services Businesses and the Closed Block Business is dependent on cash flows arising from the activities noted above, which in turn, under the historical allocation methodology, could change the allocation of the facility's assets between the two Businesses. A proportionate share of any realized investment gain or loss was recorded by each Business based upon their respective ownership percentages in the facility as of the date of the realized gain or loss. Beginning

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**PRUDENTIAL FINANCIAL, INC.**

**Notes to Unaudited Interim Supplemental Combining Financial Information (Continued)**

April 1, 2008, management implemented changes in the facility in order to permit each Business to hold discrete ownership of its investments in the facility without affecting or being affected by the level of participation in the facility by the other Business. With these changes, any realized investment gain or loss will be recorded by the respective Business based upon their discrete ownership of investments in the facility. Pending the implementation of these changes, the facility was managed so that the proportionate interests of the Financial Services Businesses and Closed Block Business in the entire facility were maintained at approximately the same proportions held as of June 30, 2007 (approximately 49% and 51%, respectively).

General corporate overhead not directly attributable to a specific business that has been incurred in connection with the generation of the businesses' revenues is generally allocated between the Financial Services Businesses and the Closed Block Business based on the general and administrative expenses of each business as a percentage of the total general and administrative expenses for all businesses.

Prudential Holdings, LLC, a wholly owned subsidiary of Prudential Financial, Inc., has outstanding senior secured notes (the IHC debt), of which net proceeds of \$1.66 billion were allocated to the Financial Services Businesses concurrent with the demutualization on December 18, 2001. The IHC debt is serviced by the cash flows of the Closed Block Business, and the results of the Closed Block Business reflect interest expense associated with the IHC debt.

Income taxes are allocated between the Financial Services Businesses and the Closed Block Business as if they were separate companies based on the taxable income or losses and other tax characterizations of each business. If a business generates benefits, such as net operating losses, it is entitled to record such tax benefits to the extent they are expected to be utilized on a consolidated basis.

Holders of Common Stock have no interest in a separate legal entity representing the Financial Services Businesses; holders of the Class B Stock have no interest in a separate legal entity representing the Closed Block Business; and holders of each class of common stock are subject to all of the risks associated with an investment in the Company.

In the event of a liquidation, dissolution or winding-up of the Company, holders of Common Stock and holders of Class B Stock would be entitled to receive a proportionate share of the net assets of the Company that remain after paying all liabilities and the liquidation preferences of any preferred stock.

The results of the Financial Services Businesses are subject to certain risks pertaining to the Closed Block. These include any expenses and liabilities from litigation affecting the Closed Block policies as well as the consequences of certain potential adverse tax determinations. In connection with the sale of the Class B Stock and IHC debt, the cost of indemnifying the investors with respect to certain matters will be borne by the Financial Services Businesses.





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### **Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**

*Management's Discussion and Analysis of Financial Condition and Results of Operations ( MD&A ) addresses the consolidated financial condition of Prudential Financial as of March 31, 2008, compared with December 31, 2007, and its consolidated results of operations for the three months ended March 31, 2008 and 2007. You should read the following analysis of our consolidated financial condition and results of operations in conjunction with the MD&A, the Risk Factors section and the Audited Consolidated Financial Statements included in the Company's Annual Report on Form 10-K for the year ended December 31, 2007, as well as the Risk Factors section, the statements under Forward-Looking Statements and the Unaudited Interim Consolidated Financial Statements included elsewhere in this Quarterly Report on Form 10-Q.*

#### **Overview**

Prudential Financial has two classes of common stock outstanding. The Common Stock, which is publicly traded (NYSE:PRU), reflects the performance of the Financial Services Businesses, while the Class B Stock, which was issued through a private placement and does not trade on any exchange, reflects the performance of the Closed Block Business. The Financial Services Businesses and the Closed Block Business are discussed below.

#### **Financial Services Businesses**

Our Financial Services Businesses consist of three operating divisions, which together encompass eight segments, and our Corporate and Other operations. The Insurance division consists of our Individual Life, Individual Annuities and Group Insurance segments. The Investment division consists of our Asset Management, Financial Advisory and Retirement segments. The International Insurance and Investments division consists of our International Insurance and International Investments segments. Our Corporate and Other operations include our real estate and relocation services business, as well as corporate items and initiatives that are not allocated to business segments. Corporate and Other operations also include businesses that have been or will be divested and businesses that we have placed in wind-down status.

We attribute financing costs to each segment based on the amount of financing used by each segment, excluding financing costs associated with corporate debt. The net investment income of each segment includes earnings on the amount of equity that management believes is necessary to support the risks of that segment.

We seek growth internally and through acquisitions, joint ventures or other forms of business combinations or investments. Our principal acquisition focus is in our current business lines, both domestic and international.

#### **Closed Block Business**

In connection with the demutualization, we ceased offering domestic participating products. The liabilities for our traditional domestic in force participating products were segregated, together with assets, in a regulatory mechanism referred to as the Closed Block. The Closed Block is

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designed generally to provide for the reasonable expectations for future policy dividends after demutualization of holders of participating individual life insurance policies and annuities included in the Closed Block by allocating assets that will be used exclusively for payment of benefits, including policyholder dividends, expenses and taxes with respect to these products. See Note 4 to the Unaudited Interim Consolidated Financial Statements for more information on the Closed Block. At the time of demutualization, we determined the amount of Closed Block assets so that the Closed Block assets initially had a lower book value than the Closed Block liabilities. We expect that the Closed Block assets will generate sufficient cash flow, together with anticipated revenues from the Closed Block policies, over the life of the Closed Block to fund payments of all expenses, taxes, and policyholder benefits to be paid to, and the reasonable dividend expectations of, holders of the Closed Block policies. We also segregated for accounting purposes the assets that we need to hold outside the Closed Block to meet capital requirements related

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to the Closed Block policies. No policies sold after demutualization will be added to the Closed Block, and its in force business is expected to ultimately decline as we pay policyholder benefits in full. We also expect the proportion of our business represented by the Closed Block to decline as we grow other businesses.

Concurrently with our demutualization, Prudential Holdings, LLC, a wholly owned subsidiary of Prudential Financial that owns the capital stock of Prudential Insurance, issued \$1.75 billion in senior secured notes, which we refer to as the IHC debt. The net proceeds from the issuances of the Class B Stock and IHC debt, except for \$72 million used to purchase a guaranteed investment contract to fund a portion of the bond insurance cost associated with that debt, were allocated to the Financial Services Businesses. However, we expect that the IHC debt will be serviced by the net cash flows of the Closed Block Business over time, and we include interest expenses associated with the IHC debt when we report results of the Closed Block Business.

The Closed Block Business consists principally of the Closed Block, assets that we must hold outside the Closed Block to meet capital requirements related to the Closed Block policies, invested assets held outside the Closed Block that represent the difference between the Closed Block assets and Closed Block liabilities and the interest maintenance reserve, deferred policy acquisition costs related to Closed Block policies, the principal amount of the IHC debt and related hedging activities, and certain other related assets and liabilities.

## **Executive Summary**

Prudential Financial, one of the largest financial services companies in the U.S., offers individual and institutional clients a wide array of financial products and services, including life insurance, annuities, mutual funds, pension and retirement-related services and administration, investment management, real estate brokerage and relocation services, and, through a joint venture, retail securities brokerage services. We offer these products and services through one of the largest distribution networks in the financial services industry.

During the latter half of 2007 and continuing through the first quarter 2008, dislocations in the credit and capital markets, initially driven by broad market concerns over the impact of sub-prime mortgage holdings of financial institutions, have generally resulted in increased cost of credit for financial institutions in the marketplace. While credit has generally become more expensive, Prudential Financial's ability to access the capital markets has not been materially impacted.

The first three months of 2008 reflect our continued efforts to redeploy capital effectively to seek enhanced returns, including the continuation of our share repurchase program. In the first three months of 2008, we repurchased 11.4 million shares of Common Stock at a total cost of \$869 million and are authorized, under a stock repurchase program authorized by Prudential Financial's Board of Directors in November 2007, to repurchase up to an additional \$2.6 billion of Common Stock during 2008.

Our consolidated net income for the first quarter of 2008 of \$69 million, a decrease from \$1.120 billion for the first quarter of 2007, primarily reflects the impact of current market conditions on the results of our segments and investment portfolio.

We analyze performance of the segments and Corporate and Other operations of the Financial Services Businesses using a measure called adjusted operating income. See Consolidated Results of Operations for a definition of adjusted operating income and a discussion of its use as a measure of segment operating performance.



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Shown below are the contributions of each segment and Corporate and Other operations to our adjusted operating income for the three months ended March 31, 2008 and 2007 and a reconciliation of adjusted operating income of our segments and Corporate and Other operations to income from continuing operations before income taxes and equity in earnings of operating joint ventures.

|  | <b>Three Months Ended<br/>March 31,</b> |             |
|--|---|-------------|
|  | <b>2008</b>                             | <b>2007</b> |
|  | <b>(in millions)</b>                    |             |
| <b>Adjusted operating income before income taxes for segments of the Financial Services Businesses:</b>                                    |   |             |
| Individual Life  | \$ 96                                   | \$ 101      |
| Individual Annuities   | 115                                     | 166         |
| Group Insurance  | 90                                      | 51          |
| Asset Management   | 119                                     | 175         |
| Financial Advisory   | 44                                      | 97          |
| Retirement   | 124                                     | 148         |
| International Insurance  | 413                                     | 412         |
| International Investments  | 26                                      | 62          |
| Corporate and Other  | (35)                                    | 9           |
| <b>Reconciling Items:</b>  |   |             |
| Realized investment gains (losses), net, and related adjustments   | (665)                                   | 147         |
| Charges related to realized investment gains (losses), net   | (13)                                    | (6)         |
| Investment gains (losses) on trading account assets supporting insurance liabilities, net  | (262)                                   | 82          |
| Change in experience-rated contractholder liabilities due to asset value changes   | 200                                     | (62)        |
| Divested businesses  | (112)                                   | 28          |
| Equity in earnings of operating joint ventures   | (60)                                    | (120)       |
| Income from continuing operations before income taxes and equity in earnings of operating joint ventures for Financial Services Businesses | 80                                      | 1,290       |
| Income (loss) from continuing operations before income taxes and equity in earnings of operating joint ventures for Closed Block Business  | (26)                                    | 137         |
| Consolidated income from continuing operations before income taxes and equity in earnings of operating joint ventures                      | \$ 54                                   | \$ 1,427    |

Results for the three months ended March 31, 2008 presented above reflect the following:

Individual Life segment results for the first quarter of 2008 decreased from the prior year quarter primarily due to a net increase in amortization of deferred policy acquisition costs net of related amortization of unearned revenue reserves, reflecting unfavorable separate account fund performance in the first quarter of 2008 as compared to the first quarter of 2007, and an increase in other costs. These items were partially offset by more favorable mortality experience, net of reinsurance, compared to the first quarter of the prior year.

Individual Annuities segment results for the first quarter of 2008 declined in comparison to the first quarter of 2007 primarily reflecting an unfavorable variance in the mark-to-market of embedded derivatives and related hedge positions associated with our living benefit features, net of a related decrease in the amortization of deferred policy acquisition and other costs, due to financial market conditions in the first quarter of 2008. In addition, a quarterly adjustment for current period experience resulted in an increase in amortization of deferred policy acquisition and other costs, and greater costs associated with guaranteed minimum death and income benefits, resulting from less favorable than expected experience.



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Group Insurance segment results improved for the first quarter of 2008, reflecting growth in our group disability business and more favorable claims experience in our group life business. Also included in current quarter results is a \$20 million benefit from a premium adjustment for updated data on a large group life insurance case.

Asset Management segment results for the first quarter of 2008 decreased in comparison to the first quarter of 2007, largely attributable to less favorable results from the segment's proprietary investing business primarily related to changes in market value in a fixed income fund as well as higher expenses. These items were partially offset by greater performance based incentive fees, primarily related to institutional real estate funds, and higher asset management fees.

Financial Advisory segment results for the first quarter of 2008 decreased from the first quarter of 2007 primarily due to lower income from our share of the retail brokerage joint venture with Wachovia, which includes transition costs in the first quarter of 2008 of \$46 million associated with the January 1, 2008 combination of the A.G. Edwards business with Wachovia Securities. Our reported share of earnings and transition costs for the first quarter of 2008 are based on our estimate of our diluted ownership percentage subsequent to this combination.

Retirement segment results for the first quarter of 2008 declined in comparison to the first quarter of 2007, primarily reflecting higher general and administrative expenses, including costs associated with the acquired retirement business of Union Bank of California, N.A. Also contributing to the decrease was a lower contribution from investment results, primarily due to a decrease in the level of mortgage prepayment income, an unfavorable variance in the mark to market of equity investments required in certain of our separate account products, and lower investment yields on certain general account defined contribution balances.

The International Insurance segment is comprised of its Life Planner and Gibraltar Life operations. Results from the segment's Life Planner operations improved primarily reflecting the continued growth of our Japanese and Korean Life Planner operations, partially offset by higher amortization of deferred policy acquisition costs. Results from the segment's Gibraltar Life operation decreased reflecting less favorable mortality experience and higher amortization of deferred policy acquisition costs.

International Investments segment results for the first quarter of 2008 declined from the prior year quarter due to a credit loss in our global commodities group, as well as lower front-end fees in our Korean asset management operation.

Corporate and Other results for the first quarter of 2008 declined from the prior year quarter, reflecting a lower contribution from investment income, net of interest expense, together with an increased loss from our real estate and relocation business.

Realized investment gains (losses), net, and related adjustments for the Financial Services Businesses in the first quarter of 2008 amounted to \$(665) million. Results for the first quarter of 2008 relate primarily to other-than-temporary impairments of fixed maturity and equity securities and decreases in the market value of certain externally managed investments in the European market.

Income (loss) from continuing operations before income taxes in the Closed Block Business decreased \$163 million in the first quarter of 2008 compared to the first quarter of 2007. Results in the first quarter of 2008 include \$110 million of net realized investment losses as compared to \$207 million of net realized investment gains in the first quarter of 2007, partially offset by a decrease in dividends to policyholders reflecting a decrease in the cumulative earnings policyholder dividend obligation expense, partially offset by an increase in dividends paid and accrued to policyholders.



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**Accounting Policies & Pronouncements**

**Application of Critical Accounting Estimates**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America, or U.S. GAAP, requires the application of accounting policies that often involve a significant degree of judgment. Management, on an ongoing basis, reviews estimates and assumptions used in the preparation of financial statements. If management determines that modifications in assumptions and estimates are appropriate given current facts and circumstances, results of operations and financial position as reported in the Consolidated Financial Statements could change significantly.

Management believes the accounting policies relating to the following areas are most dependent on the application of estimates and assumptions:

Valuation of investments;

Policyholder liabilities;

Deferred policy acquisition costs;

Goodwill;

Pension and other postretirement benefits;

Taxes on income; and

Reserves for contingencies, including reserves for losses in connection with unresolved legal matters.

**Accounting Pronouncements Adopted**

See Note 2 to the Unaudited Interim Consolidated Financial Statements for a discussion of recently adopted accounting pronouncements, including the adoption of SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities and SFAS No. 157, Fair Value Measurements.

**Recent Accounting Pronouncements**

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See Note 2 to the Unaudited Interim Consolidated Financial Statements for a discussion of recently issued accounting pronouncements.

**Table of Contents****Consolidated Results of Operations**

The following table summarizes income from continuing operations for the Financial Services Businesses and the Closed Block Business as well as other components comprising net income.

|  | <b>Three Months Ended<br/>March 31,<br/>2008      2007<br/>(in millions)</b> |                 |
|--|--|-----------------|
| <b>Financial Services Businesses by segment:</b>   |  |                 |
| Individual Life  | \$ (40)  | \$ 89           |
| Individual Annuities   | 79   | 158             |
| Group Insurance  | 3  | 65              |
| <b>Total Insurance Division</b>  | <b>42</b>  | <b>312</b>      |
| Asset Management   | 131  | 177             |
| Financial Advisory   | (7)  | (14)            |
| Retirement   | (120)  | 158             |
| <b>Total Investment Division</b>   | <b>4</b>   | <b>321</b>      |
| International Insurance  | 318  | 547             |
| International Investments  | 20   | 53              |
| <b>Total International Insurance and Investments Division</b>  | <b>338</b>   | <b>600</b>      |
| Corporate and Other  | (304)  | 57              |
| Income from continuing operations before income taxes and equity in earnings of operating joint ventures for Financial Services Businesses | 80   | 1,290           |
| Income tax expense   | 47   | 379             |
| Income from continuing operations before equity in earnings of operating joint ventures for Financial Services Businesses                  | 33   | 911             |
| Equity in earnings of operating joint ventures, net of taxes   | 43   | 77              |
| Income from continuing operations for Financial Services Businesses  | 76   | 988             |
| Income from discontinued operations, net of taxes  | 1  | 37              |
| <b>Net income - Financial Services Businesses</b>  | <b>\$ 77</b>   | <b>\$ 1,025</b> |
| Basic income from continuing operations per share - Common Stock   | \$ 0.20  | \$ 2.14         |
| Diluted income from continuing operations per share - Common Stock   | \$ 0.20  | \$ 2.10         |
| Basic net income per share - Common Stock  | \$ 0.20  | \$ 2.22         |
| Diluted net income per share - Common Stock  | \$ 0.20  | \$ 2.18         |
| <b>Closed Block Business:</b>  |  |                 |
| Income (loss) from continuing operations before income taxes for Closed Block Business   | \$ (26)  | \$ 137          |
| Income tax expense (benefit)   | (18)   | 44              |
| Income (loss) from continuing operations for Closed Block Business   | (8)  | 93              |

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|  |            |          |   |
|--|------------|----------|---|
| Income from discontinued operations, net of taxes                                  |            |          | 2 |
| Net income (loss) Closed Block Business  | \$ (8)     | \$ 95    |   |
| Basic and diluted income (loss) from continuing operations per share Class B Stock | \$ (10.00) | \$ 39.00 |   |
| Basic and diluted net income (loss) per share Class B Stock                        | \$ (10.00) | \$ 40.00 |   |
| <b>Consolidated:</b>   |            |          |   |
| Net income   | \$ 69      | \$ 1,120 |   |

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### **Results of Operations Financial Services Businesses**

*2008 to 2007 Three Month Comparison.* Income from continuing operations attributable to the Financial Services Businesses decreased \$912 million, from \$988 million in the first quarter of 2007 to \$76 million in the first quarter of 2008. This decrease resulted primarily from net realized investment losses in the first quarter of 2008 compared to net realized investment gains in the prior year quarter. On a diluted per share basis, income from continuing operations attributable to the Financial Services Businesses for the three months ended March 31, 2008 of \$0.20 per share of Common Stock decreased from \$2.10 per share of Common Stock for the three months ended March 31, 2007. This decrease reflects the decline in earnings discussed above, partially offset by the benefit of a lower number of shares of Common Stock outstanding due to our share repurchase program. We analyze the operating performance of the segments included in the Financial Services Businesses using adjusted operating income as described in Segment Measures, below. For a discussion of our segment results on this basis see Results of Operations for Financial Services Businesses by Segment, below. In addition, for a discussion of the realized investment gains (losses), net attributable to the Financial Services Businesses, see Realized Investment Gains and Losses and General Account Investments Realized Investment Gains and Losses, below.

The direct equity adjustment increased income from continuing operations available to holders of the Common Stock for earnings per share purposes by \$12 million for the three months ended March 31, 2008, compared to \$15 million for the three months ended March 31, 2007. The direct equity adjustment modifies earnings available to holders of the Common Stock and the Class B Stock for earnings per share purposes. The holders of the Common Stock will benefit from the direct equity adjustment as long as reported administrative expenses of the Closed Block Business are less than the cash flows for administrative expenses determined by the policy servicing fee arrangement that is based upon insurance and policies in force and statutory cash premiums. As statutory cash premiums and policies in force in the Closed Block Business decline, we expect the benefit to the Common Stock holders from the direct equity adjustment to decline accordingly. If the reported administrative expenses of the Closed Block Business exceed the cash flows for administrative expenses determined by the policy servicing fee arrangement, the direct equity adjustment will reduce income available to holders of the Common Stock for earnings per share purposes.

### **Results of Operations Closed Block Business**

*2008 to 2007 Three Month Comparison.* Income (loss) from continuing operations attributable to the Closed Block Business for the three months ended March 31, 2008, was \$(8) million, or \$(10.00) per share of Class B Stock, compared to \$93 million, or \$39.00 per share of Class B Stock, for the three months ended March 31, 2007. The direct equity adjustment decreased income from continuing operations available to the Class B Stock holders for earnings per share purposes by \$12 million for the three months ended March 31, 2008, compared to \$15 million for the three months ended March 31, 2007. For a discussion of the results of operations for the Closed Block Business, see Results of Operations of Closed Block Business, below.

### **Segment Measures**

In managing our business, we analyze operating performance separately for our Financial Services Businesses and our Closed Block Business. For the Financial Services Businesses, we analyze our segments' operating performance using adjusted operating income. Results of the Closed Block Business for all periods are evaluated and presented only in accordance with U.S. GAAP. Adjusted operating income does not equate to income from continuing operations before income taxes and equity in earnings of operating joint ventures or net income as determined in accordance with U.S. GAAP but is the measure of segment profit or loss we use to evaluate segment performance and allocate resources, and consistent with SFAS No. 131, Disclosures about Segments of an Enterprise and Related Information, is our measure of segment performance.



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Adjusted operating income is calculated for the segments of the Financial Services Businesses by adjusting each segment's income from continuing operations before income taxes and equity in earnings of operating joint ventures for the following items:

realized investment gains (losses), net, except as indicated below, and related charges and adjustments;

net investment gains and losses on trading account assets supporting insurance liabilities and changes in experience-rated contractholder liabilities due to asset value changes;

the contribution to income/loss of divested businesses that have been or will be sold or exited that do not qualify for discontinued operations accounting treatment under U.S. GAAP; and

equity in earnings of operating joint ventures.

The items above are important to an understanding of our overall results of operations. Adjusted operating income is not a substitute for income determined in accordance with U.S. GAAP, and our definition of adjusted operating income may differ from that used by other companies. However, we believe that the presentation of adjusted operating income as we measure it for management purposes enhances understanding of our results of operations by highlighting the results from ongoing operations and the underlying profitability of the Financial Services Businesses.

Effective with the first quarter of 2008, we have amended our definition of adjusted operating income as it relates to certain externally managed investments in the European market held within the general account portfolio. These investments are medium term notes that are collateralized by investment portfolios primarily consisting of investment grade European fixed income securities, including corporate bonds and asset-backed securities, and derivatives, as well as varying degrees of leverage. The notes have a stated coupon and provide a return based on the performance of the underlying portfolios and the level of leverage. We invest in these notes to earn a coupon through maturity, consistent with our investment purpose for other debt securities. The notes are accounted for under U.S. GAAP as available for sale fixed maturity securities with bifurcated embedded derivatives (total return swaps). Changes in the value of the fixed maturity securities are reported in Stockholders' Equity under the heading Accumulated Other Comprehensive Income and changes in the market value of the embedded total return swaps are included in current period earnings in Realized investment gains (losses), net. Historically, adjusted operating income included cumulative losses and recoveries of such losses on the embedded derivatives in the period they occurred, while cumulative net gains on the embedded derivatives were deferred and amortized into adjusted operating income over the remaining life of the notes.

Adjusted operating income under the amended definition excludes any amounts related to changes in the market value of the embedded derivatives. Adjusted operating income for all periods presented has been revised to conform with the amended definition. We view adjusted operating income under the amended definition as a more meaningful presentation of our results for purposes of analyzing the operating performance of, and allocating resources to, our business segments, as the amended definition presents the results of these investments on a basis generally consistent with similar investments held directly within the general account portfolio. We believe the mark to market losses discussed below, resulting primarily from unprecedented credit spread widening, are not representative of the fundamental value of the underlying investments over the long term. Adjusted operating income continues to include the coupon on these notes, which reflects the market based interest rate and spread of securities comparable to the underlying securities that existed at the time we entered into the investments. The accounting for these investments under U.S. GAAP has not changed.

For the three months ended March 31, 2008 and 2007, we recorded a loss of \$208 million and a gain of \$8 million, respectively, within Realized investment gains (losses), net related to the change in value on the embedded derivatives associated with these investments, which are excluded from adjusted operating income under the amended definition. The loss of \$208 million for the three months ended March 31, 2008 is reflected

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within the U.S. GAAP results of the following segments: Individual Life \$12 million, Individual Annuities \$11 million, Group Insurance \$10 million, Retirement \$39 million, and International Insurance \$136



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million. Adjusted operating income under the former definition included a \$1 million gain for the three months ended March 31, 2007, which represented the amortization of cumulative deferred gains.

In reporting adjusted operating income for the three months ended March 31, 2008, we have classified our commercial mortgage securitization operations as a divested business, reflecting our decision to exit this business. As a result of this decision, these operations, which involved the origination and purchase of commercial mortgage loans for sale into commercial mortgage-backed securitization transactions, together with related hedging activities, previously reported within the Asset Management segment, have been classified within divested businesses and are reflected in our Corporate and Other operations. Accordingly, these results are excluded from adjusted operating income, with prior period results being adjusted to reflect such reclassification. These operations had a pre-tax loss of \$107 million for the first quarter of 2008.

Adjusted operating income excludes Realized investment gains (losses), net, except as indicated below, and related charges and adjustments. A significant element of realized investment gains and losses are impairments and credit-related and interest rate-related gains and losses. Impairments and losses from sales of credit-impaired securities, the timing of which depends largely on market credit cycles, can vary considerably across periods. The timing of other sales that would result in gains or losses, such as interest rate-related gains or losses, is largely subject to our discretion and influenced by market opportunities, as well as our tax profile. Trends in the underlying profitability of our businesses can be more clearly identified without the fluctuating effects of these transactions. Similarly, adjusted operating income excludes investment gains and losses on trading account assets supporting insurance liabilities and changes in experience-rated contractholder liabilities due to asset value changes, because these recorded changes in asset and liability values will ultimately accrue to the contractholders. Adjusted operating income excludes the results of divested businesses because they are not relevant to understanding our ongoing operating results. The contributions to income/loss of wind-down businesses that we have not divested remain in adjusted operating income. See Note 8 to the Unaudited Interim Consolidated Financial Statements for further information on the presentation of segment results.

As noted above, certain Realized investment gains (losses), net, are included in adjusted operating income. We include in adjusted operating income the portion of our realized investment gains and losses on derivatives that arise from the termination of contracts used to hedge our foreign currency earnings in the same period that the expected earnings emerge. Similarly, we include in adjusted operating income the portion of our realized investment gains and losses on derivatives that represent current period yield adjustments. The realized investment gains or losses from products that are free standing derivatives, or contain embedded derivatives, along with the realized investment gains or losses from associated derivative portfolios that are part of an economic hedging program related to the risk of these products, are included in adjusted operating income. Adjusted operating income also includes those realized investment gains and losses that represent profit or loss of certain of our businesses which primarily originate investments for sale or syndication to unrelated investors.

**Table of Contents****Results of Operations for Financial Services Businesses by Segment****Insurance Division***Individual Life**Operating Results*

The following table sets forth the Individual Life segment's operating results for the periods indicated.

|   | <b>Three Months Ended<br/>March 31,</b> |             |
|---|---|-------------|
|   | <b>2008</b>                             | <b>2007</b> |
|   | <b>(in millions)</b>                    |             |
| <b>Operating results:</b>   |   |             |
| Revenues  | \$ 680                                  | \$ 631      |
| Benefits and expenses   | 584                                     | 530         |
| Adjusted operating income   | 96                                      | 101         |
| Realized investment gains (losses), net, and related adjustments(1)   | (136)                                   | (12)        |
| Income (loss) from continuing operations before income taxes and equity in earnings of operating joint ventures | \$ (40)                                 | \$ 89       |

- (1) Revenues exclude Realized investment gains (losses), net, and related adjustments. See Realized Investment Gains and Losses and General Account Investments Realized Investment Gains and Losses. Realized investments gains (losses), net includes \$(12) million and \$1 million for the three months ended March 31, 2008 and 2007, respectively, related to certain externally managed investments in the European market. See Consolidated Results of Operations Segment Measures for information on the amendment to our adjusted operating income definition related to the treatment of these investments.

*Adjusted Operating Income*

*2008 to 2007 Three Month Comparison.* Adjusted operating income decreased \$5 million, from \$101 million in the first quarter of 2007 to \$96 million in the first quarter of 2008. The decrease in adjusted operating income primarily reflects a net increase in amortization of deferred policy acquisition costs net of related amortization of unearned revenue reserves, reflecting unfavorable separate account fund performance and policy persistency in the first quarter of 2008 consistent with expected levels, compared to a level more favorable than expectations in the first quarter of 2007, an increase in other costs and a decline in separate account fees. This decrease was partially offset by more favorable mortality experience, net of reinsurance, compared to the first quarter of the prior year.

*Revenues*

*2008 to 2007 Three Month Comparison.* Revenues, as shown in the table above under Operating Results, increased by \$49 million, from \$631 million in the first quarter of 2007 to \$680 million in the first quarter of 2008. Premiums increased \$22 million, primarily due to increased premiums on term life insurance reflecting continued growth of our in force block of term insurance. Net investment income increased \$25 million, reflecting higher asset balances primarily from the financing of regulatory capital requirements associated with statutory reserves for certain term and universal life insurance policies. An increase in policy charges and fee income reflecting the increase in amortization of unearned revenue reserves, discussed above, was partially offset by lower asset based fees due to lower separate account asset balances reflecting market value changes.

*Benefits and Expenses*

*2008 to 2007 Three Month Comparison.* Benefits and expenses, as shown in the table above under Operating Results, increased by \$54 million, from \$530 million in the first quarter of 2007 to \$584 million in the first quarter of 2008. Amortization of deferred policy acquisition costs increased \$33 million, reflecting

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unfavorable separate account fund performance and policy persistency in the first quarter of 2008 consistent with expected levels, compared to a level more favorable than expectations in the first quarter of 2007. Interest expense increased \$14 million, primarily reflecting interest on borrowings related to the financing of regulatory capital requirements associated with statutory reserves for certain term and universal life insurance policies.

*Sales Results*

The following table sets forth individual life insurance business sales, as measured by scheduled premiums from new sales on an annualized basis and first year excess premiums and deposits on a cash-received basis, for the periods indicated. Sales of the individual life insurance business do not correspond to revenues under U.S. GAAP. They are, however, a relevant measure of business activity. In managing our individual life insurance business, we analyze new sales on this basis because it measures the current sales performance of the business, while revenues primarily reflect the renewal persistency and aging of in force policies written in prior years and net investment income as well as current sales.

|  | <b>Three Months Ended<br/>March 31,<br/>2008                      2007<br/>(in millions)</b> |        |
|--|--|--------|
| <b>Life insurance sales(1):</b>                |  |        |
| Excluding corporate-owned life insurance:      |  |        |
| Variable life                                  | \$ 16  | \$ 48  |
| Universal life                                 | 40   | 44     |
| Term life                                      | 51   | 49     |
| Total excluding corporate-owned life insurance | 107  | 141    |
| Corporate-owned life insurance                 |  | 5      |
| Total  | \$ 107   | \$ 146 |

|   | <b>Three Months Ended<br/>March 31,<br/>2008                      2007<br/>(in millions)</b> |        |
|---|--|--------|
| <b>Life insurance sales by distribution channel, excluding corporate-owned life insurance(1):</b> |  |        |
| Prudential Agents   | \$ 40  | \$ 42  |
| Third party   | 67   | 99     |
| Total   | \$ 107   | \$ 141 |

(1) Scheduled premiums from new sales on an annualized basis and first year excess premiums and deposits on a cash-received basis.

*2008 to 2007 Three Month Comparison.* Sales of new life insurance, excluding corporate-owned life insurance, measured as described above, decreased \$34 million, from \$141 million in the first quarter of 2007 to \$107 million in the first quarter of 2008, primarily due to lower sales of variable life products as the prior year quarter included the benefit of several large case sales which have uneven quarterly sales patterns. The level of universal life sales in the first quarter of 2008 is reflective of highly competitive pricing in the marketplace and our continued avoidance of both investor oriented and aggressive financing sales. These decreases were partially offset by continued strong term life product sales.

The decrease in sales of life insurance, excluding corporate-owned life insurance, reflects a \$32 million decrease in sales from the third party distribution channel, which reflects the lower sales of variable life products, as discussed above, and a decrease in universal life sales. Sales by Prudential Agents were slightly lower than during the first quarter of 2007, reflecting a decline in the number of agents from 2,505 at March 31, 2007 to 2,436 at March 31, 2008. Although the number of agents has declined, per agent productivity, including investment products, has increased.

**Table of Contents***Policy Surrender Experience*

The following table sets forth the individual life insurance business' policy surrender experience for variable and universal life insurance, measured by cash value of surrenders, for the periods indicated. These amounts do not correspond to expenses under U.S. GAAP. In managing this business, we analyze the cash value of surrenders because it is a measure of the degree to which policyholders are maintaining their in force business with us, a driver of future profitability. Generally, our term life insurance products do not provide for cash surrender values.

|   | <b>Three Months Ended<br/>March 31,</b> |             |
|---|---|-------------|
|   | <b>2008</b>                             | <b>2007</b> |
|   | (\$ in millions)                        |             |
| Cash value of surrenders  | \$ 178                                  | \$ 167      |
| Cash value of surrenders as a percentage of mean future benefit reserves,<br>policyholders' account balances, and separate account balances | 3.1%                                    | 3.0%        |

*2008 to 2007 Three Month Comparison.* The total cash value of surrenders increased \$11 million, from \$167 million in the first quarter of 2007 to \$178 million in the first quarter of 2008, reflecting a greater volume of surrenders in the first quarter of 2008 compared to the first quarter of 2007. Cash value of surrenders as a percentage of mean future policy benefit reserves, policyholders' account balances and separate account balances increased from 3.0% in the first quarter of 2007 to 3.1% in the first quarter of 2008.

*Individual Annuities**Operating Results*

The following table sets forth the Individual Annuities segment's operating results for the periods indicated.

|  | <b>Three Months Ended<br/>March 31,</b> |             |
|--|---|-------------|
|  | <b>2008</b>                             | <b>2007</b> |
|  | (in millions)                           |             |
| <b>Operating results:</b>  |   |             |
| Revenues   | \$ 573                                  | \$ 604      |
| Benefits and expenses  | 458                                     | 438         |
| Adjusted operating income  | 115                                     | 166         |
| Realized investment gains (losses), net, and related adjustments(1)                                      | (53)                                    | (8)         |
| Related charges(1)(2)  | 17                                      |             |
| Income from continuing operations before income taxes and equity in earnings of operating joint ventures | \$ 79                                   | \$ 158      |

- (1) Revenues exclude Realized investment gains (losses), net, and related charges and adjustments. The related charges represent payments related to the market value adjustment features of certain of our annuity products. See Realized Investment Gains and Losses and General Account Investments Realized Investment Gains and Losses. Realized investments gains (losses), net includes \$(11) million and \$0 million for the three months ended March 31, 2008 and 2007, respectively, related to certain externally managed investments in the European market. See Consolidated Results of Operations Segment Measures for information on the amendment to our adjusted operating income definition related to the treatment of these investments.
- (2) Benefits and expenses exclude related charges which represent the unfavorable (favorable) impact of Realized investment gains (losses), net, on change in reserves and the amortization of deferred policy acquisition costs, deferred sales inducements and value of business acquired.

**Table of Contents***Adjusted Operating Income*

*2008 to 2007 Three Month Comparison.* Adjusted operating income decreased \$51 million, from \$166 million in the first quarter of 2007 to \$115 million in the first quarter of 2008. Contributing to this decrease is a \$24 million unfavorable variance in the mark-to-market of embedded derivatives and related hedge positions associated with our living benefit features, net of related amortization of deferred policy acquisition and other costs. The unfavorable variance reflects a net charge of \$17 million in the first quarter of 2008 compared to a net benefit of \$7 million in the first quarter of 2007, and was largely driven by financial market conditions in the first quarter of 2008.

Also contributing to the decrease in adjusted operating income in the first quarter of 2008 is a \$22 million unfavorable variance due to increased amortization of deferred policy acquisition and other costs, and higher charges relating to the reserves for the guaranteed minimum death and income benefit features of our variable annuity products, resulting from the quarterly adjustment for current period experience. The first quarter of 2008 reflects a charge of \$15 million relating to this quarterly adjustment, due to less favorable than expected experience, while the first quarter of 2007 reflects a benefit of \$7 million due to better than expected experience. The quarterly adjustment for current period experience reflects the cumulative impact of differences between actual gross profits for the period and the previously estimated expected gross profits for the period, as well as an update for current and future expected claims costs associated with these contract guarantees. Total estimated gross profits, including actual experience and estimates for future periods, are used as the basis for amortizing deferred policy acquisition and other costs. In addition, total estimated revenues and guaranteed benefit claims, which are components of total gross profits, are used for establishing the reserves for the guaranteed minimum death and income benefit features of our variable annuity products. To the extent each period's actual experience differs from the previous estimate for that period, the assumed level of total gross profits may change, and a cumulative adjustment to previous periods' costs, referred to as an adjustment for current period experience, may be required. Less favorable than expected gross profits in the current period were primarily due to lower than expected fee income and higher actual and expected contract guarantee claims costs in the first quarter of 2008, primarily driven by financial market conditions.

Management estimates the amortization of deferred policy acquisition and other costs, and the costs relating to the reserves for the guaranteed minimum death and income benefit features of our variable annuity products in the first quarter of 2008 would have increased approximately \$30 million had we adjusted our estimate of future gross profits to reflect the actual fund performance and corresponding changes to the future rate of return assumptions. For purposes of evaluating deferred policy acquisition and other costs and these reserves, the future rate of return assumptions are derived using a reversion to the mean approach, a common industry practice. As part of our approach, we develop a range of total estimated gross profits each period using statistically generated future rates of return that take into consideration the latest actual rates of return experienced to date. For the first quarter of 2008, since the previously determined total estimated gross profits were within the current period's range, we did not adjust our future rate of return assumptions.

*Revenues*

*2008 to 2007 Three Month Comparison.* Revenues, as shown in the table above under Operating Results, decreased \$31 million, from \$604 million in the first quarter of 2007 to \$573 million in the first quarter of 2008, primarily relating to a \$39 million decrease in policy charges and fees and asset management fees and other income, reflecting a \$54 million unfavorable variance in the mark-to-market of embedded derivatives and related hedge positions associated with our living benefit features, as discussed above, partially offset by an increase in fee income. The unfavorable variance in the mark-to-market of embedded derivatives and related hedge positions associated with our living benefit features reflects a net charge of \$40 million in the first quarter of 2008 compared to a net benefit of \$14 million in the first quarter of 2007. The increase in fee income was driven by higher average variable annuity account values and higher election rates relating to our optional living benefit features, which generate higher percentage fee rates. The increase in average variable annuity account values was due to consistent positive net asset flows since the first quarter of 2007 and market value increases in





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the second and third quarters of 2007, partially offset by equity market declines in the first quarter of 2008. Net investment income increased \$10 million reflecting higher average annuity account values invested in our general account. The increase in account values invested in our general account resulted from transfers relating to an automatic rebalancing element in some of our living benefit product features, which, as part of our overall risk management strategy, transferred investments out of equity sensitive separate accounts during the period due to equity market declines.

*Benefits and Expenses*

*2008 to 2007 Three Month Comparison.* Benefits and expenses, as shown in the table above under Operating Results, increased \$20 million, from \$438 million in the first quarter of 2007 to \$458 million in the first quarter of 2008. Policyholders' benefits, including interest credited to policyholders' account balances, increased \$25 million reflecting higher charges for the reserves for our guaranteed minimum death and income benefit features, as discussed above, as well as an increase in interest credited to policyholders due to higher average annuity account values invested in our general account. In addition, general and administrative expenses, net of capitalization, increased \$5 million, reflecting higher distribution and asset management costs associated with growth in variable annuity account values. Partially offsetting these increases was an \$11 million decrease in the amortization of deferred policy acquisition costs, resulting from the net impact on gross profits of the unfavorable variance relating to the hedging of our living benefit features, and the adjustment for current period experience, as discussed above.

*Account Values*

The following table sets forth changes in account values for the individual annuity business, for the periods indicated. For our individual annuity business, assets are reported at account value, and net sales (redemptions) are gross sales minus redemptions or surrenders and withdrawals, as applicable.

|  | <b>Three Months Ended<br/>March 31,</b> |             |
|--|---|-------------|
|  | <b>2008</b>                             | <b>2007</b> |
|  | <b>(in millions)</b>                    |             |
| <b>Variable Annuities(1):</b>                                |   |             |
| Beginning total account value                                | \$ 80,330                               | \$ 74,555   |
| Sales  | 2,829                                   | 2,779       |
| Surrenders and withdrawals                                   | (2,173)                                 | (2,310)     |
| Net sales  | 656                                     | 469         |
| Benefit payments   | (294)                                   | (306)       |
| Net flows  | 362                                     | 163         |
| Change in market value, interest credited and other activity | (5,409)                                 | 1,168       |
| Policy charges   | (306)                                   | (295)       |
| Ending total account value(2)                                | \$ 74,977                               | \$ 75,591   |
| <b>Fixed Annuities:</b>                                      |   |             |
| Beginning total account value                                | \$ 3,488                                | \$ 3,748    |
| Sales  | 17                                      | 21          |
| Surrenders and withdrawals                                   | (53)                                    | (81)        |

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|                                      |          |          |
|--------------------------------------|----------|----------|
| Net redemptions                      | (36)     | (60)     |
| Benefit payments                     | (43)     | (43)     |
| Net flows                            | (79)     | (103)    |
| Interest credited and other activity | 32       | 35       |
| Policy charges                       | (1)      | (1)      |
| Ending total account value           | \$ 3,440 | \$ 3,679 |

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- (1) Variable annuities include only those sold as retail investment products. Investments through defined contribution plan products are included with such products within the Retirement segment.
- (2) As of March 31, 2008, variable annuity account values are invested in equity funds (\$35 billion or 46%), balanced funds (\$20 billion or 27%), bond funds (\$8 billion or 11%), and other (\$12 billion or 16%). Variable annuity account values with living benefit features were \$36.0 billion and \$30.3 billion as of March 31, 2008 and 2007, respectively.

