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Lincoln National Corp. (LNC)

Analysts and Investors Meeting

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MANAGEMENT DISCUSSION SECTION

Christopher A. Giovanni

Senior Vice President & Head-Investor Relations, Lincoln National Corp.

Good morning. Thank you, everyone, for making the trip for Philadelphia. For those that are in the room and for those that are on the webcast, thanks for joining us as well. We appreciate if you could just turn your phones down, if you have them on. And again, I'm Chris Giovanni the Head of Investor Relations here at Lincoln Financial Group. Welcome to 2017 Conference for Analysts, Investors and Bankers.

We are going to kick things off, you should have the agenda in front of you, with Dennis Glass for an overview. We'll then move to presentations from distribution, our operating businesses and the investment portfolio before wrapping up with Randy Freitag with the financial overview.

We're going to have plenty of time for Q&A over the course of the day. We'll have three sessions for that. As always, we ask that you identify yourself, your firm, limit yourself to one question and one follow-up. We can get back to you at the end if there are additional questions. After the second Q&A session, we'll have a quick lunch just in the back of the room there, and then I ask if everyone could rejoin us to finish up the presentations over the course of the day.

Lastly, just want to turn your attention to the cautionary language statements that you can find in the booklets. As you can see, we will be making forward-looking statements. These forward-looking statements involve risks and uncertainties that could cause actual results to differ materially. We described these cautionary statements and disclosures that you can find in the appendix in our forms 10-K, 10-Q and 8-K that was filed this morning.

Today's presentations do contain non-GAAP financial measures and where appropriate we will have included reconciliations to their most comparable GAAP measure as well as explanatory notes and how we measure these and for the reasons that we do so.

So, with that out of the way, let's start to begin the session and I'd like to welcome Denis Glass, President and CEO, to the stage.

Dennis R. Glass

President, Chief Executive Officer & Director, Lincoln National Corp.

Well, good morning, everybody, and thank you for being here. This is a great venue. I guess, it falls into the category. We're going to work very hard, but have a little bit of fun at the same time. It also because the Eagles so far are having a winning season sort of sets the backdrop for what you're going to see this morning. So, again, thanks everyone for joining us either here or on the webcast. We greatly appreciate you taking the time to learn more about Lincoln.

Let me start by saying our share price has closed some of the gap between where we think it should be based on performance and where it is. Our thought is that the best way to further close the gap is to continue to report good earnings, ROE development and growth. Today is structured to demonstrate why we are confident that we can accomplish this.

Another opportunity for today is to provide more sunlight on some of the issues that folks either on here or elsewhere had asked about our operations. So the more sunlight information that we can give you to help you draw better conclusions or good conclusions about what we're doing is a good thing.

Management and execution drive results and we've added a number of presenters today to the list of people you've seen in the past to give you a better understanding of our businesses and the depth of our leadership. So you will hear additionally today from Dick Mucci, who has executed with his team the turnaround at Group Protection. You will hear from Jamie Ohl, who runs our Retirement business and has been the driver behind the terrific increase in sales and positive net flows and also has recruited a very good team underneath her. And you'll also hear from Mike Burns who's been running very successfully our Life Insurance business for quite a number of years.

Just stepping back, you all know we've reached 110-year high in both earnings, and although the stock price has dropped off a little bit, we've reached an all-time high with our share price. I took a look at that and thought well, the indexes are as high as they've ever been, we've all seen that. But I compared our success on reaching a all-time high in share price to our large cap competitors and discovered in fact there's only a handful of us that have been able to achieve that level. So we are differentiated.

These achievements in earnings and share price reflect the consistency and effectiveness of our strategies and, at the same time, the capacity to adapt the changes in capital markets regulation and consumer preferences. We are confident as we move forward that we will achieve more for our shareholders.

Let me pause for a second and shift gears away from our businesses and how we are executing and just about tax reform for just a second as part of the leadership that the ACLI have been involved in some of these conversations and let me just give you my thoughts.

First, the industry supports tax reform, in general. Second, based on my current understanding, there is no indication from either the Senate or House again to my knowledge that there is an intent to raise more revenue from the industry than is commensurate with the amount by which we will benefit from the rate cuts.

Now, there's a lot of parliamentary things that are going on to keep the process moving. And let me cite one issue. As you know, again, on this specific issue, the House included, as Speaker Ryan said a placeholder, specifically the 8% tax surcharge. This is a placeholder, the surtax is not intended to be in a final bill, but again was used procedurally to keep the process moving. So, there will be new and significant information unfolding everyday as these bills work their way through the House and the Senate. Lincoln and the industry both continues to watch what's going on and influenced to the best of our ability as things change. So, let me leave it at that.

So, turning back to-do, what we're doing to continue our strong execution and strong results. I want to repeat that although our high level strategy remains consistent, our business model and balance sheet give us the capacity to both seize opportunities and address headwinds. So, looking to the next few years, you will see much of what you've seen in the past, new product development and further diversification of our product line, which will result in top-line growth and reduce our concentration risk, continued leverage of distribution strength with select pockets of distribution and shelf space expansion, a continued focus on growing on the balance – excuse me – continued focus on balancing growth, capital management and our sources of earnings, and, of course, our new digital initiative, which will improve the customer experience and drive expense savings.

So, this is a great slide to remind you how we have been able to successfully respond and adapt to many of the things that have been thrown at us in the past couple of years. So first, we all know that interest rates have been low. So what have we done? We've taken action. We've repriced and pivoted our product portfolio achieving strong returns. We have initiated discrete expense saving programs on top of and already rigorous budgeting process where we force the business units to have expenses grow at a slower rate than revenues, and we have [ph] thought (09:04) opportunities in the investment portfolio to boost yield, while at the same time maintaining a good credit profile and maintaining our ALM discipline.

The capital markets have been volatile at times, but we have weathered better than many of our peers. We have not had large below-the-line charges like many have had and we have continued to improve our free cash flow. Importantly, we have returned this free cash flow to our shareholders. We continue to invest in our industry-leading VA hedge program, which has served us exceptionally well. And as you know, we have a long-term strategy of increasing our mortality and morbidity sources of earnings to buy more stability during periods of capital market uncertainty.

We do operate in a competitive industry, but we are able to successfully navigate this environment. We focus exclusively in areas where we have scale and competitive advantages combined with attractive growth opportunities. We benefit from our broad distribution reach and we also have been able to leverage our business model and use the competitive environment to our advantage in a lot of ways, but one specifically negotiating lower fees [ph] and creating (10:32) more revenue across our investment portfolio, more revenue for our shareholders.

And lastly, the regulatory landscape continues to change. I am pleased that Lincoln has proven ability to respond, influence and adapt to key regulatory and policy matters. AG38, life captives and DOL are a few examples of influence. Some of these actions have produced the numbers on this slide. Our financial results have been very strong, as Randy will discuss later have differentiated us relative to peers, as you can see here double-digit earnings per share growth, ROE expansion, a significant amount of capital return to shareholders through both buybacks and dividend increases.

We said at the last Investor Day that these types of results are repeatable. And since then, again, we have posted record EPS in several quarters. Our ROE has expanded another 60 basis points this year and we continue to return a lot of capital. These results have paid off for our shareholders. Again, as you can see here, we have been the best performing stock over these periods, as our strong execution is creating significant value for shareholders.

Now let's move to provide a little bit more sunlight on the future game plan. You're hopefully familiar with this waterfall chart we have been showing for years now. It shows the key drivers of how we can achieve our 8% to 10% earnings per share growth target over time. I think it's one of the best helps to the folks in the audience and trying to understand what we're doing, and where the levers are that we can pull to take advantage of opportunities and take advantage or – excuse me – beat headwinds.

We've done this at the corporate level, but today we're kind of drop down and [indiscernible] (12:01) each of the business units. And again by business units, the drivers of earnings growth are different. And the levers they will be pulling to achieve their growth are different and we want to dig into that quite a bit.