*2008 to 2007 Three Month Comparison.* Total account values for fixed and variable annuities amounted to \$78.4 billion as of March 31, 2008, a decrease of \$5.4 billion from December 31, 2007. The decrease came primarily from decreases in the market value of customers' variable annuities due to significant equity market declines in the first quarter of 2008. Total account values as of March 31, 2008 decreased \$853 million from March 31, 2007, primarily reflecting decreases in the market value of customers' variable annuities, partially offset by positive variable annuity net flows. Individual variable annuity gross sales increased by \$50 million, despite market volatility and equity market declines, reflecting sustained momentum in the growth of our distribution relationships, and the introduction of additional optional living benefit product features in the first quarter of 2008. Individual variable annuity surrenders and withdrawals decreased by \$137 million, from \$2.3 billion in the first quarter of 2007 to \$2.2 billion in the first quarter of 2008.

**Group Insurance***Operating Results*

The following table sets forth the Group Insurance segment's operating results for the periods indicated.

|  | <b>Three Months Ended<br/>March 31,<br/>2008      2007<br/>(in millions)</b> |          |
|--|--|----------|
| <b>Operating results:</b>  |  |          |
| Revenues   | \$ 1,257   | \$ 1,205 |
| Benefits and expenses  | 1,167  | 1,154    |
| Adjusted operating income  | 90   | 51       |
| Realized investment gains (losses), net, and related adjustments(1)                                      | (87)   | 14       |
| Related charges(2)   |  |          |
| Income from continuing operations before income taxes and equity in earnings of operating joint ventures | \$ 3   | \$ 65    |

- (1) Revenues exclude Realized investment gains (losses), net, and related adjustments. See Realized Investment Gains and Losses and General Account Investments Realized Investment Gains and Losses. Realized investment gains (losses), net includes \$(10) million and \$0 million for the three months ended March 31, 2008 and 2007, respectively, related to certain externally managed investments in the European market. See Consolidated Results of Operations Segment Measures for information on the amendment to our adjusted operating income definition related to the treatment of these investments.
- (2) Benefits and expenses exclude related charges which represent the unfavorable (favorable) impact of Realized investment gains (losses), net, on interest credited to policyholders' account balances.

*Adjusted Operating Income*

*2008 to 2007 Three Month Comparison.* Adjusted operating income increased \$39 million, from \$51 million in the first quarter of 2007 to \$90 million in the first quarter of 2008, reflecting growth in our group disability business. In addition, our group life business benefited from more favorable claims experience, which was

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partially offset by reduced business in force. Also included in current quarter results is a \$20 million benefit from a premium adjustment for updated data on a large group life insurance case.

*Revenues*

*2008 to 2007 Three Month Comparison.* Revenues, as shown in the table above under Operating Results, increased by \$52 million, from \$1.205 billion in the first quarter of 2007 to \$1.257 billion in the first quarter of 2008. Group life premiums decreased by \$26 million, from \$719 million in the first quarter of 2007 to \$693 million in the first quarter of 2008, primarily reflecting lower net premiums from experience-rated group life business resulting from the decrease in policyholder benefits on these contracts as discussed below. Also contributing to this decrease were lower premiums from non-experience-rated group life business due to reduced business in force. Lapse activity increased slightly as group life persistency deteriorated from 96% in the first quarter of 2007 to 95% in the first quarter of 2008. Offsetting these decreases is a premium adjustment for updated data on a large case. Group disability premiums, which include long-term care products, increased by \$67 million from \$207 million in the first quarter of 2007 to \$274 million in the first quarter of 2008. This increase reflects growth in business in force resulting from new sales, which included the assumption of existing liabilities from third parties during the first quarter of 2008, exceeding the level of lapses, which increased slightly as persistency deteriorated from 92% in the first quarter of 2007 to 91% in the first quarter of 2008. The slight declines in group life and group disability persistency are reflective of continuing competitive pricing in the marketplace and the pricing discipline we apply in writing business. Net investment income was relatively unchanged, as the benefit from growth in invested assets was offset by lower investment yields.

*Benefits and Expenses*

The following table sets forth the Group Insurance segment's benefits and administrative operating expense ratios for the periods indicated.

|   | Three Months Ended<br>March 31, |       |
|---|---------------------------------|-------|
|   | 2008                            | 2007  |
| <b>Benefits ratio(1):</b>                         |                                 |       |
| Group life  | 87.1%                           | 91.5% |
| Group disability                                  | 91.1                            | 91.0  |
| <b>Administrative operating expense ratio(2):</b> |                                 |       |
| Group life  | 8.2                             | 9.6   |
| Group disability                                  | 17.4                            | 22.1  |

- (1) Ratio of policyholder benefits to earned premiums, policy charges and fee income. Group disability ratios include long-term care products.
- (2) Ratio of administrative operating expenses (excluding commissions) to gross premiums, policy charges and fee income. Group disability ratios include long-term care products.

*2008 to 2007 Three Month Comparison.* Benefits and expenses, as shown in the table above under Operating Results, increased by \$13 million, from \$1.154 billion in the first quarter of 2007 to \$1.167 billion in the first quarter of 2008. This increase is due to a \$10 million increase in policyholders' benefits, including the change in policy reserves, primarily reflecting growth of business in force in our group disability business, partially offset by more favorable claims experience in our group life businesses, which resulted in lower premiums from experience-rated group life business as discussed above.

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The group life benefits ratio improved 4.4 percentage points from the first quarter of 2007 to the first quarter of 2008, due to the benefit from a premium adjustment for updated data on a large case combined with more favorable mortality experience in our group life business. The group disability benefits ratio was relatively stable. The group life administrative operating expense ratio improved from the first quarter of 2007 to the first quarter of 2008, as gross premiums increased, primarily from the experience-rated group life business, while operating expenses were relatively unchanged. The group disability administrative operating expense ratio improved from the first quarter of 2007 to the first quarter of 2008, reflecting growth in the business from new sales as noted above, while maintaining stable operating expenses.

**Table of Contents***Sales Results*

The following table sets forth the Group Insurance segment's new annualized premiums for the periods indicated. In managing our group insurance business, we analyze new annualized premiums, which do not correspond to revenues under U.S. GAAP, because new annualized premiums measure the current sales performance of the business unit, while revenues primarily reflect the renewal persistency and aging of in force policies written in prior years and net investment income, in addition to current sales.

|                                    | <b>Three Months Ended<br/>March 31,</b> |               |
|------------------------------------|---|---------------|
|                                    | <b>2008</b>                             | <b>2007</b>   |
|                                    | <b>(in millions)</b>                    |               |
| <b>New annualized premiums(1):</b> |   |               |
| Group life                         | \$ 112                                  | \$ 103        |
| Group disability(2)                | 114                                     | 92            |
| <b>Total</b>                       | <b>\$ 226</b>                           | <b>\$ 195</b> |

- (1) Amounts exclude new premiums resulting from rate changes on existing policies, from additional coverage under our Servicemembers Group Life Insurance contract and from excess premiums on group universal life insurance that build cash value but do not purchase face amounts, and include premiums from the takeover of claim liabilities.
- (2) Includes long-term care products.

*2008 to 2007 Three Month Comparison.* Total new annualized premiums increased \$31 million, or 16%, from \$195 million in the first quarter of 2007 to \$226 million in the first quarter of 2008. This increase is primarily attributable to higher sales in our group disability business reflecting premiums related to the assumption of existing liabilities from a third party and higher long-term care sales. Our sales are reflective of the continuing competitive pricing in the marketplace and the pricing discipline we apply in writing business.

**Investment Division***Asset Management**Operating Results*

The following table sets forth the Asset Management segment's operating results for the periods indicated.

| <b>Three Months Ended<br/>March 31,</b> |             |
|---|-------------|
| <b>2008</b>                             | <b>2007</b> |
| <b>(in millions)</b>                    |             |



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| <b>Operating results:</b>  |        |        |
|--|--------|--------|
| Revenues   | \$ 548 | \$ 545 |
| Expenses   | 429    | 370    |
| Adjusted operating income  | 119    | 175    |
| Realized investment gains (losses), net, and related adjustments(1)                                      | 12     | 2      |
| Income from continuing operations before income taxes and equity in earnings of operating joint ventures | \$ 131 | \$ 177 |

(1) Revenues exclude Realized investment gains (losses), net, and related adjustments. See Realized Investment Gains and Losses and General Account Investments Realized Investment Gains and Losses.

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In reporting results for the three months ended March 31, 2008, we have classified our commercial mortgage securitization operations as a divested business, reflecting our decision to exit this business. As a result of this decision, these operations, which involved the origination and purchase of commercial mortgage loans for sale into commercial mortgage-backed securitization transactions, together with related hedging activities, are excluded from the Asset Management segment and included in Corporate and Other operations as a divested business. Accordingly, these results are excluded from adjusted operating income, with prior period results being adjusted to reflect such reclassification. These operations had a pre-tax loss of \$107 million for the first quarter of 2008. We will retain and continue the remainder of our commercial mortgage origination, servicing and other commercial mortgage related activities, which remain a part of our Asset Management segment.

*Adjusted Operating Income*

*2008 to 2007 Three Month Comparison.* Adjusted operating income decreased \$56 million, from \$175 million in the first quarter of 2007 to \$119 million in the first quarter of 2008. Results of the segment's proprietary investing business included losses of \$31 million in the first quarter of 2008, compared to income of \$20 million in the first quarter of 2007, from changes in market value in a fixed income fund, of which our investment at March 31, 2008 totaled \$490 million. The segment's proprietary investing business also includes losses of \$4 million in the first quarter of 2008, compared to a gain of \$6 million in the first quarter of 2007, primarily from changes in the market value of equity funds, net of related hedges, of which our investment at March 31, 2008 totaled \$266 million. In addition, results in the current quarter reflect lower transaction fees and higher compensation costs. These items were partially offset by greater performance based incentive fees, primarily related to institutional real estate funds, increased asset management fees, and higher income related to securities lending services.

*Revenues*

The following tables set forth the Asset Management segment's revenues, presented on a basis consistent with the table above under Operating Results, by type, asset management fees by source and assets under management for the periods indicated. In managing our business we analyze assets under management, which do not correspond to U.S. GAAP assets, because a principal source of our revenues are fees based on assets under management.

|  | <b>Three Months Ended<br/>March 31,</b> |               |
|--|---|---------------|
|  | <b>2008</b>                             | <b>2007</b>   |
|  | <b>(in millions)</b>                    |               |
| <b>Revenues by type:</b>   |   |               |
| Asset management fees  | \$ 281                                  | \$ 262        |
| Incentive, transaction, principal investing and capital markets revenues | 101                                     | 131           |
| Service, distribution and other revenues(1)                              | 166                                     | 152           |
| <b>Total revenues</b>  | <b>\$ 548</b>                           | <b>\$ 545</b> |

- (1) Includes revenues under a contractual arrangement with Wachovia Securities, related to managed account services, which was originally scheduled to expire on July 1, 2006. This contract was amended effective July 1, 2005 to provide essentially a fixed fee for managed account services and is now scheduled to expire on July 1, 2008. Revenues in the first quarter of 2008 included \$8 million for those management account services. Also includes payments from Wachovia Corporation under an agreement dated as of July 30, 2004 implementing arrangements with respect to money market mutual funds in connection with the combination of our retail securities brokerage and clearing operations with those of Wachovia Corporation. The agreement extends for ten years after termination of the joint venture. The revenue from Wachovia Corporation under this agreement was \$14 million and \$13 million in the three months ended

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March 31, 2008 and 2007, respectively.

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|   | <b>Three Months Ended<br/>March 31,</b> |               |
|---|---|---------------|
|   | <b>2008</b>                             | <b>2007</b>   |
|   | <b>(in millions)</b>                    |               |
| <b>Asset management fees by source:</b> |   |               |
| Institutional customers                 | \$ 133                                  | \$ 117        |
| Retail customers(1)                     | 81                                      | 84            |
| General account                         | 67                                      | 61            |
| <b>Total asset management fees</b>      | <b>\$ 281</b>                           | <b>\$ 262</b> |

- (1) Consists of individual mutual funds and both variable annuities and variable life insurance asset management revenues from our separate accounts. This also includes funds invested in proprietary mutual funds through our defined contribution plan products. Revenues from fixed annuities and the fixed rate options of both variable annuities and variable life insurance are included in the general account.

|  | <b>March 31,</b>     | <b>March 31,</b> |
|--|----------------------|------------------|
|  | <b>2008</b>          | <b>2007</b>      |
|  | <b>(in billions)</b> |                  |
| <b>Assets Under Management (at fair market value):</b> |                      |                  |
| Institutional customers(1)                             | \$ 174               | \$ 161           |
| Retail customers(2)                                    | 82                   | 84               |
| General account  | 178                  | 169              |
| <b>Total</b>   | <b>\$ 434</b>        | <b>\$ 414</b>    |

- (1) Consists of third party institutional assets and group insurance contracts.
- (2) Consists of individual mutual funds and both variable annuities and variable life insurance assets in our separate accounts. This also includes funds invested in proprietary mutual funds through our defined contribution plan products. Fixed annuities and the fixed rate options of both variable annuities and variable life insurance are included in the general account.

*2008 to 2007 Three Month Comparison.* Revenues, as shown in the table above under Operating Results, increased \$3 million, from \$545 million in the first quarter of 2007 to \$548 million in the first quarter of 2008. Asset management fees increased \$19 million, primarily from the management of institutional customer assets as a result of increased asset values due to market appreciation and net asset flows. Service, distribution and other revenues increased \$14 million, primarily due to higher income related to securities lending services due to improved yields. Revenues from incentive, transaction, principal investing and capital markets decreased \$30 million, primarily reflecting a decline in revenues from the segment's proprietary investing business driven by changes in market value in a fixed income fund and lower transaction fees, partially offset by an increase in incentive based fees primarily related to institutional real estate funds, a portion of which are offset in incentive compensation expense in accordance with the terms of the contractual agreements. Certain of our incentive fees are subject to positive or negative future adjustment based on cumulative fund performance in relation to specified benchmarks. As of March 31, 2008, approximately \$180 million of cumulative incentive fee revenue, net of compensation, is subject to future adjustment.

*Expenses*

*2008 to 2007 Three Month Comparison.* Expenses, as shown in the table above under Operating Results, increased \$59 million, from \$370 million in the first quarter of 2007 to \$429 million in the first quarter of 2008, driven by higher costs related to incentive fees, as discussed above, and higher compensation costs primarily reflecting increased headcount.



**Table of Contents****Financial Advisory***Operating Results*

The following table sets forth the Financial Advisory segment's operating results for the periods indicated.

|   | <b>Three Months Ended<br/>March 31,</b> |             |
|---|---|-------------|
|   | <b>2008</b>                             | <b>2007</b> |
|   | <b>(in millions)</b>                    |             |
| <b>Operating results:</b>   |   |             |
| Revenues  | \$ 51                                   | \$ 111      |
| Expenses  | 7                                       | 14          |
| Adjusted operating income   | 44                                      | 97          |
| Equity in earnings of operating joint ventures(1)   | (51)                                    | (111)       |
| Income (loss) from continuing operations before income taxes and equity in earnings of operating joint ventures | \$ (7)                                  | \$ (14)     |

- (1) Equity in earnings of operating joint ventures are included in adjusted operating income but excluded from income from continuing operations before income taxes and equity in earnings of operating joint ventures as they are reflected on a U.S. GAAP basis on an after-tax basis as a separate line in our Unaudited Interim Consolidated Statements of Operations.

On July 1, 2003, we combined our retail securities brokerage and clearing operations with those of Wachovia Corporation, or Wachovia, and formed Wachovia Securities Financial Holdings, LLC, or Wachovia Securities, a joint venture headquartered in St. Louis, Missouri. As of December 31, 2007, we had a 38% ownership interest in the joint venture with Wachovia owning the remaining 62%. The transaction included certain assets and liabilities of our securities brokerage operations; however, we retained certain assets and liabilities related to the contributed businesses, including liabilities for certain litigation and regulatory matters. We have agreed with Wachovia to indemnify each other for certain losses, including losses resulting from litigation and regulatory matters relating to certain events arising from the operations of our respective contributed businesses prior to March 31, 2004.

On October 1, 2007, Wachovia completed the acquisition of A.G. Edwards, Inc., or A.G. Edwards, for \$6.8 billion and on January 1, 2008 combined the retail securities brokerage business of A.G. Edwards with Wachovia Securities. As discussed in Note 10 to the Unaudited Interim Consolidated Financial Statements, we have elected the "lookback" option under the terms of the agreements relating to the joint venture. The "lookback" option permits us to delay for two years following the combination of the A.G. Edwards business with Wachovia Securities our decision to make or not to make payments to avoid or limit dilution of our ownership interest in the joint venture. During this "lookback" period, our share in the earnings of the joint venture and one-time costs associated with the combination of the A.G. Edwards business with Wachovia Securities is based on our diluted ownership level, which is in the process of being determined. Any payments at the end of the "lookback" period to restore all or part of our ownership interest in the joint venture will be based on the appraised or agreed value of the joint venture excluding the A.G. Edwards business as well as the A.G. Edwards business. In such event, we would also need to make a true-up payment of one-time costs incurred during the "lookback" period associated with the combination to reflect the incremental increase in our ownership interest in the joint venture. Alternatively, at the end of the "lookback" period, we may put our joint venture interests to Wachovia based on the appraised value of the joint venture, excluding the A.G. Edwards business, as of January 1, 2008, the date of the combination of the A.G. Edwards business with Wachovia Securities.

We also retain our separate right to put our joint venture interests to Wachovia at any time after July 1, 2008 based on the appraised value of the joint venture, including the A.G. Edwards business, determined as if it were a public company and including a control premium such as would apply in the case of a sale of 100% of its

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common equity. However, if in connection with the lookback option we elect at the end of the lookback period to make payments to avoid or limit dilution, we may not exercise this put option prior to the first anniversary of the end of the lookback period. The agreement between Prudential Financial and Wachovia also gives us put rights, and Wachovia call rights, in certain other specified circumstances, at prices determined in accordance with the agreement.

We are currently negotiating with Wachovia possible modifications to the terms of the existing agreements relating to the joint venture. Based upon the existing agreements and our estimates of the values of the A.G. Edwards business and the joint venture excluding the A.G. Edwards business, we adjusted the carrying value of our ownership interest in the joint venture effective as of January 1, 2008 to reflect the addition of that business and the dilution of our 38% ownership level and to record the value of the above described rights under the lookback option. As a result, effective January 1, 2008, we recognized an increase to Additional paid-in capital of \$977 million, net of tax. Our recorded share of pre-tax earnings from the joint venture of \$51 million for the three months ended March 31, 2008, reflects our estimated diluted ownership level based upon the existing agreements and our estimates of the values of the A.G. Edwards business and the joint venture excluding the A.G. Edwards business. As noted above, we are negotiating with Wachovia possible modifications to the terms of the existing agreements relating to the joint venture. Such modifications, if agreed to, as well as the establishment of definitive agreed or appraised values for the A.G. Edwards business and the joint venture excluding the A.G. Edwards business, will result in an adjustment to the credit to equity and a true-up to the earnings from the joint venture for any difference between the diluted ownership percentage used to record earnings for the three months ended March 31, 2008 and the finally determined diluted ownership percentage. We do not anticipate any such adjustment to have a material effect on our reported results of operations.

*2008 to 2007 Three Month Comparison.* Adjusted operating income decreased \$53 million, from \$97 million in the first quarter of 2007 to \$44 million in the first quarter of 2008. The segment's results for the first quarter of 2008 include our share of earnings from Wachovia Securities, on a pre-tax basis, of \$51 million, based on our estimated diluted ownership level, as discussed above, compared to \$111 million in the first quarter of 2007, including transition costs in the first quarter of 2008 of \$46 million related to the combination of the A.G. Edwards business with Wachovia Securities. In addition, the prior year quarter benefited from a greater contribution from equity syndication activity. The segment's results also include expenses of \$7 million in the first quarter of 2008 related to obligations and costs we retained in connection with the contributed businesses, primarily for litigation and regulatory matters, compared to \$14 million in the first quarter of 2007.

**Retirement***Operating Results*

The following table sets forth the Retirement segment's operating results for the periods indicated.

|   | <b>Three Months Ended<br/>March 31,</b> |             |
|---|---|-------------|
|   | <b>2008</b>                             | <b>2007</b> |
|   | <b>(in millions)</b>                    |             |
| <b>Operating results:</b>   |   |             |
| Revenues  | \$ 1,267                                | \$ 1,163    |
| Benefits and expenses   | 1,143                                   | 1,015       |
| Adjusted operating income   | 124                                     | 148         |
| Realized investment gains (losses), net, and related adjustments(1) | (179)                                   | (7)         |
| Related charges(2)  | (3)                                     | (1)         |



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|   |          |        |
|---|----------|--------|
| Investment gains (losses) on trading account assets supporting insurance liabilities, net(3)                    | (105)    | 58     |
| Change in experience-rated contractholder liabilities due to asset value changes(4)                             | 43       | (40)   |
| Income (loss) from continuing operations before income taxes and equity in earnings of operating joint ventures | \$ (120) | \$ 158 |

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- (1) Revenues exclude Realized investment gains (losses), net, and related adjustments. See Realized Investment Gains and Losses and General Account Investments Realized Investment Gains and Losses. Realized investments gains (losses), net includes \$(39) million and \$1 million for the three months ended March 31, 2008 and 2007, respectively, related to certain externally managed investments in the European market. See Consolidated Results of Operations Segment Measures for information on the amendment to our adjusted operating income definition related to the treatment of these investments.
- (2) Benefits and expenses exclude related charges which represent the unfavorable (favorable) impact of Realized investment gains (losses), net, on change in reserves and the amortization of deferred policy acquisition costs.
- (3) Revenues exclude net investment gains and losses on trading account assets supporting insurance liabilities. See Trading Account Assets Supporting Insurance Liabilities.
- (4) Benefits and expenses exclude changes in contractholder liabilities due to asset value changes in the pool of investments supporting these experience-rated contracts. See Trading Account Assets Supporting Insurance Liabilities.

On December 31, 2007 we acquired a portion of Union Bank of California, N.A.'s retirement business, including \$7.3 billion in full service retirement account values, for \$103 million of cash consideration. The retirement account values related to this acquisition primarily consist of mutual funds and other client assets we administer, and are not reported on our balance sheet.

*Adjusted Operating Income*

*2008 to 2007 Three Month Comparison.* Adjusted operating income for the Retirement segment decreased \$24 million, from \$148 million in the first quarter of 2007 to \$124 million in the first quarter of 2008, reflecting lower adjusted operating income in our full service business and essentially unchanged results for our institutional investment products business. The decrease relating to the full service business was primarily attributable to higher general and administrative expenses and a lower contribution from investment results due to lower investment yields on certain general account defined contribution balances. Also contributing to the decrease in the full service business was a \$4 million loss in the first quarter of 2008 relating to the acquired retirement business of Union Bank of California, N.A., including costs related to an interim service agreement with Union Bank of California, N.A., which covers the integration period. In our institutional investment products business, a decrease in the level of mortgage prepayment income and an unfavorable variance in the mark to market of equity investments required in certain of our separate account products, was offset by more favorable case experience related to a group annuity block of business.

*Revenues*

*2008 to 2007 Three Month Comparison.* Revenues, as shown in the table above under Operating Results, increased \$104 million, from \$1.163 billion in the first quarter of 2007 to \$1.267 billion in the first quarter of 2008. Premiums increased \$104 million, driven by higher single premium group annuity and life-contingent structured settlement sales, and resulted in a corresponding increase in policyholders' benefits, including the change in policy reserves, as discussed below. In addition, the first quarter of 2008 included \$6 million of revenues associated with the acquired retirement business of Union Bank of California, N.A., which is primarily reflected within asset management fees and other income. Net investment income decreased slightly, as the benefit from a larger base of invested assets due to sales of guaranteed investment products in the institutional and retail markets was offset by lower balances of investments supported by borrowings, a decrease in the level of mortgage prepayment income, an unfavorable variance in the mark to market of equity investments required in certain of our separate account products, and lower investment yields on certain general account defined contribution balances.

**Table of Contents***Benefits and Expenses*

*2008 to 2007 Three Month Comparison.* Benefits and expenses, as shown in the table above under Operating Results, increased \$128 million, from \$1.015 billion in the first quarter of 2007 to \$1.143 billion in the first quarter of 2008. Policyholders' benefits, including the change in policy reserves, increased \$90 million primarily reflecting the increase in premiums on higher single premium group annuity and life-contingent structured settlement sales discussed above, partially offset by more favorable case experience related to a group annuity block of business in the first quarter of 2008. Interest credited to policyholders' account balances increased \$41 million, primarily reflecting higher interest credited on a greater base of guaranteed investment products sold in the institutional and retail markets. General and administrative expenses, net of capitalization, increased \$14 million, and included \$10 million of costs in the first quarter of 2008 associated with the acquired retirement business of Union Bank of California, N.A., including costs related to an interim services agreement with Union Bank of California, N.A., which covers the integration period. Partially offsetting these items was a \$19 million decrease in interest expense reflecting lower borrowings used to support investments.

*Sales Results and Account Values*

The following table shows the changes in the account values and net additions (withdrawals) of Retirement segment products for the periods indicated. Net additions (withdrawals) are deposits and sales or additions, as applicable, minus withdrawals and benefits. These concepts do not correspond to revenues under U.S. GAAP, but are used as a relevant measure of business activity.

|   | <b>Three Months Ended<br/>March 31,<br/>2008      2007<br/>(in millions)</b> |           |
|---|--|-----------|
| <b>Full Service(1):</b>                                       |  |           |
| Beginning total account value                                 | \$ 112,192   | \$ 97,430 |
| Deposits and sales  | 4,586  | 4,003     |
| Withdrawals and benefits                                      | (3,933)  | (3,433)   |
| Change in market value, interest credited and interest income | (5,785)  | 1,558     |
| Ending total account value                                    | \$ 107,060   | \$ 99,558 |
| Net additions   | \$ 653   | \$ 570    |
| <b>Institutional Investment Products(2):</b>                  |  |           |
| Beginning total account value                                 | \$ 51,591  | \$ 50,269 |
| Additions   | 1,810  | 1,533     |
| Withdrawals and benefits(3)                                   | (1,702)  | (1,743)   |
| Change in market value, interest credited and interest income | 561  | 607       |
| Other(3)(4)   | (593)  | (5)       |
| Ending total account value                                    | \$ 51,667  | \$ 50,661 |
| Net additions (withdrawals)                                   | \$ 108   | \$ (210)  |

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- (1) Ending total account value for the full service business includes assets of Prudential's retirement plan of \$5.5 billion and \$5.7 billion as of March 31, 2008 and 2007, respectively.
- (2) Ending total account value for the institutional investment products business includes assets of Prudential's retirement plan of \$5.2 billion and \$5.3 billion as of March 31, 2008 and 2007, respectively.
- (3) Transfers between the Retirement and Asset Management segments, previously presented within Withdrawals and benefits, have been reclassified to Other for all periods presented.
- (4) Other includes transfers from (to) the Asset Management segment of \$(206) million for the three months ended March 31, 2008. Remaining amounts for all periods presented primarily represents changes in asset balances for externally managed accounts.

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*2008 to 2007 Three Month Comparison.* Account values in our full service business amounted to \$107.1 billion as of March 31, 2008, a decrease of \$5.1 billion from December 31, 2007. The decrease in account values was driven primarily by a decrease in the market value of customer funds due to declines in the equity markets, partially offset by net additions of \$653 million. Account values in our full service business as of March 31, 2008 increased \$7.5 billion from March 31, 2007, primarily reflecting \$7.3 billion of account values acquired from Union Bank of California, N.A. Net additions increased \$83 million, from \$570 million in the first quarter of 2007 to \$653 million in the first quarter of 2008, reflecting higher participant contributions and new plan sales, partially offset by higher plan lapses.

Account values in our institutional investment products business amounted to \$51.7 billion as of March 31, 2008, an increase of \$76 million from December 31, 2007, primarily reflecting interest on general account business and net additions of \$108 million, partially offset by declines in the value of asset balances for externally managed accounts. Account values in our institutional investment products business as of March 31, 2008 increased \$1.0 billion from March 31, 2007, primarily reflecting interest on general account business and an increase in the market value of customer funds, partially offset by net withdrawals. Net additions (withdrawals) increased \$318 million, from net withdrawals of \$210 million in the first quarter of 2007 to net additions of \$108 million in the first quarter of 2008. This increase primarily reflects higher additions driven by higher sales of structured settlements and single premium group annuities.

**International Insurance and Investments Division*****Impact of foreign currency exchange rate movements on earnings***

As a U.S.-based company with significant business operations outside the U.S., we seek to mitigate the risk that future unfavorable foreign currency exchange rate movements will reduce our U.S. dollar equivalent earnings. The operations of our International Insurance and International Investments segments are subject to currency fluctuations that can materially affect their U.S. dollar results from period to period even if results on a local currency basis are relatively constant. As discussed further below, we enter into forward currency derivative contracts, as well as dual currency and synthetic dual currency investments, as part of our strategy to effectively fix the currency exchange rates for a portion of our prospective non-U.S. dollar denominated earnings streams.

***Forward currency hedging program***

The financial results of our International Insurance segment and International Investments segment, excluding the global commodities group, for all periods presented reflect the impact of an intercompany arrangement with Corporate and Other operations pursuant to which the segments non-U.S. dollar denominated earnings in all countries are translated at fixed currency exchange rates. The fixed rates are determined in connection with a currency income hedging program designed to mitigate the risk that unfavorable exchange rate changes will reduce the segments U.S. dollar equivalent earnings. Pursuant to this program, Corporate and Other operations executes forward currency contracts with third parties to sell the hedged currency in exchange for U.S. dollars at specified exchange rates. The maturities of these contracts correspond with the future periods in which the identified non-U.S. dollar denominated earnings are expected to be generated. This program is primarily associated with the International Insurance segment's businesses in Japan, Korea and Taiwan and the International Investments segment's businesses in Korea and Europe. The intercompany arrangement with Corporate and Other operations increased (decreased) revenues and adjusted operating income of each segment as follows for the periods indicated:

| <b>Three Months Ended</b> |             |
|---------------------------|-------------|
| <b>March 31,</b>          |             |
| <b>2008</b>               | <b>2007</b> |

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|  | (in millions) |       |
|--|---------------|-------|
| Impact on revenues and adjusted operating income:      |               |       |
| International Insurance                                | \$            | \$ 28 |
| International Investments                              |               | (3)   |
| Total International Insurance and Investments Division | \$            | \$ 25 |

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Results of Corporate and Other operations include any differences between the translation adjustments recorded by the segments and the gains or losses recorded from the forward currency contracts that settled during the period. The consolidated net impact of this program recorded within the Corporate and Other operations were gains of \$1 million and losses of \$4 million for the three months ended March 31, 2008 and 2007, respectively.

*Dual currency and synthetic dual currency investments*

In addition, our Japanese insurance operations also hold dual currency investments in the form of fixed maturities and loans. The principal of these dual currency investments are yen-denominated while the related interest income is U.S. dollar denominated. These investments are the economic equivalent of exchanging what would otherwise be fixed streams of yen-denominated interest income for fixed streams of U.S. dollars. Our Japanese insurance operations also hold investments in yen-denominated investments that have been coupled with cross-currency coupon swap agreements, creating synthetic dual currency investments. The yen/U.S. dollar exchange rate is effectively fixed, as we are obligated in future periods to exchange fixed amounts of Japanese yen interest payments generated by the yen-denominated investments for U.S. dollars at the yen/U.S. dollar exchange rates specified by the cross-currency coupon swap agreements. As of both March 31, 2008 and December 31, 2007, the notional amount of these investments was ¥538 billion, or \$4.8 billion based upon the foreign currency exchange rates applicable at the time these investments were acquired. For the three months ended March 31, 2008 and 2007, the weighted average yields generated by these investments were 2.4% and 2.3%, respectively.

Presented below is the fair value of these instruments as reflected on our balance sheet for the periods presented.

|   | March 31,<br>2008 | December 31,<br>2007 |
|---|-------------------|----------------------|
|   | (in millions)     |                      |
| Cross-currency coupon swap agreements                               | \$ 8              | \$ 40                |
| Foreign exchange component of interest on dual currency investments | (45)              | (11)                 |
| <b>Total</b>  | <b>\$ (37)</b>    | <b>\$ 29</b>         |

The table below presents as of March 31, 2008, the yen-denominated earnings subject to our dual currency and synthetic dual currency investments and the related weighted average exchange rates resulting from these investments.

| Year              | (1)<br>Interest component<br>of dual<br>currency<br>investments | Cross-currency<br>coupon swap element<br>of synthetic<br>dual<br>currency investments<br>(in billions) | Yen-denominated<br>earnings subject to<br>these investments | Weighted average<br>exchange rate per<br>U.S. Dollar<br>(Yen per \$) |
|-------------------|---|--|---|--|
| Remainder of 2008 | ¥ 2.9   | ¥ 6.5  | ¥ 9.4   | 90.8   |
| 2009              | 3.4   | 5.8  | 9.2   | 88.7   |
| 2010              | 3.2   | 4.9  | 8.1   | 87.4   |
| 2011              | 3.1   | 3.8  | 6.9   | 85.6   |
| 2012-2034         | 36.0  | 56.4   | 92.4  | 79.5   |
| <b>Total</b>      | <b>¥48.6</b>  | <b>¥ 77.4</b>  | <b>¥126.0</b>   | <b>81.7</b>  |

- (1) Yen amounts are imputed from the contractual U.S. dollar denominated interest cash flows.

The table above does not reflect the forward currency income hedging program discussed above. In establishing the level of yen-denominated earnings that will be hedged through the forward currency income hedging program we take into account the anticipated level of U.S. dollar denominated earnings that will be generated by dual currency and synthetic dual currency investments, as well as the anticipated level of U.S.



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dollar denominated earnings that will be generated by U.S. dollar denominated products and investments, which are discussed in greater detail below.

### *Impact of foreign currency exchange rate movements on equity*

#### *Hedges of U.S. GAAP equity and available economic capital*

We also seek to mitigate the risk that future unfavorable foreign currency exchange rate movements will reduce our U.S. dollar equivalent equity in foreign subsidiaries through various hedging strategies. In the case of our Japanese insurance operations, which constitute our most significant foreign insurance operations, we hedge 100% of our U.S. GAAP equity in these subsidiaries, excluding Accumulated other comprehensive income components of Stockholders Equity and certain other adjustments. In addition, in our Japanese insurance operations we seek to hedge a portion of the amount by which available economic capital exceeds the current value of the U.S. GAAP equity. Available economic capital represents the excess of the fair value of assets over the fair value of liabilities for the current in force block of business. We are in the process of developing an economic capital framework, which includes available economic capital, as discussed in Liquidity and Capital Resources Prudential Financial Economic Capital. We hedge a portion of the available economic capital, including that portion represented by U.S. GAAP equity, in our Japanese insurance operations primarily by maintaining U.S. dollar denominated investments financed with yen-denominated liabilities. In certain of our other foreign insurance operations, the U.S. GAAP equity exposure is mitigated by entering into forward currency contracts that qualify for hedge accounting treatment, and by holding U.S. dollar denominated investments.

As of March 31, 2008, the amortized cost of available for sale U.S. dollar denominated investments, as well as cash and cash equivalents, serving as a hedge of our available economic capital amounted to \$5.0 billion, unchanged from December 31, 2007. During the first quarter of 2008, we increased by \$1.0 billion the portion of available economic capital hedged in our Japanese insurance operations through U.S. dollar denominated investments that are designated as held to maturity. As of March 31, 2008, our U.S. dollar denominated investments and other assets supporting the portion of our available economic capital above our U.S. GAAP equity totaled \$2.2 billion and were acquired at an average exchange rate of 106 yen. These amounts do not reflect the forward currency income hedging program or dual currency and synthetic dual currency investments discussed above.

The available for sale investments under U.S. GAAP are recorded at fair value on the balance sheet with unrealized changes in fair value (except as described below for impairments), including those from changes in foreign currency exchange rate movements, recorded as unrealized gains or losses in Accumulated other comprehensive income within Stockholders Equity. Changes in the U.S. GAAP equity of our Japanese insurance operations due to foreign currency exchange rate movements are also recorded in Accumulated other comprehensive income as a Currency translation adjustment and are largely offset by the related changes in fair value due to foreign currency exchange rate movements of the portion of the available for sale investments that supports our Japanese insurance operations U.S. GAAP equity, hence creating a natural equity hedge. To the extent U.S. dollar denominated investments support the portion of available economic capital above our U.S. GAAP equity there is no offsetting impact to equity.

The investments designated as held to maturity under U.S. GAAP are recorded at amortized cost on the balance sheet, but are remeasured for foreign currency exchange rate movements with the related change in value recorded within Asset management fees and other income. The remeasurement related to the change in value for foreign currency exchange rate movements for these investments is excluded from adjusted operating income, as part of our application of the hedge of available economic capital.

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The U.S. dollar denominated investments that hedge a portion of our available economic capital in our Japanese insurance operations pay a coupon, which is reflected within Net investment income, and, therefore, included in adjusted operating income, which is approximately 200 to 300 basis points greater than what a

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similar yen-based investment would pay. The incremental impact of this higher yield will vary over time, and is dependent on the duration of the underlying investment, as well as interest rate environments in the U.S. and Japan at the time of the investment. See [Realized Investment Gains and Losses and General Account Investments](#) [General Account Investments](#) [Investment Results](#) for a discussion of the investment yields generated by our Japanese insurance operations.

Because these U.S. dollar denominated investments are recorded on the books of yen-based entities, foreign currency exchange movements will impact their value. To the extent the value of the yen strengthens as compared to the U.S. dollar, the value of these U.S. dollar denominated investments will decrease as a result of changes in the foreign currency exchange rates. Upon the ultimate sale or maturity of the U.S. dollar denominated investments, any realized change in value related to changes in the foreign currency exchange rates will be included in [Realized gains \(losses\), net](#) within the income statement and, excluded from adjusted operating income. Similarly, any impairment recognized on these investments, including those for an other-than-temporary decline in value that may include the impact of changes in foreign currency exchange rates, will be included in [Realized gains \(losses\), net](#) within the income statement, and, as such, excluded from adjusted operating income. See

[Realized Investment Gains and Losses and General Account Investments](#) [General Account Investments](#) [Fixed Maturity Securities](#) [Other-than-Temporary Impairments of Fixed Maturity Securities](#) for a discussion of our policies regarding impairments.

During the first quarter of 2008, we began incorporating the impact of foreign currency exchange rate movements on certain other U.S. dollar denominated assets, primarily accrued investment income, within our Japanese insurance operations as part of our overall application of the hedge of available economic capital. The U.S. dollar denominated assets are remeasured for foreign currency exchange rate movements, as they are non-yen denominated items on the books of yen-based entities, and the related change in value is recorded within [Asset management fees and other income](#). As these U.S. dollar denominated assets are included in the determination of the Japanese insurance operations' level of available economic capital, it is appropriate to exclude all remeasurement related to these items from adjusted operating income.

Prospectively, we will seek to continue to hedge 100% of the U.S. GAAP equity as discussed above, and, to varying degrees, the available economic capital of the Japanese insurance operations, which we may accomplish through holding U.S. dollar investments within the Japanese insurance operations or through yen-denominated borrowings issued within our U.S. operations.

In addition, as of March 31, 2008 and December 31, 2007, our Japanese insurance operations also had \$4.7 billion and \$4.3 billion, respectively, of foreign currency exposure from U.S. liabilities for U.S. dollar denominated products issued by these operations. The Japanese insurance operations hold U.S. dollar denominated investments, including a significant portion that are designated as available for sale, and other related U.S. dollar denominated assets, primarily accrued investment income, to support these products. The change in value due to changes in foreign currency exchange rate movements, or remeasurement, of the related U.S. dollar denominated assets and liabilities associated with these products is excluded from adjusted operating income.

***International Insurance***

The results of our International Insurance operations are translated on the basis of weighted average monthly exchange rates, and inclusive of the effects of the intercompany arrangement discussed above. To provide a better understanding of operating performance within the International Insurance segment, where indicated below, we have analyzed our results of operations excluding the effect of the year over year change in foreign currency exchange rates. Our results of operations excluding the effect of foreign currency fluctuations were derived by translating foreign currencies to U.S. dollars at uniform exchange rates for all periods presented, including, for constant dollar information discussed below, Japanese yen at a rate of 106 yen per U.S. dollar; Korean won at a rate of 950 won per U.S. dollar. New annualized premiums presented on a constant exchange rate basis in the [Sales Results](#) section below reflect translation based on these same uniform exchange rates.



**Table of Contents***Operating Results*

The following table sets forth the International Insurance segment's operating results for the periods indicated.

|  | <b>Three Months Ended<br/>March 31,<br/>2008                      2007<br/>(in millions)</b> |          |
|--|--|----------|
| <b>Operating results:</b>  |  |          |
| Revenues:  |  |          |
| Life Planner operations  | \$ 1,577   | \$ 1,359 |
| Gibraltar Life   | 748  | 694      |
|  | 2,325  | 2,053    |
| Benefits and expenses:   |  |          |
| Life Planner operations  | 1,292  | 1,090    |
| Gibraltar Life   | 620  | 551      |
|  | 1,912  | 1,641    |
| Adjusted operating income:   |  |          |
| Life Planner operations  | 285  | 269      |
| Gibraltar Life   | 128  | 143      |
|  | 413  | 412      |
| Realized investment gains (losses), net, and related adjustments(1)                                      | (68)   | 140      |
| Related charges(1)(2)  | (27)   | (5)      |
| Investment gains (losses) on trading account assets supporting insurance liabilities, net(3)             | (157)  | 22       |
| Change in experience-rated contractholder liabilities due to asset value changes(4)                      | 157  | (22)     |
| Income from continuing operations before income taxes and equity in earnings of operating joint ventures | \$ 318   | \$ 547   |

- (1) Revenues exclude Realized investment gains (losses), net, and related charges and adjustments. The related charges represent the impact of Realized investment gains (losses), net, on the amortization of unearned revenue reserves. See *Realized Investment Gains and Losses and General Account Investments Realized Investment Gains and Losses*. Realized investment gains (losses), net includes \$(136) million and \$6 million for the three months ended March 31, 2008 and 2007, respectively, related to certain externally managed investments in the European market. See *Consolidated Results of Operations Segment Measures* for information on the amendment to our adjusted operating income definition related to the treatment of these investments.
- (2) Benefits and expenses exclude related charges that represent the element of *Dividends to policyholders* that is based on a portion of certain realized investment gains required to be paid to policyholders and the impact of Realized investment gains (losses), net, on the amortization of deferred policy acquisition costs.
- (3) Revenues exclude net investment gains and losses on trading account assets supporting insurance liabilities. See *Trading Account Assets Supporting Insurance Liabilities*.
- (4) Benefits and expenses exclude changes in contractholder liabilities due to asset value changes in the pool of investments supporting these experience-rated contracts. See *Trading Account Assets Supporting Insurance Liabilities*.

*Adjusted Operating Income*

*2008 to 2007 Three Month Comparison.* Adjusted operating income from Life Planner operations increased \$16 million, from \$269 million in the first quarter of 2007 to \$285 million in first quarter of 2008, including a \$1 million favorable impact of currency fluctuations. These currency fluctuations reflect the year over year change

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in foreign currency exchange rates. Excluding the impact of currency fluctuations, adjusted operating income of our Life Planner operations increased \$15 million reflecting the continued growth of our Japanese and Korean Life Planner operations and more favorable mortality experience. Partially offsetting these items, was increased amortization of deferred policy acquisition costs reflecting less favorable persistency on traditional products in Korea and a reduction in actual and expected gross profits for certain seasoned Japanese products with account values linked to Japanese equity market performance.

Gibraltar Life's adjusted operating income decreased \$15 million, from \$143 million in the first quarter of 2007 to \$128 million in the first quarter of 2008, including a \$2 million unfavorable impact of currency fluctuations. Excluding the impact of currency fluctuations, adjusted operating income for Gibraltar Life decreased \$13 million, reflecting less favorable mortality experience, increased amortization of deferred policy acquisition costs driven by less favorable persistency experience, and a higher level of expenses including costs associated with parallel testing of a new claims system.

*Revenues*

*2008 to 2007 Three Month Comparison.* Revenues, as shown in the table above under Operating Results, increased \$272 million, from \$2.053 billion in the first quarter of 2007 to \$2.325 billion in the first quarter of 2008, including a net favorable impact of \$152 million relating to currency fluctuations. Excluding the impact of currency fluctuations, revenues increased \$120 million, from \$2.219 billion in the first quarter of 2007 to \$2.339 billion in the first quarter of 2008.

Revenues from our Life Planner operations increased \$218 million, from \$1.359 billion in the first quarter of 2007 to \$1.577 billion in the first quarter of 2008, including a net favorable impact of currency fluctuations of \$105 million. Excluding the impact of currency fluctuations, revenues increased \$113 million from the first quarter of 2007 to the first quarter of 2008. This increase in revenues came primarily from increases in premiums and policy charges and fee income of \$77 million, from \$1.242 billion in the first quarter of 2007 to \$1.319 billion in the first quarter of 2008. Premiums and policy charges and fee income from our Japanese Life Planner operation increased \$56 million, from \$885 million in the first quarter of 2007 to \$941 million in the first quarter of 2008. Premiums and policy charges and fee income from our Korean operation increased \$17 million, from \$282 million in the first quarter of 2007 to \$299 million in the first quarter of 2008. The increase in premiums and policy charges and fee income in both operations was primarily the result of growth in business in force from new sales and strong persistency. Overall policy persistency for the 13-month period remained relatively stable at 92% in the first quarter of 2008. Net investment income also increased \$28 million, from \$202 million in the first quarter of 2007 to \$230 million in the first quarter of 2008, due to asset growth and higher investment yields reflecting our continuing desire to lengthen the duration of our Japanese investment portfolio.

Revenues from Gibraltar Life increased \$54 million, from \$694 million in the first quarter of 2007 to \$748 million in the first quarter of 2008, including a favorable impact from currency fluctuations of \$47 million. Excluding the impact of currency fluctuations, revenues for Gibraltar Life increased \$7 million, from \$763 million in the first quarter of 2007 to \$770 million in the first quarter of 2008. This increase reflects a \$11 million increase in net investment income, from \$211 million in the first quarter of 2007 to \$222 million in the first quarter of 2008, driven by the continued growth of our U.S. dollar denominated annuity product, as well as higher portfolio yields from duration lengthening, increased credit exposure and increased utilization of U.S. dollar denominated investments. Premiums were relatively unchanged, as an increase in new sales of U.S. dollar denominated products was offset by a decrease in renewal premiums reflecting the attrition of existing business. Policy persistency for the 13-month period declined from 94% in the three months ended March 31, 2007 to 91% in the first quarter of 2008. Our renewal premiums have declined as the market has continued to transition from traditional products, on which we record premiums, to newer products such as those with a retirement and savings objective, for which customer funds received are recorded as deposits.

**Table of Contents***Benefits and Expenses*

*2008 to 2007 Three Month Comparison.* Benefits and expenses, as shown in the table above under Operating Results, increased \$271 million, from \$1.641 billion in the first quarter of 2007 to \$1.912 billion in the first quarter of 2008, including a net unfavorable impact of \$153 million related to currency fluctuations. Excluding the impact of currency fluctuations, benefits and expenses increased \$118 million, from \$1.801 billion in the first quarter of 2007 to \$1.919 billion in the first quarter of 2008.

Benefits and expenses of our Life Planner operations increased \$202 million, from \$1.090 billion in the first quarter of 2007 to \$1.292 billion in the first quarter of 2008, including a net unfavorable impact of \$104 million from currency fluctuations. Excluding the impact of currency fluctuations, benefits and expenses increased \$98 million, from \$1.183 billion in the first quarter of 2007 to \$1.281 billion in the first quarter of 2008. Benefits and expenses of our Japanese Life Planner operation increased \$63 million, from \$816 million in the first quarter of 2007 to \$879 million in the first quarter of 2008. Benefits and expenses from our Korean operation increased \$24 million, from \$260 million in the first quarter of 2007 to \$284 million in first quarter of 2008. The increase in benefits and expenses in both operations reflects an increase in policyholder benefits, including changes in reserves, which was driven by the growth in business in force. Also contributing to the increase in benefits and expenses was higher amortization of deferred policy acquisition costs. Partially offsetting these increases was more favorable mortality experience.

Gibraltar Life's benefits and expenses increased \$69 million, from \$551 million in the first quarter of 2007 to \$620 million in the first quarter of 2008, including a \$49 million unfavorable impact of currency fluctuations. Excluding the impact of currency fluctuations, benefits and expenses increased \$20 million, from \$618 million in the first quarter of 2007 to \$638 million in the first quarter of 2008. This increase is primarily due to less favorable mortality experience, increased amortization of deferred policy acquisition costs, and a higher level of expenses including costs associated with parallel testing of a new claims system. In addition, higher interest credited to policyholders' account balances resulting from growth in our U.S. dollar denominated annuity product contributed to this increase.

*Sales Results*

In managing our international insurance business, we analyze revenues, as well as new annualized premiums, which do not correspond to revenues under U.S. GAAP. New annualized premiums measure the current sales performance of the segment, while revenues primarily reflect the renewal persistency of policies written in prior years and net investment income, in addition to current sales. New annualized premiums include 10% of first year premiums or deposits from single pay products. New annualized premiums on an actual and constant exchange rate basis are as follows for the periods indicated.

|                                   | <b>Three Months Ended<br/>March 31,<br/>2008                      2007<br/>(in millions)</b> |               |
|-----------------------------------|--|---------------|
| <b>New annualized premiums:</b>   |  |               |
| On an actual exchange rate basis: |  |               |
| Life Planner operations           | \$ 235   | \$ 223        |
| Gibraltar Life                    | 94   | 73            |
| <b>Total</b>                      | <b>\$ 329</b>  | <b>\$ 296</b> |

On a constant exchange rate basis:



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|                         |               |               |
|-------------------------|---------------|---------------|
| Life Planner operations | \$ 233        | \$ 236        |
| Gibraltar Life          | 96            | 79            |
| <b>Total</b>            | <b>\$ 329</b> | <b>\$ 315</b> |

*2008 to 2007 Three Month Comparison.* On a constant exchange rate basis, new annualized premiums increased \$14 million, from \$315 million in the first quarter of 2007 to \$329 million in the first quarter of 2008.

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New annualized premiums, on a constant exchange rate basis, from our Japanese Life Planner operation decreased \$4 million, reflecting lower sales of retirement income and term life products, partially offset by an increase in sales of other life products. Sales in all other countries, also on a constant exchange rate basis, were relatively flat.

The number of Life Planners increased 245, or 4%, from 5,893 as of March 31, 2007 to 6,138 as of March 31, 2008. This increase was driven by increases of 107 and 70 in our Life Planner operations in Japan and Taiwan, respectively, as well as an increase of 63 in our Mexico operation, which began recruiting Life Planners in the second quarter of 2007, and was partially offset by a decrease of 22 in Korea. In addition, during 2007 and the first quarter of 2008, 95 Life Planners in Japan were transferred to Gibraltar primarily to support our efforts to expand our bank channel distribution. Factoring in these transfers, the number of Life Planners would have increased 340, or 6%, from March 31, 2007 to March 31, 2008.

New annualized premiums, on a constant exchange rate basis, from our Gibraltar Life operation increased \$17 million, from \$79 million in the first quarter of 2007 to \$96 million in the first quarter of 2008, primarily reflecting sales of a new U.S. dollar denominated retirement income product launched in the first quarter of 2008. In addition, higher sales of other U.S. dollar denominated products, were mostly offset by lower sales of Japanese yen denominated products, and the level of sales in the bank distribution channel was unchanged. The number of Life Advisors increased by 83, from 5,952 as of March 31, 2007 to 6,035 as of March 31, 2008, reflecting our continued focus on hiring practices to enhance productivity and retention.

### *Investment Margins and Other Profitability Factors*

Many of our insurance products sold in international markets provide for the buildup of cash values for the policyholder at mandated guaranteed interest rates. Japanese authorities regulate interest rates guaranteed in our Japanese insurance contracts. The regulated guaranteed interest rates do not necessarily match the actual returns on the underlying investments. The spread between the actual investment returns and these guaranteed rates of return to the policyholder is an element of the profit or loss that we will experience on these products. With regulatory approval, guaranteed rates may be changed on new business. While these actions enhance our ability to set rates commensurate with available investment returns, the major sources of profitability on our products sold in Japan, other than those sold by Gibraltar Life, are margins on mortality, morbidity and expense charges rather than investment spreads.

We base premiums and cash values in most countries in which we operate on mandated mortality and morbidity tables. Our mortality and morbidity experience in the International Insurance segment on an overall basis in the first three months of 2008 and the first three months of 2007 was well within our pricing assumptions and below the guaranteed levels reflected in the premiums we charge.

**Table of Contents****International Investments***Operating Results*

The following table sets forth the International Investments segment's operating results for the periods indicated.

|  | <b>Three Months Ended<br/>March 31,</b> |             |
|--|---|-------------|
|  | <b>2008</b>                             | <b>2007</b> |
| <b>(in millions)</b>   |   |             |
| <b>Operating results:</b>  |   |             |
| Revenues   | \$ 176                                  | \$ 177      |
| Expenses   | 150                                     | 115         |
| Adjusted operating income  | 26                                      | 62          |
| Realized investment gains (losses), net, and related adjustments(1)                                      | 3                                       |             |
| Related charges(2)   |   |             |
| Equity in earnings of operating joint ventures(3)  | (9)                                     | (9)         |
| Income from continuing operations before income taxes and equity in earnings of operating joint ventures | \$ 20                                   | \$ 53       |

- (1) Revenues exclude Realized investment gains (losses), net, and related adjustments. See Realized Investment Gains and Losses and General Account Investments Realized Investment Gains and Losses.
- (2) Benefits and expenses exclude related charges which represent the unfavorable (favorable) impact of Realized investment gains (losses), net, on minority interest.
- (3) Equity in earnings of operating joint ventures are included in adjusted operating income but excluded from income from continuing operations before income taxes and equity in earnings of operating joint ventures as they are reflected on a U.S. GAAP basis on an after-tax basis as a separate line in our Unaudited Interim Consolidated Statements of Operations.

In 2004, we acquired an 80 percent interest in Hyundai Investment and Securities Co., Ltd., a Korean asset management firm, from an agency of the Korean government. We subsequently renamed the company Prudential Investment & Securities Co., Ltd, or PISC. On January 25, 2008, we completed the acquisition of the remaining 20 percent for \$90 million and PISC is now a wholly owned operation.

On January 18, 2008, we made an additional investment of \$154 million in our UBI Pramerica operating joint venture in Italy, which we account for under the equity method. This additional investment was necessary to maintain our ownership interest at 35% and was a result of the merger of our joint venture partner with another Italian bank, and their subsequent consolidation of their asset management companies into the UBI Pramerica joint venture.

*Adjusted Operating Income*

*2008 to 2007 Three Month Comparison.* Adjusted operating income decreased \$36 million, from \$62 million in the first quarter of 2007 to \$26 million in the first quarter of 2008. The primary driver of the decrease is a \$19 million credit loss reserve related to a brokerage client that was

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recorded in our global commodities group in the first quarter of 2008. Excluding the impact of this credit loss, results for the global commodities group were essentially unchanged, as more favorable sales and trading results were offset by a lower benefit in the current quarter from market value changes on securities relating to exchange memberships. Also contributing to the decrease in adjusted operating income were lower results from the segment's asset management businesses as the prior year quarter benefited both from higher fees in our Korean operation due to strong sales of mutual funds that carry a front-end load and income recognized from an equity-related investment.

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The adjusted operating income of our Korean asset management operation includes \$5 million in both the first quarter of 2008 and 2007 of fee revenue from the Korean government under an agreement entered into in connection with the acquisition of PISC, related to the provision of asset management and brokerage services, which agreement extends until February 27, 2009.

*Revenues*

*2008 to 2007 Three Month Comparison.* Revenues, as shown in the table above under Operating Results, decreased \$1 million, from \$177 million in the first quarter of 2007 to \$176 million in the first quarter of 2008. This decrease primarily reflects the decrease in front-end fees in our Korean asset management operation and the lower benefit in the current quarter from market value changes on securities relating to exchange memberships. Largely offsetting these items were higher revenues from the sales and trading activity of our global commodities group.

*Expenses*

*2008 to 2007 Three Month Comparison.* Expenses, as shown in the table above under Operating Results, increased \$35 million, from \$115 million in the first quarter of 2007 to \$150 million in the first quarter of 2008, primarily due to the credit loss in our global commodities group and higher expenses corresponding with the higher level of revenues generated by the sales and trading activity of our global commodities group.

**Corporate and Other**

Corporate and Other includes corporate operations, after allocations to our business segments, and real estate and relocation services.

Corporate operations consist primarily of: (1) corporate-level income and expenses, after allocations to any of our business segments, including income and expense from our qualified pension and other employee benefit plans and investment returns on capital that is not deployed in any of our segments; (2) returns from investments that we do not allocate to any of our business segments, including debt-financed investment portfolios, as well as tax credit investments and other tax enhanced investments financed by our business segments; and (3) businesses that we have placed in wind-down status but have not divested as well as the impact of transactions with other segments.

|   | <b>Three Months Ended<br/>March 31,</b> |             |
|---|---|-------------|
|   | <b>2008</b>                             | <b>2007</b> |
|   | <b>(in millions)</b>                    |             |
| <b>Operating results:</b>   |   |             |
| Corporate Operations(1)   | \$ (12)                                 | \$ 12       |
| Real Estate and Relocation Services   | (23)                                    | (3)         |
| Adjusted operating income   | (35)                                    | 9           |
| Realized investment gains (losses), net, and related adjustments(2)               | (157)                                   | 18          |
| Investment gains on trading account assets supporting insurance liabilities(1)(3) |   | 2           |

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|   |          |       |
|---|----------|-------|
| Divested businesses(4)  | (112)    | 28    |
| Income (loss) from continuing operations before income taxes and equity in earnings of operating joint ventures | \$ (304) | \$ 57 |

- (1) Includes consolidating adjustments.
- (2) Revenues exclude Realized investment gains (losses), net, and related adjustments. See Realized Investment Gains and Losses and General Account Investments Realized Investment Gains and Losses. The related charges represent the impact of Realized investment gains (losses), net, on the amortization of unearned revenue reserves. See Realized Investment Gains and Losses and General Account Investments Realized Investment Gains and Losses.

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- (3) Revenues exclude net investment gains and losses on trading account assets supporting insurance liabilities. See Trading Account Assets Supporting Insurance Liabilities.
- (4) See Divested Businesses.

*2008 to 2007 Three Month Comparison.* Adjusted operating income decreased \$44 million, from income of \$9 million in the first quarter of 2007 to a loss of \$35 million in the first quarter of 2008. Adjusted operating income from corporate operations decreased \$24 million, from income of \$12 million in the first quarter of 2007 to a loss of \$12 million in the first quarter of 2008. Corporate operations investment income, net of interest expense, decreased \$24 million, primarily reflecting the impact of less favorable income from equity method investments, including tax credit investments and lower earnings from the investment of proceeds from our convertible debt issues. The \$2 billion November 2005 convertible debt securities, for which investment of proceeds in fixed income securities contributed to results for the first quarter of 2007, were repaid in May 2007. The proceeds from our \$2 billion December 2006 convertible debt issuance were used to fund an investment portfolio of fixed income securities until December 2007; which also benefited results for the prior year quarter. These proceeds, as well as the proceeds from our \$3 billion December 2007 convertible debt issuance, are now invested in short-term investments or are used to support short-term capital and operating needs in lieu of other short-term borrowings. We anticipate our investment income, net of interest expense within our corporate operations will continue to decline in future periods as we continue to repurchase shares and experience less pre-tax earnings on a growing book of equity method tax credit investments. The benefit to corporate operations earnings from our equity method tax credit investments is realized on an after-tax basis.

Corporate operations includes income from our qualified pension plan of \$72 million in the first quarter of 2008, a decrease of \$19 million from \$91 million in the first quarter of 2007. The decrease primarily reflects the impact of the transfer of \$1 billion in plan assets within the qualified pension plan under Section 420 of the Internal Revenue Code from assets supporting pension benefits to assets supporting retiree medical benefits. As a result of the transfer, the decline in income from our qualified pension plan was offset by a corresponding decline in other postretirement benefit expenses.

Corporate operations benefited from a decline in our deferred compensation liabilities in the first quarter of 2008 versus the prior year quarter. This benefit was offset by increased costs related to our retained obligations relating to policyholders with whom we had previously agreed to provide insurance for reduced or no premium in accordance with contractual settlements related to prior individual life sales practices remediation. Both our deferred compensation liabilities and our retained obligations to certain policyholders are impacted by volatility in the financial markets.

Adjusted operating income of our real estate and relocation services business decreased \$20 million, from a loss of \$3 million in the first quarter of 2007 to a loss of \$23 million in the first quarter of 2008. Less favorable residential real estate market conditions resulted in lower royalty fees, increased bad debt reserves and lower relocation revenue from real estate referral fees and fixed fee homesale transactions. Certain of our clients utilize a fixed fee homesale program under which we assume the benefits and burdens of ownership with respect to a relocating employee's home that is purchased by us, including carrying costs and any loss on sale. As of March 31, 2008, we held in unsold inventory homes with a net value of approximately \$90 million under these types of programs.

**Results of Operations of Closed Block Business**

We established the Closed Block Business effective as of the date of demutualization. The Closed Block Business includes our in force traditional domestic participating life insurance and annuity products and assets that are used for the payment of benefits and policyholder dividends on these policies, as well as other assets and equity and related liabilities that support these policies. We no longer offer these traditional domestic participating policies. See Overview Closed Block Business for additional details.





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At the end of each year, the Board of Directors of Prudential Insurance determines the dividends payable on participating policies for the following year based on the experience of the Closed Block, including investment income, net realized and unrealized investment gains, mortality experience and other factors. Although Closed Block experience for dividend action decisions is based upon statutory results, at the time the Closed Block was established, we developed, as required by U.S. GAAP, an actuarial calculation of the timing of the maximum future earnings from the policies included in the Closed Block. If actual cumulative earnings in any given period are greater than the cumulative earnings we expected, we will record this excess as a policyholder dividend obligation. We will subsequently pay this excess to Closed Block policyholders as an additional dividend unless it is otherwise offset by future Closed Block performance that is less favorable than we originally expected. The policyholder dividends we charge to expense within the Closed Block Business will include any change in policyholder dividend obligations that we recognize for the excess of actual cumulative earnings in any given period over the cumulative earnings we expected in addition to the actual policyholder dividends declared by the Board of Directors of Prudential Insurance.

As of March 31, 2008, the Company recognized a policyholder dividend obligation to Closed Block policyholders for the excess of actual cumulative earnings over the expected cumulative earnings of \$579 million. Actual cumulative earnings, as required by U.S. GAAP, reflect the recognition of realized investment gains in the current period, as well as changes in assets and related liabilities that support the policies. As of March 31, 2008, net unrealized investment losses have arisen subsequent to the establishment of the Closed Block due to the impact of the credit environment and associated interest rates on the market value of fixed maturities available for sale. The impact of these net unrealized investment losses have been reflected as a decrease to the policyholder dividend obligation of \$128 million, as of March 31, 2008, with an offsetting amount reported in accumulated other comprehensive income (loss).

*Operating Results*

Management does not consider adjusted operating income to assess the operating performance of the Closed Block Business. Consequently, results of the Closed Block Business for all periods are presented only in accordance with U.S. GAAP. The following table sets forth the Closed Block Business U.S. GAAP results for the periods indicated.

|   | <b>Three Months Ended<br/>March 31,<br/>2008      2007<br/>(in millions)</b> |          |
|---|--|----------|
| <b>U.S. GAAP results:</b>   |  |          |
| Revenues  | \$ 1,671   | \$ 1,991 |
| Benefits and expenses   | 1,697  | 1,854    |
| Income (loss) from continuing operations before income taxes and equity in earnings of operating joint ventures | \$ (26)  | \$ 137   |

*Income (loss) from Continuing Operations Before Income Taxes and Equity in Earnings of Operating Joint Ventures*

*2008 to 2007 Three Month Comparison.* Income (loss) from continuing operations before income taxes and equity in earnings of operating joint ventures decreased \$163 million, from income of \$137 million in the first quarter of 2007 to a loss of \$26 million in the first quarter of 2008. First quarter 2008 results reflect a decrease of \$317 million in net realized investment gains, from gains of \$207 million in the first quarter of 2007 to losses of \$110 million in the first quarter of 2008. For a discussion of Closed Block Business realized investment gains (losses), net, see

Realized Investment Gains and Losses and General Account Investments Realized Investment Gains and Losses. The decrease in net realized investment gains was partially offset by a decrease in dividends to policyholders of \$181 million, reflecting a decrease in the cumulative earnings policyholder



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dividend obligation expense of \$240 million, partially offset by an increase in dividends paid and accrued to policyholders primarily due to an increase in the 2008 dividend scale.

### *Revenues*

*2008 to 2007 Three Month Comparison.* Revenues, as shown in the table above under Operating Results, decreased \$320 million, from \$1.991 billion in the first quarter of 2007 to \$1.671 billion in the first quarter of 2008, principally driven by the \$317 million decrease in net realized investment gains.

### *Benefits and Expenses*

*2008 to 2007 Three Month Comparison.* Benefits and expenses, as shown in the table above under Operating Results, decreased \$157 million, from \$1.854 billion in the first quarter of 2007 to \$1.697 billion in the first quarter of 2008. This decrease reflects a \$181 million decrease in dividends to policyholders reflecting a decrease in the cumulative earnings policyholder dividend obligation expense of \$240 million, partially offset by an increase in dividends paid and accrued to policyholders primarily due to an increase in the 2008 dividend scale.

## **Income Taxes**

Our income tax provision amounted to \$29 million in the first quarter of 2008 compared to \$423 million in the first quarter of 2007. The decline in income tax expense is primarily caused by a decline in income from continuing operations before income taxes and equity in earnings of operating joint ventures from the first quarter of 2007 to the first quarter of 2008. Income tax expense for the first quarter of 2008 includes \$18 million in period costs primarily from interest related to tax uncertainties, which is reported as income tax expense.

We employ various tax strategies, including strategies to minimize the amount of taxes resulting from realized capital gains.

In December 2006, the Service completed all fieldwork with regards to its examination of the consolidated federal income tax returns for tax years 2002-2003. The final report was submitted to the Joint Committee on Taxation for their review in April 2007 and in March 2008. The Joint Committee returned the report to the Service for additional review of an industry issue regarding the methodology for calculating the dividends received deduction related to variable life insurance and annuity contracts. The Company has responded to the Service's request for additional information. The report has been resubmitted to the Joint Committee. The statute of limitations for the 2002-2003 tax years expires in 2009.

The dividends received deduction reduces the amount of dividend income subject to tax and in recent years is the primary component of the difference between our effective tax rate and the federal statutory tax rate of 35%. In August 2007, the Internal Revenue Service, or Service, released Revenue Ruling 2007-54, which included, among other items, guidance on the methodology to be followed in calculating the dividends received deduction related to variable life insurance and annuity contracts. In September 2007, the Service released Revenue Ruling 2007-61. Revenue Ruling 2007-61 suspends Revenue Ruling 2007-54 and informs taxpayers that the U.S. Treasury Department and the Service intend to address through new regulations the issues considered in Revenue Ruling 2007-54, including the methodology to be followed in determining the

dividends received deduction related to variable life insurance and annuity contracts. These activities had no impact on our 2008 results.

**Table of Contents****Discontinued Operations**

Included within net income are the results of businesses which are reflected as discontinued operations under U.S. GAAP. A summary of the results of discontinued operations by business is as follows for the periods indicated:

|   | <b>Three Months Ended<br/>March 31,</b> |             |
|---|---|-------------|
|   | <b>2008</b>                             | <b>2007</b> |
|   | <b>(in millions)</b>                    |             |
| Equity sales, trading and research operations                                     | \$ (1)                                  | \$ 2        |
| Real estate investments sold or held for sale                                     | 1                                       | 18          |
| International securities operations Real estate investments sold or held for sale | 1                                       | (3)         |
| Healthcare operations   |   | 5           |
| Income from discontinued operations before income taxes                           | 1                                       | 22          |
| Income tax expense (benefit)  |   | (17)        |
| Income from discontinued operations, net of taxes                                 | \$ 1                                    | \$ 39       |

The three months ended March 31, 2007 includes a \$26 million tax benefit associated with a discontinued international business. Real estate investments sold or held for sale reflects the income from discontinued real estate investments.

For additional information regarding discontinued operations, see Note 3 of the Unaudited Interim Consolidated Financial Statements.

**Divested Businesses**

Our income from continuing operations includes results from several businesses that have been or will be sold or exited that do not qualify for discontinued operations accounting treatment under U.S. GAAP. The results of these divested businesses are reflected in our Corporate and Other operations, but excluded from adjusted operating income. A summary of the results of the divested businesses that have been excluded from adjusted operating income is as follows for the periods indicated:

|   | <b>Three Months Ended<br/>March 31,</b> |             |
|---|---|-------------|
|   | <b>2008</b>                             | <b>2007</b> |
|   | <b>(in millions)</b>                    |             |
| Commercial mortgage securitization operations                     | \$ (107)                                | \$ 9        |
| Exchange shares previously held by Prudential Equity Group        | (5)                                     |             |
| Prudential Securities capital markets                             | 1                                       | 8           |
| Prudential Home Mortgage Company                                  |   | 7           |
| Property and casualty insurance                                   | (1)                                     | 4           |
| Total divested businesses excluded from adjusted operating income | \$ (112)                                | \$ 28       |

In reporting adjusted operating income for the three months ended March 31, 2008, we have classified our commercial mortgage securitization operations as a divested business, reflecting our decision to exit this business. As a result of this decision, these operations, which involved the origination and purchase of commercial mortgage loans for sale into commercial mortgage-backed securitization transactions, together with related hedging activities, previously reported within the Asset Management segment, have been classified within divested businesses and are reflected in our Corporate and Other operations. Accordingly, these results are

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excluded from adjusted operating income, with prior period results being adjusted to reflect such reclassification. We will retain and continue the remainder of our commercial mortgage origination, servicing and other commercial mortgage related activities, which remain a part of our Asset Management segment. We do not anticipate incurring material costs (including employee severance, retention and other employee related costs) in connection with this decision. As of March 31, 2008, our commercial mortgage securitization operations held \$431 million of bonds (at par value) it retained from 2007 securitizations and loans with a carrying value of \$413 million. Net of the derivatives purchased as hedges, about \$160 million of these positions continue to be subject to changes in credit spreads. This represents a decrease from about \$750 million as of December 31, 2007. The loss of \$107 million in the first quarter of 2008 reflects net realized and unrealized losses on the loans, bonds and hedges from unprecedented instability in the commercial mortgage-backed securities market during the quarter.

**Trading Account Assets Supporting Insurance Liabilities**

Trading account assets supporting insurance liabilities, at fair value include assets that support certain products included in the Retirement and International Insurance segments, which are experience-rated, meaning that the investment results associated with these products will ultimately accrue to contractholders. Realized and unrealized gains and losses for these investments are reported in Asset management fees and other income. Investment income for these investments is reported in Net investment income.

Results for the three months ended March 31, 2008 and 2007 include the recognition of \$262 million of investment losses and \$82 million of investment gains, respectively, on Trading account assets supporting insurance liabilities, at fair value. These gains and losses primarily represent interest-rate related mark-to-market adjustments on fixed maturity securities. Consistent with our treatment of Realized investment gains (losses), net, these gains and losses, which will ultimately accrue to the contractholders, are excluded from adjusted operating income. In addition, results for the three months ended March 31, 2008 and 2007 include decreases of \$200 million and increases of \$62 million, respectively, in contractholder liabilities due to asset value changes in the pool of investments that support these experience-rated contracts. These liability changes are reflected in Interest credited to policyholders account balances and are also excluded from adjusted operating income. As prescribed by U.S. GAAP, changes in the fair value of commercial loans held in our general account, other than when associated with impairments, are not recognized in income in the current period, while the impact of these changes in commercial loan value are reflected as a change in the liability to contractholders in the current period. Included in the amounts above related to the change in the liability to contractholders are increases related to commercial loans of \$11 million and decreases related to commercial loans of \$3 million for the three months ended March 31, 2008 and 2007, respectively.

**Valuation of Assets and Liabilities****Fair Value of Assets and Liabilities**

As discussed in Notes 2 and 9 to the Unaudited Interim Consolidated Financial Statements, the Company adopted SFAS No. 157 effective January 1, 2008. SFAS No. 157 establishes a framework for measuring fair value that includes a hierarchy used to classify the inputs used in measuring fair value. The hierarchy prioritizes the inputs to valuation techniques used to measure fair value into three levels. The level in the fair value hierarchy within which the fair value measurement falls is determined based on the lowest level input that is significant to the fair value measurement. The levels of the fair value hierarchy are as follows:

Level 1 Fair value is based on unadjusted quoted prices in active markets that are accessible to the Company for identical assets or liabilities. These generally provide the most reliable evidence and are used to measure fair value whenever available. The Company's Level 1 assets and liabilities primarily include equity securities and derivative contracts that are traded in an active exchange market. Valuations are obtained from

readily available pricing sources for market transactions involving identical assets or liabilities.



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Level 2 Fair value is based on significant inputs, other than Level 1 inputs, that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the asset or liability through corroboration with observable market data. Level 2 inputs include quoted market prices in active markets for similar assets and liabilities, quoted market prices in markets that are not active for identical or similar assets or liabilities and other observable inputs. The Company's Level 2 assets and liabilities include: fixed maturities (corporate public and private bonds, most government securities, certain asset- and mortgage-backed securities, etc.) certain equity securities, commercial loans, short-term investments and cash equivalents (primarily commercial paper and money market funds) and certain over-the-counter derivatives. Valuations are generally obtained from third party pricing services for identical or comparable assets or liabilities (and validated through backtesting to trade data or confirmation that the pricing service significant inputs are observable) or determined through use of valuation methodologies using observable market inputs.

Level 3 Fair value is based on significant unobservable inputs for the asset or liability. These inputs reflect the Company's or pricing service assumptions about the assumptions market participants would use in pricing the asset or liability. The Company's Level 3 assets and liabilities primarily include: certain private fixed maturities and equity securities, certain manually priced public equity securities and fixed maturities, including certain asset-backed securities, certain highly structured over-the-counter derivative contracts, and embedded derivatives resulting from certain products with guaranteed benefits. Valuations are determined using valuation methodologies such as option pricing models, discounted cash flow models and other similar techniques.

The table below presents the balances of assets and liabilities measured at fair value on a recurring basis as of March 31, 2008.

|   | Level 1   | Level 2    | Level 3(3)<br>(in millions) | Netting(2) | Total      |
|---|-----------|------------|-----------------------------|------------|------------|
| Fixed maturities, available for sale                    | \$ 5      | \$ 161,368 | \$ 3,099                    | \$         | \$ 164,472 |
| Trading Account Assets Supporting Insurance Liabilities | 601       | 13,850     | 193                         |            | 14,644     |
| Other trading account assets                            | 428       | 5,211      | 626                         | (3,432)    | 2,833      |
| Equity securities, available for sale                   | 5,372     | 2,570      | 187                         |            | 8,129      |
| Commercial loans  |           | 657        |                             |            | 657        |
| Other long-term investments                             | 308       | 336        | 877                         |            | 1,521      |
| Short term investments                                  |           | 4,100      |                             |            | 4,100      |
| Cash and cash equivalents                               | 115       | 7,393      |                             |            | 7,508      |
| Other assets  | 88        | 2,696      |                             |            | 2,784      |
| Sub-total excluding separate account assets             | 6,917     | 198,181    | 4,982                       | (3,432)    | 206,648    |
| Separate account assets(1)                              | 82,027    | 77,767     | 22,108                      |            | 181,902    |
| Total assets  | \$ 88,944 | \$ 275,948 | \$ 27,090                   | \$ (3,432) | \$ 388,550 |
| Future policy benefits                                  |           |            | 452                         |            | 452        |
| Long-term debt  |           |            | 184                         |            | 184        |
| Other liabilities                                       | 13        | 4,209      | 118                         | (3,109)    | 1,231      |
| Total liabilities                                       | \$ 13     | \$ 4,209   | \$ 754                      | \$ (3,109) | \$ 1,867   |

- (1) Separate account assets represent segregated funds that are invested for certain customers. Investment risks associated with market value changes are borne by the customers, except to the extent of minimum guarantees made by the Company with respect to certain accounts. Separate account assets classified as Level 3 consist primarily of real estate and real estate investment funds. Separate account liabilities are not included in the above table as they are reported at contract value and not fair value in the Company's consolidated Statement of Financial Position.



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- (2) Netting amounts represent cash collateral and the impact of offsetting asset and liability positions held with the same counterparty as permitted per FASB Interpretation No. 39, *Offsetting of Amounts Related to Certain Contracts and FSP FIN 39-1, Amendment of FASB Interpretation No. 39*.
- (3) The amount of Level 3 assets taken as a percentage of total assets measured at fair value on a recurring basis totaled 7%. Excluding separate account assets for which the risk is borne by the policyholder, the amount of Level 3 assets taken as a percentage of total assets measured at fair value on a recurring basis totaled 2%. The amount of Level 3 liabilities was immaterial to the Company's balance sheet.

For additional information regarding the balances of assets and liabilities measured at fair value by hierarchy level see Note 9 to the Unaudited Interim Consolidated Financial Statements.

The determination of fair value, which for certain assets and liabilities is dependent on the application of estimates and assumptions, can have a significant impact on our results of operations. The following sections describe the key estimates and assumptions surrounding certain assets and liabilities, measured at fair value on a recurring basis, that could have a significant impact on our results of operations or involve the use of significant unobservable inputs. Information regarding Trading Account Assets Supporting Insurance Liabilities as well as Separate Account Assets is excluded as the risk of assets for these categories is ultimately borne by our customers and policyholders.

**Valuation of Fixed Maturity Securities**

Our public fixed maturity securities include investments in corporate securities, government securities and various structured securities, including asset-backed and mortgage-backed securities. The fair values of our public fixed maturity securities are generally based on quoted market prices or prices obtained from independent pricing services. In order to validate reasonability, prices are obtained from multiple independent services and are also reviewed by our internal asset managers through comparison with directly observed recent market trades or comparison of all significant inputs used by the pricing service to our observations of those inputs in the market. Consistent with the fair value hierarchy described above, securities with quoted market prices or validated quotes from pricing services are generally reflected within Level 2. In circumstances where prices from pricing services cannot be validated to observable market data as noted above, these security values are recorded in Level 3 in our fair value hierarchy. In circumstances where market data such as quoted market prices or vendor pricing is not available, internal estimates are used to determine fair value. These estimates may use significant unobservable inputs, which reflect our own assumptions about the inputs market participants would use in pricing the asset, and are therefore included in Level 3 in our fair value hierarchy. Circumstances where observable market data is not available may include events such as market illiquidity and other credit events related to the security.

Our private fixed maturities are primarily comprised of investments in private placement securities originated by our internal private asset managers. The fair values of these private fixed maturities are primarily determined using a discounted cash flow model, which relies upon the average of spread surveys collected from private market intermediaries who are active in both primary and secondary transactions, and takes into account, among other factors, the credit quality of the issuer and the reduced liquidity associated with private placements. Generally, these securities have been reflected within Level 2 in our fair value hierarchy. For certain of these securities, including those that are distressed, the discounted cash flow model may also incorporate significant unobservable inputs, which reflect our own assumptions about the inputs market participants would use in pricing the asset. Accordingly, these securities have been reflected within Level 3 in our fair value hierarchy.

Private fixed maturities also include debt investments in funds that, in addition to a stated coupon, pay a return based upon the results of the underlying portfolios. The fair values of these securities are determined by reference to the funds' net asset value (NAV). Any restrictions on the Company's ability to redeem its interests in these funds at NAV are considered to have a de minimis effect on the fair value. Since the NAV that the funds trade at can be observed by redemption and subscription transactions between third parties, the fair values of these investments have been reflected within Level 2 in our fair value hierarchy.



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Our Level 3 securities generally include certain public fixed maturities and distressed private fixed maturities priced internally based on observable and unobservable inputs. Significant unobservable inputs used include: issue specific credit adjustments, material non-public financial statements, management judgment, estimation of future earnings and cashflows, default rate assumptions and non-binding quotes from market makers. These inputs are usually considered unobservable, as not all market participants will have access to this data. Net realized and unrealized losses for Level 3 Available for Sale fixed maturities totaled \$144 million and \$122 million, respectively, for the first quarter of 2008.

Within fixed maturities, the Company holds asset-backed securities collateralized by sub-prime mortgages, as discussed in greater detail in

Realized Investment Gains and Losses and General Account Investments General Account Investments Fixed Maturity Securities . While the fair value of these investments, as well as others within our portfolio of fixed maturities, has declined in recent quarters due to increased credit spreads in the financial markets, we believe the investment fundamentals remain sound, and the ultimate value that will be realized from these investments is greater than that reflected by their current fair value.

### ***Valuation of Equity Securities***

Equity securities consist principally of investments in common and preferred stock of publicly traded companies as well as common stock mutual fund shares. The fair values of most equity securities are based on quoted market prices in active markets for identical assets and are classified within Level 1 in our fair value hierarchy. The fair values of common stock mutual fund shares that transact regularly (but do not trade in active markets because they are not publicly available) are based on transaction prices of identical fund shares and are classified within Level 2 in our fair value hierarchy. The fair values of preferred equity securities are based on prices obtained from independent pricing services and, in order to validate reasonability, are compared with recent market trades we have directly observed. Accordingly, these securities are classified within Level 2 in our fair value hierarchy.

### ***Impact of Fixed Maturities and Equity Securities on Results of Operations***

The impact our determination of fair value for fixed maturity and equity securities has on our results of operations is dependent on our classification of the security as either trading, available for sale, or held to maturity. For our investments classified as trading, the impact of changes in fair value is recorded within Asset management fees and other income. For our investments classified as available for sale, the impact of changes in fair value is recorded as an unrealized gain or loss in Accumulated other comprehensive income (loss), net, a separate component of equity. In addition, investments classified as available for sale, as well as those classified as held to maturity, are subject to impairment reviews to identify when a decline in fair value is other-than-temporary. When it is determined that a decline in value is other-than-temporary, the carrying value of the security is impaired to its fair value, with a corresponding charge to Realized investment gains (losses), net in the statements of operations and are included in income from continuing operations under U.S. GAAP but excluded from adjusted operating income. The level of impairment losses can be expected to increase when economic conditions worsen and decrease when economic conditions improve. See Realized Investment Gains and Losses and General Account Investments Realized Investment Gains and Losses for a discussion of the effects of impairments on our operating results for the three months ended March 31, 2008 and 2007.

For a further discussion of our policies regarding other-than-temporary declines in investment value and the related methodology for recording fixed maturity other-than-temporary impairments, see General Account Investments Fixed Maturity Securities Other-than-Temporary Impairments of Fixed Maturity Securities below. For a further discussion of our policies regarding other-than-temporary declines in investment value and the related methodology for recording equity impairments, see General Account Investments Equity Securities Other-than-Temporary Impairments of Equity Securities below.

*Valuation of Commercial Loans*

Upon the adoption of SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities, the Company elected the fair value option for certain loans held within the commercial mortgage

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operations of the asset management segment. Specifically, the fair value option was elected for funded commercial loans held for sale originated beginning January 1, 2008. In addition, the Company elected the fair value option for fixed rate commercial loans held for investment that were held at December 31, 2007 and for such loans originated beginning January 1, 2008. The Company elected the fair value option for the loan programs mentioned above primarily to eliminate the need for hedge accounting under SFAS No. 133, while still achieving an offset in earnings from the associated interest rate derivative hedges.