This is not guidance, but is intended to give you a better sense of how we are managing each business and how they are contributing to our target growth. The bottom of the page is summary of targets by line of business, but a lot more information to come over the course of the day as you see this displayed by each of the business unit leaders.

Team get into details on this slide much more today. But, again, I think it is important to remind you that Lincoln is differentiated by the power of our distribution franchise and markets we serve and the depth of products we bring to those markets. As you can see here, we have more than 700 wholesalers and access to more than 90,000 independent producer and behind these producers are hundreds of thousands of potential customers.

And this framework is what allows us with a strong distribution and reach to the ultimate customer is really the driver of why we're able to adapt and pivot as reasons developed that we have to adapt and pivot. We have a lot of activity taking place to further expand our comprehensive set of retail products, some new products contributed [ph] in day (13:45), and you'll hear about this Max 6 Select in the annuity business, the Director in the RPS business, and of course MoneyGuard. We're also positioning ourselves for emerging growth opportunities and index variable annuity which is selling well in the marketplace today, and we're not selling them. We will be in the first part of next year, term insurance for millennials and new accident and critical illness products in our group business.

Even without several of these initiatives underway, our sales growth is pretty strong across most of our businesses. We have really accelerated our sales momentum in 2017, and, importantly, returns are above 12% in every segment. RPS is just knocking it out of the park with a growth rate more than two times previous years. Group protection isn't facing the repricing headwinds they've had in prior years, enabling them to put together back-to-back years of double-digit sales growth.

We've had a ton of success on our Life business as we captured demographic trends with MoneyGuard and term sales remain near record levels. And we are leveraging digital technology to expand distribution and reach new customers.

Annuities is the one segment that is down relative to recent years, but as I noted on our recent earnings call we have seen very significant acceleration of sales since the summer giving us the confidence that we'll be able to turn this trend around.

The last item I want to highlight is the digital initiative we have in place to help sustain our success. The focus here is to improve the customer experience as consumer expectations continue to rise across the industry.

As I have said to you before we are no longer, from a customer service perspective competing, against the Met or Transamerica or competing against the born-digital companies like Uber and Airbnb. Those companies are setting the expectations and those are the kind of customer service interactions that people are going to expect from Lincoln and other insurance companies.

We've already seen some success of innovation across the enterprise. In the past we've talked about our predictive analytics to identify producers in our distribution organizations. TermAccel, which utilizes automated underwriting in our Life business, and Click-to-Contribute in RPS. New advances include chat box to resolve certain customer questions, improve policy statements and the implementation of robotic technology, all of which really improve the customer experience and lower expenses.

So stepping back, we have a proven ability to successfully respond to industry opportunities and headwinds. We have strong, resilient and repeatable financial results creating significant shareholder value, our powerful retail franchise with great long-term opportunities in front of us and leveraging technological innovation to continue our success.

So with this brief overview, we have a lot to work through today. So, I'm now going to turn it over to Will Fuller, who will start with a deeper dive into our great distribution network. Once again, thank you for being here, and I hope it's a productive day, and I expect it will be. Thank you very much.

Will H. Fuller

President-Lincoln Financial Group Annuity Solutions, Lincoln Financial Distributors & Lincoln Financial Network, Lincoln National Corp.

Thank you very much, Dennis. Good morning everyone. We're going to try something a little bit different to start today, and just reflecting on the last year to two years where we've had a lot of conversations around the DOL and topics such as that, often the question would be what are your partners thinking? How are they thinking about their business? Importantly, how are they thinking about their relationship with Lincoln? And so we thought what we do is bring their thoughts to you. We asked several of our senior management of strategic partners these questions and here is what they had to say.

[Video Presentation] (19:52-21:52)

So today I'm going to be talking a lot about strategic partners, because this is the cornerstone of our strategy. This is where we focus our time and attention, where we spend our resources. It's also where we get 80% of our sales. And the lifeblood of any business is to be able to reach your customers and provide something of value that they're willing to pay for.

And so our strategic partnership model mirrors that strategy. It also mirrors the principle that you want to keep the clients you have, you want to do more business with them, and you want to go get new clients, in that order. And you'll see these two principles kind of woven throughout the distribution section today and then carry forward over into the business unit presentations later in the day.

What's our formula? There's a couple of tenets that we tell our strategic partners that they can count on and that we commit to as a company. It always starts with the anchor to a strategy of consistent market presence. It means that we're committed to the business lines that we're in, we don't enter and exit, we stay committed to them even in tough times.

We offer a broad portfolio of solutions. And I mean a broad portfolio within each line of business and that portfolio is getting broader through additional product expansion.

We sell through independent producers. I'll talk a little bit later about why, very compelling growth and it's where the sales are in the industry. We lead with a high-touch, high-service, high-support model. You see that in a very large best-in-class group of sophisticated wholesalers and we're known for our partners to innovate, that innovation could be in the form of a product like i4LIFE or MoneyGuard, it could be an innovation of a service and support.

This is what we're known for and it's a very, very effective formula. When you step back and think about the marketplace that we go into, we sell through financial professionals. And there's 850 financial professionals in the United States that can choose to participate in the value propositions that you see here on the left and the products and solutions that as an industry and as a company we manufacture and we take to them.

And increasingly, these professionals over the course of the last few decades, have gone from very focused – think stockbroker, insurance agent, health insurance broker, they've all become more generalist, more seeking to advise on a broader portfolio of products and services.

And this is where our wholesaler specialization comes into the equation is as you become more of a generalist, you really do need the support of a specialist. When you think about some of these value propositions and planning concepts on the left, planning for guaranteed lifetime income and protecting against increasing longevity or estate planning. These are very technical in nature, require a lot of education and that's what our high touch, high service wholesaler model does.

In addition, when you step back and look at the trends in the businesses that we're in, you see very favorable trends. On one hand, the vast majority of the assets, investable assets in America are in the hands of those at or near retirement.

And as you'll see later today, that continues to grow. It actually doubles the dollars of investable assets, double over the course of next 15 years. And this is a generation of Americans that are having to increasingly rely on their own savings and their own investments to generate the income they need in retirement and deal with increasing life expectancy, that is not theoretical, it is real. And then on the other hand, you've got this very large vibrant workforce, low unemployment.

The entrance of this growing and dynamic population of the millennials, where the vast majority of income is and the work side is becoming a place, where folks really activate a lot of their financial lives, whether it'd be starting their with, building their retirement plan, their retirement accumulation or buying important benefits for them and their family. And our distribution models are lined to support that. So positive tailwinds.

And when you combine wholesale, retail, worksite distribution and all of those product activities, what you see from in that consistent market presence is the ability for a company to sell in a significant way through a full cycle. And you see that reflected here. This represents over $60 billion in positive net flows since 2008. And, in fact, the enterprise as a whole across all of our products, we have not had a single quarter of negative net flows, not even in the depth of the financial crisis.

You see it in the market leaderships and the target markets that we have. You see it in that 90,000 producers who have a choice, they're independent, they have a choice, and they choose to actively sell Lincoln. And many of them selling across our product portfolios, selling multiple products. And you see it in the diverse sales mix. No one product disproportionate to the other. Very strong impressive platform for Lincoln and positive catalyst to execute on Lincoln's strategic priorities in the future.

So how do we do it? First, we go to where the money is. Independent distribution is where most of the sales are, and that is growing. Second, we go to where the producers are. The reason that we have a strategic partner strategy is because the largest group of producers and customers happening to be with the industry icons. I want you to think about our strategic partners of the names you know, it's the Morgan Stanley, in UBS, who you heard from today, it's Merrill Lynch, it's Wells Fargo, it's Raymond James, it's Primerica, it's Edward Jones. They offer that large base of producers and even larger base of customers. They offer a prominent shelf space, where we can be active with the full range and full suite of solutions that we have across life and annuity – an RPS in this case. And it's where we spend most of our time and effort and it's where we get 80% of our sales.