Due to recent volatility in the credit markets, the Company experienced unexpected volatility in the fair value of the aforementioned fixed rate commercial loans held for investment that was not substantially offset by the associated interest rate derivative hedges during the quarter ended March 31, 2008. Therefore, the Company will no longer elect the fair value option on loans held for investment that are originated after March 31, 2008, and will be pursuing hedge accounting under SFAS No. 133.

The fair value of these loans is determined based on the present value of the expected future cash flows discounted at the appropriate U.S. Treasury rate, adjusted for the current market spread for similar quality loans. Since the interest rate and market spread assumptions for similar quality loans are generally observable based upon market transactions, the fair value of loans held for investment has been reflected within Level 2 in our fair value hierarchy.

### ***Valuation of Other Long-Term Investments***

Other long-term investments carried at fair value include limited partnerships which the Company consolidates because it is either deemed to exercise control or is considered the primary beneficiary of a variable interest entity. These entities are considered investment companies and follow specialized industry accounting whereby their assets are carried at fair value. The investments held by these entities include various feeder fund investments in underlying master funds (whose underlying holdings generally include public fixed maturities and equity securities), as well as wholly-owned real estate held within other investment funds.

The fair value of the feeder fund investments in master funds is determined by reference to the master funds' net asset value (NAV). Any restrictions on the Company's ability to redeem its interests in these funds at NAV are considered to have a de minimis effect on fair value. Since the NAV at which these funds trade can be observed by redemption and subscription transactions with third parties, the fair values of feeder fund investments in master funds have been reflected within Level 2 in our fair value hierarchy.

The fair value of wholly-owned real estate held in consolidated investment funds is determined through an independent appraisal process. The appraisals generally utilize a discounted cash flow model, following an income approach, that incorporates various assumptions including rental revenue, operating expenses and discount rates. These appraisals and the related assumptions are updated at least annually, and incorporate historical property experience and any observable market data, including any market transactions. Since many of the assumptions utilized are unobservable and are considered to be significant inputs to the valuation, the real estate investments within other long-term investments have been reflected within Level 3 in our fair value hierarchy.

### ***Valuation of Derivative Instruments***

Derivatives are recorded either as assets, within Other trading account assets, or Other long-term investments, or as liabilities, within Other liabilities, except for embedded derivatives which are recorded with the associated host contract. The fair values of derivative contracts are

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determined based on quoted prices in active exchanges or through the use of valuation models. The fair values of derivative contracts can be affected by changes in interest rates, foreign exchange rates, commodity prices, credit spreads, market volatility, expected returns and liquidity as well as other factors. Fair values can also be affected by changes in estimates and assumptions including those related to counterparty behavior used in valuation models.



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The Company's exchange traded futures and options include treasury futures, Eurodollar futures, commodity futures, Eurodollar options and commodity options. Exchange traded futures and options are valued using quoted prices in active markets and are classified within Level 1 in our fair value hierarchy.

The majority of the Company's derivative positions is traded in the over-the-counter (OTC) derivative market and is classified within Level 2 in our fair value hierarchy. OTC derivatives classified within Level 2 are valued using models generally accepted in the financial services industry that use actively quoted or observable market input values from external market data providers, broker-dealer quotations, third-party pricing vendors and/or recent trading activity. The fair values of most OTC derivatives, including forward rate agreements, interest rate and cross currency swaps, commodity swaps, commodity forward contracts, single name credit default swaps and to be announced forward contracts on highly rated mortgage-backed securities issued by U.S. government sponsored entities are determined using discounted cash flow models. The fair values of European style option contracts are determined using Black-Scholes option pricing models. These models' key assumptions include the contractual terms of the respective contract, along with significant observable inputs, including interest rates, currency rates, credit spreads, yield curves, equity prices, index dividend yields, and volatility.

Most OTC derivative contracts have bid and ask prices that can be readily observed in the market place. The Company's policy is to use mid-market pricing consistent with the Company's best estimate of fair value. The bid-ask spreads for derivatives classified within Level 3 of the fair value hierarchy are generally wider than derivatives classified within Level 2 thus requiring more judgment in estimating the mid-market price of such derivatives.

Derivatives that are valued based upon models with unobservable market input values or input values from less actively traded or less-developed markets are classified within Level 3 in our fair value hierarchy. Derivatives classified as Level 3 include first-to-default credit basket swaps, look-back equity options and other structured options. For additional information regarding embedded derivatives in our annuity and retirement products classified as Level 3, see "Valuation of Variable Annuity Optional Living Benefit Features" below. The fair values of first-to-default credit basket swaps are derived from relevant observable inputs such as: individual credit default spreads, interest rates, recovery rates and unobservable model-specific input values such as correlation between different credits within the same basket. Look-back equity options and other structured options and derivatives are valued using simulation models such as the Monte Carlo technique. The input values for look-back equity options are derived from observable market indices such as interest rates, dividend yields, equity indices as well as unobservable model-specific input values such as certain volatility parameters. Level 3 methodologies are validated through periodic comparison of our fair values to broker-dealer's values.

All realized and unrealized changes in fair value of non-dealer related derivatives, with the exception of the effective portion of cash flow hedges and effective hedges of net investments in foreign operations, are recorded in current earnings. Generally, the changes in fair value of non-dealer related derivatives, excluding those that qualify for hedge accounting, are recorded in "Realized investment gains (losses), net." For additional information regarding the impact of changes in fair value of derivative instruments on our results of operations see "Realized Investment Gains and Losses and General Account Investments" "Realized Investment Gains and Losses" below.

The Company holds externally managed investments in the European market, as discussed in greater detail under "Realized Investment Gains and Losses and General Account Investments" "General Account Investments" "Fixed Maturity Securities" "Fixed Maturity Securities and Unrealized Gains and Losses by Industry Category." These investments are classified as Level 2 for fair value reporting. While the fair value of the embedded derivatives associated with these investments has declined in recent quarters due to increased credit spreads in the financial markets, we believe the investment fundamentals remain sound, and the ultimate value that will be realized from these investments is greater than that reflected by the current fair value of the embedded derivatives.

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### ***Valuation of Variable Annuity Optional Living Benefit Features***

The Company's liability for future policy benefits includes general account liabilities for guarantees on variable annuity contracts, including guaranteed minimum accumulation benefits ( GMAB ), guaranteed minimum withdrawal benefits ( GMWB ) and guaranteed minimum income and withdrawal benefits ( GMIWB ). These benefits are accounted for as embedded derivatives and are carried at fair value with changes in fair value included in Realized investment gains (losses), net.

The fair values of the GMAB, GMWB and GMIWB liabilities are calculated as the present value of future expected payments to customers less the present value of assessed rider fees attributable to the embedded derivative feature. Since there is no observable active market for the transfer of these obligations, the valuations are calculated using internally developed models. Significant inputs to these models include capital market assumptions, such as interest rates and equity market assumptions, as well as various policyholder behavior assumptions that are actuarially determined, including lapse rates, benefit utilization rates, mortality rates and withdrawal rates. These assumptions are reviewed at least annually, and updated based upon historical experience and give consideration to any observable market data, including market transactions such as acquisitions and reinsurance transactions. Since many of the assumptions utilized are unobservable and are considered to be significant inputs to the liability valuation, the liability included in future policy benefits has been reflected within Level 3 in our fair value hierarchy. The change in fair value of the GMAB, GMWB and GMIWB resulted in an increase in the total liability of \$284 million for the current quarter. This change was significantly offset by changes in value of related hedging instruments as described in more detail under Results of Operations for Financial Services Businesses by Segment Insurance Division Individual Annuities.

### ***Valuation of Other Assets and Other Liabilities***

Other assets carried at fair value include U.S. Treasury bills held within our global commodities group whose fair values are determined consistent with similar securities described above under Fixed Maturities . Included in other liabilities are various derivatives contracts executed within our global commodities group, including exchange-traded futures, foreign currency and commodity contracts. The fair values of these derivative instruments are determined consistent with similar derivative instruments described above under Derivatives.

### ***Valuation of Other Trading Account Assets***

Other trading account assets consist primarily of public corporate bonds, treasuries, equity securities and derivatives whose fair values are determined consistent with similar instruments described above in Valuation of Fixed Maturities , Valuation of Equity Securities and Valuation of Derivative Instruments.

### ***Valuation of Cash Equivalents and Short-term Investments***

Cash equivalents and short-term investments carried at fair value include money market instruments, commercial paper and other highly liquid debt instruments. These instruments are typically not traded in active markets; however, their fair values are based on market observable inputs and, accordingly, these investments have been classified within Level 2 in our fair value hierarchy.

**Realized Investment Gains and Losses and General Account Investments**

**Realized Investment Gains and Losses**

Realized investment gains and losses are generated from numerous sources, including the sale of fixed maturity securities, equity securities, investments in joint ventures and limited partnerships and other types of investments, as well as adjustments to the cost basis of investments for other-than-temporary impairments.

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Realized investment gains and losses are also generated from prepayment premiums received on private fixed maturity securities, recoveries of principal on previously impaired securities, provisions for losses on commercial loans, fair value changes on commercial mortgage operations loans, fair value changes on embedded derivatives and derivatives that do not qualify for hedge accounting treatment, except those derivatives used in our capacity as a broker or dealer.

We perform impairment reviews on an ongoing basis to determine when a decline in value is other-than-temporary. In evaluating whether a decline in value is other-than-temporary, we consistently consider several factors including, but not limited to, the following: the extent and duration of the decline in value; the reasons for the decline (credit event, currency, or interest-rate related, including spread widening); our ability and intent to hold our investment for a period of time to allow for a recovery of value; and the financial condition of and near-term prospects of the issuer. When we determine that there is an other-than-temporary impairment, we write down the value of the security to its fair value, with a corresponding charge recorded in Realized investment gains (losses), net. The causes of the other-than-temporary impairments discussed below were specific to each individual issuer and did not directly result in impairments to other securities within the same industry or geographic region.

In addition, for our impairment review of asset-backed securities with a credit rating below AA, we forecast the prospective future cash flows of the security and determine if the present value of those cash flows, discounted using the effective yield of the most recent interest accrual rate, has decreased from the previous reporting period. When a decrease from the prior reporting period has occurred and the security's market value is less than its carrying value, an other-than-temporary impairment is recognized by writing the security down to fair value.

For a further discussion of our policies regarding other-than-temporary declines in investment value and the related methodology for recording fixed maturity other-than-temporary impairments, see General Account Investments Fixed Maturity Securities Other-than-Temporary Impairments of Fixed Maturity Securities below. For a further discussion of our policies regarding other-than-temporary declines in investment value and the related methodology for recording equity impairments, see General Account Investments Equity Securities Other-than-Temporary Impairments of Equity Securities below.

The level of other-than-temporary impairments generally reflects economic conditions and is expected to increase when economic conditions worsen and to decrease when economic conditions improve. We may realize additional credit and interest rate related losses through sales of investments pursuant to our credit risk and portfolio management objectives. Other-than-temporary impairments, interest rate related losses and credit losses (other than those related to certain of our businesses which primarily originate investments for sale or syndication to unrelated investors) are excluded from adjusted operating income. In periods subsequent to the recognition of an other-than-temporary impairment, the impaired security is accounted for as if it had been purchased on the measurement date of the impairment. Accordingly, the discount (or reduced premium) based on the new cost basis is accreted into net investment income, and included in adjusted operating income in future periods based upon the amount and timing of expected future cash flows of the security, if the recoverable value of the investment based upon those cash flows is greater than the carrying value of the investment after the impairment.

We require most issuers of private fixed maturity securities to pay us make-whole yield maintenance payments when they prepay the securities. Prepayments are driven by factors specific to the activities of our borrowers as well as the interest rate environment.

We use interest and currency swaps and other derivatives to manage interest and currency exchange rate exposures arising from mismatches between assets and liabilities, including duration mismatches. We use derivative contracts to mitigate the risk that unfavorable changes in currency exchange rates will reduce U.S. dollar equivalent earnings generated by certain of our non-U.S. businesses. We also use equity-based derivatives to hedge the equity risks embedded in some of our annuity products. Derivative contracts also include forward



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purchases and sales of to-be-announced mortgage-backed securities primarily related to our mortgage dollar roll program. Many of these derivative contracts do not qualify for hedge accounting, and, consequently, we recognize the changes in fair value of such contracts from period to period in current earnings, although we do not necessarily account for the related assets or liabilities the same way. Accordingly, realized investment gains and losses from our derivative activities can contribute significantly to fluctuations in net income.

Adjusted operating income excludes Realized investment gains (losses), net, (other than those representing profit or loss of certain of our businesses which primarily originate investments for sale or syndication to unrelated investors, and those associated with terminating hedges of foreign currency earnings, current period yield adjustments, or product derivatives and the effect of any related economic hedging program) and related charges and adjustments.

The following tables set forth Realized investment gains (losses), net, by investment type for the Financial Services Businesses and Closed Block Business, as well as related charges and adjustments associated with the Financial Services Businesses, for the three months ended March 31, 2008 and 2007, respectively, and gross realized investment gains and losses on fixed maturity securities by segment for the three months ended March 31, 2008 and 2007, respectively. For a discussion of our general account investment portfolio and related results, including overall income yield and investment income, as well as our policies regarding other-than-temporary declines in investment value and the related methodology for recording impairment charges, see General Account Investments below. For additional details regarding adjusted operating income, which is our measure of performance for the segments of our Financial Services Businesses, see Note 8 to the Unaudited Interim Consolidated Financial Statements.

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|   | <b>Three Months Ended<br/>March 31,</b> |             |
|---|---|-------------|
|   | <b>2008</b>                             | <b>2007</b> |
|   | <b>(in millions)</b>                    |             |
| <b>Realized investment gains (losses), net:</b>   |   |             |
| Financial Services Businesses   | \$ (802)                                | \$ 213      |
| Closed Block Business   | (110)                                   | 207         |
| Consolidated realized investment gains (losses), net  | \$ (912)                                | \$ 420      |
| <b>Financial Services Businesses:</b>   |   |             |
| Realized investment gains (losses), net   |   |             |
| Fixed maturity securities(1)  | \$ (398)                                | \$ 27       |
| Equity securities   | (56)                                    | 132         |
| Derivative instruments(2)   | (331)                                   | (1)         |
| Other   | (17)                                    | 55          |
| Total   | (802)                                   | 213         |
| Related adjustments(3)  | 137                                     | (66)        |
| Realized investment gains (losses), net, and related adjustments  | \$ (665)                                | \$ 147      |
| Related charges (4)   | \$ (13)                                 | \$ (6)      |
| <b>Closed Block Business:</b>   |   |             |
| Realized investment gains (losses), net   |   |             |
| Fixed maturity securities(1)  | \$ (28)                                 | \$ 96       |
| Equity securities   | (93)                                    | 114         |
| Derivative instruments  | 14                                      | 3           |
| Other   | (3)                                     | (6)         |
| Total   | \$ (110)                                | \$ 207      |
| <b>Realized investment gains (losses) by segment    Fixed Maturity Securities    Financial Services Businesses:</b> |   |             |
| <b>Gross realized investment gains:</b>   |   |             |
| Individual Life   | \$ 4                                    | \$ 2        |
| Individual Annuities  | 12                                      | 6           |
| Group Insurance   | 6                                       | 15          |
| Asset Management  |   |             |
| Financial Advisory  |   |             |
| Retirement  | 23                                      | 12          |
| International Insurance   | 35                                      | 26          |
| International Investments   |   |             |
| Corporate and Other Operations  |   | 2           |
| Total   | 80                                      | 63          |
| <b>Gross realized investment losses:</b>  |   |             |
| Individual Life   | (34)                                    | (4)         |
| Individual Annuities  | (34)                                    | (11)        |
| Group Insurance   | (82)                                    | (1)         |
| Asset Management  | (13)                                    |             |
| Financial Advisory  |   |             |
| Retirement  | (161)                                   | (18)        |
| International Insurance   | (97)                                    | (1)         |
| International Investments   |   |             |

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|   |          |        |
|---|----------|--------|
| Corporate and Other Operations  | (57)     | (1)    |
| Total   | (478)    | (36)   |
| Realized investment gains (losses), net Financial Services Businesses | \$ (398) | \$ 27  |
| <b>Closed Block Business:</b>   |          |        |
| Gross realized investment gains                                       | \$ 217   | \$ 151 |
| Gross realized investment losses                                      | (245)    | (55)   |
| Realized investment gains (losses), net Closed Block Business         | \$ (28)  | \$ 96  |



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- (1) The Financial Services Businesses include \$290 million of other-than-temporary impairments in the first quarter of 2008, related to asset-backed securities collateralized by sub-prime mortgages. The Closed Block Business includes \$113 million of other-than-temporary impairments in the first quarter of 2008, related to asset-backed securities collateralized by sub-prime mortgages.
- (2) Includes \$208 million of losses on embedded derivatives associated with certain externally managed investments in the European market in the first quarter of 2008.
- (3) Related adjustments include that portion of Realized investment gains (losses), net, that are included in adjusted operating income, including those pertaining to certain derivative contracts, as well as those that represent profit or loss of certain of our businesses which primarily originate investments for sale or syndication to unrelated investors. Related adjustments also include that portion of Asset management fees and other income that are excluded from adjusted operating income, including the change in value due to the impact of changes in foreign currency exchange rates during the period on certain assets and liabilities for which we economically hedge the foreign currency exposure. See Note 8 to the Unaudited Interim Consolidated Financial Statements for additional information on these related adjustments.
- (4) Reflects charges that are related to realized investment gains (losses), net, and excluded from adjusted operating income, as described more fully in Note 8 to the Unaudited Interim Consolidated Financial Statements.

**2008 to 2007 Three Month Comparison***Financial Services Businesses*

The Financial Services Businesses net realized investment losses in the first quarter of 2008 were \$802 million, compared to net realized investment gains of \$213 million in the first quarter of 2007. Net realized losses on fixed maturity securities were \$398 million in the first quarter of 2008, compared to net gains of \$27 million in the first quarter of 2007, as set forth in the following table:

|  | Three Months Ended<br>March 31, |              |
|--|---------------------------------|--------------|
|  | 2008                            | 2007         |
| (in millions)  |                                 |              |
| <b>Realized investment gains (losses) Fixed Maturity Securities</b>      |                                 |              |
| <b>Financial Services Businesses</b>                                     |                                 |              |
| Gross realized investment gains:   |                                 |              |
| Gross gains on sales and maturities                                      | \$ 78                           | \$ 62        |
| Private bond prepayment premiums   | 2                               | 1            |
| <b>Total</b>   | <b>80</b>                       | <b>63</b>    |
| Gross realized investment losses:  |                                 |              |
| Gross losses on sales and maturities(1)                                  | (67)                            | (23)         |
| Other-than-temporary impairments   | (388)                           | (11)         |
| Credit related losses  | (23)                            | (2)          |
| <b>Total</b>   | <b>(478)</b>                    | <b>(36)</b>  |
| <b>Realized investment gains (losses), net Fixed Maturity Securities</b> | <b>\$ (398)</b>                 | <b>\$ 27</b> |

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- (1) Amounts exclude credit related losses through sales of investments pursuant to our credit risk and portfolio management objectives.

Gross losses on sales and maturities of fixed maturity securities of \$67 million in the first quarter of 2008, mainly in the International Insurance, Retirement, and Individual Life segments, were primarily related to credit spread increases in the credit markets, which initially resulted from broad market concerns over sub-prime mortgage exposures in the latter half of 2007, and liquidity concerns. There were no gross losses on sales and

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maturities of asset-backed securities collateralized by sub-prime mortgages in the first quarter of 2008. See [General Account Investments Fixed Maturity Securities](#) for additional information regarding our exposure to sub-prime mortgages. Gross losses on sales and maturities of fixed maturity securities of \$23 million in the first quarter of 2007 were primarily interest-rate related. See below for additional information regarding the \$388 million of other-than-temporary impairments of fixed maturity securities in the first quarter of 2008.

Net realized losses on equity securities were \$56 million in the first quarter of 2008, of which net losses on sales of equity securities were \$8 million, and other-than-temporary impairments were \$48 million. Net realized gains on equity securities were \$132 million in the first quarter of 2007, of which net gains on sales of equity securities were \$147 million, partially offset by other-than-temporary impairments of \$15 million. Net realized gains on equity securities in 2007 were primarily due to sales of Japanese equities in our Gibraltar Life and Japanese Life Planner operations from portfolio restructuring and equity sales in our Korean Life Planner operations. See below for additional information regarding the \$48 million of other-than-temporary impairments of equity securities in the first quarter of 2008.

Net realized losses on derivatives were \$331 million in the first quarter of 2008, compared to net derivative losses of \$1 million in the first quarter of 2007. The net derivative losses in 2008 primarily reflect net mark-to-market losses of \$208 million on embedded derivatives associated with certain externally managed investments in the European market, due to spread widening, and negative mark-to-market adjustments of \$139 million on foreign currency forward contracts used to hedge the future income of non-U.S. businesses, due to the weakening of the U.S. dollar. Also contributing to the net derivative losses in 2008 were net losses of \$40 million on embedded derivatives within certain variable domestic annuity contracts, net of the effect of a related derivative hedging portfolio. Partially offsetting these losses were net gains of \$100 million on interest rate derivatives used to manage the duration of the fixed maturity investment portfolio, as interest rates declined. The derivative losses in the first quarter of 2007 were primarily the result of net losses of \$35 million on interest rate derivatives used to manage the duration of the fixed maturity investment portfolio. Offsetting these losses were gains of \$14 million on embedded derivatives within certain variable annuity contracts, net of the effect of a related derivative hedging portfolio, as well as positive mark-to-market adjustments of \$14 million on foreign currency forward contracts used to hedge the future income of non-U.S. businesses. For information regarding our externally managed investments in the European market, see [General Account Investments Fixed Maturity Securities Fixed Maturity Securities and Unrealized Gains and Losses by Industry Category](#). For information regarding our methodology for determining the fair value of our derivative instruments, see [Valuation of Assets and Liabilities Fair Value of Assets and Liabilities Valuation of Derivative Instruments](#).

Net realized investment losses on other investments were \$17 million in the first quarter of 2008, primarily related to mark-to-market losses on mortgage loans due primarily to credit spread increases in the credit markets. Net realized investment gains on other investments were \$55 million in the first quarter of 2007, primarily related to gains from real estate related investments and loan securitizations.

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As set forth in the following table, during the first quarter of 2008 we recorded total other-than-temporary impairments of \$437 million attributable to the Financial Services Businesses, compared to total other-than-temporary impairments of \$27 million attributable to the Financial Services Businesses in the first quarter of 2007.

|   | Three Months Ended<br>March 31, |              |
|---|---------------------------------|--------------|
|   | 2008                            | 2007         |
| (in millions)   |                                 |              |
| <b>Other-than-temporary impairments Financial Services Businesses</b> |                                 |              |
| Public fixed maturity securities                                      | \$ 377                          | \$ 10        |
| Private fixed maturity securities                                     | 11                              | 1            |
| Total fixed maturity securities                                       | 388                             | 11           |
| Equity securities   | 48                              | 15           |
| Other invested assets(1)  | 1                               | 1            |
| <b>Total</b>  | <b>\$ 437</b>                   | <b>\$ 27</b> |

(1) Includes other-than-temporary impairments relating to real estate investments and investments in joint ventures and partnerships.

Other-than-temporary impairments recorded on fixed maturities in the first quarter of 2008 included \$290 million related to asset-backed securities collateralized by sub-prime mortgages. Fixed maturity other-than-temporary impairments in the first quarter of 2008 were concentrated in asset-backed securities and the services, finance, and manufacturing sectors of our corporate securities, and were primarily driven by credit spread increases as discussed above, liquidity concerns, downgrades in credit, bankruptcy or other adverse financial conditions of the respective issuers. Approximately \$64 million of fixed maturity other-than-temporary impairments in the first quarter of 2008, including \$46 million related to asset-backed securities collateralized by sub-prime mortgages, represent circumstances where we believe credit events or other adverse conditions of the respective issuers have caused, or will lead to, a deficiency in the contractual cash flows related to the investment. For the remaining \$324 million of fixed maturity other-than-temporary impairments in the first quarter of 2008, the decrease in fair value was caused primarily by credit spread widening or liquidity concerns, and we believe the recoverable value of the investment, based on the expected future cash flows, is greater than the current fair value. Fixed maturity other-than-temporary impairments in the first quarter of 2007 were concentrated in the finance and services sectors of our corporate securities and were primarily driven by interest rates, downgrades in credit, bankruptcy or other adverse financial conditions of the respective issuers. Equity security other-than-temporary impairments were primarily driven by overall declines in the Japanese equity markets. For information regarding the fair value methodology used in determining our other-than-temporary impairments, see Valuation of Assets and Liabilities Fair Value of Assets and Liabilities Valuation of Fixed Maturity Securities, and Valuation of Assets and Liabilities Fair Value of Assets and Liabilities Valuation of Equity Securities.

**Table of Contents***Closed Block Business*

For the Closed Block Business, net realized investment losses in the first quarter of 2008 were \$110 million, compared to net realized investment gains of \$207 million in the first quarter of 2007. Net realized losses on fixed maturity securities were \$28 million in the first quarter of 2008, compared to net realized gains of \$96 million in the first quarter of 2007, as set forth in the following table:

|   | <b>Three Months Ended<br/>March 31,</b> |              |
|---|---|--------------|
|   | <b>2008</b>                             | <b>2007</b>  |
| <b>(in millions)</b>  |   |              |
| <b>Realized investment gains (losses) Fixed Maturity Securities Closed Block Business</b> |   |              |
| Gross realized investment gains:  |   |              |
| Gross gains on sales and maturities   | \$ 216                                  | \$ 150       |
| Private bond prepayment premiums  | 1                                       | 1            |
| <b>Total</b>  | <b>217</b>                              | <b>151</b>   |
| Gross realized investment losses:   |   |              |
| Gross losses on sales and maturities(1)   | (68)                                    | (47)         |
| Other-than-temporary impairments  | (151)                                   | (7)          |
| Credit related losses   | (26)                                    | (1)          |
| <b>Total</b>  | <b>(245)</b>                            | <b>(55)</b>  |
| <b>Realized investment gains (losses), net Fixed Maturity Securities</b>                  | <b>\$ (28)</b>                          | <b>\$ 96</b> |

(1) Amounts exclude credit related losses through sales of investments pursuant to our credit risk and portfolio management objectives.

Gross losses on sales and maturities of fixed maturity securities were \$68 million in the first quarter of 2008, none of which related to asset-backed securities collateralized by sub-prime mortgages. See General Account Investments Fixed Maturity Securities for additional information regarding our exposure to sub-prime mortgages. See below for additional information regarding the \$151 million of other-than-temporary impairments of fixed maturity securities in the first quarter of 2008. Gross gains on sales and maturities of fixed maturity securities of \$216 million in the first quarter of 2008 were primarily due to sales related to our total return strategy.

Net realized losses on equity securities were \$93 million in the first quarter of 2008, of which net losses on sales of equity securities were \$41 million, and other-than-temporary impairments were \$52 million. Net realized gains on equity securities were \$114 million in the first quarter of 2007, of which net gains on sales of equity securities were \$115 million, partially offset by other-than-temporary impairments of \$1 million. These gains were a result of sales pursuant to our active management strategy. See below for additional information regarding the \$52 million of other-than-temporary impairments of equity securities in the first quarter of 2008.

Net gains on derivatives were \$14 million in the first quarter of 2008, compared to net gains of \$3 million in the first quarter of 2007. Derivative gains in the first quarter of 2008 primarily reflect the impact of interest rate derivatives used to manage the duration of the fixed maturity investment portfolio partially offset by net losses on currency derivatives used to hedge foreign investments. Derivative gains in the first quarter of 2007 were largely attributable to gains on forward contracts of to-be-announced securities primarily related to our dollar roll program. For information regarding our methodology for determining the fair value of our derivative instruments, see Valuation of Assets and Liabilities Fair

Value of Assets and Liabilities Valuation of Derivative Instruments.

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As set forth in the following table, during the first quarter of 2008 we recorded total other-than-temporary impairments of \$204 million attributable to the Closed Block Business, compared to total other-than-temporary impairments of \$10 million attributable to the Closed Block Business in the first quarter of 2007.

|   | <b>Three Months Ended<br/>March 31,</b> |              |
|---|---|--------------|
|   | <b>2008</b>                             | <b>2007</b>  |
|   | <b>(in millions)</b>                    |              |
| <b>Other-than-temporary impairments Closed Block Business</b> |   |              |
| Public fixed maturity securities                              | \$ 149                                  | \$ 2         |
| Private fixed maturity securities                             | 2                                       | 5            |
| Total fixed maturity securities                               | 151                                     | 7            |
| Equity securities   | 52                                      | 1            |
| Other invested assets(1)                                      | 1                                       | 2            |
| <b>Total</b>  | <b>\$ 204</b>                           | <b>\$ 10</b> |

(1) Includes other-than-temporary impairments relating to real estate investments and investments in joint ventures and partnerships.

Other-than-temporary impairments recorded on fixed maturities in the first quarter of 2008 included \$113 million related to asset-backed securities collateralized by sub-prime mortgages. Other-than-temporary impairments in the first quarter of 2008 were concentrated in asset-backed securities and the services, finance, and manufacturing sectors of our corporate securities and were primarily driven by credit spread increases as discussed above, liquidity concerns, downgrades in credit, bankruptcy or other adverse financial conditions of the respective issuers. Approximately \$25 million of fixed maturity other-than-temporary impairments in the first quarter of 2008, including \$17 million related to asset-backed securities collateralized by sub-prime mortgages, represent circumstances where we believe credit events or other adverse conditions of the respective issuers have caused, or will lead to, a cash flow deficiency related to the investment. For the remaining \$126 million of fixed maturity other-than-temporary impairments in the first quarter of 2008, the decrease in fair value was caused primarily by credit spread widening or liquidity concerns, and we believe the recoverable value of the investment, based on the expected future cash flows, is greater than the current fair value. Other-than-temporary impairments of fixed maturity securities include amounts that are currently expected to be accreted into net investment income in future periods based on the future estimated cash flows of the securities. Other-than-temporary impairments in the first quarter of 2007 were concentrated in the services sector of our corporate securities and were primarily driven by downgrades in credit, bankruptcy or other adverse financial conditions of the respective issuers. Equity security other-than-temporary impairments were primarily driven by overall declines in the equity markets. For information regarding the fair value methodology used in determining our other-than-temporary impairments, see Valuation of Assets and Liabilities Fair Value of Assets and Liabilities Valuation of Fixed Maturity Securities, and Valuation of Assets and Liabilities Fair Value of Assets and Liabilities Valuation of Equity Securities.

**General Account Investments****Portfolio Composition**

Our investment portfolio consists of public and private fixed maturity securities, commercial loans, equity securities and other invested assets. The composition of our general account reflects, within the discipline provided by our risk management approach, our need for competitive results and the selection of diverse investment alternatives available primarily through our Asset Management segment. The size of our portfolio enables us to invest in asset classes that may be unavailable to the typical investor.

Our total general account investments were \$236.9 billion and \$232.5 billion as of March 31, 2008 and December 31, 2007, respectively, which are segregated between the Financial Services Businesses and the



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Closed Block Business. Total general account investments attributable to the Financial Services Businesses were \$170.0 billion and \$163.0 billion as of March 31, 2008 and December 31, 2007, respectively, while total general account investments attributable to the Closed Block Business were \$66.9 billion and \$69.5 billion as of March 31, 2008 and December 31, 2007, respectively. The following table sets forth the composition of the investments of our general account as of the dates indicated. The average duration of our general account investment portfolio attributable to the domestic Financial Services Businesses as of March 31, 2008 is between 4 and 5 years.

|  | Financial<br>Services<br>Businesses | March 31, 2008              |                   | % of<br>Total |
|--|-------------------------------------|-----------------------------|-------------------|---------------|
|  |                                     | Closed<br>Block<br>Business | Total             |               |
| (\$ in millions)   |                                     |                             |                   |               |
| <b>Fixed Maturities:</b>   |                                     |                             |                   |               |
| Public, available for sale, at fair value                              | \$ 96,107                           | \$ 34,315                   | \$ 130,422        | 55.0%         |
| Public, held to maturity, at amortized cost                            | 3,015                               |                             | 3,015             | 1.3           |
| Private, available for sale, at fair value                             | 20,172                              | 12,243                      | 32,415            | 13.7          |
| Private, held to maturity, at amortized cost                           | 720                                 |                             | 720               | 0.3           |
| Trading account assets supporting insurance liabilities, at fair value | 14,644                              |                             | 14,644            | 6.2           |
| Other trading account assets, at fair value                            | 210                                 | 149                         | 359               | 0.2           |
| Equity securities, available for sale, at fair value                   | 4,543                               | 3,578                       | 8,121             | 3.4           |
| Commercial loans, at book value  | 21,180                              | 8,494                       | 29,674            | 12.5          |
| Policy loans, at outstanding balance                                   | 4,147                               | 5,391                       | 9,538             | 4.0           |
| Other long-term investments(1)   | 2,693                               | 1,139                       | 3,832             | 1.6           |
| Short-term investments(2)  | 2,614                               | 1,555                       | 4,169             | 1.8           |
| <b>Total general account investments</b>                               | <b>170,045</b>                      | <b>66,864</b>               | <b>236,909</b>    | <b>100.0%</b> |
| Invested assets of other entities and operations(3)                    | 10,694                              |                             | 10,694            |               |
| <b>Total investments</b>   | <b>\$ 180,739</b>                   | <b>\$ 66,864</b>            | <b>\$ 247,603</b> |               |
|  | Financial<br>Services<br>Businesses | December 31, 2007           |                   | % of<br>Total |
|  |                                     | Closed<br>Block<br>Business | Total             |               |
| (\$ in millions)   |                                     |                             |                   |               |
| <b>Fixed Maturities:</b>   |                                     |                             |                   |               |
| Public, available for sale, at fair value                              | \$ 90,962                           | \$ 37,168                   | \$ 128,130        | 55.1%         |
| Public, held to maturity, at amortized cost                            | 2,879                               |                             | 2,879             | 1.2           |
| Private, available for sale, at fair value                             | 20,313                              | 12,246                      | 32,559            | 14.0          |
| Private, held to maturity, at amortized cost                           | 669                                 |                             | 669               | 0.3           |
| Trading account assets supporting insurance liabilities, at fair value | 14,473                              |                             | 14,473            | 6.2           |
| Other trading account assets, at fair value                            | 204                                 | 142                         | 346               | 0.2           |
| Equity securities, available for sale, at fair value                   | 4,629                               | 3,940                       | 8,569             | 3.7           |
| Commercial loans, at book value  | 19,603                              | 7,954                       | 27,557            | 11.9          |
| Policy loans, at outstanding balance                                   | 3,942                               | 5,395                       | 9,337             | 4.0           |
| Other long-term investments(1)   | 2,724                               | 1,268                       | 3,992             | 1.7           |
| Short-term investments(2)  | 2,598                               | 1,385                       | 3,983             | 1.7           |
| <b>Total general account investments</b>                               | <b>162,996</b>                      | <b>69,498</b>               | <b>232,494</b>    | <b>100.0%</b> |
| Invested assets of other entities and operations(3)                    | 11,063                              |                             | 11,063            |               |
| <b>Total investments</b>   | <b>\$ 174,059</b>                   | <b>\$ 69,498</b>            | <b>\$ 243,557</b> |               |

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- (1) Other long-term investments consist of real estate and non-real estate related investments in joint ventures (other than our investment in operating joint ventures, which includes our investment in Wachovia Securities) and partnerships, investment real estate held through direct ownership and other miscellaneous investments.
- (2) Short-term investments consist primarily of money market funds with virtually no sub-prime exposure.

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- (3) Includes invested assets of securities brokerage, securities trading, banking operations, real estate and relocation services, and asset management operations. Excludes assets of our asset management operations managed for third parties and those assets classified as Separate account assets on our balance sheet. For additional information regarding these investments, see Invested Assets of Other Entities and Operations below.

The increase in general account investments attributable to the Financial Services Businesses in 2008 was primarily a result of the impact of foreign currency and net operating and capital inflows, partially offset by net declines in market value, primarily attributable to increased credit spreads. The decrease in general account investments attributable to the Closed Block Business in 2008 was primarily due to reductions in leverage and a net decrease in market value, partially offset by portfolio growth as a result of reinvestment of net investment income.

We have substantial insurance operations in Japan, with 32% and 31% of our Financial Services Businesses general account investments relating to our Japanese insurance operations as of March 31, 2008 and December 31, 2007, respectively. Total general account investments related to our Japanese insurance operations were \$54.5 billion and \$50.7 billion as of March 31, 2008 and December 31, 2007, respectively. The average duration of our general account investment portfolio related to our Japanese insurance operations as of March 31, 2008 is approximately 11 years. The increase in general account investments related to our Japanese insurance operations in 2008 is primarily attributable to portfolio growth as a result of business growth, the reinvestment of net investment income and changes in foreign currency exchange rates. The following table sets forth the composition of the investments of our Japanese insurance operations general account as of the dates indicated.

|  | March 31,<br>2008 | December 31,<br>2007 |
|--|-------------------|----------------------|
|  | (in millions)     |                      |
| <b>Fixed Maturities:</b>   |                   |                      |
| Public, available for sale, at fair value                              | \$ 38,163         | \$ 34,752            |
| Public, held to maturity, at amortized cost                            | 3,015             | 2,879                |
| Private, available for sale, at fair value                             | 3,576             | 3,467                |
| Private, held to maturity, at amortized cost                           | 720               | 668                  |
| Trading account assets supporting insurance liabilities, at fair value | 1,136             | 1,132                |
| Other trading account assets, at fair value                            | 49                | 48                   |
| Equity securities, available for sale, at fair value                   | 2,545             | 2,550                |
| Commercial loans, at book value  | 3,046             | 2,881                |
| Policy loans, at outstanding balance                                   | 1,287             | 1,133                |
| Other long-term investments (1)  | 918               | 993                  |
| Short-term investments   | 54                | 239                  |
| <b>Total Japanese general account investments (2)</b>                  | <b>\$ 54,509</b>  | <b>\$ 50,742</b>     |

- (1) Other long-term investments consist of real estate and non-real estate related investments in joint ventures and partnerships, investment real estate held through direct ownership, and other miscellaneous investments.
- (2) Excludes assets classified as Separate accounts assets on our balance sheet.

Our Japanese insurance operations use the yen as their functional currency, as it is the currency in which they conduct the majority of their operations. Although the majority of the Japanese general account is invested in yen denominated investments, our Japanese insurance operations also hold significant investments denominated in U.S. dollars. As of March 31, 2008, our Japanese insurance operations had \$10.7 billion of investments denominated in U.S. dollars, including \$0.6 billion that were hedged to yen through third party derivative contracts and \$4.5 billion that support liabilities denominated in U.S. dollars. As of December 31, 2007, our Japanese insurance operations had \$10.2 billion of investments denominated in U.S. dollars, including \$1.1 billion that were hedged to yen through third party derivative contracts and \$4.1 billion that support liabilities denominated in U.S. dollars. For additional information regarding U.S. dollar investments held in our



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Japanese insurance operations see, Results of Operations for Financial Services Businesses by Segment International Insurance and Investments Division.

**Investment Results**

The following tables set forth the income yield and investment income, excluding realized investment gains (losses), for each major investment category of our general account for the periods indicated.

|   | Three months ended March 31, 2008 |          |                          |        |          |          |
|---|-----------------------------------|----------|--------------------------|--------|----------|----------|
|   | Financial Services<br>Businesses  |          | Closed Block<br>Business |        | Combined |          |
|   | Yield(1)                          | Amount   | Yield(1)                 | Amount | Yield(1) | Amount   |
|   | (\$ in millions)                  |          |                          |        |          |          |
| Fixed maturities  | 4.77%                             | 1,380    | 6.32%                    | \$ 708 | 5.19%    | \$ 2,088 |
| Trading account assets supporting insurance liabilities | 5.13                              | 185      |                          |        | 5.13     | 185      |
| Equity securities                                       | 4.01                              | 46       | 2.91                     | 24     | 3.55     | 70       |
| Commercial loans  | 5.81                              | 294      | 6.57                     | 134    | 6.03     | 428      |
| Policy loans  | 5.05                              | 51       | 6.19                     | 83     | 5.70     | 134      |
| Short-term investments and cash equivalents             | 4.18                              | 99       | 12.58                    | 35     | 4.57     | 134      |
| Other investments                                       | 4.95                              | 36       | 5.99                     | 20     | 5.28     | 56       |
| Gross investment income before investment expenses      | 4.89                              | 2,091    | 6.19                     | 1,004  | 5.23     | 3,095    |
| Investment expenses                                     | (0.13)                            | (80)     | (0.24)                   | (98)   | (0.16)   | (178)    |
| Investment income after investment expenses             | 4.76%                             | 2,011    | 5.95%                    | 906    | 5.07%    | 2,917    |
| Investment results of other entities and operations(2)  |                                   | 110      |                          |        |          | 110      |
| Total investment income                                 |                                   | \$ 2,121 |                          | \$ 906 |          | \$ 3,027 |

|   | Three months ended March 31, 2007 |          |                          |        |          |          |
|---|-----------------------------------|----------|--------------------------|--------|----------|----------|
|   | Financial Services<br>Businesses  |          | Closed Block<br>Business |        | Combined |          |
|   | Yield(1)                          | Amount   | Yield(1)                 | Amount | Yield(1) | Amount   |
|   | (\$ in millions)                  |          |                          |        |          |          |
| Fixed maturities  | 4.95%                             | \$ 1,414 | 6.35%                    | \$ 757 | 5.35%    | \$ 2,171 |
| Trading account assets supporting insurance liabilities | 4.83                              | 171      |                          |        | 4.83     | 171      |
| Equity securities                                       | 4.61                              | 44       | 2.67                     | 21     | 3.75     | 65       |
| Commercial loans  | 5.99                              | 256      | 7.34                     | 132    | 6.39     | 388      |
| Policy loans  | 4.98                              | 44       | 6.06                     | 81     | 5.64     | 125      |
| Short-term investments and cash equivalents             | 5.45                              | 96       | 9.26                     | 39     | 5.80     | 135      |
| Other investments                                       | 6.61                              | 47       | 18.07                    | 41     | 9.46     | 88       |
| Gross investment income before investment expenses      | 5.09                              | 2,072    | 6.46                     | 1,071  | 5.48     | 3,143    |
| Investment expenses                                     | (0.14)                            | (139)    | (0.21)                   | (138)  | (0.16)   | (277)    |
| Investment income after investment expenses             | 4.95%                             | 1,933    | 6.25%                    | 933    | 5.32%    | 2,866    |

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|  |          |        |          |
|--|----------|--------|----------|
| Investment results of other entities and Operations(2) | 69       |        | 69       |
| Total investment income                                | \$ 2,002 | \$ 933 | \$ 2,935 |

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- (1) Yields are annualized, for interim periods, and based on quarterly averages calculated using beginning and end of period balances. Yields are based on carrying values except for fixed maturities, equity securities and securities lending activity. Yields for fixed maturities are based on amortized cost. Yields for equity securities are based on cost. Yields for securities lending activity are calculated net of corresponding liabilities and rebate expenses. Yields exclude investment income on assets other than those included in invested assets of the Financial Services Businesses. Prior periods yields are presented on a basis consistent with the current period presentation.
- (2) Includes investment income of securities brokerage, securities trading, banking operations, real estate and relocation services, and asset management operations.

The net investment income yield on our general account investments after investment expenses, excluding realized investment gains (losses), was 5.07% and 5.32% for the three months ended March 31, 2008 and 2007, respectively. The net investment income yield attributable to the Financial Services Businesses was 4.76% for the three months ended March 31, 2008, compared to 4.95% for the three months ended March 31, 2007. See below for a discussion of the change in the Financial Services Businesses' yields.

The net investment income yield attributable to the Closed Block Business was 5.95% for the three months ended March 31, 2008, compared to 6.25% for the three months ended March 31, 2007. The decrease was primarily due to a decrease in fixed maturity and commercial loan yields as a result of reinvestment of proceeds from sales and maturities of fixed maturities at lower available interest rates and the impact of unfavorable rate resets on floating rate investments.

The following tables set forth the income yield and investment income, excluding realized investment gains (losses), for each major investment category of the Financial Services Business general account, excluding the Japanese operations' portion of the general account which is presented separately below, for the periods indicated.

|   | Three Months Ended<br>March 31, 2008 |          | Three Months Ended<br>March 31, 2007 |          |
|---|--------------------------------------|----------|--------------------------------------|----------|
|   | Yield(1)                             | Amount   | Yield(1)                             | Amount   |
|   | (\$ in millions)                     |          |                                      |          |
| Fixed maturities  | 6.00%                                | \$ 1,080 | 6.24%                                | \$ 1,162 |
| Trading account assets supporting insurance liabilities | 5.33                                 | 177      | 5.06                                 | 165      |
| Equity securities                                       | 6.36                                 | 32       | 6.80                                 | 31       |
| Commercial loans  | 6.02                                 | 261      | 6.31                                 | 226      |
| Policy loans  | 5.57                                 | 39       | 5.51                                 | 35       |
| Short-term investments and cash equivalents             | 4.45                                 | 96       | 5.89                                 | 91       |
| Other investments                                       | 2.81                                 | 13       | 4.56                                 | 22       |
| Gross investment income before investment expenses      | 5.77                                 | 1,698    | 6.05                                 | 1,732    |
| Investment expenses                                     | (0.11)                               | (57)     | (0.12)                               | (116)    |
| Investment income after investment expenses             | 5.66%                                | 1,641    | 5.93%                                | 1,616    |
| Investment results of other entities and operations(2)  |                                      | 110      |                                      | 69       |
| Total investment income                                 |                                      | \$ 1,751 |                                      | \$ 1,685 |

- (1) Yields are annualized, for interim periods, and based on quarterly averages calculated using beginning and end of period balances. Yields are based on carrying values except for fixed maturities, equity securities and securities lending activity. Yields for fixed maturities are

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based on amortized cost. Yields for equity securities are based on cost. Yields for securities lending activity are calculated net of corresponding liabilities and rebate expenses. Yields exclude investment income on assets other than those included in invested assets of the Financial Services Businesses. Prior periods yields are presented on a basis consistent with the current period presentation.



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- (2) Includes investment income of securities brokerage, securities trading, banking operations, real estate and relocation services, and asset management operations.

The net investment income yield attributable to the non-Japanese operations portion of the Financial Services Businesses portfolio was 5.66% for the three months ended March 31, 2008, compared to 5.93% for the three months ended March 31, 2007. The decrease was primarily due to a decrease in fixed maturity yields as a result of unfavorable rate resets on floating rate investments and the impact of reinvestment of proceeds from sales and maturities of fixed maturities at lower available interest rates.

The following tables set forth the income yield and investment income, excluding realized investment gains (losses), for each major investment category of our Japanese operations general account for the periods indicated.

|   | Three Months Ended<br>March 31, 2008 |                            | Three Months Ended<br>March 31, 2007 |        |
|---|--------------------------------------|----------------------------|--------------------------------------|--------|
|   | Yield(1)                             | Amount<br>(\$ in millions) | Yield(1)                             | Amount |
| Fixed maturities  | 2.78%                                | \$ 300                     | 2.61%                                | \$ 252 |
| Trading account assets supporting insurance liabilities | 2.77                                 | 8                          | 2.09                                 | 6      |
| Equity securities                                       | 2.20                                 | 14                         | 2.64                                 | 13     |
| Commercial loans  | 4.54                                 | 33                         | 4.32                                 | 30     |
| Policy loans  | 3.84                                 | 12                         | 3.71                                 | 9      |
| Short-term investments and cash equivalents             | 1.55                                 | 3                          | 2.67                                 | 5      |
| Other investments                                       | 9.06                                 | 23                         | 10.61                                | 25     |
| Gross investment income before investment expenses      | 2.97                                 | 393                        | 2.89                                 | 340    |
| Investment expenses                                     | (0.18)                               | (23)                       | (0.16)                               | (23)   |
| Total investment income                                 | 2.79%                                | \$ 370                     | 2.73%                                | \$ 317 |

- (1) Yields are annualized, for interim periods, and based on quarterly averages calculated using beginning and end of period balances. Yields are based on carrying values except for fixed maturities, equity securities and securities lending activity. Yields for fixed maturities are based on amortized cost. Yields for equity securities are based on cost. Yields for securities lending activity are calculated net of corresponding liabilities and rebate expenses. Yields exclude investment income on assets other than those included in invested assets of the Financial Services Businesses. Prior periods yields are presented on a basis consistent with the current period presentation.

The net investment income yield attributable to the Japanese insurance operations portfolios was 2.79% for the three months ended March 31, 2008, compared to 2.73% for the three months ended March 31, 2007. The increase in yield on the Japanese insurance portfolio is primarily attributable to an increase in unhedged U.S. dollar investments, the lengthening of the duration of the investment portfolio, and an increase in credit exposure. The U.S. dollar denominated fixed maturities that are not hedged to yen through third party derivative contracts provide a yield that is substantially higher than the yield on comparable Japanese fixed maturities. The average value of U.S. dollar denominated fixed maturities that are not hedged to yen through third party derivative contracts for the three months ended March 31, 2008 and 2007 was approximately \$9.0 billion and \$7.2 billion, respectively, based on amortized cost. For additional information regarding U.S. dollar investments held in our Japanese insurance operations see, Results of Operations for Financial Services Businesses by Segment International Insurance and Investments Division.

**Table of Contents****Fixed Maturity Securities***Investment Mix*

Our fixed maturity securities portfolio consists of publicly traded and privately placed debt securities across an array of industry categories. The fixed maturity securities relating to our international insurance operations are primarily comprised of foreign government securities.

*Fixed Maturity Securities and Unrealized Gains and Losses by Industry Category*

The following table sets forth the composition of the portion of our fixed maturity securities portfolio by industry category attributable to the Financial Services Businesses as of the dates indicated and the associated gross unrealized gains and losses.

| Industry(1)                 | March 31, 2008 |                           |                            | December 31, 2007 |                           |                            | Fair Value |            |
|-----------------------------|----------------|---------------------------|----------------------------|-------------------|---------------------------|----------------------------|------------|------------|
|                             | Amortized Cost | Gross Unrealized Gains(2) | Gross Unrealized Losses(2) | Amortized Cost    | Gross Unrealized Gains(2) | Gross Unrealized Losses(2) |            |            |
| (in millions)               |                |                           |                            |                   |                           |                            |            |            |
| Corporate Securities:       |                |                           |                            |                   |                           |                            |            |            |
| Manufacturing               | \$ 15,436      | \$ 557                    | \$ 476                     | \$ 15,517         | \$ 14,754                 | \$ 523                     | \$ 248     | \$ 15,029  |
| Finance                     | 10,187         | 141                       | 405                        | 9,923             | 11,009                    | 141                        | 247        | 10,903     |
| Utilities                   | 10,316         | 386                       | 309                        | 10,393            | 10,170                    | 408                        | 191        | 10,387     |
| Services                    | 8,682          | 227                       | 415                        | 8,494             | 8,238                     | 237                        | 191        | 8,284      |
| Energy                      | 4,075          | 157                       | 133                        | 4,099             | 4,009                     | 157                        | 69         | 4,097      |
| Transportation              | 3,181          | 115                       | 65                         | 3,231             | 2,872                     | 112                        | 38         | 2,946      |
| Retail and Wholesale        | 2,934          | 70                        | 94                         | 2,910             | 2,722                     | 64                         | 50         | 2,736      |
| Other                       | 877            | 11                        | 42                         | 846               | 742                       | 11                         | 20         | 733        |
| Total Corporate Securities  | 55,688         | 1,664                     | 1,939                      | 55,413            | 54,516                    | 1,653                      | 1,054      | 55,115     |
| Foreign Government          | 29,934         | 1,149                     | 64                         | 31,019            | 27,606                    | 904                        | 98         | 28,412     |
| Asset-Backed Securities     | 13,363         | 74                        | 1,328                      | 12,109            | 13,833                    | 123                        | 747        | 13,209     |
| Residential Mortgage-Backed | 10,826         | 189                       | 90                         | 10,925            | 7,782                     | 104                        | 46         | 7,840      |
| Commercial Mortgage-Backed  | 6,956          | 46                        | 146                        | 6,856             | 6,581                     | 102                        | 25         | 6,658      |
| U.S. Government             | 2,641          | 443                       | 6                          | 3,078             | 2,585                     | 379                        |            | 2,964      |
| State & Municipal(3)        | 582            | 39                        | 1                          | 620               | 583                       | 37                         |            | 620        |
| Total(4)(5)                 | \$ 119,990     | \$ 3,604                  | \$ 3,574                   | \$ 120,020        | \$ 113,486                | \$ 3,302                   | \$ 1,970   | \$ 114,818 |

- (1) Investment data has been classified based on Lehman industry categorizations for domestic public holdings and similar classifications by industry for all other holdings.
- (2) Includes \$57 million of gross unrealized gains and \$51 million of gross unrealized losses as of March 31, 2008, compared to \$36 million of gross unrealized gains and \$41 million of gross unrealized losses as of December 31, 2007 on securities classified as held to maturity, which are not reflected in other comprehensive income.
- (3) State and municipal securities were previously presented within U.S. Government.
- (4)

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Excluded from the above are securities held outside the general account in other entities and operations. For additional information regarding investments held outside the general account, see [Invested Assets of Other Entities and Operations](#) below.

- (5) The table above excludes fixed maturity securities classified as trading. See [Trading Account Assets Supporting Insurance Liabilities](#) for additional information.

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As a percentage of amortized cost, fixed maturity investments attributable to the Financial Services Businesses as of March 31, 2008, consist primarily of 25% foreign government securities, 13% manufacturing sector, 11% asset-backed securities and 9% residential mortgage-backed sector, compared to 24% foreign government securities, 13% manufacturing sector, 12% asset-backed securities and 10% finance sector as of December 31, 2007. As of March 31, 2008, 98% of the residential mortgage-backed securities in the Financial Services Businesses were publicly traded agency pass-through securities, which are supported by implicit or explicit government guarantees and have credit ratings of AAA. Collateralized mortgage obligations, including approximately \$58 million secured by ALT-A mortgages, represented the remaining 2% of residential mortgage-backed securities (and less than 1% of total fixed maturities in the Financial Services Businesses), and all have credit ratings of A or above.

The gross unrealized losses related to our fixed maturity portfolio attributable to the Financial Services Businesses increased from \$2.0 billion as of December 31, 2007 to \$3.6 billion as of March 31, 2008, primarily due to credit spread increases in the credit markets and liquidity concerns. The gross unrealized losses as of March 31, 2008 were concentrated primarily in asset-backed securities and the manufacturing, service, and finance sectors of our corporate securities. The gross unrealized losses as of December 31, 2007 were concentrated primarily in asset-backed securities and the manufacturing and finance sectors of our corporate securities.

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As of March 31, 2008, included within asset-backed securities attributable to the Financial Services Businesses on an amortized cost basis is approximately \$7.1 billion (\$6.0 billion fair value) of securities collateralized by sub-prime mortgages. While there is no market standard definition, we define sub-prime mortgages as residential mortgages that are originated to weaker quality obligors as indicated by weaker credit scores, as well as mortgages with higher loan to value ratios, or limited documentation. The slowing U.S. housing market, high interest rate resets, and relaxed underwriting standards for some originators of sub-prime mortgages have recently led to higher delinquency rates, particularly for those mortgages issued in 2006 and 2007. The following tables set forth the amortized cost and fair value of our asset-backed securities attributable to the Financial Services Businesses as of the dates indicated, by credit quality, and for asset-backed securities collateralized by sub-prime mortgages, by year of issuance (vintage).

| Vintage   | Amortized Cost as of March 31, 2008<br>Lowest Rating Agency Rating |          |          |          |                 | Total<br>Amortized<br>Cost | Total<br>Amortized<br>Cost as of<br>December 31,<br>2007 |
|---|--|----------|----------|----------|-----------------|----------------------------|--|
|   | AAA  | AA       | A        | BBB      | BB and<br>below |                            |  |
| Collateralized by sub-prime mortgages:                |  |          |          |          |                 |                            |  |
| Enhanced short-term portfolio(1)                      |  |          |          |          |                 |                            |  |
| 2007  | \$ 535   | \$ 104   | \$ 57    | \$       | \$              | \$ 696                     | \$ 737   |
| 2006  | 1,913  | 162      | 238      |          |                 | 2,313                      | 2,622  |
| 2005  | 75   |          | 24       |          |                 | 99                         | 142  |
| 2004  |  |          |          |          |                 |                            |  |
| 2003 & Prior  |  |          |          |          |                 |                            |  |
| Total enhanced short-term portfolio                   | 2,523  | 266      | 319      |          |                 | 3,108                      | 3,501  |
| All other portfolios                                  |  |          |          |          |                 |                            |  |
| 2007  | 227  | 68       | 74       |          |                 | 369                        | 420  |
| 2006  | 877  | 346      | 423      | 26       | 5               | 1,677                      | 1,811  |
| 2005  | 19   | 457      | 161      | 21       | 4               | 662                        | 677  |
| 2004  | 43   | 362      | 332      | 7        |                 | 744                        | 763  |
| 2003 & Prior  | 51   | 214      | 218      | 74       | 18              | 575                        | 640  |
| Total all other portfolios                            | 1,217  | 1,447    | 1,208    | 128      | 27              | 4,027                      | 4,311  |
| Total collateralized by sub-prime mortgages(2)        | 3,740  | 1,713    | 1,527    | 128      | 27              | 7,135                      | 7,812  |
| Other asset-backed securities:                        |  |          |          |          |                 |                            |  |
| Externally managed investments in the European market |  |          |          |          |                 |                            |  |
| Collateralized by auto loans                          | 1,025  | 65       | 91       | 82       | 3               | 1,266                      | 1,187  |
| Collateralized by credit cards                        | 143  |          | 7        | 761      |                 | 911                        | 907  |
| Collateralized by non-sub-prime mortgages             | 704  | 53       | 13       | 36       | 16              | 822                        | 771  |
| Other asset-backed securities(4)                      | 739  | 170      | 173      | 65       | 198             | 1,345                      | 1,315  |
| Total asset-backed securities(5)                      | \$ 6,351   | \$ 2,001 | \$ 3,094 | \$ 1,658 | \$ 259          | \$ 13,363                  | \$ 13,833  |

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| Vintage  | Fair Value as of March 31, 2008 |          |          |          |              | Total Fair Value | Total Fair Value as of December 31, 2007 |
|--|---------------------------------|----------|----------|----------|--------------|------------------|--|
|  | Lowest Rating Agency Rating     |          |          |          |              |                  |  |
|  | AAA                             | AA       | A        | BBB      | BB and below |                  |  |
| Collateralized by sub-prime mortgages:                   |                                 |          |          |          |              |                  |  |
| Enhanced short-term portfolio(1)                         |                                 |          |          |          |              |                  |  |
| 2007   | \$ 477                          | \$ 91    | \$ 48    | \$       | \$           | \$ 616           | \$ 692                                   |
| 2006   | 1,785                           | 145      | 216      |          |              | 2,146            | 2,532                                    |
| 2005   | 72                              |          | 23       |          |              | 95               | 140                                      |
| 2004   |                                 |          |          |          |              |                  |  |
| 2003 & Prior   |                                 |          |          |          |              |                  |  |
| Total enhanced short-term portfolio                      | 2,334                           | 236      | 287      |          |              | 2,857            | 3,364                                    |
| All other portfolios                                     |                                 |          |          |          |              |                  |  |
| 2007   | 174                             | 48       | 54       |          |              | 276              | 341                                      |
| 2006   | 717                             | 268      | 290      | 16       | 3            | 1,294            | 1,539                                    |
| 2005   | 20                              | 355      | 122      | 17       | 3            | 517              | 604                                      |
| 2004   | 40                              | 283      | 259      | 5        |              | 587              | 711                                      |
| 2003 & Prior   | 46                              | 168      | 176      | 59       | 15           | 464              | 576                                      |
| Total all other portfolios                               | 997                             | 1,122    | 901      | 97       | 21           | 3,138            | 3,771                                    |
| Total collateralized by sub-prime mortgages              | 3,331                           | 1,358    | 1,188    | 97       | 21           | 5,995            | 7,135                                    |
| Other asset-backed securities:                           |                                 |          |          |          |              |                  |  |
| Externally managed investments in the European market(3) |                                 |          |          |          |              |                  |  |
|  |                                 |          | 1,297    | 593      | 15           | 1,905            | 1,898                                    |
| Collateralized by auto loans                             | 1,025                           | 64       | 90       | 75       | 3            | 1,257            | 1,188                                    |
| Collateralized by credit cards                           | 142                             |          | 8        | 668      |              | 818              | 874                                      |
| Collateralized by non-sub-prime mortgages                | 717                             | 53       | 13       | 36       | 16           | 835              | 778                                      |
| Other asset-backed securities(4)                         | 722                             | 168      | 168      | 54       | 187          | 1,299            | 1,336                                    |
| Total asset-backed securities(5)                         | \$ 5,937                        | \$ 1,643 | \$ 2,764 | \$ 1,523 | \$ 242       | \$ 12,109        | \$ 13,209                                |

- (1) Our enhanced short-term portfolio is used primarily to invest cash proceeds of securities lending and repurchase activities, and cash generated from certain trading and operating activities. The investment policy statement of this portfolio requires that securities purchased for this portfolio have a remaining expected average life of 2 years or less when acquired.
- (2) Included within the \$7.1 billion of asset-backed securities collateralized by sub-prime mortgages as of March 31, 2008 are \$1.3 billion of securities supported by guarantees from monoline bond insurers, of which \$1.1 billion are collateralized by second-lien exposures. See *Fixed Maturity Securities Credit Quality* for additional information regarding guarantees from monoline bond insurers.
- (3) Excludes the \$(432) million impact of the bifurcated embedded derivative described below.
- (4) Includes collateralized debt obligations with amortized cost of \$199 million and fair value of \$169 million, with less than 2% secured by sub-prime mortgages. Also includes asset-backed securities collateralized by education loans, equipment leases, timeshares, aircraft, and franchises.
- (5) Excluded from the table above are available for sale asset-backed securities held outside the general account in other entities and operations. For additional information regarding asset-backed securities held outside the general account, see *Invested Asset of Other Entities and Operations* below. Also excluded from the table above are asset-backed securities classified as trading and carried at fair value. See *Trading Account Assets Supporting Insurance Liabilities* for information regarding \$1.2 billion of such securities. An additional \$32 million held within the general account are classified as other trading, 31% of which have credit ratings of AAA and the remaining 69% of which have BBB credit ratings.

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The tables above provide ratings as assigned by nationally recognized rating agencies as of March 31, 2008, and reflect credit rating downgrades on asset-backed securities collateralized by sub-prime mortgages processed by the rating agencies in the first quarter of 2008. As of March 31, 2008, based on amortized cost, approximately 53% of asset-backed securities collateralized by sub-prime mortgages attributable to the Financial Services Businesses had AAA credit ratings, 24% had AA credit ratings, 21% had A credit ratings, 2% had BBB credit ratings, and less than 1% had below investment grade credit ratings, compared to 71% with AAA credit ratings, 19% with AA credit ratings, 9% with A credit ratings, 1% with BBB credit ratings, and less than 1% with below investment grade credit ratings, as of December 31, 2007. In making our investment decisions we assign internal ratings to our asset-backed securities based upon our dedicated asset-backed securities unit's independent evaluation of the underlying collateral and securitization structure, including any guarantees from monoline bond insurers. See Fixed Maturity Securities Credit Quality for additional information regarding guarantees from monoline bond insurers. Gross unrealized losses related to our asset-backed securities collateralized by sub-prime mortgages attributable to the Financial Services Businesses were \$1.1 billion as of March 31, 2008 and \$0.7 billion as of December 31, 2007, respectively. For additional information regarding sales and other-than-temporary impairments of asset-backed securities collateralized by sub-prime mortgages see Realized Investment Gains and Losses above.

The weighted average estimated subordination percentage of our general account available for sale asset-backed securities collateralized by sub-prime mortgages attributable to the Financial Services Businesses, excluding those supported by guarantees from monoline bond insurers, was 33% as of March 31, 2008. The subordination percentage represents the current weighted average estimated percentage of the capital structure subordinated to our investment holding that is available to absorb losses before the security incurs the first dollar loss of principal. As of March 31, 2008, based on amortized cost, approximately 89% of the asset-backed securities collateralized by sub-prime mortgages attributable to the Financial Services Businesses have estimated credit subordination percentages of 20% or more, and 49% have estimated credit subordination percentages of 30% or more.

The \$1.9 billion of externally managed investments in the European market, included above in asset-backed securities of the Financial Services Businesses, reflects our investment in medium term notes that are collateralized by investment portfolios primarily consisting of European fixed income securities, including 49% European corporate and bank bonds, 21% bank capital, 18% European asset-backed securities, and 12% other, as well as derivatives and varying degrees of leverage. Our investment in these notes further diversifies our credit risk. None of the underlying investments are securities collateralized by U.S. sub-prime mortgages, and 91% of the underlying investments are rated investment grade. The notes have a stated coupon and provide a return based on the return of the underlying portfolios and the level of leverage. The notes are accounted for as available for sale fixed maturity securities with bifurcated embedded derivatives (total return swaps). Changes in the value of the fixed maturity securities are reported in Stockholders' Equity under the heading Accumulated Other Comprehensive Income. Changes in the market value of the embedded total return swaps are included in current period earnings in Realized investment gains (losses), net. As discussed further in Note 8 to the Unaudited Interim Consolidated Financial Statements, any changes in market value of the embedded total return swaps are excluded from adjusted operating income. While the fair value of the embedded derivatives associated with these investments have declined in recent quarters due to increased credit spreads in the financial markets, we believe the investment fundamentals remain sound, and the ultimate value that will be realized from these investments is greater than reflected by the current fair value of the embedded derivatives. During the second quarter of 2008, we restructured certain of these investments, which included an additional investment of approximately \$500 million to fund our share of leverage in certain of the existing portfolios. As a result of the restructuring, beginning in the second quarter of 2008, the underlying restructured portfolio of investments and derivatives, totaling approximately \$680 million, will be held directly on our balance sheet within the general account portfolio.

While delinquency rates on commercial mortgages have been stable in recent years, we recognized several market factors that influenced our investment decisions on commercial mortgage-backed securities issued in 2006 and 2007, including less stringent loan underwriting, higher levels of leverage, and rapid real estate price

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appreciation. The following tables set forth the amortized cost and fair value of our commercial mortgage-backed securities attributable to the Financial Services Businesses as of the dates indicated by credit quality and by year of issuance (vintage).

| Vintage   | Amortized Cost as of March 31, 2008 |               |              |               |               | Total Amortized Cost | Total Amortized Cost as of December 31, 2007 |
|---|-------------------------------------|---------------|--------------|---------------|---------------|----------------------|--|
|   | Lowest Rating Agency Rating         |               |              |               |               |                      |  |
|   | AAA                                 | AA            | A            | BBB           | BB and below  |                      |  |
|   | (\$ in millions)                    |               |              |               |               |                      |  |
| 2008  | \$ 21                               | \$            | \$           | \$ 12         | \$            | \$ 33                | \$   |
| 2007  | 740                                 |               | 3            | 68            | 76            | 887                  | 713  |
| 2006  | 2,776                               | 6             |              | 7             | 23            | 2,812                | 2,546  |
| 2005  | 1,441                               |               |              | 11            | 39            | 1,491                | 1,509  |
| 2004  | 409                                 |               |              |               | 4             | 413                  | 423  |
| 2003 & Prior  | 1,023                               | 171           | 60           | 57            | 9             | 1,320                | 1,390  |
| <b>Total commercial mortgage-backed securities(1)</b> | <b>\$ 6,410</b>                     | <b>\$ 177</b> | <b>\$ 63</b> | <b>\$ 155</b> | <b>\$ 151</b> | <b>\$ 6,956</b>      | <b>\$ 6,581</b>                              |

| Vintage   | Fair Value as of March 31, 2008 |               |              |               |               | Total Fair Value | Total Fair Value as of December 31, 2007 |
|---|---------------------------------|---------------|--------------|---------------|---------------|------------------|--|
|   | Lowest Rating Agency Rating     |               |              |               |               |                  |  |
|   | AAA                             | AA            | A            | BBB           | BB and below  |                  |  |
|   | (in millions)                   |               |              |               |               |                  |  |
| 2008  | \$ 22                           | \$            | \$           | \$ 12         | \$            | \$ 34            | \$                                       |
| 2007  | 743                             |               | 3            | 68            | 75            | 889              | 727                                      |
| 2006  | 2,739                           | 5             |              | 6             | 23            | 2,773            | 2,588                                    |
| 2005  | 1,406                           |               |              | 11            | 38            | 1,455            | 1,517                                    |
| 2004  | 396                             |               |              |               | 3             | 399              | 421                                      |
| 2003 & Prior  | 1,017                           | 168           | 56           | 55            | 10            | 1,306            | 1,405                                    |
| <b>Total commercial mortgage-backed securities(1)</b> | <b>\$ 6,323</b>                 | <b>\$ 173</b> | <b>\$ 59</b> | <b>\$ 152</b> | <b>\$ 149</b> | <b>\$ 6,856</b>  | <b>\$ 6,658</b>                          |

- (1) Excluded from the table above are available for sale commercial mortgage-backed securities held outside the general account in other entities and operations. For additional information regarding commercial mortgage-backed securities held outside the general account, see *Invested Assets of Other Entities and Operations* below. Also excluded from the table above are commercial mortgage-backed securities classified as trading and carried at fair value. See *Trading Account Assets Supporting Insurance Liabilities* for information regarding \$2.5 billion of such securities.

Loan to value and debt service coverage ratios are measures commonly used to assess the quality of commercial mortgage-backed securities. The loan to value ratio compares the amount of the loan to the fair value of the underlying property collateralizing the loan, and is commonly expressed as a percentage. Loan to value ratios greater than 100% percent indicate that the loan amount is greater than the collateral value. Therefore, all else being equal, a smaller loan to value ratio generally indicates a higher quality security. The debt service coverage ratio compares a property's net operating income to its debt service payments. Debt service coverage ratios less than 1.0 times indicate that property operations do not generate enough income to cover its current debt payments. Therefore, all else being equal, a larger debt service coverage ratio generally indicates a higher quality security. The following tables set forth the amortized cost and fair value of our commercial mortgage-backed securities attributable to the Financial Services Businesses as of March 31, 2008 by loan to value and debt service coverage ratios.





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|   | March 31, 2008    |                 |
|---|-------------------|-----------------|
|   | Amortized<br>Cost | Fair<br>Value   |
|   | (in millions)     |                 |
| Commercial mortgage-backed securities by loan to value ratio: |                   |                 |
| 0% - 50%  | \$ 253            | \$ 251          |
| 50% - 60%   | 294               | 292             |
| 60% - 70%   | 3,415             | 3,362           |
| 70% - 80%   | 2,943             | 2,900           |
| 80% - 90%   | 51                | 51              |
| 90% - 100%  |                   |                 |
| Greater than 100%   |                   |                 |
| <b>Total</b>  | <b>\$ 6,956</b>   | <b>\$ 6,856</b> |

|   | March 31, 2008    |                 |
|---|-------------------|-----------------|
|   | Amortized<br>Cost | Fair<br>Value   |
|   | (in millions)     |                 |
| Commercial mortgage-backed securities by debt service coverage ratio: |                   |                 |
| Greater than 1.8 times  | \$ 960            | \$ 949          |
| 1.5 times 1.8 times   | 2,559             | 2,509           |
| 1.2 times 1.5 times   | 3,401             | 3,364           |
| 1.0 times 1.2 times   | 26                | 25              |
| Less than 1.0 times   | 10                | 9               |
| <b>Total</b>  | <b>\$ 6,956</b>   | <b>\$ 6,856</b> |

As of March 31, 2008, based on amortized cost, the weighted average loan to value and debt service coverage ratios of commercial mortgage-backed securities attributable to the Financial Services Businesses is 68% and 1.54 times, respectively. The weighted average estimated subordination percentage of our general account available for sale commercial mortgage-backed securities attributable to the Financial Services Businesses was 35% as of March 31, 2008. The subordination percentage represents the current weighted average estimated percentage of the capital structure subordinated to our investment holding that is available to absorb losses before the security incurs the first dollar loss of principal. The estimated subordination percentage includes an adjustment for that portion of the capital structure which has been effectively defeased by US Treasury securities. As of March 31, 2008, based on amortized cost, approximately 89% of the commercial mortgage-backed securities attributable to the Financial Services Businesses have estimated credit subordination percentages of 20% or more, and 70% have estimated credit subordination percentages of 30% or more.

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The following table sets forth the composition of the portion of our fixed maturity securities portfolio by industry category attributable to the Closed Block Business as of the dates indicated and the associated gross unrealized gains and losses.

| Industry(1)                       | March 31, 2008    |                              |                               | December 31, 2007 |                   |                              |                               |                  |
|-----------------------------------|-------------------|------------------------------|-------------------------------|-------------------|-------------------|------------------------------|-------------------------------|------------------|
|                                   | Amortized<br>Cost | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Fair<br>value     | Amortized<br>Cost | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Fair<br>Value    |
| (in millions)                     |                   |                              |                               |                   |                   |                              |                               |                  |
| Corporate Securities:             |                   |                              |                               |                   |                   |                              |                               |                  |
| Manufacturing                     | \$ 8,641          | \$ 364                       | \$ 167                        | \$ 8,838          | \$ 8,455          | \$ 346                       | \$ 91                         | \$ 8,710         |
| Utilities                         | 5,523             | 254                          | 146                           | 5,631             | 5,338             | 280                          | 73                            | 5,545            |
| Services                          | 4,663             | 182                          | 152                           | 4,693             | 4,566             | 184                          | 77                            | 4,673            |
| Finance                           | 3,229             | 55                           | 74                            | 3,210             | 3,997             | 53                           | 71                            | 3,979            |
| Energy                            | 2,070             | 96                           | 24                            | 2,142             | 2,103             | 99                           | 13                            | 2,189            |
| Retail and Wholesale              | 1,683             | 66                           | 32                            | 1,717             | 1,631             | 59                           | 19                            | 1,671            |
| Transportation                    | 1,281             | 64                           | 31                            | 1,314             | 1,274             | 65                           | 21                            | 1,318            |
| <b>Total Corporate Securities</b> | <b>27,090</b>     | <b>1,081</b>                 | <b>626</b>                    | <b>27,545</b>     | <b>27,364</b>     | <b>1,086</b>                 | <b>365</b>                    | <b>28,085</b>    |
| Asset-Backed Securities           | 7,598             | 29                           | 1,001                         | 6,626             | 8,091             | 14                           | 478                           | 7,627            |
| Residential Mortgage-Backed       | 3,997             | 75                           | 21                            | 4,051             | 5,163             | 61                           | 18                            | 5,206            |
| Commercial Mortgage-Backed        | 4,230             | 21                           | 116                           | 4,135             | 4,265             | 46                           | 21                            | 4,290            |
| U.S. Government                   | 3,137             | 271                          | 4                             | 3,404             | 3,184             | 291                          | 1                             | 3,474            |
| State & Municipal(2)              | 171               | 21                           |                               | 192               | 169               | 18                           |                               | 187              |
| Foreign Government                | 560               | 53                           | 8                             | 605               | 496               | 53                           | 4                             | 545              |
| <b>Total</b>                      | <b>\$ 46,783</b>  | <b>\$ 1,551</b>              | <b>\$ 1,776</b>               | <b>\$ 46,558</b>  | <b>\$ 48,732</b>  | <b>\$ 1,569</b>              | <b>\$ 887</b>                 | <b>\$ 49,414</b> |

- (1) Investment data has been classified based on Lehman industry categorizations for domestic public holdings and similar classifications by industry for all other holdings.
- (2) State and municipal securities were previously presented within U.S. Government.

As a percentage of amortized cost, fixed maturity investments attributable to the Closed Block Business as of March 31, 2008 consist primarily of 18% manufacturing sector, 16% asset-backed securities, 12% utilities sector, 10% services sector, 9% residential mortgage-backed securities and 9% commercial mortgage-backed securities compared to 17% asset-backed securities, 17% manufacturing sector, 11% utilities sector, 11% residential mortgage-backed securities, 9% services sector, and 9% commercial mortgage-backed securities, as of December 31, 2007. As of March 31, 2008, 84% of the residential mortgage-backed securities in the Closed Block Business were publicly traded agency pass-through securities, which are supported by implicit or explicit government guarantees and have credit ratings of AAA. Collateralized mortgage obligations, including approximately \$3 million secured by ALT-A mortgages, represented the remaining 16% of residential mortgage-backed securities (and less than 1% of total fixed maturities in the Closed Block Business), and all have AAA credit ratings.

The gross unrealized losses related to our fixed maturity portfolio attributable to the Closed Block Business increased from \$0.9 billion as of December 31, 2007 to \$1.8 billion as of March 31, 2008, primarily due to credit spread increases in the credit markets and liquidity concerns. The gross unrealized losses as of March 31, 2008 and December 31, 2007 were concentrated primarily in asset-backed securities and the manufacturing, services, and utilities sectors of our corporate securities.

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As of March 31, 2008, included within asset-backed securities attributable to the Closed Block Business on an amortized cost basis is approximately \$5.8 billion (\$4.9 billion fair value) of securities collateralized by sub-prime mortgages. See above for a description of asset-backed securities collateralized by sub-prime mortgages. The following tables set forth the amortized cost and fair value of our asset-backed securities attributable to the Closed Block Business as of the dates indicated, by credit quality, and for asset-backed securities collateralized by sub-prime mortgages, by year of issuance (vintage).

| Vintage   | Amortized Cost as of March 31, 2008<br>Lowest Rating Agency Rating |          |          |                         |                 | Total<br>Amortized<br>Cost | Total<br>Amortized<br>Cost as of<br>December 31,<br>2007 |
|---|--|----------|----------|-------------------------|-----------------|----------------------------|--|
|   | AAA  | A        | A A      | BBB<br>(\$ in millions) | BB and<br>below |                            |  |
| Collateralized by sub-prime mortgages:                |  |          |          |                         |                 |                            |  |
| Enhanced short-term portfolio(1)                      |  |          |          |                         |                 |                            |  |
| 2007  | \$ 552   | \$ 107   | \$ 59    | \$                      | \$              | \$ 718                     | \$ 768   |
| 2006  | 1,972  | 167      | 246      |                         |                 | 2,385                      | 2,735  |
| 2005  | 77   |          | 25       |                         |                 | 102                        | 148  |
| 2004  |  |          |          |                         |                 |                            |  |
| 2003 & Prior  |  |          |          |                         |                 |                            |  |
| Total enhanced short-term portfolio                   | 2,601  | 274      | 330      |                         |                 | 3,205                      | 3,651  |
| All other portfolios                                  |  |          |          |                         |                 |                            |  |
| 2007  | 167  | 22       | 22       |                         |                 | 211                        | 211  |
| 2006  | 614  | 193      | 240      | 7                       |                 | 1,054                      | 1,074  |
| 2005  | 30   | 404      | 16       |                         |                 | 450                        | 456  |
| 2004  | 9  | 304      | 51       |                         |                 | 364                        | 370  |
| 2003 & Prior  | 48   | 340      | 100      | 32                      | 7               | 527                        | 568  |
| Total all other portfolios                            | 868  | 1,263    | 429      | 39                      | 7               | 2,606                      | 2,679  |
| Total collateralized by sub-prime mortgages(2)        | 3,469  | 1,537    | 759      | 39                      | 7               | 5,811                      | 6,330  |
| Other asset-backed securities:                        |  |          |          |                         |                 |                            |  |
| Collateralized by credit cards                        | 38   |          | 21       | 480                     |                 | 539                        | 544  |
| Collateralized by auto loans                          | 362  | 16       | 56       | 25                      |                 | 459                        | 387  |
| Externally managed investments in the European market |  |          | 281      |                         |                 | 281                        | 281  |
| Collateralized by education loans                     | 234  | 20       |          |                         |                 | 254                        | 215  |
| Other asset-backed securities(4)                      | 160  | 23       | 27       | 13                      | 31              | 254                        | 334  |
| Total asset-backed securities                         | \$ 4,263   | \$ 1,596 | \$ 1,144 | \$ 557                  | \$ 38           | \$ 7,598                   | \$ 8,091   |

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| Vintage  | Fair Value as of March 31, 2008<br>Lowest Rating Agency Rating |          |          |                      |                 | Total Fair<br>Value | Total Fair<br>Value as of<br>December 31,<br>2007 |
|--|--|----------|----------|----------------------|-----------------|---------------------|---|
|  | AAA  | AA       | A        | BBB<br>(in millions) | BB and<br>below |                     |   |
| Collateralized by sub-prime mortgages:                   |  |          |          |                      |                 |                     |   |
| Enhanced short-term portfolio(1)                         |  |          |          |                      |                 |                     |   |
| 2007   | \$ 492   | \$ 94    | \$ 49    | \$                   | \$              | \$ 635              | \$ 721  |
| 2006   | 1,841  | 150      | 222      |                      |                 | 2,213               | 2,640   |
| 2005   | 75   |          | 24       |                      |                 | 99                  | 147   |
| 2004   |  |          |          |                      |                 |                     |   |
| 2003 & Prior   |  |          |          |                      |                 |                     |   |
| Total enhanced short-term portfolio                      | 2,408  | 244      | 295      |                      |                 | 2,947               | 3,508   |
| All other portfolios                                     |  |          |          |                      |                 |                     |   |
| 2007   | 113  | 15       | 15       |                      |                 | 143                 | 175   |
| 2006   | 459  | 133      | 164      | 4                    |                 | 760                 | 926   |
| 2005   | 25   | 306      | 13       |                      |                 | 344                 | 412   |
| 2004   | 8  | 231      | 40       |                      |                 | 279                 | 344   |
| 2003 & Prior   | 44   | 262      | 82       | 26                   | 5               | 419                 | 518   |
| Total all other portfolios                               | 649  | 947      | 314      | 30                   | 5               | 1,945               | 2,375   |
| Total collateralized by sub-prime mortgages              | 3,057  | 1,191    | 609      | 30                   | 5               | 4,892               | 5,883   |
| Other asset-backed securities:                           |  |          |          |                      |                 |                     |   |
| Collateralized by credit cards                           | 38   |          | 21       | 416                  |                 | 475                 | 522   |
| Collateralized by auto loans                             | 363  | 16       | 56       | 22                   |                 | 457                 | 386   |
| Externally managed investments in the European market(3) |  |          | 296      |                      |                 | 296                 | 283   |
| Collateralized by education loans                        | 232  | 20       |          |                      |                 | 252                 | 215   |
| Other asset-backed securities(4)                         | 158  | 23       | 27       | 12                   | 34              | 254                 | 338   |
| Total asset-backed securities(5)                         | \$ 3,848   | \$ 1,250 | \$ 1,009 | \$ 480               | \$ 39           | \$ 6,626            | \$ 7,627  |

- (1) Our enhanced short-term portfolio is used primarily to invest cash proceeds of securities lending and repurchase activities, and cash generated from certain trading and operating activities. The investment policy statement of this portfolio requires that securities purchased for this portfolio have a remaining expected average life of 2 years or less when acquired.
- (2) Included within the \$5.8 billion of asset-backed securities collateralized by sub-prime mortgages are \$0.8 billion of securities supported by guarantees from monoline bond insurers, of which \$0.7 billion are collateralized by second-lien exposures. See Fixed Maturity Securities Credit Quality for additional information regarding guarantees from monoline bond insurers.
- (3) Excludes the \$(55) million impact of the embedded derivative described below.
- (4) Includes collateralized debt obligations with amortized cost of \$22 million and fair value of \$26 million, with none secured by sub-prime mortgages. Also includes asset-backed securities collateralized by equipment leases, timeshares, aircraft, and franchises.
- (5) Excluded from the table above are \$17 million of asset-backed securities classified as other trading and carried at fair value, all of which have BBB credit ratings as of March 31, 2008.