We're also diverse by channels. We recognize that those strategic partners are organized in unique different business models. They serve their clients in unique ways. We align to them in the way that they serve their client, whether you're concentrating as insurance broker, or you're a banker, an independent producer. Let me point out that no one partner has a disproportionate share of our sales. Our largest seller of product as a company is our own retail network, LFN, which is both in part an insurance brokerage network, retail and in part an independent broker dealer. It's 15% of our sales. All of their strategic partnerships contribute single-digit sales individually, again, very diversified by partners.

And this model, this approach that we have is in demand by our partners. They want Lincoln in their system. Why do they want us in their system? Consistent market presence cannot be overlooked. It is so important. Our partners depend on products and solutions to serve their customers. Companies that come in and out that enter and exit, cause a lot of disruption and we do not do that. We've never done that. And they know it. They know we're committed to the lines of business and being consistent.

With Lincoln, you can partner with one company and get more than 20 different products. Almost all forms of individual life, almost all forms of individual annuity, two retirement plan services options and money guards. And so that is an efficiency for a partner to have the company like Lincoln, and able to get a full array of products from a single source versus having a collection of model lines that are concentrated in one product area or another.

And again, when you've got more than 550 wholesalers in your market, we can provide that high-touch service, which means we can go into your local branch office, we can interact with your advisor teams face to face, educate and support them as needed.

Now, the strategic partner strategy benefits us, too. And in one way in which it benefits us, I think, is particularly compelling is the ability for us to see a market or a product that we're not in and get in there and take share. And our small market retirement plan services strategy, which is helping to drive a lot of that growth in Jamie Ohl's area that Dennis talked about, in part, it's a perfect example of that.

In 2011, we saw in LFD strategic partners that we had leading sellers of retirement plans to small businesses. We were not focused in that market. We narrowed our focus to those strategic partners. We gained access to their system. We gained access to their shelf space. In addition, we have their data, because we're in that system, we know their producers. Armed with that insight, it gave us the confidence to invest in assembling a large and experienced wholesaler network for retirement plans, today which is 80 people strong. But we also had all those other wholesaling teams, in Annuities, in Life, MoneyGuard in that system. And we can leverage to that. We can leverage their relationships with joint meetings and being able to have referral programs. And the combination of those activities have generated for us a business that's selling at $1.2 billion annually and growing consistently in the 20% range.

This trend has continued into 2017. And I'd note the percentage of sales from strategic partners is 80% in the third quarter higher than even where we were in 2016. So a great example of the ability to use not the strategic partner, not only to grow and do more business with them where you are, but to add something new; new product and new market. And we've got a number of those opportunities in front of us at Lincoln that I think you'll hear about today.

We also have to be able to manage distribution, to deal with those varying market conditions that Dennis outlined in general. If you've got a business broad enough and if you're in it long enough, you're going to be faced with the type of issues and challenges that you've seen Dennis walk through and we have. You see that in the Life pivots, in the Annuity pivots, you see it in the DOL engagement. And what I have basically just simply done here is to highlight in the same timeframe two very different businesses dealing with different conditions in our distribution.

First is the Annuity business. The Annuity business that in 2013 was selling the most annuities we had ever sold and the highest level of living benefits we had ever sold, in part, because major carriers had exited the business and their market share came to us. You remember this as a shift in pivot to non-guaranteed and lower living benefit sales, well along the way, we then have the second leg of disruption with DOL and sales fell to their lowest levels.

We've resized our sales force to the expected level of sales, making sure that we could retain the experience and successful wholesalers that we have within our franchise. And then with product actions and with sales improvement that we believe is encouraging and sustainable, you see us then begin to expand the sales force again and I expect that we will be above 2016 levels over the course of the near term.

Same time, MoneyGuard, a very different scenario, growing business, broadening the product portfolio, expanding and channelizing distribution. And you see that. We have a proven track record of being able to deal with these varying market conditions, even if different businesses are being confronted with different issues at the same time.

Now what I'd like to do is just do a light touch on DOL. There's still a lot that we don't know. So I'm going to concentrate on what we do know. There were two major decisions that we were tracking that we thought major decisions that the industry would make as related to the implementation of the rule. Let me put that in clarity. And as you all know, this rule is subject to interpretation. So the two decisions we were tracking that our partners would make were related to shelf space and compensation.

Well, in terms of shelf space, I can tell you that we came out a winner. Half of our distribution partners narrowed their product offering as we thought there was some reason that they would do that, which was either the removal of products, or in some cases, the removal of entire companies from their system. We didn't lose a single account. We protected all of our shelf space, and in fact, we've expanded it as big as it's ever been, because we've added additional annuity products and additional annuity riders that were added into our strategic partner portfolios. So from a shelf space perspective, we come out an absolute winner in this deal. And it's another proof point that you want Lincoln to be your partner evidenced by these decisions.

On compensation, commissions, in particular, virtually every company except for a handful two or three stragglers are offering their customers and advisors the choice of commissions or fee-based compensation. And as you've heard us say before, commissions can be right for consumers, particularly, for insurance products. Insurance products are fundamentally guarantees; very different than traditional investments. Generally, long duration, long term, I think, lifetime guarantees; it's a long-term buy-and-hold investments. Commissions are particularly favorable to consumers as a affordable way to pay for advice.

Now, the next leg to drop, I think, here is the delay proposal that the DOL has submitted to OMB. We're awaiting the context of that. That would extend the second phase of the implementation from January of next year to July of 2019. We view the delay favorably, because it gives the DOL the opportunity to improve certain elements of the rule that are problematic. And it gives industry more time to prepare for rule of this magnitude. And as we've said before, Lincoln supports the broad objectives of the rule, can't imagine particularly in something as important as retirement [ph] facing (39:13) that the industry shouldn't be serving the best interests of customers, but we do believe the rule can be improved, so that you do not have unintended consequences and effect.

Now in a bit, you're going to hear from the business units about expectations for future earnings growth. You saw Dennis' waterfall chart. One thing that you would have seen there is that the largest source of organic earnings growth comes from the generation of new business and sales. So how do we think about driving growth from here? Simply put, I think of it three ways, and it's very much aligned to the principle of keep the customers you have, do more with them, and then go get new customers in that order.

First, we're growing share in our core products, the core products that we're known for. You see that and we see our confidence in those actions and that we're increasing our wholesalers and investing in more wholesalers in each line of business. Second, we're penetrating markets we aren't in, where we can go in as strategic partners and we can take share that already exist. And you're going to hear about product actions, which are needed to support that strategy, like the indexed variable annuity that Dennis talked about, like term insurance for younger consumers as well. And we'll give you more examples.

And then the third, building out new strategic partners and building out new distribution. Some examples of that are our efforts to build out Insuretech and aggregators like SelectQuote and PolicyGenius for the distribution of term insurance. We think that's a really exciting strategy. Another example is the RIA channel and fee-based advisors. The difference about this third leg to keep in mind is that it takes time for new markets to develop. So you can think about these contributing in the midterm to long term where the first two strategies able to make an impact in the short term.

So to make all this come alive, it is a combination of what's distribution going to do to improve effectiveness and expansion. But, at Lincoln, it's always integrated with what are we doing in the product areas in terms of product development. And so the rest of the presentations today are really going to get into the meat of what it is that we're doing.

So let me wrap up and let me tell you emphatically that the quality of your distribution is a driver of the positive catalyst for your company in the future. Let me say that at Lincoln, it's woven into the fabric of what we do, right in line with disciplined product pricing, right in line with end-to-end risk management. We have strategic partnerships that most companies will give both arms and legs to have. It's broad. It's deep. And we're entrenched with them. And as I finished, we've got multiple ways to grow and we've demonstrated our agility and nimbleness in doing exactly that across the board for a long period of time.