The tables above provide ratings as assigned by nationally recognized rating agencies as of March 31, 2008, and reflect credit rating downgrades on asset-backed securities collateralized by sub-prime mortgages processed by the rating agencies in the first quarter of 2008. As of March 31, 2008, based on amortized cost, approximately 60% of asset-backed securities collateralized by sub-prime mortgages attributable to the Closed Block Business

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had AAA credit ratings, 26% had AA credit ratings, 13% had A credit ratings, 1% had BBB credit ratings, and less than 1% had below investment grade credit ratings, compared to 79% with AAA credit ratings, 18% with AA credit ratings, 3% with A credit ratings, and less than 1% with BBB or below investment grade credit ratings, as of December 31, 2007. In making our investment decisions we assign internal ratings to our asset-backed securities based upon our dedicated asset-backed securities unit's independent evaluation of the underlying collateral and securitization structure, including any guarantees from monoline bond insurers. See [Fixed Maturity Securities Credit Quality](#) for additional information regarding guarantees from monoline bond insurers. Gross unrealized losses related to our asset-backed securities collateralized by sub-prime mortgages attributable to the Closed Block Business were \$0.9 billion as of March 31, 2008 and \$0.4 billion as of December 31, 2007, respectively. For additional information regarding sales and other-than-temporary impairments of asset-backed securities collateralized by sub-prime mortgages see [Realized Investment Gains and Losses](#) above.

The weighted average estimated subordination percentage of available for sale asset-backed securities collateralized by sub-prime mortgages attributable to the Closed Block Business, excluding those supported by guarantees from monoline bond insurers, was 34% as of March 31, 2008. The subordination percentage represents the current weighted average estimated percentage of the capital structure subordinated to our investment holding that is available to absorb losses before the security incurs the first dollar loss of principal. As of March 31, 2008, based on amortized cost, approximately 95% of the asset-backed securities collateralized by sub-prime mortgages attributable to the Closed Block Business have estimated credit subordination percentages of 20% or more, and 54% have estimated credit subordination percentages of 30% or more.

The \$0.3 billion of externally managed investments in the European market, included in asset-backed securities of the Closed Block Business, reflects our investment in medium term notes that are collateralized by investment portfolios primarily consisting of European fixed income securities, including 49% European corporate and bank bonds, 21% bank capital, 18% European asset-backed securities, and 12% other, as well as derivatives and varying degrees of leverage. Our investment in these notes further diversifies our credit risk. None of the underlying investments are securities collateralized by U.S. sub-prime mortgages, and 91% of the underlying investments are rated investment grade. The notes have a stated coupon and provide a return based on the return of the underlying portfolios and the level of leverage. The notes are accounted for as available for sale fixed maturity securities with bifurcated embedded derivatives (total return swaps). Changes in the value of the fixed maturity securities are reported in Stockholders' Equity under the heading [Accumulated Other Comprehensive Income](#). Changes in the market value of the embedded total return swaps are included in current period earnings in [Realized investment gains \(losses\), net](#). While the fair value of the embedded derivatives associated with these investments have declined in recent quarters due to increased credit spreads in the financial markets, we believe the investment fundamentals remain sound, and the ultimate value that will be realized from these investments is greater than reflected by the current fair value of the embedded derivatives.

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While delinquency rates on commercial mortgages have been stable in recent years, we recognized several market factors that influenced our investment decisions on commercial mortgage-backed securities issued in 2006 and 2007, including less stringent loan underwriting, higher levels of leverage, and rapid real estate price appreciation. The following tables set forth the amortized cost and fair value of our commercial mortgage-backed securities attributable to the Closed Block Business as of the dates indicated, by credit quality and by year of issuance (vintage).

| Vintage  | Amortized Cost as of March 31, 2008<br>Lowest Rating Agency Rating |              |              |              |                                     | Total<br>Amortized<br>Cost | Total<br>Amortized<br>Cost as of<br>December 31,<br>2007 |
|--|--|--------------|--------------|--------------|-------------------------------------|----------------------------|--|
|  | AAA  | AA           | A            | BBB          | BB and<br>below<br>(\$ in millions) |                            |  |
| 2008   | \$ 9   | \$           | \$           | \$           | \$                                  | \$ 9                       | \$   |
| 2007   | 268  |              | 19           |              |                                     | 287                        | 277  |
| 2006   | 1,138  |              |              |              |                                     | 1,138                      | 1,207  |
| 2005   | 1,391  |              |              |              |                                     | 1,391                      | 1,375  |
| 2004   | 396  |              |              |              |                                     | 396                        | 397  |
| 2003 & Prior                                       | 888  | 48           | 52           | 21           |                                     | 1,009                      | 1,009  |
| <b>Total commercial mortgage-backed securities</b> | <b>\$ 4,090</b>  | <b>\$ 48</b> | <b>\$ 71</b> | <b>\$ 21</b> | <b>\$</b>                           | <b>\$ 4,230</b>            | <b>\$ 4,265</b>  |

| Vintage  | Fair Value as of March 31, 2008<br>Lowest Rating Agency Rating |              |              |              |                                  | Total Fair<br>Value | Total Fair<br>Value as of<br>December 31,<br>2007 |
|--|--|--------------|--------------|--------------|----------------------------------|---------------------|---|
|  | AAA  | AA           | A            | BBB          | BB and<br>below<br>(in millions) |                     |   |
| 2008   | \$ 9   | \$           | \$           | \$           | \$                               | \$ 9                | \$  |
| 2007   | 265  |              | 11           |              |                                  | 276                 | 279   |
| 2006   | 1,121  |              |              |              |                                  | 1,121               | 1,221   |
| 2005   | 1,348  |              |              |              |                                  | 1,348               | 1,375   |
| 2004   | 379  |              |              |              |                                  | 379                 | 392   |
| 2003 & Prior                                       | 886  | 47           | 48           | 21           |                                  | 1,002               | 1,023   |
| <b>Total commercial mortgage-backed securities</b> | <b>\$ 4,008</b>  | <b>\$ 47</b> | <b>\$ 59</b> | <b>\$ 21</b> | <b>\$</b>                        | <b>\$ 4,135</b>     | <b>\$ 4,290</b>                                   |

Loan to value and debt service coverage ratios are measures commonly used to assess the quality of commercial mortgage-backed securities. See above for a description of these ratios. The following tables set forth the amortized cost and fair value of our commercial mortgage-backed securities attributable to the Closed Block Business as of March 31, 2008 by loan to value and debt service coverage ratios.

| Commercial mortgage-backed securities by loan to value ratio: | March 31, 2008                     |               |
|---|------------------------------------|---------------|
|   | Amortized<br>Cost<br>(in millions) | Fair<br>Value |
| 0% - 50%  | \$ 99                              | \$ 92         |
| 50% - 60%   | 194                                | 189           |
| 60% - 70%   | 2,015                              | 1,975         |
| 70% - 80%   | 1,922                              | 1,879         |
| 80% - 90%   |                                    |               |
| 90% - 100%  |                                    |               |

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Greater than 100%

|       |          |          |
|-------|----------|----------|
| Total | \$ 4,230 | \$ 4,135 |
|-------|----------|----------|



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|   | March 31, 2008 |            |
|---|----------------|------------|
|   | Amortized Cost | Fair Value |
| (in millions)   |                |            |
| Commercial mortgage-backed securities by debt service coverage ratio: |                |            |
| Greater than 1.8 times  | \$ 483         | \$ 473     |
| 1.5 times 1.8 times   | 2,436          | 2,361      |
| 1.2 times 1.5 times   | 1,311          | 1,301      |
| 1.0 times 1.2 times   |                |            |
| Less than 1.0 times   |                |            |
| Total   | \$ 4,230       | \$ 4,135   |

As of March 31, 2008, based on amortized cost, the weighted average loan to value and debt service coverage ratios of commercial mortgage-backed securities attributable to the Closed Block Business is 68% and 1.59 times, respectively. The weighted average estimated subordination percentage of available for sale commercial mortgage-backed securities attributable to the Closed Block Business was 32% as of March 31, 2008. The subordination percentage represents the current weighted average estimated percentage of the capital structure subordinated to our investment holding that is available to absorb losses before the security incurs the first dollar loss of principal. The estimated subordination percentage includes an adjustment for that portion of the capital structure which has been effectively defeased by US Treasury securities. As of March 31, 2008, based on amortized cost, approximately 89% of the commercial mortgage-backed securities attributable to the Closed Block Business have estimated credit subordination percentages of 20% or more, and 57% have estimated credit subordination percentages of 30% or more.

*Fixed Maturity Securities Credit Quality*

The Securities Valuation Office, or SVO, of the National Association of Insurance Commissioners, or NAIC, evaluates the investments of insurers for regulatory reporting purposes and assigns fixed maturity securities to one of six categories called NAIC Designations. NAIC designations of 1 or 2 include fixed maturities considered investment grade, which include securities rated Baa3 or higher by Moody's or BBB- or higher by Standard & Poor's. NAIC Designations of 3 through 6 are referred to as below investment grade, which include securities rated Ba1 or lower by Moody's and BB+ or lower by Standard & Poor's. As a result of time lags between the funding of investments, the finalization of legal documents and the completion of the SVO filing process, the fixed maturity portfolio generally includes securities that have not yet been rated by the SVO as of each balance sheet date. Pending receipt of SVO ratings, the categorization of these securities by NAIC designation is based on the expected ratings indicated by internal analysis.

Investments of our international insurance companies are not subject to NAIC guidelines. Investments of our Japanese insurance operations are regulated locally by the Financial Services Agency, an agency of the Japanese government. The Financial Services Agency has its own investment quality criteria and risk control standards. Our Japanese insurance companies comply with the Financial Services Agency's credit quality review and risk monitoring guidelines. The credit quality ratings of the non-U.S. dollar denominated investments of our Japanese insurance companies are based on ratings assigned by Moody's, Standard & Poor's, or rating equivalents based on ratings assigned by Japanese credit ratings agencies.

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Certain of the Company's fixed maturity investments are supported by guarantees from monoline bond insurers. The following table sets forth the amortized cost and fair value of our fixed maturity investments supported by guarantees from monoline bond insurers as of the dates indicated.

|  | March 31, 2008                   |               |                          |               |
|--|----------------------------------|---------------|--------------------------|---------------|
|  | Financial Services<br>Businesses |               | Closed Block<br>Business |               |
|  | Amortized<br>Cost                | Fair<br>Value | Amortized<br>Cost        | Fair<br>Value |
|  | (in millions)                    |               |                          |               |
| <b>Fixed maturities guaranteed by monoline bond insurers</b> |                                  |               |                          |               |
| Asset-backed securities:                                     |                                  |               |                          |               |
| Collateralized by sub-prime mortgages                        | \$ 1,339                         | \$ 1,135      | \$ 814                   | \$ 754        |
| Other  | 526                              | 500           | 168                      | 166           |
| Total asset-backed securities                                | 1,865                            | 1,635         | 982                      | 920           |
| Municipal bonds  | 420                              | 447           | 123                      | 138           |
| Total  | \$ 2,285                         | \$ 2,082      | \$ 1,105                 | \$ 1,058      |

|  | December 31, 2007                |               |                          |               |
|--|----------------------------------|---------------|--------------------------|---------------|
|  | Financial Services<br>Businesses |               | Closed Block<br>Business |               |
|  | Amortized<br>Cost                | Fair<br>Value | Amortized<br>Cost        | Fair<br>Value |
|  | (in millions)                    |               |                          |               |
| <b>Fixed maturities guaranteed by monoline bond insurers</b> |                                  |               |                          |               |
| Asset-backed securities:                                     |                                  |               |                          |               |
| Collateralized by sub-prime mortgages                        | \$ 1,623                         | \$ 1,490      | \$ 1,060                 | \$ 1,024      |
| Other  | 607                              | 622           | 184                      | 186           |
| Total asset-backed securities                                | 2,230                            | 2,112         | 1,244                    | 1,210         |
| Municipal bonds  | 421                              | 447           | 119                      | 132           |
| Commercial mortgage- backed securities                       | 5                                | 5             | 5                        | 5             |
| Total  | \$ 2,656                         | \$ 2,564      | \$ 1,368                 | \$ 1,347      |

As of March 31, 2008, on an amortized cost basis, \$2.3 billion, or 2%, of general account available for sale fixed maturity investments attributable to the Financial Services Businesses, and \$1.1 billion, or 2%, of fixed maturity investments attributable to the Closed Block Business were supported by guarantees from monoline bond insurers. As of March 31, 2008, 99% of these investments had A credit ratings or higher, reflecting the credit quality of the monoline bond insurers. Management estimates, taking into account the structure and credit quality of the underlying investments and giving no effect to the support of these securities by guarantees from monoline bond insurers, that 76% of the \$2.3 billion total attributable to the Financial Services Businesses as of March 31, 2008 (based upon amortized cost) would have investment grade credit ratings, including 66% of the asset-backed securities collateralized by sub-prime mortgages, 80% of the other asset-backed securities, and all of the municipal bonds. As of March 31, 2008, the bond insurance is provided by five insurance companies, with no company representing more than 31% of the overall amortized cost of the securities supported by bond insurance attributable to the Financial Services Businesses. For additional information regarding the use of credit derivatives to hedge certain monoline exposures see Credit Derivative Exposure to Public Fixed Maturities, below.

Management estimates, taking into account the structure and credit quality of the underlying investments and giving no effect to the support of these securities by guarantees from monoline bond insurers, that 88% of the \$1.1 billion attributable to the Closed Block Business as of March 31, 2008 (based upon amortized cost) would have investment grade credit ratings, including 85% of the asset-backed securities

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collateralized by sub-prime mortgages, 94% of the other asset-backed securities, and all of the municipal bonds. As of March 31, 2008, the bond insurance is provided by five insurance companies, with no company representing more than 34% of the overall amortized cost of the securities supported by bond insurance attributable to the Closed Block Business.

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The amortized cost of our public and private below investment grade fixed maturities attributable to the Financial Services Businesses totaled \$7.5 billion, or 6%, of the total fixed maturities as of March 31, 2008 and \$7.5 billion, or 7%, of the total fixed maturities as of December 31, 2007. Below investment grade fixed maturities represented 12% of the gross unrealized losses attributable to the Financial Services Businesses as of March 31, 2008 and December 31, 2007, respectively.

The amortized cost of our public and private below investment grade fixed maturities attributable to the Closed Block Business totaled \$5.5 billion, or 12%, of the total fixed maturities as of March 31, 2008 and \$5.7 billion, or 12%, of the total fixed maturities as of December 31, 2007. Below investment grade fixed maturities represented 14% of the gross unrealized losses attributable to the Closed Block Business as of March 31, 2008, compared to 18% of gross unrealized losses as of December 31, 2007.

*Public Fixed Maturities Credit Quality*

The following table sets forth our public fixed maturity portfolios by NAIC rating attributable to the Financial Services Businesses as of the dates indicated.

| (1)(2)<br>NAIC<br>Designation | Rating Agency Equivalent             | March 31, 2008    |                                 |                                  | December 31, 2007              |                   |                                 |                                  |                  |
|-------------------------------|--------------------------------------|-------------------|---------------------------------|----------------------------------|--------------------------------|-------------------|---------------------------------|----------------------------------|------------------|
|                               |                                      | Amortized<br>Cost | Gross<br>Unrealized<br>Gains(3) | Gross<br>Unrealized<br>Losses(3) | Fair<br>Value<br>(in millions) | Amortized<br>Cost | Gross<br>Unrealized<br>Gains(3) | Gross<br>Unrealized<br>Losses(3) | Fair<br>Value    |
| 1                             | Aaa, Aa,A                            | \$ 79,733         | \$ 2,418                        | \$ 1,958                         | \$ 80,193                      | \$ 74,678         | \$ 2,036                        | \$ 1,184                         | \$ 75,530        |
| 2                             | Baa                                  | 14,811            | 443                             | 795                              | 14,459                         | 13,573            | 490                             | 351                              | 13,712           |
|                               | Subtotal Investment Grade            | 94,544            | 2,861                           | 2,753                            | 94,652                         | 88,251            | 2,526                           | 1,535                            | 89,242           |
| 3                             | Ba                                   | 2,976             | 52                              | 192                              | 2,836                          | 2,830             | 68                              | 102                              | 2,796            |
| 4                             | B                                    | 1,586             | 24                              | 139                              | 1,471                          | 1,681             | 38                              | 82                               | 1,637            |
| 5                             | C and lower                          | 129               | 3                               | 14                               | 118                            | 115               | 5                               | 6                                | 114              |
| 6                             | In or near default                   | 28                | 7                               | 2                                | 33                             | 34                | 5                               | 1                                | 38               |
|                               | Subtotal Below Investment Grade      | 4,719             | 86                              | 347                              | 4,458                          | 4,660             | 116                             | 191                              | 4,585            |
|                               | <b>Total Public Fixed Maturities</b> | <b>\$ 99,263</b>  | <b>\$ 2,947</b>                 | <b>\$ 3,100</b>                  | <b>\$ 99,110</b>               | <b>\$ 92,911</b>  | <b>\$ 2,642</b>                 | <b>\$ 1,726</b>                  | <b>\$ 93,827</b> |

- (1) Reflects equivalent ratings for investments of the international insurance operations that are not rated by U.S. insurance regulatory authorities.
- (2) Includes, as of March 31, 2008 and December 31, 2007, respectively, 16 securities with amortized cost of \$29 million (fair value, \$22 million) and 14 securities with amortized cost of \$49 million (fair value, \$46 million) that have been categorized based on expected NAIC designations pending receipt of SVO ratings.
- (3) Includes \$38 million of gross unrealized gains and \$50 million gross unrealized losses as of March 31, 2008, compared to \$25 million of gross unrealized gains and \$39 million of gross unrealized losses as of December 31, 2007 on securities classified as held to maturity that are not reflected in other comprehensive income.

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The following table sets forth our public fixed maturity portfolios by NAIC rating attributable to the Closed Block Business as of the dates indicated.

| (1)                           | NAIC Designation                | Rating Agency Equivalent | March 31, 2008 |                        |                         | December 31, 2007 |                |                        |                         |            |
|-------------------------------|---------------------------------|--------------------------|----------------|------------------------|-------------------------|-------------------|----------------|------------------------|-------------------------|------------|
|                               |                                 |                          | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value        | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value |
|                               |                                 |                          |                |                        |                         | (in millions)     |                |                        |                         |            |
| 1                             | Aaa, Aa, A                      |                          | \$ 25,398      | \$ 602                 | \$ 1,202                | \$ 24,798         | \$ 27,437      | \$ 618                 | \$ 578                  | \$ 27,477  |
| 2                             | Baa                             |                          | 6,122          | 175                    | 239                     | 6,058             | 5,915          | 199                    | 101                     | 6,013      |
|                               | Subtotal Investment Grade       |                          | 31,520         | 777                    | 1,441                   | 30,856            | 33,352         | 817                    | 679                     | 33,490     |
| 3                             | Ba                              |                          | 2,011          | 32                     | 90                      | 1,953             | 1,992          | 46                     | 61                      | 1,977      |
| 4                             | B                               |                          | 1,405          | 13                     | 92                      | 1,326             | 1,588          | 23                     | 58                      | 1,553      |
| 5                             | C and lower                     |                          | 177            | 5                      | 20                      | 162               | 131            | 5                      | 8                       | 128        |
| 6                             | In or near default              |                          | 18             | 1                      | 1                       | 18                | 19             | 1                      |                         | 20         |
|                               | Subtotal Below Investment Grade |                          | 3,611          | 51                     | 203                     | 3,459             | 3,730          | 75                     | 127                     | 3,678      |
| Total Public Fixed Maturities |                                 |                          | \$ 35,131      | \$ 828                 | \$ 1,644                | \$ 34,315         | \$ 37,082      | \$ 892                 | \$ 806                  | \$ 37,168  |

(1) Includes, as of March 31, 2008 and December 31, 2007, respectively, 17 securities with amortized cost of \$48 million (fair value, \$44 million) and 14 securities with amortized cost of \$45 million (fair value, \$47 million) that have been categorized based on expected NAIC designations pending receipt of SVO ratings.

*Private Fixed Maturities Credit Quality*

The following table sets forth our private fixed maturity portfolios by NAIC rating attributable to the Financial Services Businesses as of the dates indicated.

| (1)(2)                         | NAIC Designation                | Rating Agency Equivalent | March 31, 2008 |                           |                            | December 31, 2007 |                |                           |                            |            |
|--------------------------------|---------------------------------|--------------------------|----------------|---------------------------|----------------------------|-------------------|----------------|---------------------------|----------------------------|------------|
|                                |                                 |                          | Amortized Cost | Gross Unrealized Gains(3) | Gross Unrealized Losses(3) | Fair Value        | Amortized Cost | Gross Unrealized Gains(3) | Gross Unrealized Losses(3) | Fair Value |
|                                |                                 |                          |                |                           |                            | (in millions)     |                |                           |                            |            |
| 1                              | Aaa, Aa, A                      |                          | \$ 7,062       | \$ 237                    | \$ 135                     | \$ 7,164          | \$ 7,139       | \$ 230                    | \$ 84                      | \$ 7,285   |
| 2                              | Baa                             |                          | 10,874         | 345                       | 255                        | 10,964            | 10,595         | 344                       | 118                        | 10,821     |
|                                | Subtotal Investment Grade       |                          | 17,936         | 582                       | 390                        | 18,128            | 17,734         | 574                       | 202                        | 18,106     |
| 3                              | Ba                              |                          | 1,638          | 51                        | 33                         | 1,656             | 1,637          | 49                        | 26                         | 1,660      |
| 4                              | B                               |                          | 747            | 6                         | 27                         | 726               | 738            | 6                         | 12                         | 732        |
| 5                              | C and lower                     |                          | 195            | 5                         | 6                          | 194               | 319            | 8                         | 4                          | 323        |
| 6                              | In or near default              |                          | 211            | 13                        | 18                         | 206               | 147            | 23                        |                            | 170        |
|                                | Subtotal Below Investment Grade |                          | 2,791          | 75                        | 84                         | 2,782             | 2,841          | 86                        | 42                         | 2,885      |
| Total Private Fixed Maturities |                                 |                          | \$ 20,727      | \$ 657                    | \$ 474                     | \$ 20,910         | \$ 20,575      | \$ 660                    | \$ 244                     | \$ 20,991  |

- (1) Reflects equivalent ratings for investments of the international insurance operations that are not rated by U.S. insurance regulatory authorities.
- (2) Includes, as of March 31, 2008 and December 31, 2007, respectively, 215 securities with amortized cost of \$2,520 million (fair value, \$2,466 million) and 182 securities with amortized cost of \$2,257 million (fair value, \$2,273 million) that have been categorized based on expected NAIC designations pending receipt of SVO ratings.

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- (3) Includes \$19 million of gross unrealized gains and \$1 million of gross unrealized losses as of March 31, 2008, compared to \$11 million of gross unrealized gains and \$2 million of gross unrealized losses as of December 31, 2007 on securities classified as held to maturity that are not reflected in other comprehensive income.

The following table sets forth our private fixed maturity portfolios by NAIC rating attributable to the Closed Block Business as of the dates indicated.

| (1)<br>NAIC<br>Designation | Rating Agency Equivalent        | March 31, 2008    |                              |                               |               | December 31, 2007 |                              |                               |               |
|----------------------------|---------------------------------|-------------------|------------------------------|-------------------------------|---------------|-------------------|------------------------------|-------------------------------|---------------|
|                            |                                 | Amortized<br>Cost | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Fair<br>Value | Amortized<br>Cost | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Fair<br>Value |
|                            |                                 |                   |                              |                               |               |                   |                              |                               |               |
|                            |                                 |                   |                              |                               |               |                   |                              |                               |               |
| 1                          | Aaa, Aa, A                      | \$ 3,216          | \$ 253                       | \$ 30                         | \$ 3,439      | \$ 3,197          | \$ 219                       | \$ 23                         | \$ 3,393      |
| 2                          | Baa                             | 6,518             | 373                          | 58                            | 6,833         | 6,495             | 363                          | 28                            | 6,830         |
|                            | Subtotal Investment Grade       | 9,734             | 626                          | 88                            | 10,272        | 9,692             | 582                          | 51                            | 10,223        |
| 3                          | Ba                              | 1,300             | 69                           | 24                            | 1,345         | 1,246             | 63                           | 21                            | 1,288         |
| 4                          | B                               | 420               | 6                            | 11                            | 415           | 442               | 6                            | 5                             | 443           |
| 5                          | C and lower                     | 100               | 5                            | 2                             | 103           | 214               | 8                            | 4                             | 218           |
| 6                          | In or near default              | 98                | 17                           | 7                             | 108           | 56                | 18                           |                               | 74            |
|                            | Subtotal Below Investment Grade | 1,918             | 97                           | 44                            | 1,971         | 1,958             | 95                           | 30                            | 2,023         |
|                            | Total Private Fixed Maturities  | \$ 11,652         | \$ 723                       | \$ 132                        | \$ 12,243     | \$ 11,650         | \$ 677                       | \$ 81                         | \$ 12,246     |

- (1) Includes, as of March 31, 2008 and December 31, 2007, respectively, 119 securities with amortized cost of \$1,815 million (fair value, \$1,805 million) and 106 securities with amortized cost of \$1,578 million (fair value, \$1,582 million) that have been categorized based on expected NAIC designations pending receipt of SVO ratings.

*Credit Derivative Exposure to Public Fixed Maturities*

In addition to the credit exposure from public fixed maturities noted above, we sell credit derivatives to enhance the return on our investment portfolio by creating credit exposure similar to an investment in public fixed maturity cash instruments.

In a credit derivative we sell credit protection on an identified name, or a basket of names in a first to default structure, and in return receive a quarterly premium. With single name credit default derivatives, this premium or credit spread generally corresponds to the difference between the yield on the referenced name's public fixed maturity cash instruments and swap rates, at the time the agreement is executed. With first-to-default baskets, because of the additional credit risk inherent in a basket of named credits, the premium generally corresponds to a high proportion of the sum of the credit spreads of the names in the basket. If there is an event of default by the referenced name or one of the referenced names in a basket, as defined by the agreement, then we are obligated to pay the counterparty the referenced amount of the contract and receive in return the referenced defaulted security or similar security. Subsequent defaults on the remaining names within such instruments require no further payment to counterparties.

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The majority of referenced names in the credit derivatives where we have sold credit protection, as well as all the counterparties to these agreements, are investment grade credit quality and our credit derivatives generally have maturities of five years or less. As of March 31, 2008 and December 31, 2007, we had \$1.8 billion and \$1.5 billion, respectively, in outstanding notional amounts of credit derivative contracts where we have sold credit protection. The Financial Services Businesses had \$1.4 billion and \$1.1 billion of outstanding notional amounts as of March 31, 2008 and December 31, 2007, respectively. The Closed Block Business had \$343 million and \$328 million of outstanding notional amounts, as March 31, 2008 and December 31, 2007, respectively. Credit



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derivative contracts are recorded at fair value with changes in fair value, including the premium received, recorded in Realized investment gains (losses), net. The premium received for the credit derivatives we sell attributable to the Financial Services Businesses was \$3 million and \$3 million for the three months ended March 31, 2008 and 2007, respectively, and is included in adjusted operating income as an adjustment to Realized investment gains (losses), net over the life of the derivative.

The following table sets forth our exposure where we have sold credit protection through credit derivatives in the Financial Services Businesses by NAIC rating of the underlying credits as of the dates indicated.

| (1)<br>NAIC<br>Designation | Rating Agency Equivalent        | March 31, 2008 |                             | December 31, 2007 |            |
|----------------------------|---------------------------------|----------------|-----------------------------|-------------------|------------|
|                            |                                 | Notional       | Fair Value<br>(in millions) | Notional          | Fair Value |
| 1                          | Aaa, Aa, A                      | \$ 647         | \$ (13)                     | \$ 392            | \$ (4)     |
| 2                          | Baa                             | 647            | (75)                        | 672               | (65)       |
|                            | Subtotal Investment Grade       | 1,294          | (88)                        | 1,064             | (69)       |
| 3                          | Ba                              | 20             | (2)                         | 20                | (1)        |
| 4                          | B                               | 38             | (10)                        | 38                | (3)        |
| 5                          | C and lower                     | 70             | (12)                        | 20                | (2)        |
| 6                          | In or near default              |                |                             |                   |            |
|                            | Subtotal Below Investment Grade | 128            | (24)                        | 78                | (6)        |
| Total                      |                                 | \$ 1,422       | \$ (112)                    | \$ 1,142          | \$ (75)    |

- (1) First-to-default credit swap baskets, which may include credits of varying qualities, are grouped above based on the lowest credit in the basket. However, such basket swaps may entail greater credit risk than the rating level of the lowest credit.

The following table sets forth our exposure where we have sold credit protection through credit derivatives in the Closed Block Business portfolios by NAIC rating of the underlying credits as of the dates indicated.

| (1)<br>NAIC<br>Designation | Rating Agency Equivalent        | March 31, 2008 |                             | December 31, 2007 |            |
|----------------------------|---------------------------------|----------------|-----------------------------|-------------------|------------|
|                            |                                 | Notional       | Fair Value<br>(in millions) | Notional          | Fair Value |
| 1                          | Aaa, Aa, A                      | \$ 263         | \$ (3)                      | \$ 253            | \$ (1)     |
| 2                          | Baa                             | 75             | (2)                         | 70                |            |
|                            | Subtotal Investment Grade       | 338            | (5)                         | 323               | (1)        |
| 3                          | Ba                              |                |                             |                   |            |
| 4                          | B                               |                |                             |                   |            |
| 5                          | C and lower                     | 5              | (2)                         | 5                 | (1)        |
| 6                          | In or near default              |                |                             |                   |            |
|                            | Subtotal Below Investment Grade | 5              | (2)                         | 5                 | (1)        |
| Total                      |                                 | \$ 343         | \$ (7)                      | \$ 328            | \$ (2)     |

- (1) First-to-default credit swap baskets, which may include credits of varying qualities, are grouped above based on the lowest credit in the basket. However, such basket swaps may entail greater credit risk than the rating level of the lowest credit.

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In addition to selling credit protection, we have purchased credit protection using credit derivatives in order to hedge specific credit exposures in our investment portfolio, including certain monoline exposures, as discussed above. As of March 31, 2008 and December 31, 2007, respectively, the Financial Services Businesses had \$946 million and \$214 million of outstanding notional amounts, reported at fair value as a \$51 million asset and a \$1 million asset. As of March 31, 2008 and December 31, 2007, respectively, the Closed Block Business had \$296 million and \$205 million of outstanding notional amounts, reported at fair value as an asset of \$29 million and \$5 million. The premium paid for the credit derivatives we purchase attributable to the Financial Services Businesses was \$3 million and \$0 million for the three months ended March 31, 2008 and 2007, respectively, and is included in adjusted operating income as an adjustment to Realized investment gains (losses), net over the life of the derivative.

*Unrealized Losses from Fixed Maturity Securities*

The following table sets forth the amortized cost and gross unrealized losses of fixed maturity securities attributable to the Financial Services Businesses where the estimated fair value had declined and remained below amortized cost by 15% or more, but less than 20% for the following timeframes:

|  | March 31, 2008 |                         | December 31, 2007 |                         |
|--|----------------|-------------------------|-------------------|-------------------------|
|  | Amortized Cost | Gross Unrealized Losses | Amortized Cost    | Gross Unrealized Losses |
|  | (in millions)  |                         |                   |                         |
| Less than three months                             | \$ 2,511       | \$ 427                  | \$ 619            | \$ 105                  |
| Three months or greater but less than six months   | 175            | 32                      | 76                | 13                      |
| Six months or greater but less than nine months    | 12             | 2                       | 9                 | 2                       |
| Nine months or greater but less than twelve months | 5              | 1                       |                   |                         |
| Greater than twelve months                         | 11             | 2                       | 10                | 2                       |
| Total  | \$ 2,714       | \$ 464                  | \$ 714            | \$ 122                  |

The following table sets forth the amortized cost and gross unrealized losses of fixed maturity securities attributable to the Financial Services Businesses where the estimated fair value had declined and remained below amortized cost by 20% or more for the following timeframes:

|  | March 31, 2008 |                         | December 31, 2007 |                         |
|--|----------------|-------------------------|-------------------|-------------------------|
|  | Amortized Cost | Gross Unrealized Losses | Amortized Cost    | Gross Unrealized Losses |
|  | (in millions)  |                         |                   |                         |
| Less than three months                             | \$ 3,319       | \$ 860                  | \$ 769            | \$ 213                  |
| Three months or greater but less than six months   | 720            | 247                     | 265               | 91                      |
| Six months or greater but less than nine months    |                |                         |                   |                         |
| Nine months or greater but less than twelve months |                |                         |                   |                         |
| Greater than twelve months                         |                |                         |                   |                         |
| Total  | \$ 4,039       | \$ 1,107                | \$ 1,034          | \$ 304                  |

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The gross unrealized losses were primarily concentrated in asset-backed securities and the services, finance and manufacturing sectors of our corporate securities as of March 31, 2008 and were primarily concentrated in asset-backed securities as of December 31, 2007. We have not recognized the gross unrealized losses shown in the tables above as other-than-temporary impairments. See [Other-Than-Temporary Impairments of Fixed Maturity Securities](#) for a discussion of the factors we consider in making these determinations.

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The following table sets forth the amortized cost and gross unrealized losses of fixed maturity securities attributable to the Closed Block Business where the estimated fair value had declined and remained below amortized cost by 15% or more, but less than 20% for the following timeframes:

|  | March 31, 2008 |                         | December 31, 2007 |                         |
|--|----------------|-------------------------|-------------------|-------------------------|
|  | Amortized Cost | Gross Unrealized Losses | Amortized Cost    | Gross Unrealized Losses |
|  | (in millions)  |                         |                   |                         |
| Less than three months                             | \$ 1,125       | \$ 195                  | \$ 278            | \$ 46                   |
| Three months or greater but less than six months   | 108            | 19                      | 34                | 6                       |
| Six months or greater but less than nine months    | 5              | 1                       |                   |                         |
| Nine months or greater but less than twelve months |                |                         |                   |                         |
| Greater than twelve months                         |                |                         |                   |                         |
| Total  | \$ 1,238       | \$ 215                  | \$ 312            | \$ 52                   |

The following table sets forth the amortized cost and gross unrealized losses of fixed maturity securities attributable to the Closed Block Business where the estimated fair value had declined and remained below amortized cost by 20% or more for the following timeframes:

|  | March 31, 2008 |                         | December 31, 2007 |                         |
|--|----------------|-------------------------|-------------------|-------------------------|
|  | Amortized Cost | Gross Unrealized Losses | Amortized Cost    | Gross Unrealized Losses |
|  | (in millions)  |                         |                   |                         |
| Less than three months                             | \$ 1,910       | \$ 532                  | \$ 369            | \$ 88                   |
| Three months or greater but less than six months   | 476            | 158                     | 99                | 31                      |
| Six months or greater but less than nine months    |                |                         |                   |                         |
| Nine months or greater but less than twelve months |                |                         |                   |                         |
| Greater than twelve months                         |                |                         |                   |                         |
| Total  | \$ 2,386       | \$ 690                  | \$ 468            | \$ 119                  |

The gross unrealized losses were primarily concentrated in asset-backed securities and the manufacturing and services sectors of our corporate securities as of March 31, 2008 while the gross unrealized losses were primarily concentrated in asset-backed securities as of December 31, 2007. We have not recognized the gross unrealized losses shown in the tables above as other-than-temporary impairments. See

Other-Than-Temporary Impairments of Fixed Maturity Securities for a discussion of the factors we consider in making these determinations.

*Other-Than-Temporary Impairments of Fixed Maturity Securities*

We maintain separate monitoring processes for public and private fixed maturities and create watch lists to highlight securities that require special scrutiny and management. Our public fixed maturity asset managers formally review all public fixed maturity holdings on a quarterly basis and more frequently when necessary to identify potential credit deterioration whether due to ratings downgrades, unexpected price variances, and/or industry specific concerns.

For private placements our credit and portfolio management processes help ensure prudent controls over valuation and management. We have separate pricing and authorization processes to establish checks and balances for new investments. We apply consistent standards of credit analysis and due diligence for all transactions, whether they originate through our own in-house origination staff or through agents. Our regional offices closely monitor the portfolios in their regions. We set all valuation standards centrally, and we assess the fair value of all investments quarterly.

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Fixed maturity securities classified as held to maturity are those securities where we have the intent and ability to hold the securities until maturity. These securities are reflected at amortized cost in our consolidated statements of financial position. Other fixed maturity securities are considered available for sale, and, as a result, we record unrealized gains and losses to the extent that amortized cost is different from estimated fair value. All held to maturity securities and all available for sale securities with unrealized losses are subject to our review to identify other-than-temporary impairments in value. In evaluating whether a decline in value is other-than-temporary, we consistently consider several factors including, but not limited to, the following:

the extent and the duration of the decline, including, but not limited to, the following general guidelines;

declines in value greater than 20%, maintained for six months or greater;

declines in value greater than 15%, maintained for more than one year on below investment grade bonds; and

declines in value less than six months where there has been a precipitous (generally 50% or greater) decline in value the reasons for the decline in value (credit event, currency or interest rate related, including spread widening);

our ability and intent to hold our investment for a period of time to allow for a recovery of value, including debt securities managed by independent third parties where we do not have management discretion; and

the financial condition of and near-term prospects of the issuer.

In addition, for our impairment review of asset-backed fixed maturity securities with a credit rating below AA, we forecast the prospective future cash flows of the security and determine if the present value of those cash flows, discounted using the effective yield of the most recent interest accrual rate, has decreased from the previous reporting period. When a decrease from the prior reporting period has occurred and the security's market value is less than its carrying value, an other-than-temporary impairment is recognized by writing the security down to fair value.

When we determine that there is an other-than-temporary impairment, we record a writedown to estimated fair value, which reduces the cost basis. The new cost basis of an impaired security is not adjusted for subsequent increases in estimated fair value. In periods subsequent to the recognition of an other-than-temporary impairment, the impaired security is accounted for as if it had been purchased on the measurement date of the impairment. Accordingly, the discount (or reduced premium) based on the new cost basis is accreted into net investment income, and included in adjusted operating income in future periods based upon the amount and timing of the expected future cash flows of the security, if the recoverable value of the investment based on those cash flows is greater than the carrying value of the investment after the impairment. Estimated fair values for fixed maturities, other than private placement securities, are generally based on quoted market prices or prices obtained from independent pricing services. For private fixed maturities, fair value is determined typically by using a discounted cash flow model, which relies upon the average of spread surveys collected from private market intermediaries who are active in both primary and secondary transactions and takes into account, among other factors, the credit quality of the issuer and the reduced liquidity associated with private placements. In determining the fair value of certain securities, including those that are distressed, the discounted cash flow model may also use unobservable inputs, which reflect our own assumptions about the inputs market participants would use in pricing the asset. Impairments on fixed maturity securities are included in Realized investment gains (losses), net and are excluded from adjusted operating income. For further information regarding the fair value methodology used in determining our other-than-temporary impairments, see Valuation of Assets and Liabilities Fair Value of Assets and Liabilities Valuation of Fixed Maturities, above.

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Other-than-temporary impairments of fixed maturity securities attributable to the Financial Services Businesses were \$376 million and \$11 million for the three months ended March 31, 2008 and 2007, respectively. Included in the other-than-temporary impairments of fixed maturities attributable to the Financial



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Services Businesses in 2008 were \$290 million of other-than-temporary impairments on asset-backed securities collateralized by sub-prime mortgages. Other-than-temporary impairments of fixed maturity securities attributable to the Closed Block Business were \$151 million and \$7 million for the three months ended March 31, 2008 and 2007, respectively. Included in the other-than-temporary impairments of fixed maturities attributable to the Closed Block Business in 2008 were \$113 million of other-than-temporary impairments on asset-backed securities collateralized by sub-prime mortgages. For a further discussion of impairments, see *Realized Investment Gains and Losses* above.

**Trading account assets supporting insurance liabilities**

Certain products included in the retirement business we acquired from CIGNA, as well as certain products included in the International Insurance segment, are experience-rated, meaning that the investment results associated with these products will ultimately accrue to contractholders. The investments supporting these experience-rated products, excluding commercial loans, are classified as trading. These trading investments are reflected on the balance sheet as *Trading account assets supporting insurance liabilities*, at fair value. *Realized and unrealized gains and losses* for these investments are reported in *Asset management fees and other income*. *Investment income* for these investments is reported in *Net investment income*. The following table sets forth the composition of this portfolio as of the dates indicated.

|   | March 31, 2008 |            | December 31, 2007 |            |
|---|----------------|------------|-------------------|------------|
|   | Amortized Cost | Fair Value | Amortized Cost    | Fair Value |
|   | (in millions)  |            |                   |            |
| Short-term Investments and Cash Equivalents                   | \$ 468         | \$ 468     | \$ 554            | \$ 554     |
| Fixed Maturities:   |                |            |                   |            |
| Corporate Securities  | 8,125          | 8,103      | 7,584             | 7,547      |
| Commercial Mortgage-Backed                                    | 2,505          | 2,470      | 2,625             | 2,644      |
| Asset-Backed Securities                                       | 1,239          | 1,122      | 1,266             | 1,207      |
| Residential Mortgage-Backed                                   | 965            | 949        | 1,147             | 1,136      |
| Foreign Government  | 388            | 394        | 347               | 354        |
| U.S. Government   | 246            | 243        | 82                | 83         |
| Total Fixed Maturities  | 13,468         | 13,281     | 13,051            | 12,971     |
| Equity Securities   | 1,097          | 895        | 1,001             | 948        |
| Total trading account assets supporting insurance liabilities | \$ 15,033      | \$ 14,644  | \$ 14,606         | \$ 14,473  |

As of March 31, 2008, as a percentage of amortized cost, 75% of the portfolio was comprised of publicly traded securities, compared to 74% of the portfolio as of December 31, 2007. As of March 31, 2008, 91% of the fixed maturity portfolio was classified as investment grade compared to 92% as of December 31, 2007. As of March 31, 2008, 75% of the residential mortgage-backed securities were publicly traded agency pass-through securities, which are supported by implicit or explicit government guarantees and all have credit ratings of AAA. Collateralized mortgage obligations, including approximately \$141 million secured by ALT-A mortgages, represented the remaining 25% of residential mortgage-backed securities, which virtually all have credit ratings of A or better. As of March 31, 2008, 94% of commercial mortgage-backed securities have AAA credit ratings, 2% have AA credit ratings, 3% have A credit ratings, and the remaining 1% have BBB or BB credit ratings. As of March 31, 2008, included within asset-backed securities is approximately \$0.6 billion of securities collateralized by sub-prime mortgages, including approximately 59% with AAA credit ratings, 23% with AA credit ratings, 16% with A credit ratings, and the remaining 2% with BBB credit ratings. As of March 31, 2008, the remaining \$0.6 billion of asset-backed securities includes \$0.3 billion of securities collateralized by auto loans, \$0.2 billion collateralized by credit cards and \$0.1 billion of other. For a discussion of changes in the fair value of our trading account assets supporting insurance liabilities see *Trading Account Assets Supporting Insurance Liabilities*, above.