So let me stop here, say thank you. And then, I have the pleasure of introducing Dick Mucci, who is going to provide us insights on the Group Protection business. Thanks.

Richard L. Mucci

President-Group Protection Business, Lincoln National Corp.

Oops. Well, I didn't plan that. Did I get your attention now? And I'm not disabled, so I don't [ph] think I can apply (42:59) for benefits.

I'm really thrilled to be here with all of you and very excited to speak to our very good progress in our group business over the last three years and a positive outlook for the future. We have worked diligently over the last three years to improve our margins, restore our margins, and to create a positive earnings growth trajectory. And we have now begun to focus on continued earnings growth and consistently achieving our 5% to 7% target margin.

Our earnings growth and margin expansion is supported by our reemerging top line growth and our sustaining favorable loss ratios. We have installed a growth strategy, anchored in our target market focus in us – and our superior distribution management. And it's critical to sustain this positive momentum going forward. And we're investing in improving our customer experience and improving our operational efficiency. Our investments in technology and process capabilities will support this effort and build a much stronger business platform to sustain us going forward.

Let me speak to our earnings growth prospects. The key earnings drivers in our business will support earnings growth in the 8% to 10% range. And when you look little bit carefully at these earnings drivers, there's a couple of things worthy of note. First, our earnings growth is almost exclusively driven by organic factors and the capital markets play a negligible role in our earnings growth. We're not tied to the equity markets and our investment returns on our reserves, primarily LTD reserves, is projected to have only a marginal impact in the near term.

Second, our organic growth is a combination of top line growth, which is sales and premium persistency, coupled with margin expansion. Improving loss ratios and improving expense efficiency will support that margin expansion as we go forward.

So in summary, our earnings growth is a function of top line growth, while sustaining favorable loss ratios and managing our expenses prudently. Let me take a step back and give you a little bit of history of our last three years, so you can better understand where we are as a business.

In 2014, our business was under strain. We had several years of rapid growth and that operating model did not keep pace with the growing volume and complexity of our business. There were service gaps. Our risk management functions in particular our disability claims management was under stress and less effective. And some of that growth was a function of overly aggressive pricing.

I arrived in mid-2014 and my immediate priority was to strengthen the talent in the business. I brought in some seasoned senior executives from some of the largest and most successful players in our industry. We immediately set in motion a very rapid and intense remediation plan. We improved our pricing discipline, increased our renewal pricing, we invested in our disability claims management function, and we systematically attacked our service gaps.

The net result was our pricing and claims management investments improved our loss ratios significantly. And as you can see, our profit margins have risen rapidly over the last two or three years. And we have already achieved the low end of our 5% to 7% range. In fact, year-to-date, our profit margin is 5.4%. So our ability to drive price, improve our claims management and invest in our service capabilities has allowed us to improve our profitability significantly.

A little bit history of premium our top line growth. Again, rapid growth followed by premium contraction because of the remediation plans we went through affected – adversely affected our sales and persistency. And now we see a re-emergence of premium growth this year, driven by sales growth returning and improving persistency. So we see these factors driving premium growth going forward to our mid to high-single-digit expectation. We have these – the factors helping us restore growth is the moderation of our renewal pricing, the improved service profile of our business and the execution of our growth strategy, built on our target market focus and our distribution strength.

Let me talk about our target markets. Our expectations in growth sales the mid-single digits and when we think about target markets, we think of it first in terms of employer size. How many employees work for the employer? A 100 to 1,000 small case market is our core market. This is where we grew up as a business. This is where we have a longstanding market presence and success. And we're overweighted in our market share.

Our plan is to continue to capitalize on our core strength in this market and we expect solid growth here. When we look at the 1,000 to 5,000 midmarket space, this is an adjacent market where we can leverage the skills we have in our small case market. We've already seen some very good growth in this market in the last couple of years. And we expect to accelerate the growth here in the midmarket to 9% and 11% range in the short term.

Across these size segments, we want to capitalize on the employee paid market. We see this as a great opportunity. It's fast growing, it's high margin, and we plan to continue to capitalize in that market.

and we expect accelerated growth here in this target market as well. So when you look at these target markets, our strategy to capitalize on this is really consist of initiatives that fall into three categories: one, product; two, service and capabilities; and three, distribution. In terms of product, for example, we have a very competitive dental product, and we've been selling our dental product – cross-selling our dental product to existing customers. We've also been packaging our dental coverages with other coverages to support new business development.

As Dennis alluded to earlier, we're working on a whole new portfolio of accident and critical illness products. These voluntary products will be available for sale mid next year and we'll offer our customers attractive benefit features coupled with benefit flexibility. And our family leave and absence management services are being enhanced and so continue to support our growth, especially in the larger cases. In terms of service, in our business, it's very much about the basic blocking and tackling. And very often companies lose sight of that. We have a program to continuously improve our basic service competencies, including implementation, account management, phone calls – contact centers, self-service, renewal process, these are very important to our business.

In addition, we are dedicated to improving the employee buying experience. As employees select and purchase employee pay coverages like voluntary products, through technology and process and marketing, we want to give them options, educate, advise and enroll to increase their participation in our employee paid voluntary programs.

In terms of distribution, we have a very strong foothold in the brokerage community. We have great relationships and we plan to broaden our reach into high gain, high value producers. In terms of distribution, we have over 160 highly productive wholesalers whose productivity by the way is targeted to increase an additional 10% this year, who serve the market. In addition, we have over 50 account managers. So the combination of wholesalers and account management really positions us well to serve the brokerage community and to help them through the sales and renewal process.

We're also refining our broker segmentation strategy and committing ourselves to increase the number of high gain, high value producers, as well as average sales productivity. Our strategy around that is to give these top-tier producers differentiated service to continue to provide attractive, incentivized compensation programs that [ph] had sent (55:00) the right behavior. To help them advise their clients on what's happening in benefit technology and benefit technology firms. And we have enhanced our analytics and continue to do so, so that we can identify the best opportunities to target high gain producers and to measure progress.

The other important part of our growth story is our investments in technology and process capabilities to improve the customer experience and to improve our operational efficiency. The two key focus areas of our investment is the complete overhaul of our administrative platform and applying new digital technology to our business processes. These two areas alone represent over $100 million of investment over the next three or four years, which has already been embedded in the earnings growth story I spoke about earlier.

In terms of the administrative platform, we're replacing, modernizing, investing in a new platform that will go a long way to streamline our processes, and essentially, modernizing almost all our back-office technology. This platform is highly scalable and can support more volume and more complexity of our business as we venture more into the employee choice, employee purchased coverages.

Our digitization effort is leveraging the enterprise investment, expertise, and program, applying it to our business. And these digital initiatives run the full gamut from applying robotics and artificial intelligence to our processes, to re-engineering important processes like our "to underwriting the sales process" and to expand and enhance how we interact with our customers every day, applying phone, Web, and mobile technologies to that interaction.

The investment here will have several beneficial effects to our business. One, we'll be able to provide products through a marketplace much faster and provide more benefit flexibility. We will streamline our business processes to make them faster, simpler, less error-prone. We will improve the whole employee buying experience as I mentioned earlier and the whole enrollment process, and will provide the much desired enhanced digital capabilities, digital self-service the customers demand especially with mobile devices.

So this is a great story, a very exciting part of our business. But there's another angle here in terms of these investments. That is the fundamental improvement in the economics of our business. Let me touch upon that. When we went through that contraction phase, a premium [ph] when we're (58:24) remediating the business, premium dropped, expense ratios rose. So these investments will allow us to offset that. And a combination of top line growth with the improving expense efficiency will drive an improvement in expense ratios of about 2 percentage points over the next five years and improve our expense run rate by over $50 million as well. And this will move us from the median level of expense profiling in our industry to top quartile.

So I hope you can understand that we feel very good about our progress and our future prospects. We have put our business on a much stronger positive trajectory in terms of growth and profit. We have growth strategies that we believe in and we believe with sound. And they will produce very compelling opportunities for us in the future. And we have a business that we're investing in to sustain profitable growth well into the future going forward.

So thank you for your time this morning. Thank you for allowing me to share this good story about our group business with you. And now we look forward to your questions.

I'm going to invite Dennis and Will and Chris to stage and so we'll take some questions, and be careful with that step there, Chris.

Christopher A. Giovanni

Senior Vice President & Head-Investor Relations, Lincoln National Corp.

Great. So we'll get started with Q&A. And again, we have a few mic runners taking place across the room. So raise your hands. I can point to you one question, one follow-up, and we'll get back to you. We'll start right here with Tom, and then, come up front with Jay next.

QUESTION AND ANSWER SECTION

Thomas Gallagher
Analyst, Evercore Group LLC

Q

Thanks. Tom Gallagher, Evercore. I had one for Will and one for Dick. Will, first question is, you mentioned what's going on with shelf space and how although there's been a culling of companies that you guys have maintained shelf space while some others have fallen off. Can you talk a bit about what's happening in that situation? Is it marginal companies that are getting bumped off? Or are there bigger companies where you're able to actually get share? I guess, is it impactful for you from a share standpoint in those situations?

Will H. Fuller
President-Lincoln Financial Group Annuity Solutions, Lincoln Financial Distributors & Lincoln Financial Network, Lincoln National Corp.

A

Yeah, thanks, Tom. Good to see you. Thanks for the question. If I think about my career over the last 25 years, the orientation has been to make as many products available to advisors as possible. So open architecture was – and the DOL change that dynamic and say no, these products need to be more narrow and higher quality. And so I do think what it has had the benefit is to call the lower quality products or providers of products, to call down to the – a certain number of products of the same category.

I don't think that we've seen that it's been market share expansion for us yet. It's still too soon to tell. But you do have the benefit in qualified versus non-qualified. So when you call your product portfolio down as a strategic partner, you're removed from the system and you're removed from the system entirely. So I think companies basically looked at a number of products they had, looked at [indiscernible] (01:02:16) high quality of products and quality of the provider.

Thomas Gallagher
Analyst, Evercore Group LLC

Q

Got you. And then, Dick, just a question on group. It looks like your persistency bond darted around 75%, and it's trending back toward the high 70s. When I look at it another competitor of yours, Unum, I think they're hovering in the high 80s right now from a persistency standpoint. Are there structural reasons why you wouldn't be able to get to that level? Or can you continue to really improve the persistency?

Richard L. Mucci
President-Group Protection Business, Lincoln National Corp.

A

That's a good question. Our target is mid 80s. You do have to adjust by relative size of the business. Larger cases tend to have better persistency than smaller cases. And when you adjust to that, we feel that the mid-80s is a competitive point, although we would certainly try to shoot higher than that, but that's our current goal.

Thomas Gallagher
Analyst, Evercore Group LLC

Q

And when do you think you might get in the mid-80s?

Richard L. Mucci
President-Group Protection Business, Lincoln National Corp.

A

I think that we're probably on target to get there in three, four years.

Thomas Gallagher
Analyst, Evercore Group LLC

Q

Thanks.

Jay Gelb
Analyst, Barclays Capital, Inc.

A

Thank you. Jay Gelb from Barclay. Dennis, on the tax rate, you put that in terms of industry impact. I was just hoping you can confirm that based on what we know now without the bill going to conference yet, would you expect essentially no change in the tax rate profile for Lincoln, which we generally assume around 24%, given the puts and takes in the bill?

Dennis R. Glass
President, Chief Executive Officer & Director, Lincoln National Corp.

A

I have to keep this conversation at a very high level. And the reason I have to keep it at a high level is that there's quite a bit of activity. We, the industry, have been working very closely with the Joint Committee on Taxation, working with them today several hours, just a little bit of civics lesson here for everybody. The road to any final bill – all roads to any final bill have to go through the Joint Committee on Taxation.

And so the scoring there is important, getting them the right data is important. And we really will not know any details until we get closer to what looks to be the final bill. But I'll come back to my general comment, very high level. I have talked to most of the influential people in the House and in the Senate along with other CEOs, and I'll just repeat at a very high level, there's no intent to harm the insurance industry at all. And I guess, I'd even add to that as the industry has worked with the players involved in setting policy, it's quite clear that not only we don't expect to be harmed, but that we're trying to get any outcomes to have an even effect across industry business models.

So if all those things turn out, the industry will come out well and individual will come out okay. And individual companies inside the industry with different business models should also come out okay. Now, that's not to say, let me be very carefully here, and let me repeat this a couple of times this is based on my impressions, although having talked to a lot of the players as part of the CEO groups that have been going to the Hill. These are my impressions. Things are changing every hour. And that's just part of the process. The administration has tried to condense something that sometimes takes years to do into a very short period. So it's hard to know how it's going to turn out.

But again, big picture, there's no intent to have anything other than a co-measured increase in paper work benefits the industry gets. And that to the extent possible, it will be applied evenly over business models. And these are the conversations that are being had. But, please, let me qualify this again. It doesn't mean that any one company can come out a little bit worse than another company. It's just too complicated and the business models are too diverse.

And finally, I'm going to say once again, my impressions and things are changing so quickly. It's hard to know where any of this is going to turn down much less what can happen to an individual company.

Jay Gelb
Analyst, Barclays Capital, Inc.

A

I appreciate that.

Dennis R. Glass
President, Chief Executive Officer & Director, Lincoln National Corp.

A

Yeah.

Jay Gelb
Analyst, Barclays Capital, Inc.

A

My separate question was on just an updated perspective from you on the potential for acquisitions. I know it hasn't been as much of a focus for Lincoln. We haven't seen many significant deals. So I'm just trying to get your latest perspective on the potential for acquisitions in terms of what areas you might be interested in and how you might balance that with the return of capital strategy?

Dennis R. Glass
President, Chief Executive Officer & Director, Lincoln National Corp.

A

Yeah, generally speaking, our first choice is to increase through non-organic ways, acquisitions, the source of earnings that come from mortality, morbidity, and given that we're number one across almost all of our markets in the life insurance industry, I think our first choice would be if we could find a good group business that's complementary to what we're doing, so that would be our first choice.

Now, Randy will get into how much trapped capital we have that can't be used for share buybacks, because there is certain amount of capital that we have is excess that you can't take outside of the company, but can be used for acquisitions. And I don't know Randy if you're going to get into that in any detail. But, as you heard me say in terms of where we believe our share price should be, we think it should be higher based on performance than multiples elsewhere in the industry. And so there's no less appetite on our part as we sit here today for our share buyback program. And we wouldn't want an acquisition to in any meaningful way to upset our plans to buy our shares back.

Now, does that mean that we wouldn't adjust it a little bit, if we did something that we thought was very strategic? Maybe – maybe not. But generally, we have excess capital that can't be used to buybacks, but can be used for acquisitions. We have some capacity on our balance sheet to raise debt if we needed to do that. And we'll continue to look. What we're not going to do is, you know I've been talking about this for three years, right? And we've had an opportunity to look at things that just didn't meet all of our criteria. So we're going to be patient. And if the right thing comes along and we can buy it at fair price, we'll do something.

Christopher A. Giovanni
Senior Vice President & Head-Investor Relations, Lincoln National Corp.

A

Here to Humphrey.

Humphrey Hung Fai Lee
Analyst, Dowling & Partners Securities LLC

Q

Humphrey Lee from Dowling & Partners. I've got couple of questions for Dick. In the Group Protection side, you talked about deeper penetration. Can you talk about maybe how in terms of the penetration to your existing customer base, like how many products you're selling per customer and where do you see Lincoln can grow in that area?

Richard L. Mucci
President-Group Protection Business, Lincoln National Corp.