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The following table sets forth our public fixed maturities included in our trading account assets supporting insurance liabilities portfolio by NAIC rating as of the dates indicated.

| (1)(2)   | NAIC Designation                | Rating Agency Equivalent | March 31, 2008 |                           |                            |            | December 31, 2007 |                           |                            |            |
|--|---------------------------------|--------------------------|----------------|---------------------------|----------------------------|------------|-------------------|---------------------------|----------------------------|------------|
|  |                                 |                          | Amortized Cost | Gross Unrealized Gains(3) | Gross Unrealized Losses(3) | Fair Value | Amortized Cost    | Gross Unrealized Gains(3) | Gross Unrealized Losses(3) | Fair Value |
|  |                                 |                          |                |                           |                            |            |                   |                           |                            |            |
| 1  | Aaa, Aa, A                      |                          | \$ 6,676       | \$ 45                     | \$ 179                     | \$ 6,542   | \$ 6,734          | \$ 54                     | \$ 96                      | \$ 6,692   |
| 2  | Baa                             |                          | 2,258          | 21                        | 41                         | 2,238      | 1,966             | 11                        | 27                         | 1,950      |
|  | Subtotal Investment Grade       |                          | 8,934          | 66                        | 220                        | 8,780      | 8,700             | 65                        | 123                        | 8,642      |
| 3  | Ba                              |                          | 499            | 1                         | 23                         | 477        | 374               | 2                         | 9                          | 367        |
| 4  | B                               |                          | 223            | 1                         | 12                         | 212        | 215               |                           | 5                          | 210        |
| 5  | C and lower                     |                          | 3              |                           | 1                          | 2          | 11                |                           |                            | 11         |
| 6  | In or near default              |                          | 3              |                           | 3                          |            | 3                 |                           | 3                          |            |
|  | Subtotal Below Investment Grade |                          | 728            | 2                         | 39                         | 691        | 603               | 2                         | 17                         | 588        |
| Total Public Trading Account Assets Supporting Insurance Liabilities |                                 |                          | \$ 9,662       | \$ 68                     | \$ 259                     | \$ 9,471   | \$ 9,303          | \$ 67                     | \$ 140                     | \$ 9,230   |

(1) See Fixed Maturity Securities Credit Quality above for a discussion on NAIC designations.

(2) Reflects equivalent ratings for investments of the international insurance operations that are not rated by U.S. insurance regulatory authorities.

(3) Amounts are reported in Asset management fees and other income.

The following table sets forth our private fixed maturities included in our trading account assets supporting insurance liabilities portfolio by NAIC rating as of the dates indicated.

| (1) (2) | NAIC Designation                | Rating Agency Equivalent | March 31, 2008 |                           |                            |            | December 31, 2007 |                           |                            |            |
|---------|---------------------------------|--------------------------|----------------|---------------------------|----------------------------|------------|-------------------|---------------------------|----------------------------|------------|
|         |                                 |                          | Amortized Cost | Gross Unrealized Gains(3) | Gross Unrealized Losses(3) | Fair Value | Amortized Cost    | Gross Unrealized Gains(3) | Gross Unrealized Losses(3) | Fair Value |
| 1       | Aaa, Aa, A                      |                          | \$ 875         | \$ 11                     | \$ 18                      | \$ 868     | \$ 887            | \$ 6                      | \$ 12                      | \$ 881     |
| 2       | Baa                             |                          | 2,437          | 45                        | 25                         | 2,457      | 2,411             | 33                        | 26                         | 2,418      |
|         | Subtotal Investment Grade       |                          | 3,312          | 56                        | 43                         | 3,325      | 3,298             | 39                        | 38                         | 3,299      |
| 3       | Ba                              |                          | 312            | 3                         | 7                          | 308        | 263               | 3                         | 8                          | 258        |
| 4       | B                               |                          | 141            | 1                         | 5                          | 137        | 144               |                           | 2                          | 142        |
| 5       | C and lower                     |                          | 9              |                           |                            | 9          | 10                |                           |                            | 10         |
| 6       | In or near default              |                          | 32             |                           | 1                          | 31         | 33                | 1                         | 2                          | 32         |
|         | Subtotal Below Investment Grade |                          | 494            | 4                         | 13                         | 485        | 450               | 4                         | 12                         | 442        |
|         |                                 |                          | \$ 3,806       | \$ 60                     | \$ 56                      | \$ 3,810   | \$ 3,748          | \$ 43                     | \$ 50                      | \$ 3,741   |

Total Private Trading Account Assets Supporting  
Insurance Liabilities

- (1) See Fixed Maturity Securities Credit Quality above for a discussion on NAIC designations.
- (2) Reflects equivalent ratings for investments of the international insurance operations that are not rated by U.S. insurance regulatory authorities.
- (3) Amounts are reported in Asset management fees and other income.

**Table of Contents****Commercial Loans**

As of March 31, 2008 and December 31, 2007 respectively, we held approximately 13% and 12% of our general account investments in commercial loans. This percentage is net of a \$0.1 billion allowance for losses as of both March 31, 2008 and December 31, 2007.

Our loan portfolio strategy emphasizes diversification by property type and geographic location. The following tables set forth the breakdown of the gross carrying values of our general account investments in commercial loans by geographic region and property type as of the dates indicated.

|                                    | March 31, 2008                   |               |                            |               | December 31, 2007                |               |                            |               |
|------------------------------------|----------------------------------|---------------|----------------------------|---------------|----------------------------------|---------------|----------------------------|---------------|
|                                    | Financial Services<br>Businesses |               | Closed Block<br>Business   |               | Financial Services<br>Businesses |               | Closed Block<br>Business   |               |
|                                    | Gross<br>Carrying<br>Value       | % of<br>Total | Gross<br>Carrying<br>Value | % of<br>Total | Gross<br>Carrying<br>Value       | % of<br>Total | Gross<br>Carrying<br>Value | % of<br>Total |
| <b>Commercial loans by region:</b> |                                  |               |                            |               |                                  |               |                            |               |
| U.S. Regions:                      |                                  |               |                            |               |                                  |               |                            |               |
| Pacific                            | \$ 5,476                         | 25.7%         | \$ 2,664                   | 31.3%         | \$ 5,244                         | 26.6%         | \$ 2,666                   | 33.4%         |
| South Atlantic                     | 4,861                            | 22.9          | 1,828                      | 21.4          | 4,421                            | 22.5          | 1,605                      | 20.1          |
| Middle Atlantic                    | 2,743                            | 12.9          | 1,856                      | 21.8          | 2,492                            | 12.6          | 1,671                      | 20.9          |
| East North Central                 | 1,747                            | 8.2           | 449                        | 5.3           | 1,654                            | 8.4           | 398                        | 5.0           |
| West South Central                 | 1,215                            | 5.7           | 557                        | 6.5           | 1,008                            | 5.1           | 558                        | 7.0           |
| Mountain                           | 1,111                            | 5.2           | 463                        | 5.4           | 968                              | 4.9           | 391                        | 4.9           |
| New England                        | 842                              | 4.0           | 329                        | 3.9           | 700                              | 3.6           | 331                        | 4.1           |
| West North Central                 | 631                              | 3.0           | 225                        | 2.6           | 622                              | 3.2           | 208                        | 2.6           |
| East South Central                 | 366                              | 1.7           | 107                        | 1.3           | 368                              | 1.9           | 109                        | 1.4           |
| Subtotal U.S.                      | 18,992                           | 89.3          | 8,478                      | 99.5          | 17,477                           | 88.8          | 7,937                      | 99.4          |
| Asia                               | 1,488                            | 7.0           |                            |               | 1,462                            | 7.4           |                            |               |
| Other                              | 794                              | 3.7           | 45                         | 0.5           | 754                              | 3.8           | 45                         | 0.6           |
| Total Commercial Loans(1)          | \$ 21,274                        | 100.0%        | \$ 8,523                   | 100.0%        | \$ 19,693                        | 100.0%        | \$ 7,982                   | 100.0%        |

|   | March 31, 2008                   |               |                            |               | December 31, 2007                |               |                            |               |
|---|----------------------------------|---------------|----------------------------|---------------|----------------------------------|---------------|----------------------------|---------------|
|   | Financial Services<br>Businesses |               | Closed Block<br>Business   |               | Financial Services<br>Businesses |               | Closed Block<br>Business   |               |
|   | Gross<br>Carrying<br>Value       | % of<br>Total | Gross<br>Carrying<br>Value | % of<br>Total | Gross<br>Carrying<br>Value       | % of<br>Total | Gross<br>Carrying<br>Value | % of<br>Total |
| <b>Commercial loans by property type:</b> |                                  |               |                            |               |                                  |               |                            |               |
| Industrial buildings                      | \$ 4,478                         | 21.0%         | \$ 1,921                   | 22.5%         | \$ 4,140                         | 21.0%         | \$ 1,908                   | 23.9%         |
| Office buildings                          | 3,820                            | 17.9          | 1,649                      | 19.4          | 3,677                            | 18.7          | 1,581                      | 19.8          |
| Apartment complexes                       | 3,587                            | 16.9          | 1,706                      | 20.0          | 3,419                            | 17.4          | 1,554                      | 19.5          |
| Other                                     | 2,613                            | 12.3          | 887                        | 10.4          | 2,525                            | 12.8          | 809                        | 10.1          |
| Retail stores                             | 3,051                            | 14.3          | 1,382                      | 16.2          | 2,576                            | 13.1          | 1,275                      | 16.0          |
| Agricultural properties                   | 1,269                            | 6.0           | 824                        | 9.7           | 1,289                            | 6.5           | 854                        | 10.7          |

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|                                  |           |        |          |        |           |        |          |        |
|----------------------------------|-----------|--------|----------|--------|-----------|--------|----------|--------|
| Residential properties           | 972       | 4.6    | 1        | 0.0    | 938       | 4.8    | 1        |        |
| Subtotal of collateralized loans | 19,790    | 93.0   | 8,370    | 98.2   | 18,564    | 94.3   | 7,982    | 100.0  |
| Uncollateralized loans           | 1,484     | 7.0    | 153      | 1.8    | 1,129     | 5.7    |          |        |
| Total Commercial Loans(1)        | \$ 21,274 | 100.0% | \$ 8,523 | 100.0% | \$ 19,693 | 100.0% | \$ 7,982 | 100.0% |

(1) Excluded from the tables above are commercial loans held outside the general account in other entities and operations. For additional information regarding commercial loans held outside the general account, see [Invested Assets of Other Entities and Operations](#) below.

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Loan to value and debt service coverage ratios are measures commonly used to assess the quality of commercial loans. The loan to value ratio compares the amount of the loan to the fair value of the underlying property collateralizing the loan, and is commonly expressed as a percentage. Loan to value ratios greater than 100% percent indicate that the loan amount is greater than the collateral value. Therefore, all else being equal, a smaller loan to value ratio generally indicates a higher quality security. The debt service coverage ratio compares a property's net operating income to its debt service payments. Debt service coverage ratios less than 1.0 times indicates that property operations do not generate enough income to cover its current debt payments. Therefore, all else being equal, a larger debt service coverage ratio generally indicates a higher quality security.

The increase in our general account investments in commercial loans as of March 31, 2008 reflects higher origination activity in 2008. Unfavorable credit market conditions beginning during the second half of 2007 led to decreased activity by securitization lenders in the commercial loan market, and therefore greater opportunities for increased originations by portfolio lenders such as our general account. The average loan-to-value ratio on 2008 general account originations was below 60%, which is consistent with originations over the last several years. As of March 31, 2008, our general account investments in commercial loans attributable to the Financial Services Businesses had an average debt service coverage ratio of 1.80 times, and an average loan-to-value ratio of 52%. As of March 31, 2008, our general account investments in commercial loans attributable to the Closed Block Business had an average debt service coverage ratio of 1.86 times, and an average loan-to-value ratio of 44%. These loan to value ratios are lower than our origination loan to value ratio due to principal payments on the loan balances and appreciation of the underlying collateral value. The values utilized in calculating these loan to value ratios were developed as part of our annual review of the commercial loan portfolio, which includes a quality re-rating as well as an internal evaluation of the underlying collateral value. The following tables set forth the gross carrying value of our general account investments in commercial loans attributable to the Financial Services Businesses and the Closed Block Business as of March 31, 2008 by loan to value and debt service coverage ratios.

|  | March 31, 2008                |            |                       |            |
|--|-------------------------------|------------|-----------------------|------------|
|  | Financial Services Businesses |            | Closed Block Business |            |
|  | Gross Carrying Value          | % of Total | Gross Carrying Value  | % of Total |
| Commercial loans by loan to value ratio: |                               |            |                       |            |
| 0% - 50%                                 | \$ 6,908                      | 34.9%      | \$ 4,211              | 50.3%      |
| 50% - 60%                                | 4,479                         | 22.6       | 1,667                 | 19.9       |
| 60% - 70%                                | 5,069                         | 25.6       | 1,635                 | 19.5       |
| 70% - 80%                                | 1,969                         | 10.0       | 775                   | 9.3        |
| 80% - 90%                                | 266                           | 1.3        | 55                    | 0.7        |
| 90% - 100%                               | 1,099                         | 5.6        | 27                    | 0.3        |
| Greater than 100%                        |                               |            |                       |            |
| Total collateralized loans               | \$ 19,790                     | 100.0%     | \$ 8,370              | 100.0%     |

|  | March 31, 2008                |            |                       |            |
|--|-------------------------------|------------|-----------------------|------------|
|  | Financial Services Businesses |            | Closed Block Business |            |
|  | Gross Carrying Value          | % of Total | Gross Carrying Value  | % of Total |
| Commercial loans by debt service coverage ratio: |                               |            |                       |            |
| Greater than 1.8 times                           | \$ 7,873                      | 41.9%      | \$ 3,935              | 47.0%      |
| 1.5 times - 1.8 times                            | 4,953                         | 26.4       | 1,679                 | 20.1       |
| 1.2 times - 1.5 times                            | 4,294                         | 22.8       | 1,979                 | 23.6       |
| 1.0 times - 1.2 times                            | 1,315                         | 7.0        | 694                   | 8.3        |
| Less than 1.0 times                              | 363                           | 1.9        | 83                    | 1.0        |
| Total collateralized loans(1)                    | \$ 18,798                     | 100.0%     | \$ 8,370              | 100.0%     |

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- (1) Excluded from the table above are commercial loans attributable to the Financial Services Businesses with a carrying value of \$31 million related to loans collateralized by aviation assets. Also excluded from the table above are commercial loans attributable to the Financial Services Businesses with carrying value of \$961 million related to Japanese recourse loans.



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The following tables set forth the breakdown of our commercial loan portfolio by year of origination as of March 31, 2008.

| Year of Origination               | March 31, 2008                |               |                       |               |
|-----------------------------------|-------------------------------|---------------|-----------------------|---------------|
|                                   | Financial Services Businesses |               | Closed Block Business |               |
|                                   | Gross Carrying Value          | % of Total    | Gross Carrying Value  | % of Total    |
|                                   | (\$ in millions)              |               |                       |               |
| 2008                              | \$ 1,338                      | 6.8           | \$ 438                | 5.2           |
| 2007                              | 4,690                         | 23.7          | 1,630                 | 19.5          |
| 2006                              | 3,714                         | 18.7          | 1,125                 | 13.4          |
| 2005                              | 2,450                         | 12.4          | 867                   | 10.4          |
| 2004                              | 1,843                         | 9.3           | 1,109                 | 13.3          |
| 2003 and prior                    | 5,755                         | 29.1          | 3,201                 | 38.2          |
| <b>Total collateralized Loans</b> | <b>\$ 19,790</b>              | <b>100.0%</b> | <b>\$ 8,370</b>       | <b>100.0%</b> |

*Commercial Loan Quality*

We establish valuation allowances for loans that are determined to be non-performing as a result of our loan review process. We define a non-performing loan as a loan for which it is probable that amounts due according to the contractual terms of the loan agreement will not be collected. Valuation allowances for a non-performing loan are recorded based on the present value of expected future cash flows discounted at the loan's effective interest rate or based on the fair value of the collateral if the loan is collateral dependent. We record subsequent adjustments to our valuation allowances when appropriate.

The following tables set forth the gross carrying value for commercial loans by loan classification as of the dates indicated:

|                                | March 31, 2008                |                       | December 31, 2007             |                       |
|--------------------------------|-------------------------------|-----------------------|-------------------------------|-----------------------|
|                                | Financial Services Businesses | Closed Block Business | Financial Services Businesses | Closed Block Business |
|                                | (in millions)                 |                       |                               |                       |
| Performing                     | \$ 21,216                     | \$ 8,522              | \$ 19,631                     | \$ 7,981              |
| Delinquent, not in foreclosure | 45                            |                       | 50                            |                       |
| Delinquent, in foreclosure     | 7                             |                       | 7                             |                       |
| Restructured                   | 6                             | 1                     | 5                             | 1                     |
| <b>Total Commercial Loans</b>  | <b>\$ 21,274</b>              | <b>\$ 8,523</b>       | <b>\$ 19,693</b>              | <b>\$ 7,982</b>       |

The following table sets forth the change in valuation allowances for our commercial loan portfolio as of the dates indicated:

March 31, 2008

December 31, 2007

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|   | <b>Financial<br/>Services<br/>Businesses</b> | <b>Closed<br/>Block<br/>Business</b> | <b>Financial<br/>Services<br/>Businesses</b> | <b>Closed<br/>Block<br/>Business</b> |
|---|--|--------------------------------------|--|--------------------------------------|
|   | (in millions)                                |                                      |  |                                      |
| Allowance, beginning of period                | \$ 90  | \$ 28                                | \$ 94  | \$ 35                                |
| (Release of)/addition to allowance for losses | 2  | 1                                    | (5)  | (7)                                  |
| Charge-offs, net of recoveries                |  |                                      |  |                                      |
| Change in foreign exchange                    | 2  |                                      | 1  |                                      |
| Allowance, end of period                      | \$ 94  | \$ 29                                | \$ 90  | \$ 28                                |

**Table of Contents***Equity Securities**Investment Mix*

The equity securities attributable to the Financial Services Businesses consist principally of investments in common and preferred stock of publicly traded companies. The following table sets forth the composition of our equity securities portfolio attributable to the Financial Services Businesses and the associated gross unrealized gains and losses as of the dates indicated:

|                     | March 31, 2008  |                              |                               |                                | December 31, 2007 |                              |                               |                 |
|---------------------|-----------------|------------------------------|-------------------------------|--------------------------------|-------------------|------------------------------|-------------------------------|-----------------|
|                     | Cost            | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Fair<br>Value<br>(in millions) | Cost              | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Fair<br>Value   |
| Public equity       | \$ 4,431        | \$ 165                       | \$ 404                        | \$ 4,192                       | \$ 4,233          | \$ 317                       | \$ 179                        | \$ 4,371        |
| Private equity      | 348             | 8                            | 5                             | 351                            | 254               | 9                            | 5                             | 258             |
| <b>Total Equity</b> | <b>\$ 4,779</b> | <b>\$ 173</b>                | <b>\$ 409</b>                 | <b>\$ 4,543</b>                | <b>\$ 4,487</b>   | <b>\$ 326</b>                | <b>\$ 184</b>                 | <b>\$ 4,629</b> |

Public equity securities include mutual fund shares representing our interest in the underlying assets of certain of our separate account investments. These mutual funds invest primarily in high yield bonds. The cost, gross unrealized gains, gross unrealized losses, and fair value of these shares as of March 31, 2008 were \$1,468 million, \$5 million, \$85 million, and \$1,388 million, respectively. The cost, gross unrealized gains, gross unrealized losses, and fair value of these shares as of December 31, 2007 were \$1,447 million, \$8 million, \$26 million, and \$1,429 million, respectively

The equity securities attributable to the Closed Block Business consist principally of investments in common and preferred stock of publicly traded companies. The following table sets forth the composition of our equity securities portfolio attributable to the Closed Block Business and the associated gross unrealized gains and losses as of the dates indicated:

|                     | March 31, 2008  |                              |                               |                                | December 31, 2007 |                              |                               |                 |
|---------------------|-----------------|------------------------------|-------------------------------|--------------------------------|-------------------|------------------------------|-------------------------------|-----------------|
|                     | Cost            | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Fair<br>Value<br>(in millions) | Cost              | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses | Fair<br>Value   |
| Public equity       | \$ 3,312        | \$ 514                       | \$ 265                        | \$ 3,561                       | \$ 3,381          | \$ 742                       | \$ 200                        | \$ 3,923        |
| Private equity      | 17              |                              |                               | 17                             | 17                |                              |                               | 17              |
| <b>Total Equity</b> | <b>\$ 3,329</b> | <b>\$ 514</b>                | <b>\$ 265</b>                 | <b>\$ 3,578</b>                | <b>\$ 3,398</b>   | <b>\$ 742</b>                | <b>\$ 200</b>                 | <b>\$ 3,940</b> |

*Unrealized Losses from Equity Securities*

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The following table sets forth the cost and gross unrealized losses of our equity securities attributable to the Financial Services Businesses where the estimated fair value had declined and remained below cost by less than 20% for the following timeframes:

|  | March 31, 2008  |                               | December 31, 2007 |                               |
|--|-----------------|-------------------------------|-------------------|-------------------------------|
|  | Cost            | Gross<br>Unrealized<br>Losses | Cost              | Gross<br>Unrealized<br>Losses |
|  | (in millions)   |                               |                   |                               |
| Less than three months                             | \$ 2,429        | \$ 91                         | \$ 3,714          | \$ 93                         |
| Three months or greater but less than six months   | 1,449           | 94                            | 231               | 17                            |
| Six months or greater but less than nine months    | 34              | 1                             | 100               | 4                             |
| Nine months or greater but less than twelve months | 64              | 7                             | 7                 | 1                             |
| Greater than twelve months                         |                 |                               | 7                 |                               |
| <b>Total</b>                                       | <b>\$ 3,976</b> | <b>\$ 193</b>                 | <b>\$ 4,059</b>   | <b>\$ 115</b>                 |

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The following table sets forth the cost and gross unrealized losses of our equity securities attributable to the Financial Services Businesses where the estimated fair value had declined and remained below cost by 20% or more for the following timeframes:

|  | March 31, 2008 |                               | December 31, 2007 |                               |
|--|----------------|-------------------------------|-------------------|-------------------------------|
|  | Cost           | Gross<br>Unrealized<br>Losses | Cost              | Gross<br>Unrealized<br>Losses |
|  | (in millions)  |                               |                   |                               |
| Less than three months                             | \$ 607         | \$ 184                        | \$ 201            | \$ 55                         |
| Three months or greater but less than six months   | 100            | 32                            | 45                | 14                            |
| Six months or greater but less than nine months    |                |                               |                   |                               |
| Nine months or greater but less than twelve months |                |                               |                   |                               |
| Greater than twelve months                         |                |                               |                   |                               |
| Total  | \$ 707         | \$ 216                        | \$ 246            | \$ 69                         |

The gross unrealized losses as of March 31, 2008 were primarily concentrated in the finance, other and manufacturing sectors compared to December 31, 2007 where the gross unrealized losses were primarily concentrated in the manufacturing and other sectors. We have not recognized the gross unrealized losses shown in the table above as other-than-temporary impairments. See [Impairments of Equity Securities](#) for a discussion of the factors we consider in making these determinations.

The following table sets forth the cost and gross unrealized losses of our equity securities attributable to the Closed Block Business where the estimated fair value had declined and remained below cost by less than 20% for the following timeframes:

|  | March 31, 2008 |                               | December 31, 2007 |                               |
|--|----------------|-------------------------------|-------------------|-------------------------------|
|  | Cost           | Gross<br>Unrealized<br>Losses | Cost              | Gross<br>Unrealized<br>Losses |
|  | (in millions)  |                               |                   |                               |
| Less than three months                             | \$ 2,456       | \$ 96                         | \$ 2,965          | \$ 96                         |
| Three months or greater but less than six months   | 389            | 30                            | 90                | 15                            |
| Six months or greater but less than nine months    | 35             | 2                             | 40                | 3                             |
| Nine months or greater but less than twelve months | 14             | 1                             | 4                 | 1                             |
| Greater than twelve months                         |                |                               | 3                 |                               |
| Total  | \$ 2,894       | \$ 129                        | \$ 3,102          | \$ 115                        |

The following table sets forth the cost and gross unrealized losses of our equity securities attributable to the Closed Block Business where the estimated fair value had declined and remained below cost by 20% or more for the following timeframes:

|  | March 31, 2008 |                               | December 31, 2007 |                               |
|--|----------------|-------------------------------|-------------------|-------------------------------|
|  | Cost           | Gross<br>Unrealized<br>Losses | Cost              | Gross<br>Unrealized<br>Losses |
|  | (in millions)  |                               |                   |                               |

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|  |        |        |        |       |
|--|--------|--------|--------|-------|
| Less than three months                             | \$ 210 | \$ 61  | \$ 241 | \$ 66 |
| Three months or greater but less than six months   | 225    | 75     | 54     | 19    |
| Six months or greater but less than nine months r  |        |        |        |       |
| Nine months or greater but less than twelve months |        |        |        |       |
| Greater than twelve months                         |        |        |        |       |
| Total  | \$ 435 | \$ 136 | \$ 295 | \$ 85 |

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The gross unrealized losses as of March 31, 2008 were primarily concentrated in the finance, services, and manufacturing sectors compared to December 31, 2007 where the gross unrealized losses were primarily concentrated in the finance and services sectors. We have not recognized the gross unrealized losses shown in the table above as other-than-temporary impairments. See [Impairments of Equity Securities](#) for a discussion of the factors we consider in making these determinations.

### *Impairments of Equity Securities*

For those equity securities classified as available for sale we record unrealized gains and losses to the extent cost is different from estimated fair value. All securities with unrealized losses are subject to our review to identify other-than-temporary impairments in value. In evaluating whether a decline in value is other-than-temporary, we consistently consider several factors including, but not limited to, the following:

the extent and the duration of the decline; including, but not limited to, the following general guidelines;

declines in value greater than 20%, maintained for six months or greater;

declines in value maintained for one year or greater; and

declines in value greater than 50%

the reasons for the decline in value (credit event, currency or market fluctuation);

our ability and intent to hold the investment for a period of time to allow for a recovery of value, including equity securities managed by independent third parties where we do not have management discretion; and

the financial condition of and near-term prospects of the issuer.

When we determine that there is an other-than-temporary impairment, we record a writedown to estimated fair value, which reduces the cost basis. The new cost basis of an impaired security is not adjusted for subsequent increases in estimated fair value. Estimated fair values for publicly traded equity securities are based on quoted market prices or prices obtained from independent pricing services. Estimated fair values for privately traded equity securities are determined using valuation and discounted cash flow models that require a substantial level of judgment. In determining the fair value of certain privately traded equity securities the discounted cash flow model may also use unobservable inputs, which reflect our own assumptions about the inputs market participants would use in pricing the asset. Impairments on equity securities are included in [Realized investment gains \(losses\), net](#) and are excluded from adjusted operating income. For further information regarding the fair value methodology used in determining our other-than-temporary impairments, see [Valuation of Assets and Liabilities](#) [Fair Value of Assets and Liabilities](#) [Valuation of Equity Securities](#), above.

Impairments of equity securities attributable to the Financial Services Businesses were \$48 million and \$15 million for the three months ended March 31, 2008 and March 31, 2007, respectively. Impairments of equity securities attributable to the Closed Block Business were \$52 million and \$1 million for the three months ended March 31, 2008 and March 31, 2007, respectively. For a further discussion of impairments, see [Realized Investment Gains and Losses](#) above.





**Table of Contents*****Other Long-Term Investments***

Other long-term investments are comprised as follows:

|   | March 31, 2008                |                       | December 31, 2007             |                       |
|---|-------------------------------|-----------------------|-------------------------------|-----------------------|
|   | Financial Services Businesses | Closed Block Business | Financial Services Businesses | Closed Block Business |
|   | (in millions)                 |                       |                               |                       |
| Joint ventures and limited partnerships:  |                               |                       |                               |                       |
| Real estate related                       | \$ 362                        | \$ 327                | \$ 342                        | \$ 308                |
| Non real estate related                   | 852                           | 1,040                 | 755                           | 1,014                 |
| Real estate held through direct ownership | 1,033                         |                       | 946                           |                       |
| Other                                     | 446                           | (228)                 | 681                           | (54)                  |
| Total other long-term investments         | \$ 2,693                      | \$ 1,139              | \$ 2,724                      | \$ 1,268              |

***Invested Assets of Other Entities and Operations***

The following table sets forth the composition of the investments held outside the general account in other entities and operations as of March 31, 2008 and December 31, 2007.

|  | March 31, 2008 | December 31, 2007 |
|--|----------------|-------------------|
|  | (in millions)  |                   |
| Fixed Maturities:                                    |                |                   |
| Public, available for sale, at fair value            | \$ 1,612       | \$ 1,431          |
| Private, available for sale, at fair value           | 23             | 42                |
| Other trading account assets, at fair value          | 2,474          | 3,267             |
| Equity securities, available for sale, at fair value | 8              | 11                |
| Commercial loans, at book value                      | 2,264          | 2,490             |
| Securities purchased under agreements to resell      | 178            | 129               |
| Other long-term investments                          | 2,573          | 2,439             |
| Short-term investments                               | 1,562          | 1,254             |
| Total investments                                    | \$ 10,694      | \$ 11,063         |

The table above includes the invested assets of our securities brokerage, securities trading, banking operations, real estate and relocation services, and asset management operations. Assets of our asset management operations managed for third parties and those assets classified as separate account assets on our balance sheet are not included.

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Our global commodities group provides advice, sales and trading on a global basis covering a wide variety of commodity, financial and foreign exchange futures, swap and forward contracts, including agricultural commodities, base and precious metals, major currencies, interest rate and stock indices. Our derivatives trading operations also engage in trading activities. We maintain trading positions in various foreign exchange instruments and commodities, primarily to facilitate transactions for our clients. We seek to use short security positions and forwards, futures, options and other derivatives to limit exposure to interest rate and other market risks associated with these positions. We also trade derivative financial instruments that allow our clients to manage exposure to interest rate, currency and other market risks. Our derivative transactions involve both exchange-listed and over-the-counter contracts. We act both as a broker, buying and selling exchange-listed contracts for our customers, and as a dealer, by entering into futures and security transactions as a principal. The positions held relating to these trading operations are primarily included in Other trading account assets.

In our banking operations, customer deposit liabilities are primarily supported by fixed maturity and short-term investments, in addition to cash and cash equivalents.

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As part of our asset management operations we make proprietary investments in real estate and private equity, as well as debt, public equity and real estate securities, including controlling interests. Certain of these investments are made primarily for purposes of co-investment in our managed funds and structured products. Other proprietary investments are made with the intention to sell or syndicate to investors, including our general account, or for placement in funds and structured products that we offer and manage. These proprietary investments are primarily included in Other long-term investments. As part of our asset management operations we also make short term loans to our managed funds that are secured by equity commitments from investors or assets of the funds.

Our asset management operations also include our commercial mortgage operations, which provide mortgage origination and servicing for our general account, institutional clients, and government sponsored entities such as Fannie Mae, the Federal Housing Administration, and Freddie Mac. We also originate shorter-term interim loans when we expect the loans will lead to securitization or other sale opportunities. These mortgage loans are included in Commercial loans, with the related derivatives and other hedging instruments primarily included in Other trading account assets and Other long-term investments. For additional information regarding our decision to exit our commercial mortgage securitization operations, which involved the origination and purchase of commercial mortgage loans for sale into commercial mortgage-backed securitization transactions, together with related hedging activities, see Divested Businesses, above.

As of March 31, 2008, invested assets held outside the general account in other entities and operations include available for sale residential mortgage-backed securities with amortized cost of \$602 million and fair value of \$611 million, all of which have credit ratings of AAA, and available for sale commercial mortgage-backed securities with amortized cost of \$12 million and fair value of \$11 million, 41% of which have credit ratings of AAA and the remaining 59% of which have credit ratings of BB. An additional \$445 million of commercial mortgage-backed securities held outside the general account are classified as other trading account assets as of March 31, 2008, of which 83% have AAA credit ratings, 7% have AA credit ratings, 7% have A credit ratings, and the remaining 3% have BBB credit ratings.

As of March 31, 2008, invested assets held outside the general account in other entities and operations also includes available for sale asset-backed securities with amortized cost of \$258 million and fair value of \$244 million. Based on amortized cost, 75% have credit ratings of AAA, and the remaining 25% have BBB or below credit ratings. Included within these asset-backed securities as of March 31, 2008, are securities collateralized by sub-prime mortgages with amortized cost and fair value of \$9 million, all of which have AAA credit ratings, with \$8 million in the 2006 vintage and \$1 million in the 2003 vintage. Also included are collateralized debt obligations with amortized cost of \$49 million and fair value of \$41 million, with none secured by sub-prime mortgages. An additional \$15 million of asset-backed securities held outside the general account as of March 31, 2008 are classified as other trading account assets, all of which have credit ratings of AAA.

## **Liquidity and Capital Resources**

### **Prudential Financial**

The principal sources of funds available to Prudential Financial, the parent holding company and registrant, to meet its obligations, including the payment of shareholder dividends, share repurchases, debt service, operating expenses, capital contributions and obligations to subsidiaries are dividends, returns of capital, interest income from its subsidiaries, and cash and short-term investments. These sources of funds are complemented by Prudential Financial's access to the capital markets and bank facilities, as well as the Alternative Sources of Liquidity described below.

During the latter half of 2007 and continuing through the first quarter 2008, dislocations in the credit and capital markets, initially driven by broad market concerns over the impact of sub-prime mortgage holdings of financial institutions, have generally resulted in increased cost of

credit for financial institutions in the

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marketplace. While credit has generally become more expensive, Prudential Financial's ability to access the capital markets has not been materially impacted.

Management monitors the liquidity of Prudential Financial and the Company on a daily basis and projects borrowing and capital needs over a multi-year time horizon through our quarterly planning process. We believe that cash flows from the sources of funds described above are sufficient to satisfy the current liquidity requirements of Prudential Financial, including reasonably foreseeable contingencies. As of March 31, 2008, Prudential Financial had cash and short-term investments of approximately \$2.972 billion, a decrease of \$1.732 billion from December 31, 2007. Prudential Financial's principal sources and uses of cash and short-term investments for the first three months of 2008 were as follows:

|  | <b>Three Months Ended<br/>March 31, 2008<br/>(in millions)</b> |
|--|--|
| <b>Sources:</b>  |  |
| Dividends and/or returns of capital from subsidiaries(1)                       | \$ 166   |
| Proceeds from the issuance of retail medium-term notes, net of repayments(2)   | 247  |
| Proceeds from the issuance of long-term debt, net of repayments(3)             | 597  |
| Proceeds from stock-based compensation and exercise of stock options           | 68   |
| <b>Total sources</b>   | <b>1,078</b>   |
| <b>Uses:</b>   |  |
| Capital contributions to subsidiaries(4)                                       | 396  |
| Share repurchases(5)   | 869  |
| Shareholder dividends  | 75   |
| Repayment of short term debts, net of issuances                                | 711  |
| Purchase of funding agreements from Prudential Insurance, net of maturities(2) | 247  |
| Net payment under intercompany loan agreements                                 | 456  |
| Other, net   | 56   |
| <b>Total uses</b>  | <b>2,810</b>   |
| <b>Net decrease in cash and short-term investments</b>                         | <b>\$ (1,732)</b>  |

- (1) Includes dividends and/or returns of capital of \$146 million from asset management subsidiaries, \$14 million from international insurance and investments subsidiaries and \$6 million from Prudential Annuities.
- (2) Proceeds from the issuance of retail medium-term notes are used primarily to purchase funding agreements from Prudential Insurance. See *Financing Activities* for a discussion of our retail note program.
- (3) See *Financing Activities*.
- (4) Includes capital contributions of \$182 million to asset management subsidiaries, \$128 million to international insurance and investments subsidiaries, and \$86 million to other insurance businesses.
- (5) See *Uses of Capital* Share Repurchases.

*Sources of Capital*

Prudential Financial is a holding company whose principal asset is its investments in subsidiaries. Prudential Financial's capitalization and use of financial leverage are consistent with its ratings targets. We also monitor Prudential Financial's ability to cover its fixed cash obligations, such as interest expense, to ensure it is at a level consistent with its ratings targets. Our long-term senior debt rating targets for Prudential Financial are A

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for Standard & Poor's Rating Services, or S&P, Moody's Investors Service, Inc., or Moody's, and Fitch Ratings Ltd., or Fitch, and a for A.M. Best Company, or A.M. Best. We seek to capitalize all of our subsidiaries and businesses in accordance with their ratings targets. Our financial strength rating targets for our domestic life insurance companies are AA/Aa/AA for S&P, Moody's and Fitch, respectively, and A+ for A.M. Best. There have been no changes during 2008 to our ratings, which were disclosed in Business Ratings in our 2007 Annual Report on Form 10-K.

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The primary components of capitalization for the Financial Services Businesses consist of the equity we attribute to the Financial Services Businesses (excluding accumulated other comprehensive income related to unrealized gains and losses on investments and pension and postretirement benefits) and outstanding capital debt of the Financial Services Businesses, as discussed below under Financing Activities. Based on these components, the capital position of the Financial Services Businesses as of March 31, 2008 was as follows:

|   | <b>March 31, 2008</b><br><b>(in millions)</b> |
|---|---|
| Attributed equity (excluding unrealized gains and losses on investments and pension /postretirement benefits) | \$ 22,499                                     |
| Capital debt(1)   | 6,365   |
| <b>Total capital</b>  | <b>\$ 28,864</b>                              |

- (1) Our capital debt to total capital ratio was 22.1% as of March 31, 2008, which includes capital debt we expect will be paid down from the dividends anticipated to be received from subsidiaries in the second quarter of 2008.

As shown in the table above, as of March 31, 2008, the Financial Services Businesses had approximately \$28.9 billion in capital, all of which was available to support the aggregate capital requirements of its three divisions and its Corporate and Other operations. Based on our assessments of these businesses and operations, we believe that this level of capital exceeds the amount required to support current business risks by over \$1.5 billion as of March 31, 2008. Although a significant portion of these resources are in our regulated subsidiaries, and their availability may be subject to prior regulatory notice, approval or non-disapproval, we believe these resources provide financial flexibility to the Company.

We believe that migrating toward a capital structure comprised of 70% attributed equity, 20% capital debt and 10% hybrid equity securities is consistent with our ratings objectives for Prudential Financial, and would support the issuance of approximately \$3.0 billion of additional capital debt and hybrid equity securities. This capital structure assumes that the hybrid equity securities we issue are attributed 75% equity credit, with the remaining 25% treated as capital debt, and that market conditions exist which make hybrid equity securities a cost effective source of capital.

The Risk Based Capital, or RBC, ratio is the primary measure by which we evaluate the capital adequacy of Prudential Insurance, which includes businesses in both the Financial Services Businesses and the Closed Block Business. We manage Prudential Insurance's RBC ratio to a level consistent with our ratings targets. RBC is determined by statutory formulas that consider risks related to the type and quality of the invested assets, insurance-related risks associated with Prudential Insurance's products, interest rate risks and general business risks. The RBC ratio calculations are intended to assist insurance regulators in measuring the adequacy of Prudential Insurance's statutory capitalization. As of the date of the most recent annual statutory financial statements filed with the insurance regulators, the total adjusted operating capital of our domestic insurance subsidiaries was in excess of the required RBC levels.

*Uses of Capital**Share Repurchases*

In November 2007, Prudential Financial's Board of Directors authorized the Company to repurchase up to \$3.5 billion of its outstanding Common Stock in calendar year 2008. The timing and amount of any repurchases under this authorization will be determined by management

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based upon market conditions and other considerations, and the repurchases may be effected in the open market, through derivative, accelerated repurchase and other negotiated transactions and through prearranged trading plans complying with Rule 10b5-1(c) of the Exchange Act. The 2008 stock repurchase program supersedes all previous repurchase programs.



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Our stock repurchase program at current levels is dependent on dividends and returns of capital from subsidiaries, as well as proceeds from the issuance of capital debt and hybrid securities. During the first quarter of 2008, we repurchased 11.4 million shares of our Common Stock at a total cost of \$869 million.

Our share repurchase program is reviewed quarterly by the Finance Committee of Prudential Financial's Board of Directors. Numerous factors could impact our share repurchase program, including increased capital needs of our businesses due to opportunities for organic growth, acquisitions, adverse market conditions impacting the earnings of our business or factors affecting our ability to access the capital markets.

### ***Restrictions on Dividends and Returns of Capital from Subsidiaries***

Our insurance and various other companies are subject to regulatory limitations on the payment of dividends and other transfers of funds to affiliates. With respect to Prudential Insurance, New Jersey insurance law provides that, except in the case of extraordinary dividends or distributions, all dividends or distributions paid by Prudential Insurance may be declared or paid only from unassigned surplus, as determined pursuant to statutory accounting principles, less unrealized investment gains and losses and revaluation of assets. Prudential Insurance must also notify the New Jersey Department of Banking and Insurance of its intent to pay a dividend or distribution. If the dividend or distribution, together with other dividends or distributions made within the preceding twelve months, exceed a specified statutory limit it is considered an extraordinary dividend or distribution and Prudential Insurance must obtain the prior non-disapproval of the Department. The current statutory limitation applicable to New Jersey life insurers generally is the greater of 10% of the prior calendar year's statutory surplus or the prior calendar year's statutory net gain from operations excluding realized investment gains and losses. In addition to these regulatory limitations, the terms of the IHC debt contain restrictions potentially limiting dividends by Prudential Insurance applicable to the Financial Services Businesses in the event the Closed Block Business is in financial distress and under certain other circumstances.