A

Well, we look at penetration of our market in several different ways. When I mentioned target markets, we look by size, we look by – in terms of our employee paid business, in terms of number of products per customer. We hover around close to 3, 2.8 or so in terms of coverages. We think of coverages per employer. In terms of coverages per employee, I don't know that number off the top of my head, but it's more around overall participation in our insurance programs.

We see employee participation of voluntary programs around 30% hovering around there. So we think there is a significant opportunity to increase that. But it's also the – besides penetration or participation rates is – we call penetration in terms of how much business they buy. So even though someone may buy life insurance, they typically are under-insured. So when you look at the penetration of the employee block, we look at the number of people participating in our programs, but also how much coverages they're buying per employee.

Humphrey Hung Fai Lee
Analyst, Dowling & Partners Securities LLC
Q

And then, on the voluntary product side, you talked about the participation rate is about 30%. That seems to be a pretty good number based on my understanding and you think the digital initiatives further improve that. I guess, in terms of maybe near to in the medium-term target, where do you think you can grow in that participation rate?

Richard L. Mucci
President-Group Protection Business, Lincoln National Corp.
A

Well, I think we estimate we can increase that by several percentage points, maybe 35%. But again, it's also the average purchase per employee in terms of the insurance as well as the number of coverages, both of those. So it's kind of a double leverage effect in terms of increasing the number of people participating in programs, but also how much they buy.

Humphrey Hung Fai Lee
Analyst, Dowling & Partners Securities LLC
Q

But do you think that is going to be achieved by just providing better digital user interface? Or is this going to be more active education to the employers and employees in order to accomplish that?

Richard L. Mucci
President-Group Protection Business, Lincoln National Corp.
A

Yeah, it's multi-faceted. First, you have to make the whole process easy. If the employee finds it more difficult to purchase, if they're confused, if the fulfillment process is difficult then that stifles the participation. So it's a combination of the whole buying process from identifying the need – no wait, the analogy I use is that we want the employee to feel like they have a real good insurance agent sitting across the table from them, but we don't have that. It's virtual, right?

So what does a good insurance agent do? They educate, they identify options in terms of what's provided. They make the fulfillment process easier. I think that's the key. So it's a combination of understanding the end consumer, marketing effectively, providing processes that educate in the fulfillment process that is easy to accomplish as well as obviously attractive products to meet the need. And this is where our voluntary products and industry voluntary products seem to be resonating with consumers as they look to fill gaps in their insurance program.

Humphrey Hung Fai Lee
Analyst, Dowling & Partners Securities LLC
Q

Thank you.

Christopher A. Giovanni
Senior Vice President & Head-Investor Relations, Lincoln National Corp. A

I think it's Jay is back there, and then go upfront here to John.

Jay A. Cohen
Analyst, Bank of America Merrill Lynch Q

Thank you, Jay Cohen, BoA Merrill. A question for Dick. Dick, I definitely got the ability to grow the business. I heard the comments on the expense ratio, but I didn't quite pick up how you plan on improving the loss ratio. If you can talk about that.

Richard L. Mucci
President-Group Protection Business, Lincoln National Corp. A

Well, we've already improved our loss ratio substantially. So we see there is maybe a little bit more movement we can make there. It's a combination of again disciplined pricing, [indiscernible] (01:14:17) there's upside in how we manage claims. But we've rung out a lot of points of our loss ratio already. So we see some modest improvement there to help with the margin expansion, but we see actually more the margin expansion being driven by expense ratios, which is a combination of top line growth and expenses.

John Bakewell Barnidge
Analyst, Sandler O'Neill & Partners LP Q

John Barnidge, Sandler O'Neill. Obviously, I want to acknowledge the impact of natural disasters, but have you seen much inorganic lift to sales as it relates to maybe Texas and Florida from September to October and then California as it relates to October to November?

Will H. Fuller
President-Lincoln Financial Group Annuity Solutions, Lincoln Financial Distributors & Lincoln Financial Network, Lincoln National Corp. A

Yeah. So we did take a look at it. We didn't see anything that would be that material. It's a good question and the reason why we looked at it for the same reason likely you're asking is just the high concentration of retirees in Florida and Texas being a larger state than California. These typically are three states that are large generators of insurance business. And we saw a little downtick in the third quarter, perhaps I could explain some softness, but it wasn't material. And it's certainly not where we're seeing the – and you hear me talk about the strength of the fourth quarter. Again, it is broad based across products; it is broad based across channels. And so you can assume it's broad based geographically as well.

Christopher A. Giovanni
Senior Vice President & Head-Investor Relations, Lincoln National Corp. A

Jimmy?

Jamminder Singh Bhullar
Analyst, JPMorgan Securities LLC Q

Hi, Jimmy Bhullar, JPMorgan. I had a couple of questions. First for Will on the DOL, there had been a fair amount of disruption in the market because of the uncertainty on what was going to happen with the DOL. And I think even though it's still not clear what will ultimately happen. Have you seen less disruption? How has that affected production in the various channels that impacted the DOL – or impacted by the DOL?

Will H. Fuller
President-Lincoln Financial Group Annuity Solutions, Lincoln Financial Distributors & Lincoln Financial Network, Lincoln National Corp.

A

Yes. I think we can put some math to this. We just take the third quarter of last year to the third quarter of this year. You really did see there to be a different path of sales in variable annuities between qualified and non-qualified. Qualified being down, somewhere in the 15% range and non-qualified actually being up modestly. That's not an industry statistic, that's Lincoln statistic, but I think the industry statistics will closely follow – should closely follow in the sense of that pattern.

What we have seen post-DOL is some improvement to that range, seems that that range is coming in. Why? More favorable decisions by strategic partners and I think those folks expected, particularly, along the lines of commissions. Secondly, there have actually been companies and we've done our own broker-dealer, where after day one, we've made additional changes to reflect as we've learned more.

So one example of a change that we're seeing across the industry is offering multiple commission options. So different variations between what's upfront and what's a trail, smaller upfront, higher trail. Again, those are proof points that advisors are paying attention to, oh, okay, I see; commissions really can be right and I feel comfortable doing them.

We've seen certain companies open up on making add-on contributions to, let's just say, annuities that were purchased in the past. They can make an add-on contribution and not be treated. So you are seeing an adaptability in the marketplace to become what I call more friendly decisions post day one. And certainly I think a lot of that is coming from the view that there's a potential for delay and potential improvement. So I think it's too soon to tell if in fact the disruption has dissipated, but there are very encouraging signs.

Jamminder Singh Bhullar
Analyst, JPMorgan Securities LLC

Q

And for Dick, can you comment on just what you are seeing in terms of competitor behavior on pricing terms and conditions as you've gone through renewal season? And then, also, you've seen a couple of your competitors combine likes of your former company Hartford buying the Aetna business, is that a threat to you, in that you've got a stronger competitor, or is there an opportunity for you to pick up some business?

Richard L. Mucci
President-Group Protection Business, Lincoln National Corp.

A

So there's two good questions. First, on the pricing regime, I think – the pricing environment, I think we feel that the industry by and large is rational. Now we have a competitive industry, it's – every case goes out to bid. It's a take-share situation in terms of getting employers. So it's pretty competitive. But we feel the pricing is rational. We feel that comfortably we can get our margins in the marketplace and still grow and we feel good about that.

In terms of the Hartford's acquisition of Aetna, it is a couple of things to think about, Aetna tends to be more skewed to the large case market and so is Hartford, especially over 5,000 lives. And that's not our target market. So they tend to be a bit more skewed to that large case market. So that we may not see as much as the head-to-head competition from that and maybe some other players will have. They have to go through a period of digestion and make sure that merger can work.

We feel very confident in our strategies. And in terms of – we think there's definitely enough room in the markets we're in and how we're growing. And our position in the marketplace especially with the brokerage community that we can continue to drive the growth. And the way I would figure is one less competitor is one way to think about it.

And Aetna brought to the marketplace a value proposition, it was tied to the medical coverages. So in one way we don't – there is one less competitor compete with in terms of that particular value proposition.

Christopher A. Giovanni
Senior Vice President & Head-Investor Relations, Lincoln National Corp.
A

Suneet?

Suneet Kamath
Analyst, Citigroup Global Markets, Inc. (Broker)
Q

Thanks, Chris. Suneet Kamath from Citi. Just going back to the DOL, any updates on the whole private right of action issue and where we are with that it seemed like that was always cited as a big unknown that could cause the DOL impact to be maybe bigger.

Will H. Fuller
President-Lincoln Financial Group Annuity Solutions, Lincoln Financial Distributors & Lincoln Financial Network, Lincoln National Corp.
A

So no specific update to right of action. I think the delay of the rule to July 2019 allows for that provision and other provisions to be evaluated more fully potentially improved its industry's point of view, and Lincoln supports industry's point of view that there is a more effective enforcement mechanism than the right of action, particularly, if you have SEC and FINRA who are already actively enforcing our – the quality of the advice and recommendations advisors provide to customers.

So I'm sure it'll be a part and parcel of a series of the elements of the rule that are viewed as challenging. That is the one if not the most challenging aspects to the rule that will likely be under the spotlight in a delay scenario.

Suneet Kamath
Analyst, Citigroup Global Markets, Inc. (Broker)
Q

Got it. And then on the wholesaler outlook, I think you talked about some numbers that suggested maybe 15% or so growth over the next year. Should we be thinking about some costs or expenses associated with that growth?

Will H. Fuller
President-Lincoln Financial Group Annuity Solutions, Lincoln Financial Distributors & Lincoln Financial Network, Lincoln National Corp.
A

I think one thing we've done really well at Lincoln over a period of time is to run distribution within our pricing allowable; in any given point in time, the timing of the investment versus when the allowable revenue comes in, in terms of when there's an active sale could be mismatched. But over time we spread that out. And I think you can view that we view these increases in wholesalers to be supportable by the level of sales that we would expect to come in the near term, not investments in wholesaling that it's going to take time to be supported by the allowable from sales.

Suneet Kamath
Analyst, Citigroup Global Markets, Inc. (Broker)
Q

Okay. And then just last one for Dick. On the $50 million of expense savings, I just want to be clear that's over five years and we would expect that that would fall to the bottom line. It's not going to be offset by investments elsewhere?

Richard L. Mucci
President-Group Protection Business, Lincoln National Corp.
A

Well, I think it is over five years. And I think we need to continue to look at what we need to do to be competitive in pricing. So we feel that a lot of it will fall to the bottom line, but we'll have to see competitive environment as we move forward. Presumably, it positions our business to be stronger competitively either through the terms of attractive pricing and margin.

Suneet Kamath
Analyst, Citigroup Global Markets, Inc. (Broker)

Q

Thanks.

Christopher A. Giovanni
Senior Vice President & Head-Investor Relations, Lincoln National Corp.

A

Great. So we're just out of time here for this Q&A session. Again, we'll have two more over the course of the day. We're going to take a quick 15-minute break. Everyone stretch out and we'll be back then. Thanks.

[Break] (01:23:41-01:38:55)

Unverified Participant

Ladies and gentlemen, please welcome back your host, Chris Giovanni.

Christopher A. Giovanni
Senior Vice President & Head-Investor Relations, Lincoln National Corp.

Very quickly. So, we're going to get into the next three business presentations; Life, RPS and Annuities, Q&A, and then lunch. So, let me turn it over to Randy Freitag and Mike Burns to run through our Life business.

Randal J. Freitag
Executive Vice President, Chief Financial Officer & Head of Individual Life, Lincoln National Corp.

Thank you, Chris, and good morning to everybody. Welcome to the discussion about our Life Insurance business. I'm joined on stage today by Mike Burns. If you haven't met Mike before, Mike runs our Life Insurance manufacturing side of the house on a day-to-day basis. And in doing that partners each and every day with our distribution partners to create the industry-leading franchise that we are going to discuss today.

We're going to do that by focusing on a few key themes today. First, I'm going to talk about our broad product portfolio, how that portfolio creates scale, how that portfolio creates a very balanced and diversified profitability and risk profile and how that portfolio gives us the ability to pivot and shift in an ever-changing world. Second, we're going to talk about some areas where we are investing, to capture slices of the market where we may not currently participate, or to capture key demographic trends that are occurring in the market place. And lastly, we'll focus on our disciplined approach to financial management.

So, what does it take to grow in the Life business? Now, I don't want to forget the fact that it's a complex process to run a retail business. When you bring it to the highest level, what it takes to grow is really not that difficult to understand. You've heard me talk in the past about how I believe that capital-intensive businesses are undervalued and underappreciated in the marketplace. And while the capital [ph] intensity (01:41:44) of our Life business has come down substantially over the last five years, as we've tilted away from products with longer term guarantees, you would still put it on a spectrum at the more capital-intensive end of that spectrum.

One of the really favorable aspects about capital-intensive businesses is the following fact. Every year, every January 1, when Mike and I wake up and open our eyes, we know a few things, one of them is the fact that roughly 95% of the earnings that we had in the previous year, they're going to be there again that year. When you know that simple fact, it makes it very easy for us to understand what we have to do. What we have to do? We have to sell enough business to fill up that 5% bucket, sell enough business to create growth above that. Today, we sell about $0.75 billion of Life Insurance in any given year that translates into about an 8% to 9% contribution from new business, and Mike will talk more about some areas where we're investing to boost that number even higher.

Facts of the Life Insurance business today that you should also think about. We've talked about the fact that this is one of our two businesses that is impacted by low interest rates, and so we have a bit of a headwind there. But as you might expect and as we definitely expect, we don't stop there, we don't just look at a headwind and say, oh, well, there it is, we're done. We focus each and every day on what we can do to overcome things like that; and over the next few years, I would expect us to have a very strong focus on expense management to overcome that particular headwind.

So that, when you wrap it all together, over the next few years, we would expect the Life business to grow in the low- to mid-single-digit range. What the success look like in the Life business? To me, it looks a lot like what you see on the slide in front of you. Take yourself back a decade ago. The top 10 publicly listed sellers of life insurance, a very impressive list of companies, look at those names out there, very impressive companies, bring yourself [ph] forward (01:44:27) today. What's happened to those 10 companies in the Life business? Nine of them have shrunk, the one who has grown is right before you on the stage. Lincoln is the only one. How and why have we done that? We've done that by leveraging the broad product portfolio I talked about, a portfolio that has allowed us to completely change the products we sell compared to 10 years ago. Completely shift from a product that featured much more long-term guarantees, a product that had much more interest sensitivity.

It's a completely different product set, term insurance, variable products, MoneyGuard focused at an emerging need, a complete shift by leveraging that product portfolio. A product portfolio that's the deepest and broadest wholesale enforce in the country, takes out each and every day to the nearly 50,000 advisors who will sell a Lincoln Life Insurance product over the next couple of years. And those advisors will access the millions of consumers who have an insurance need in this great country of ours. That is what success looks like in the LIFE INSURANCE business.

With that introduction, I'm going to turn it over to Mike and he's going to take you through a few of the very attractive opportunities or a couple of the very attractive opportunities we have in the Life business and a few other aspects of the business that we think about on a regular basis. There you go, Mike.

Michael J. Burns

Senior Vice President, Head of Life Solutions, Lincoln Financial Group, Lincoln National Corp.

All right. Well, thanks, Randy. And so, while Randy just shared our success over the past decade, we remain well-positioned to continue to outpace the industry really by leveraging our core strengths in capturing significant growth opportunities. And so, first, I'm going to start with permanent life. And our permanent life portfolio provides a comprehensive set of solutions for core multi-generational insurance needs; protection, accumulation, wealth preservation. And from the period listed, 2012 to 2016, we've seen 10% growth. As we think about these needs, they have been there in the past. They are there today and they will continue to be there in the future.