The laws regulating dividends of the other states and foreign jurisdictions where our other insurance companies are domiciled are similar, but not identical, to New Jersey's. Pursuant to Gibraltar Life's reorganization, in addition to regulatory restrictions, there are certain restrictions on Gibraltar Life's ability to pay dividends to Prudential Financial. We anticipate that it will be several years before these restrictions will allow Gibraltar Life to pay such dividends. There are also regulatory restrictions on the payment of dividends by The Prudential Life Insurance Company, Ltd., or Prudential of Japan, which began paying dividends in 2006. The ability of our asset management subsidiaries, and the majority of our other operating subsidiaries, to pay dividends is largely unrestricted.

### ***Alternative Sources of Liquidity***

Prudential Financial, the parent holding company, maintains an intercompany liquidity account that is designed to maximize the use of cash by facilitating the lending and borrowing of funds between the parent holding company and its affiliates on a daily basis. Depending on the overall availability of cash, the parent holding company invests excess cash on a short-term basis or borrows funds in the capital markets. Additional longer term liquidity is available through inter-affiliate borrowing arrangements. It also has access to bank facilities. See Lines of Credit and Other Credit Facilities.

### ***Economic Capital***

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We are in the process of developing an economic capital framework, and have begun using economic capital as an additional source of information for our business decisions. As we continue developing the framework, we will be assessing our overall capital position, including our view of excess capital, using both economic capital and our current framework, which is primarily based on risk based capital measures.

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### **Liquidity of Subsidiaries**

#### *Domestic Insurance Subsidiaries*

##### *General Liquidity*

Liquidity refers to a company's ability to generate sufficient cash flows to meet the needs of its operations. We manage the liquidity of our domestic insurance operations to ensure stable, reliable and cost-effective sources of cash flows to meet all of our obligations. Liquidity is provided by a variety of sources, as described more fully below, including portfolios of liquid assets. The investment portfolios of our domestic operations are integral to the overall liquidity of those operations. We segment our investment portfolios and employ an asset/liability management approach specific to the requirements of our product lines. This enhances the discipline applied in managing the liquidity, as well as the interest rate and credit risk profiles, of each portfolio in a manner consistent with the unique characteristics of the product liabilities. We use a projection process for cash flows from operations to ensure sufficient liquidity to meet projected cash outflows, including claims.

Liquidity is measured against internally developed benchmarks that take into account the characteristics of the asset portfolio. The results are affected substantially by the overall asset type and quality of our investments.

##### *Cash Flow*

The principal sources of liquidity for Prudential Insurance and our other domestic insurance subsidiaries are premiums and annuity considerations, investment and fee income and investment maturities and sales associated with our insurance and annuity operations. The principal uses of that liquidity include benefits, claims, dividends paid to policyholders, and payments to policyholders and contractholders in connection with surrenders, withdrawals and net policy loan activity. Other uses of liquidity include commissions, general and administrative expenses, purchases of investments, and payments in connection with financing activities.

We believe that the cash flows from our insurance and annuity operations are adequate to satisfy the current liquidity requirements of these operations, including under reasonably foreseeable stress scenarios. The continued adequacy of this liquidity will depend upon factors such as future securities market conditions, changes in interest rate levels and policyholder perceptions of our financial strength, each of which could lead to reduced cash inflows or increased cash outflows. In addition, market volatility can impact the level of capital required to support our businesses, particularly in our annuity business.

Our domestic insurance operations' cash flows from investment activities result from repayments of principal, proceeds from maturities and sales of invested assets and investment income, net of amounts reinvested. The primary liquidity risks with respect to these cash flows are the risk of default by debtors or bond insurers, our counterparties' willingness to extend repurchase and/or securities lending arrangements and market volatility. As of March 31, 2008 and December 31, 2007, our domestic insurance entities had lendable assets of \$73.7 billion and \$76.5 billion, respectively. Of this amount, \$13.0 billion and \$16.3 billion, as of March 31, 2008 and December 31, 2007, respectively, were on loan, the remainder of which, depending on market conditions, are available to be financed through repurchase agreements or securities lending arrangements. We closely manage these risks through our credit risk management process and regular monitoring of our liquidity position.



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In managing the liquidity of our domestic insurance operations, we also consider the risk of policyholder and contractholder withdrawals of funds earlier than our assumptions when selecting assets to support these contractual obligations. We use surrender charges and other contract provisions to mitigate the extent, timing and profitability impact of withdrawals of funds by customers from annuity contracts and deposit liabilities. The following table sets forth withdrawal characteristics of our general account annuity reserves and deposit liabilities (based on statutory liability values) as of the dates indicated.

|  | March 31, 2008 |            | December 31, 2007 |            |
|--|----------------|------------|-------------------|------------|
|  | Amount         | % of Total | Amount            | % of Total |
| Not subject to discretionary withdrawal provisions   | \$ 34,877      | 46%        | \$ 33,837         | 46%        |
| Subject to discretionary withdrawal, with adjustment:  |                |            |                   |            |
| With market value adjustment   | 19,210         | 25         | 18,636            | 26         |
| At market value  | 1,204          | 2          | 1,162             | 2          |
| At contract value, less surrender charge of 5% or more   | 2,392          | 3          | 1,594             | 2          |
| Subtotal   | 57,683         | 76         | 55,229            | 76         |
| Subject to discretionary withdrawal at contract value with no surrender charge or surrender charge of less than 5% | 17,883         | 24         | 17,506            | 24         |
| Total annuity reserves and deposit liabilities   | \$ 75,566      | 100%       | \$ 72,735         | 100%       |

Individual life insurance policies are less susceptible to withdrawal than our annuity reserves and deposit liabilities because policyholders may incur surrender charges and be subject to a new underwriting process in order to obtain a new insurance policy. Annuity benefits under group annuity contracts are generally not subject to early withdrawal.

Gross account withdrawals for our domestic insurance operations products amounted to approximately \$4.6 billion and \$5.4 billion for the first three months of 2008 and 2007, respectively. Because these withdrawals were consistent with our assumptions in asset/liability management, the associated cash outflows did not have a material adverse impact on our overall liquidity.

*Liquid Assets*

Liquid assets include cash, cash equivalents, short-term investments, fixed maturities that are not designated as held to maturity and public equity securities. As of March 31, 2008 and December 31, 2007, our domestic insurance operations had liquid assets of \$135.1 billion and \$137.0 billion, respectively, which includes assets financed with \$13.0 billion and \$16.3 billion of securities lent through repurchase agreements or securities lending arrangements as of March 31, 2008 and December 31, 2007, respectively. The portion of liquid assets comprised of cash and cash equivalents and short-term investments was \$7.7 billion and \$7.1 billion as of March 31, 2008 and December 31, 2007, respectively. As of March 31, 2008, \$110.8 billion, or 90%, of the fixed maturity investments that are not designated as held to maturity within our domestic insurance company general account portfolios were rated investment grade. The remaining \$12.6 billion, or 10%, of these fixed maturity investments were rated non-investment grade. We consider attributes of the various categories of liquid assets (for example, type of asset and credit quality) in calculating internal liquidity measures in order to evaluate the adequacy of our domestic insurance operations liquidity under a variety of stress scenarios. We believe that the liquidity profile of our assets is sufficient to satisfy current liquidity requirements, including under foreseeable stress scenarios.

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Given the size and liquidity profile of our investment portfolios, we believe that claim experience varying from our projections does not constitute a significant liquidity risk. Our asset/liability management process takes into account the expected maturity of investments and expected claim payments as well as the specific nature and risk profile of the liabilities. Historically, there has been no significant variation between the expected maturities of our investments and the payment of claims.

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Our domestic insurance companies' liquidity is managed through access to substantial investment portfolios as well as a variety of instruments available for funding and/or managing short-term cash flow mismatches, including from time to time those arising from claim levels in excess of projections. To the extent we need to pay claims in excess of projections, we may borrow temporarily or sell investments sooner than anticipated to pay these claims, which may result in realized investment gains or losses or increased borrowing costs affecting results of operations. For a further discussion of realized investment gains or losses, see *Realized Investment Gains and Losses and General Account Investments' Realized Investment Gains and Losses*. We believe that borrowing temporarily or selling investments earlier than anticipated will not have a material impact on the liquidity of our domestic insurance companies. Payment of claims and sale of investments earlier than anticipated would have an impact on the reported level of cash flow from operating and investing activities, respectively, in our financial statements.

### *Prudential Funding, LLC*

Prudential Funding, LLC, or Prudential Funding, a wholly owned subsidiary of Prudential Insurance, serves as an additional source of financing to meet the working capital needs of Prudential Insurance and its subsidiaries. Prudential Funding also lends to other subsidiaries of Prudential Financial up to limits established with the New Jersey Department of Banking and Insurance. To the extent that other subsidiaries of Prudential Financial have financing needs in excess of these limits, these needs are met through financing from Prudential Financial directly or from third parties. Prudential Funding operates under a support agreement with Prudential Insurance whereby Prudential Insurance has agreed to maintain Prudential Funding's positive tangible net worth at all times. Prudential Funding borrows funds primarily through the direct issuance of commercial paper. The impact of Prudential Funding's financing capacity on liquidity is considered in the internal liquidity measures of the domestic insurance operations.

As of March 31, 2008, Prudential Financial, Prudential Insurance and Prudential Funding had unsecured committed lines of credit totaling \$5.0 billion. There were no outstanding borrowings under these facilities as of March 31, 2008. For a further discussion of lines of credit, see *Lines of Credit and Other Credit Facilities*.

### *International Insurance Subsidiaries*

In our international insurance operations, liquidity is provided through ongoing operations as well as portfolios of liquid assets. In managing the liquidity and the interest and credit risk profiles of our international insurance portfolios, we employ a discipline similar to the discipline employed for domestic insurance subsidiaries. We monitor liquidity through the use of internal liquidity measures, taking into account the liquidity of the asset portfolios.

As with our domestic operations, in managing the liquidity of these operations, we consider the risk of policyholder and contractholder withdrawals of funds earlier than our assumptions in selecting assets to support these contractual obligations. As of March 31, 2008 and December 31, 2007, our international insurance subsidiaries had total general account insurance related liabilities (other than dividends payable to policyholders) of \$59.0 billion and \$54.4 billion, respectively. Of those amounts, \$31.4 billion and \$29.5 billion, respectively, were associated with Gibraltar Life.

Concurrent with our acquisition of Gibraltar Life in April 2001, substantially all of its insurance liabilities were restructured under a plan of reorganization to include special surrender penalties on existing policies. These charges, initially 15%, declining to their current 4% level, and reducing to 2% in April 2008 and then to 0% in April 2009, were designed to mitigate the extent, timing, and profitability impact of withdrawals of funds by customers. The charges apply to \$22.2 billion and \$21.1 billion of Gibraltar Life's insurance related reserves as of March 31, 2008 and December 31, 2007, respectively.

Policies issued by Gibraltar Life post-acquisition are not subject to the above restructured policy surrender charge schedule. Policies issued post-acquisition are generally subject to discretionary withdrawal at contract value, less applicable surrender charges, which currently start at 5% or more.



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A special dividend to certain Gibraltar Life policyholders was payable in 2005 and will again be payable in 2009. The special dividend is based on 70% of the net increase in the fair value, through March 2009, of certain real estate and loans, net of transaction costs and taxes, included in the Gibraltar Life reorganization plan. As of March 31, 2008, a liability of \$485 million related to the special dividend is included in

Policyholders' dividends. The special dividend will take the form of either additional policy values or cash. Gibraltar Life's investment portfolio is structured to provide adequate liquidity for the special dividend.

Prudential of Japan had \$21.8 billion and \$19.2 billion of general account insurance related liabilities, other than dividends to policyholders, as of March 31, 2008 and December 31, 2007, respectively. Prudential of Japan did not have a material amount of general account annuity reserves or deposit liabilities subject to discretionary withdrawal as of March 31, 2008 or December 31, 2007. Additionally, we believe that the individual life insurance policies sold by Prudential of Japan do not have significant withdrawal risk because policyholders may incur surrender charges and must undergo a new underwriting process in order to obtain a new insurance policy.

As of March 31, 2008 and December 31, 2007, our international insurance subsidiaries had cash and short-term investments of approximately \$1.5 billion and \$1.1 billion, respectively, and fixed maturity investments, other than those designated as held to maturity, with fair values of \$46.0 billion and \$42.1 billion, respectively. As of March 31, 2008, \$44.7 billion, or 97%, of the fixed maturity investments that are not designated as held to maturity within our international insurance subsidiaries were rated investment grade. The remaining \$1.3 billion, or 3%, of these fixed maturity investments were rated non-investment grade. Of those amounts, \$24.7 billion of the investment grade fixed maturity investments and \$0.7 billion of the non-investment grade fixed maturity investments were associated with Gibraltar Life. We consider attributes of the various categories of liquid assets (for example, type of asset and credit quality) in calculating internal liquidity measures to evaluate the adequacy of our international insurance operations' liquidity under stress scenarios. We believe that ongoing operations and the liquidity profile of our international insurance assets provide sufficient liquidity under reasonably foreseeable stress scenarios.

We employ various hedging strategies to manage potential exposure to foreign currency exchange rate movements as discussed in Results of Operations for Financial Services Businesses by Segment International Insurance and Investments Division. Cash settlements from this hedging activity result in cash flows to or from Prudential Financial and is dependent on changes in foreign currency exchange rates and the notional amount of the exposures hedged.

### ***Asset Management Subsidiaries***

Our asset management businesses, which include real estate, public and private fixed income and public equity asset management, as well as commercial mortgage origination and servicing, proprietary investing and retail investment products, such as mutual funds and other retail services, are largely unregulated from the standpoint of dividends and distributions. Our asset management subsidiaries through which we conduct these businesses generally do not have restrictions on the amount of distributions they can make, and provide a relatively stable source of significant cash flow to Prudential Financial.

The principal sources of liquidity for our asset management subsidiaries include asset management fees, revenues from proprietary investments, including commercial mortgage operations, and available borrowing lines from internal sources including Prudential Funding and Prudential Financial, as well as from third parties. The principal uses of liquidity include the financing associated with our proprietary investments, including commercial mortgage operations, general and administrative expenses, and distribution of dividends and returns of capital to Prudential Financial.

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The primary liquidity risks for our asset management subsidiaries relate to their profitability, which is impacted by market conditions and our investment management performance. Our asset management subsidiaries continue to maintain sufficiently liquid balance sheets. As of March 31, 2008 and December 31,

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2007, our asset management subsidiaries had cash and cash equivalents and short-term investments of \$1.773 billion and \$1.153 billion, respectively. We believe the cash flows from our asset management businesses are adequate to satisfy the current liquidity requirements of their operations, as well as requirements that could arise under foreseeable stress scenarios, which are monitored through the use of internal measures.

In reporting results for the three months ended March 31, 2008, we have classified our commercial mortgage securitization operations as a divested business for all periods reported, reflecting our decision to exit this business. We will retain and continue the remainder of our commercial mortgage origination, servicing and other commercial mortgage related activities, which remain a part of our Asset Management segment. We do not expect this decision to have a material impact on the liquidity of our Asset Management subsidiaries. For further details, see Divested Businesses.

***Prudential Securities Group***

As of March 31, 2008 and December 31, 2007, Prudential Securities Group's assets totaled \$10.8 billion and \$8.1 billion, respectively. Prudential Securities Group owns our investment in Wachovia Securities, which we account for under the equity method, as well as other wholly owned businesses. On October 1, 2007, Wachovia completed the acquisition of A.G. Edwards, Inc., or A.G. Edwards, for \$6.8 billion and on January 1, 2008 combined the retail securities brokerage business of A.G. Edwards with Wachovia Securities. See Note 10 to the Unaudited Interim Consolidated Financial Statements for additional information concerning this acquisition and its effect on our investment in Wachovia Securities. Distributions from our investment in Wachovia Securities to Prudential Securities Group totaled \$65 million and \$86 million for the three months ended March 31, 2008 and 2007, respectively.

The other wholly owned businesses in Prudential Securities Group continue to maintain sufficiently liquid balance sheets, consisting mostly of cash and cash equivalents, segregated client assets, and short-term receivables from clients, broker-dealers, and exchanges. As registered broker-dealers and members of various self-regulatory organizations, our U.S. registered broker-dealer subsidiaries and Wachovia Securities are subject to the SEC's Uniform Net Capital Rule, as well as the net capital requirements of the Commodity Futures Trading Commission and the various securities and commodities exchanges of which they are members. Compliance with these capital requirements could limit the ability of these operations to pay dividends.

**Financing Activities**

As of March 31, 2008 and December 31, 2007, total short- and long-term debt of the Company on a consolidated basis was \$31.3 billion and \$29.8 billion, respectively, which includes \$16.9 billion and \$16.7 billion, respectively, related to the parent company, Prudential Financial.

Prudential Financial is authorized to borrow funds from various sources to meet its capital needs, as well as the capital needs of its subsidiaries. The following table sets forth the outstanding short- and long-term debt of Prudential Financial, other than debt to consolidated subsidiaries, as of the dates indicated:

| March 31,<br>2008 | December 31,<br>2007 |
|-------------------|----------------------|
| (in millions)     |                      |

**Borrowings:**

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|  |                  |                  |
|--|------------------|------------------|
| General obligation short-term debt:    |                  |                  |
| Commercial paper                       | \$ 574           | \$ 1,293         |
| Floating rate convertible senior notes | 4,883            | 4,883            |
| Current portion of long-term debt      | 1,138            | 973              |
| General obligation long-term debt:     |                  |                  |
| Senior debt                            | 7,277            | 6,875            |
| Retail medium-term notes               | 2,980            | 2,688            |
| <b>Total general obligations</b>       | <b>\$ 16,852</b> | <b>\$ 16,712</b> |

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The following table presents, as of March 31, 2008, Prudential Financial's contractual maturities of its general obligation long-term debt:

|                     | Senior Debt     | Retail Medium-term<br>Notes<br>(in millions) |
|---------------------|-----------------|--|
| 2010                | \$ 25           | \$ 28  |
| 2011                | 25              | 67   |
| 2012                | 350             | 101  |
| 2013                | 850             | 100  |
| 2014 and thereafter | 6,027           | 2,684  |
| <b>Total</b>        | <b>\$ 7,277</b> | <b>\$ 2,980</b>                              |

Prudential Financial's short-term debt includes commercial paper borrowings that are primarily used to fund the working capital needs of Prudential Financial's subsidiaries and Prudential Financial. Prudential Financial's commercial paper program has a current authorized capacity of \$5.0 billion. Prudential Financial's outstanding commercial paper borrowings decreased \$719 million, from \$1.293 billion as of December 31, 2007 to \$574 million as of March 31, 2008, as a result of commercial paper being replaced by the proceeds from the floating rate convertible senior notes. The weighted average interest rate on the commercial paper borrowings under this program was 4.31% and 5.30% for the three months ended March 31, 2008 and 2007, respectively.

During the latter half of 2007 and continuing through the first quarter of 2008, the credit markets, and specifically the commercial paper market, were adversely impacted by concerns over the sub-prime mortgage exposure of certain financial institutions and asset-backed commercial paper programs. As a result, the financing cost of Prudential Financial commercial paper increased versus its historical cost basis relative to the target federal funds rate as investors demanded a premium for top-tier split rated commercial paper; that is, commercial paper rated A-1 by Standard & Poor's, P-2 by Moody's and F1 by Fitch.

While the cost of financing Prudential Financial commercial paper has increased, relative to our historical cost basis versus the target federal funds rate, we experienced no material change in investor demand for our commercial paper, which remains sufficient to meet our financing needs. We continue to monitor market conditions and believe we have sufficient flexibility to reduce our borrowings under the Prudential Financial commercial paper program, if needed, through our alternative sources of liquidity, as discussed under Alternative Sources of Liquidity, liquidation of assets, drawing on our available lines of credit or pursuing other options as appropriate.

In March 2006, Prudential Financial filed an updated shelf registration statement with the SEC, superseding its previous shelf registration statement, which permits the issuance of public debt, equity and hybrid securities. The updated shelf registration statement was established under the SEC rules adopted in 2005 that allow for automatic effectiveness upon filing, pay-as-you-go fees and the ability to add securities by filing automatically effective amendments for companies qualifying as Well-Known Seasoned Issuers. As a result, this new shelf registration statement has no stated issuance capacity.

In March 2006, Prudential Financial filed a prospectus supplement for a new Medium-Term Notes, Series D program under the shelf registration statement, which superseded its Medium-Term Notes, Series C program. In January 2008, the authorized issuance capacity of the Series D program was increased by \$5 billion to \$10 billion, and as of March 31, 2008 approximately \$4.9 billion remained available under the program. In January 2008, Prudential Financial issued \$600 million of 5-year medium term notes under this program. The net proceeds from the sale of these notes were used to fund operating needs of our subsidiaries and for general corporate purposes. The weighted average interest rates on Prudential Financial's medium-term and senior notes, including the effect of interest rate hedging activity, were 5.50% and 5.43% for the three months ended March 31, 2008 and 2007, respectively, excluding the effect of debt issued to consolidated subsidiaries.



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In March 2006, Prudential Financial filed a prospectus supplement under the shelf registration statement for its retail medium-term notes, including the InterNotes® program, which superseded the 2005 retail medium-term notes program. In March 2008, the authorized issuance capacity of the retail medium-term notes program was increased by \$2.5 billion to \$5 billion, and as of March 31, 2008 approximately \$2.8 billion remained available under the program. This retail medium-term notes program serves as a funding source for a spread product of our Retirement segment that is economically similar to funding agreement-backed medium-term notes issued to institutional investors, except that the retail notes are senior obligations of Prudential Financial and are purchased by retail investors. The weighted average interest rates on Prudential Financial's retail medium-term notes were 5.95% and 5.55% for the three months ended March 31, 2008 and 2007, respectively, excluding the effect of debt issued to consolidated subsidiaries.

In January 2008, Prudential Financial filed prospectus supplements to register under the shelf registration statement resales of the floating rate convertible senior notes that were issued in a private placement in December 2006 (\$2.0 billion). These convertible senior notes are convertible by the holders at any time after issuance into cash and shares of Prudential Financial's Common Stock. The conversion price, \$104.21 per share, is subject to adjustment upon certain corporate events. The conversion feature requires net settlement in shares; therefore, upon conversion, a holder would receive cash equal to the par amount of the convertible notes surrendered for conversion and shares of Prudential Financial Common Stock only for the portion of the settlement amount in excess of the par amount, if any. The interest rate on these convertible senior notes is a floating rate equal to 3-month LIBOR minus 2.4%, to be reset quarterly. These convertible senior notes are redeemable by Prudential Financial, at par plus accrued interest, any time on or after December 13, 2007. Holders of the notes may also require Prudential Financial to repurchase the notes, at par plus accrued interest, on contractually specified dates, of which the first such date was December 12, 2007. On December 12, 2007, \$117 million of senior notes were repurchased by Prudential Financial at the request of the holders. The next date on which holders of the notes may require Prudential Financial to repurchase the notes is December 12, 2008. A majority of the proceeds from the original issuance of these notes were initially invested in an investment grade fixed income portfolio, while the remainder of the proceeds was used for general corporate purposes. Prior to the first date that holders of the notes could require us to repurchase the notes, December 12, 2007, we liquidated the investment portfolio. Currently, the remaining proceeds are invested in short-term instruments and may be used to fund operations or short-term capital needs in lieu of other short-term borrowings in future periods. See Note 12 to our Consolidated Financial Statements included in our 2007 Annual Report on Form 10-K for additional information concerning these convertible senior notes. Prudential Financial is obligated to file once per quarter a prospectus supplement to register any resales of these convertible senior notes and shares of Prudential Financial Common Stock, if any, issued to holders of these convertible senior notes.

In April 2008, Prudential Financial filed prospectus supplements to register under the shelf registration statement resales of the floating rate convertible senior notes that were issued in a private placement in December 2007 (\$3.0 billion). These convertible senior notes are convertible by the holders at any time after issuance into cash and shares of Prudential Financial's Common Stock. The conversion price, \$132.39 per share, is subject to adjustment upon certain corporate events. The conversion feature requires net settlement in shares; therefore, upon conversion, a holder would receive cash equal to the par amount of the convertible notes surrendered for conversion and shares of Prudential Financial Common Stock only for the portion of the settlement amount in excess of the par amount, if any. Prudential Financial used the majority of the offering proceeds to fund operating needs of our subsidiaries, purchase short-term investment grade fixed income investments, and general corporate purposes, as well as to repurchase shares of its common stock under the 2007 share repurchase authorization. A portion of the offering proceeds used to fund the operating needs of subsidiaries were used to reduce Prudential Financial's commercial paper borrowings and to extend the duration of our borrowings to better match the duration of the subsidiaries' related assets. These convertible senior notes are redeemable by Prudential Financial, at par plus accrued interest, on or after June 16, 2009. Holders of the notes may also require Prudential Financial to repurchase the notes, at par plus accrued interest, on contractually specified dates, of which the first such date is June 15, 2009. The interest rate on these convertible senior notes is a floating rate equal to 3-month LIBOR minus 1.63%, to be reset quarterly. See Note 12 to our Consolidated Financial Statements included in our

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2007 Annual Report on Form 10-K for additional information concerning these convertible senior notes. Prudential Financial is obligated to file once per quarter a prospectus supplement under the shelf registration statement to register any resales of these convertible senior notes and shares of Prudential Financial Common Stock, if any, issued to holders of these convertible senior notes.

In March 2008, Prudential Financial updated its European medium-term notes program under a shelf registration statement. The Company is authorized to issue up to \$1.5 billion of notes under the program. As of March 31, 2008, there was no debt outstanding under this program.

Current capital markets activities for the Company on a consolidated basis principally consist of unsecured short-term and long-term debt borrowings issued by Prudential Funding and Prudential Financial, unsecured third party bank borrowings, and asset-based or secured financing. The secured financing arrangements include transactions such as securities lending and repurchase agreements, which we generally use to finance liquid securities in our short-term spread portfolios, primarily within Prudential Insurance. These short-term spread portfolios hold asset-backed securities, a portion of which is collateralized by sub-prime mortgages. See Realized Investment Gains and Losses and General Account Investments General Account Investments Fixed Maturity Securities for a further discussion of our asset-backed securities collateralized by sub-prime holdings. We continue to have significant unused secured financing capacity (as discussed under Liquidity of Subsidiaries Domestic Insurance Subsidiaries Cash Flow ); however, the availability of this financing to roll-over existing financing and to access our unused capacity is contingent on market conditions and may not be available to us on terms that are cost effective.

The following table sets forth total consolidated borrowings of the Company as of the dates indicated:

|  | March 31,<br>2008 | December 31,<br>2007 |
|--|-------------------|----------------------|
|  | (in millions)     |                      |
| <b>Borrowings:</b>                                 |                   |                      |
| General obligation short-term debt                 | \$ 15,925         | \$ 15,349            |
| General obligation long-term debt:                 |                   |                      |
| Senior debt  | 10,774            | 10,103               |
| Surplus notes(1)                                   | 2,294             | 2,044                |
| Total general obligation long-term debt            | 13,068            | 12,147               |
| <b>Total general obligations</b>                   | <b>28,993</b>     | <b>27,496</b>        |
| Limited and non-recourse borrowing:                |                   |                      |
| Limited and non-recourse short-term debt           | 299               | 308                  |
| Limited and non-recourse long-term debt(2)         | 1,984             | 1,954                |
| Total limited and non-recourse borrowing           | 2,283             | 2,262                |
| <b>Total borrowings(3)</b>                         | <b>31,276</b>     | <b>29,758</b>        |
| Total asset-based financing                        | 14,331            | 18,236               |
| <b>Total borrowings and asset-based financings</b> | <b>\$ 45,607</b>  | <b>\$ 47,994</b>     |



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- (1) As of March 31, 2008 and December 31, 2007, includes \$1.850 billion and \$1.600 billion, respectively, of floating rate surplus notes issued by subsidiaries of Prudential Insurance to fund regulatory reserves, as well as \$444 million of fixed rate surplus notes issued by Prudential Insurance.
- (2) As of both March 31, 2008 and December 31, 2007, \$1.750 billion of limited and non-recourse debt outstanding was attributable to the Closed Block Business.
- (3) Does not include \$8.7 billion and \$8.5 billion of medium-term notes of consolidated trust entities secured by funding agreements purchased with the proceeds of such notes as of March 31, 2008 and December 31, 2007, respectively. These notes are included in Policyholders' account balances. For additional information see Funding Agreement Notes Issuance Program.

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Total general debt obligations increased by \$1.497 billion from December 31, 2007 to March 31, 2008, reflecting a \$921 million net increase in long-term debt and a \$576 million net increase in short-term debt. The net increase in long-term debt was primarily driven by the net issuance of medium-term notes, retail medium-term notes, and surplus notes, partially offset by the reclassification of long-term debt to short-term debt, in the first quarter of 2008. The net increase in short-term debt was primarily due to an increase in outstanding commercial paper supporting our operating businesses at Prudential Funding, as well as the reclassification of long-term debt to short-term debt, partially offset by a decrease in outstanding commercial paper at Prudential Financial.

Prudential Funding's commercial paper and master note borrowings were \$8.5 billion and \$7.3 billion as of March 31, 2008 and December 31, 2007, respectively. Prudential Funding's commercial paper program has a current authorized capacity of \$12.0 billion. The weighted average interest rates on the commercial paper borrowings and master notes were 3.37% and 5.26% for the three months ended March 31, 2008 and 2007, respectively. Prudential Financial has issued a subordinated guarantee covering Prudential Funding's domestic commercial paper program.

During the latter half of 2007 and continuing through the first quarter of 2008, the financing cost of Prudential Funding's commercial paper remained relatively unchanged versus its historical cost basis relative to the target federal funds rate. Prudential Funding's commercial paper is rated A-1+, P-1, F1+ by Standard & Poor's, Moody's, and Fitch, respectively.

The total principal amount of debt outstanding under Prudential Funding's domestic medium-term note programs was \$772 million, as of March 31, 2008 and December 31, 2007, of which \$600 million was reflected in the general obligation short-term debt as of March 31, 2008 and December 31, 2007. The weighted average interest rates on Prudential Funding's long-term debt, including the effect of interest rate hedging activity, were 4.94%, and 6.18% for the three months ended March 31, 2008 and 2007, respectively.

During 2006, a subsidiary of Prudential Insurance entered into a surplus note purchase agreement with an unaffiliated financial institution that provides for the issuance of up to \$3 billion of ten-year floating rate surplus notes for the purpose of financing certain regulatory reserves required to be held by subsidiary life insurers in connection with the intercompany reinsurance of certain term life insurance policies. Surplus notes issued under this facility are subordinated to policyholder obligations and are subject to regulatory approvals for principal and interest payments. In the first quarter of 2008, the subsidiary issued an additional \$250 million of surplus notes, resulting in total outstanding notes under this facility of \$1.350 billion and \$1.100 billion as of March 31, 2008 and December 31, 2007, respectively. See Note 12 to our Consolidated Financial Statements included in our 2007 Annual Report on Form 10-K for additional information.

Our total borrowings consist of capital debt, investment related debt, securities business related debt and debt related to specified other businesses. Capital debt is borrowing that is used or will be used to meet the capital requirements of Prudential Financial as well as borrowings invested in equity or debt securities of direct or indirect subsidiaries of Prudential Financial and subsidiary borrowings utilized for capital requirements. Investment related borrowings consist of debt issued to finance specific investment assets or portfolios of investment assets, including institutional spread lending investment portfolios, real estate and real estate related investments held in consolidated joint ventures, as well as institutional and insurance company portfolio cash flow timing differences. Securities business related debt consists of debt issued to finance primarily the liquidity of our broker-dealers and our capital markets and other securities business related operations. Debt related to specified other businesses consists of borrowings associated with our individual annuity business, real estate franchises and relocation services. Borrowings under which either the holder is entitled to collect only against the assets pledged to the debt as collateral, or has only very limited rights to collect against other assets, have been classified as limited and non-recourse debt. Consolidated borrowings as of March 31, 2008 and December 31, 2007 included \$1.750 billion of limited and non-recourse debt attributable to the Closed Block Business.

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The following table summarizes our borrowings, categorized by use of proceeds, as of the dates indicated:

|   | March 31,<br>2008 | December 31,<br>2007 |
|---|-------------------|----------------------|
|   | (in millions)     |                      |
| <b>General obligations:</b>                 |                   |                      |
| Capital debt                                | \$ 6,365          | \$ 4,781             |
| Investment related                          | 16,333            | 16,379               |
| Securities business related                 | 4,618             | 4,776                |
| Specified other businesses                  | 1,677             | 1,560                |
| <b>Total general obligations</b>            | <b>28,993</b>     | <b>27,496</b>        |
| Limited and non-recourse debt               | 2,283             | 2,262                |
| <b>Total borrowings</b>                     | <b>\$ 31,276</b>  | <b>\$ 29,758</b>     |
| Short-term debt                             | \$ 16,224         | \$ 15,657            |
| Long-term debt                              | 15,052            | 14,101               |
| <b>Total borrowings</b>                     | <b>\$ 31,276</b>  | <b>\$ 29,758</b>     |
| Borrowings of Financial Services Businesses | \$ 27,090         | \$ 26,865            |
| Borrowings of Closed Block Business         | 4,186             | 2,893                |
| <b>Total borrowings</b>                     | <b>\$ 31,276</b>  | <b>\$ 29,758</b>     |

*Funding Agreement Notes Issuance Program*

In 2003, Prudential Insurance established a Funding Agreement Notes Issuance Program pursuant to which a Delaware statutory trust issues medium-term notes (which are included in our statements of financial position in Policyholders' account balances and not included in the foregoing table) secured by funding agreements issued to the trust by Prudential Insurance and included in our Retirement segment. The funding agreements provide cash flow sufficient for the debt service on the related medium-term notes. The medium-term notes are sold in transactions not requiring registration under the Securities Act of 1933, as amended. As of March 31, 2008 and December 31, 2007, the outstanding aggregate principal amount of such notes totaled approximately \$8.7 billion and \$8.5 billion, respectively, out of a total authorized amount of up to \$15 billion. The notes have fixed or floating interest rates and original maturities ranging from two to seven years.

**Lines of Credit and Other Credit Facilities**

As of March 31, 2008, Prudential Financial, Prudential Insurance and Prudential Funding had unsecured committed lines of credit totaling \$5.0 billion. This amount includes a \$500 million 364-day credit agreement that expires in December 2008, which includes eight financial institutions, a \$2.0 billion 5-year credit facility that expires in May 2012, which includes 23 financial institutions, and an additional \$2.5 billion credit facility, of which \$200 million expires on Dec 2011 and \$2.3 billion expires in December 2012, which includes 21 financial institutions. Borrowings under the outstanding facilities will mature no later than the respective expiration dates of the facilities. We use these facilities primarily as back-up liquidity lines for our commercial paper programs, and there were no outstanding borrowings under any of these facilities as of March 31, 2008.

Our ability to borrow under these facilities is conditioned on the continued satisfaction of customary conditions, including maintenance at all times by Prudential Insurance of total adjusted capital of at least \$5.5 billion based on statutory accounting principles prescribed under New Jersey law. Prudential Insurance's total adjusted capital as of December 31, 2007 was \$11.0 billion and continues to be above the \$5.5 billion threshold. The ability of Prudential Financial to borrow under these facilities is also conditioned on its maintenance of consolidated net worth of at least \$12.5 billion, calculated in accordance with GAAP. Prudential Financial's net worth on a consolidated basis totaled \$22.7 billion and \$23.5 billion as of March 31, 2008 and December 31, 2007, respectively. We also use uncommitted lines of credit from banks and other financial institutions.

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### **Item 3. *Quantitative and Qualitative Disclosures About Market Risk***

Market risk is the risk of change in the value of financial instruments as a result of absolute or relative changes in interest rates, foreign currency exchange rates or equity or commodity prices. To varying degrees, the investment and trading activities supporting all of our products and services generate market risks. There have been no material changes in our market risk exposures from December 31, 2007, a description of which may be found in our Annual Report on Form 10-K for the year ended December 31, 2007, Item 7A, *Quantitative and Qualitative Disclosures About Market Risk*, filed with the Securities and Exchange Commission.

### **Item 4. *Controls and Procedures***

In order to ensure that the information we must disclose in our filings with the Securities and Exchange Commission is recorded, processed, summarized, and reported on a timely basis, the Company's management, including our Chief Executive Officer and Chief Financial Officer, have reviewed and evaluated the effectiveness of our disclosure controls and procedures, as defined in Exchange Act Rule 13a-15(e), as of March 31, 2008. Based on such evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that, as of March 31, 2008, our disclosure controls and procedures were effective. No change in our internal control over financial reporting, as defined in Exchange Act Rule 13a-15(f), occurred during the quarter ended March 31, 2008, that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

## **PART II OTHER INFORMATION**

### **Item 1. *Legal Proceedings***

We are subject to legal and regulatory actions in the ordinary course of our businesses, including class action lawsuits. Our pending legal and regulatory actions include proceedings specific to us and proceedings generally applicable to business practices in the industries in which we operate including, in both cases, businesses that have either been divested or placed in wind-down status. We are also subject to litigation arising out of our general business activities, such as our investments, contracts, leases and labor and employment relationships, including claims of discrimination and harassment. In some of our pending legal and regulatory actions, parties are seeking large and/or indeterminate amounts, including punitive or exemplary damages.

In January and February 2008, in *In Re Employee Benefit Insurance Brokerage Antitrust Litigation*, the United States District Court for the District of New Jersey dismissed the federal claims with prejudice and the state law claims without prejudice. Plaintiffs have filed a notice of appeal to the Third Circuit Court of Appeals.

In March 2008, in *Bouder v. Prudential Financial, Inc. and The Prudential Insurance Company of America*, the United States District Court for the District of New Jersey granted plaintiffs' motion to conditionally certify a nationwide class.

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In April 2008, Prudential Insurance reached a settlement of proceedings relating to payments to insurance intermediaries and certain other practices with the District Attorneys of San Diego, Los Angeles and Alameda counties. Pursuant to this settlement, Prudential Insurance paid \$350,000 in penalties and costs.

Our litigation and regulatory matters are subject to many uncertainties, and given their complexity and scope, the outcomes cannot be predicted. It is possible that our results of operations or cash flow in a particular quarterly or annual period could be materially affected by an ultimate unfavorable resolution of pending litigation and regulatory matters depending, in part, upon the results of operations or cash flow for such period. In light of the unpredictability of the Company's litigation and regulatory matters, it is also possible that in certain cases an ultimate unfavorable resolution of one or more pending litigation or regulatory matters could have a material adverse effect on our financial position. Management believes, however, that, based on

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information currently known to it, the ultimate outcome of all pending litigation and regulatory matters, after consideration of applicable reserves and rights to indemnification, is not likely to have a material adverse effect on our financial position.

The foregoing discussion is limited to recent material developments concerning our legal and regulatory proceedings. See Note 11 to the Unaudited Interim Consolidated Financial Statements included herein for additional discussion of our litigation and regulatory matters, including those referred to above.

**Item 1A. Risk Factors**

You should carefully consider the risks described under **Risk Factors** in our Annual Report on Form 10-K for the year ended December 31, 2007. These risks could materially affect our business, results of operations or financial condition, cause the trading price of our Common Stock to decline materially or cause our actual results to differ materially from those expected or those expressed in any forward looking statements made by or on behalf of the Company. These risks are not exclusive, and additional risks to which we are subject include, but are not limited to, the factors mentioned under **Forward-Looking Statements** above and the risks of our businesses described elsewhere in our Annual Report on Form 10-K and in this Quarterly Report on Form 10-Q.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

(c) The following table provides information about purchases by the Company during the quarter ended March 31, 2008, of its Common Stock.

| Period                                     | Total Number of Shares Purchased(1)(2) | Average Price Paid per Share | Total Number of Shares Purchased as Part of Publicly Announced Program(1) | Approximate Dollar Value of Shares that May Yet be Purchased under the Program(1) |
|--|--|------------------------------|---|---|
| January 1, 2008 through January 31, 2008   | 3,448,280                              | \$ 85.96                     | 3,447,500   |   |
| February 1, 2008 through February 29, 2008 | 5,476,870                              | \$ 73.25                     | 5,027,000   |   |
| March 1, 2008 through March 31, 2008       | 2,893,024                              | \$ 70.38                     | 2,888,000   |   |
| Total                                      | 11,818,174                             | \$ 76.25                     | 11,362,500  | \$ 2,630,945,886  |

- (1) In November 2007, Prudential Financial's Board of Directors authorized the Company to repurchase up to \$3.5 billion of its outstanding Common Stock during calendar year 2008.
- (2) Includes shares of Common Stock withheld from participants for income tax withholding purposes whose shares of restricted stock, restricted stock units, and performance shares vested during the period. Restricted stock, restricted stock units, and performance shares were issued to participants pursuant to the Prudential Financial, Inc. Omnibus Incentive Plan that was adopted by the Company's Board of Directors in March 2003 (as subsequently amended and restated).

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**Item 6. Exhibits**

- 10.1 Prudential Financial, Inc. Non-Employee Director Compensation Summary (as adopted on October 9, 2007, effective January 1, 2008). (Corrected) \*
- 10.2 First Amendment to the Prudential Supplemental Employee Savings Plan, effective as of January 1, 2006. \*
- 12.1 Statement of Ratio of Earnings to Fixed Charges.
- 31.1 Section 302 Certification of the Chief Executive Officer.
- 31.2 Section 302 Certification of the Chief Financial Officer.
- 32.1 Section 906 Certification of the Chief Executive Officer.
- 32.2 Section 906 Certification of the Chief Financial Officer.

\* This exhibit is a management contract or compensatory plan or arrangement.

Prudential Financial, Inc. will furnish upon request a copy of any exhibit listed above upon the payment of a reasonable fee covering the expense of furnishing the copy. Requests should be directed to:

Shareholder Services

Prudential Financial, Inc.

751 Broad Street, 6th Floor

Newark, NJ 07102



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**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

PRUDENTIAL FINANCIAL, INC.

By: */s/* RICHARD J. CARBONE  
**Richard J. Carbone**

**Executive Vice President and Chief Financial Officer**

**(Authorized signatory and principal financial officer)**

Date: May 1, 2008

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**Exhibit Index**

***Exhibit Number and Description***

|      |   |
|------|---|
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