So, as we think about what permanent life insurance does, it has and will continue to maintain very strong relevance in the marketplace. And just as we had in the past, we will continue to be industry leaders in the core space, leveraging the breadth of our portfolio, the strength of our distribution and the access to the wide array of independent advisors that sell these products. The reality is that, over time, consumer sentiment changes, but the fundamental need for permanent life insurance continues to be there.

Next is linked benefits, where Lincoln is the industry leader with our MoneyGuard product. And we remain excited about this market, where the industry has seen double-digit growth and we have maintained nearly 60% market share. We continue to expect strong demand for this product. There's 10,000 boomers turn retirement age each and every day.

Now, switching to term. We have been able to grow in a highly competitive environment over the past several years, outpacing the industry with 17% growth, with the laser focus on a large face market targeting ages 40 and older. However, we now see more opportunities for growth in this space, as the wave of millennials will be initiating their insurance journeys with the purchase of term insurance and the investments in digital capabilities will allow us to access the lower face market in a low cost manner and do so in a way that provides an experience consistent with the next-generation of consumer.

And so, now rounding out the rest of our portfolio is executive benefits, which provides a complementary offering to our broad portfolio of retail solutions and we maintain an opportunistic approach to this market. And so, to sum it up, our product suite is a competitive differentiator positioned to capture current needs, demographic shifts and long-term growth opportunities.

I'm now going to highlight two long-term growth opportunities, both of which are driven by demographic forces. The first eye takes us into our linked benefit leadership or MoneyGuard. And linked benefit solutions have a compelling upside as they have become the premier solution for solving long-term care funding needs. Baby boomers with their sheer numbers and considerable asset base continue to display a strong need for long-term care funding protection. One out of every two Americans turning 65 today will need long term care services at some point or in their lifetime. And in 2015, Life long-term care combination products like MoneyGuard actually outsold in numbers standalone LTC. Both consumers and advisors recognize the value of linked benefit solution and it's this adaption that has helped fuel the growth of MoneyGuard and similar solutions that you see from the double-digit growth that has been recently achieved industry-wide and delayed.

Now, MoneyGuard was at the forefront of the industry evolution, actually being launched in 1988. But since then, MoneyGuard has shown an unparalleled ability to innovate, evolve and expand. It has done that through enhancing the ease of doing business, broadening the product appeal with new features and benefits, and deepening the distribution strength.

And if you take a look at the table at the right, relative to the key competitors in the MoneyGuard space, the MoneyGuard solution and its versatility and all of those attributes, ease of business, broadening the appeal with features and the distribution reach is unparalleled by any other competitor. So, based on the historic and current strength of our manufacturing capabilities, distribution reach, MoneyGuard will continue to be the industry-leading solution by what is – and what is by all accounts a significant growth opportunity for the entire industry.

The next broad category where Lincoln is well-positioned for long-term growth is our term franchise. Going back to 2012, we really weren't recognized as a major term rider. But since then, our focus in the large-face advisor based market has positioned us as a top 10 rider in term insurance overall and captured and positioned us with 8% market share in that large face segment and that's face amounts of $500,000 and greater.

And when we think about opportunities for growth, it's the lower face amount market that provides untapped potential that could be captured by leveraging digital efficiencies, as we expand customer reach and market share. And so, this means broader product positioning, enhancing our underwriting experience with paperless processes from issue to delivery of the policy and automated underwriting capabilities, and deepening and expanding our distribution breadth.

And while capturing the lower face market will play a large part in our future growth in the term space. The larger face market will continue to remain an important focus. And then lastly and importantly, many of the investments that we are making to reach the term markets will ultimately be scalable to our entire portfolio of solutions, driving efficiencies and an enhanced customer experience across the entirety of our full individual Life portfolio solution set.

And now that we've discussed the strength of the new business franchise from a sales perspective, let's focus briefly on the profitability profile. Since 2012, we have managed exposure to long-term guarantees to about a third of our portfolio, and sales of products that are less interest-sensitive represent about 60% of our total life sales. With equally impressive has been our ability to improve returns.

In 2012, returns were slightly below our targeted 12% to 15% range, to now in 2016 where total returns pierced the top-end of our 12% to 15% target, accomplished through a diverse set of well-designed products, all our product returns performed well under our expectations, under low interest rate scenarios and under stress scenarios from mortality and morbidity.

The bottom line is, the profitability of our new business is strong and will drive well-balanced results. And before I hand it back over to Randy, I'm going to talk briefly about our underwriting and mortality profile. Our underwriting results remain strong. We have demonstrated stable, consistent long-term mortality results over the last five years with actual results coming in at roughly 1% of expectations. As we talked about in the past, we do experience seasonality in the first half of the year that gets reversed in the second half of the year. But again, looking at results over the long-term, mortality has been consistent and in-line with our expectations.

Additionally, our insured experience remains strong, stable and unaffected by recent trends in general population mortality, specifically as they relate to accidents and suicides. And you can see this in the chart at the bottom right, which shows the percentage of total claim count attributable to those causes, accidents and suicides. The red line demonstrating our experience continuing to be consistent, stable and lower than general population. So, ultimately, maintaining stable and consistent underwriting and mortality risk profiles enhances our overall earnings potential.

And now, with that, let me hand it back over to Randy.

Randal J. Freitag

Executive Vice President, Chief Financial Officer & Head of Individual Life, Lincoln National Corp.

Thank you, Mike. So, according to a little clock that gives us up here, we ran out of time about three minutes ago. So, I better wrap this up pretty quick. What does it all mean? What does this all mean that Mike and I have talked about up here today? It means that we've built a franchise that has demonstrated the ability to grow, with revenue growing roughly 5% a year for the last five years.

It means that we've created a franchise that has the ability to leverage its scale to create expense efficiencies, bring our expense ratios down steadily over that same period. When you wrap it all together, it means we've created a franchise that ultimately has the ability to grow the bottom line. And looking forward, we'd expect nothing less than what we experienced over the last five years, for all the reasons we've talked about today.

It's all of the things we've talked about it, it's our unmatched product portfolio, when combined with the best distribution force in the country that creates the confidence you've heard from us today. The ability that we have to invest in additional creative solutions is only going to enhance that attractiveness. This is a business we're excited about. It's a business that where we're a leader today, it's a business that where we were a leader 10 years ago, and it's a business where we'll be a leader 10 years from now.

Thank you very much for spending some time listening to the Life – about the Life business today. With that, we're going to turn it over to Jamie and she's going to tell you about the Retirement business.

Jamie B. Ohl

President, Retirement Plan Services, Lincoln Financial Group, Lincoln National Corp.

Great. Thank you, Randy. Good morning, everyone. This is a great time to be in the Retirement business and specifically a great time to be in the Retirement business at Lincoln. I noted the quote that [indiscernible] (01:58:48) our strategic partners had a little video and she said it's not about price, it's about value. And what I hope to share with you today is the unique value proposition that we're bringing to the marketplace in Retirement that is resonating with our customers and helping to drive the results that you see now and into the future.

And it starts with a very simple yet powerful three pronged strategy; growing our target markets, own a differentiated customer experience that drives measurable outcomes, and take profitable actions to offset the continued pressure from spread compression headwinds.

Let's start with growth. I think about growth in three major areas that are driving results. One, sale; number two, recurring deposits; and three, retention. That's really three of the four cylinders we need for this car to get us down the road very successfully.

On the sales front, we're up 54% year-to-date in new sales. From a recurring deposit standpoint, new tools and innovation, along with our historically market-leading on-site high-touch capability is driving consistent and record recurring deposits. And finally, on the retention front, we have record retention with more than 97% of our employer plan sponsors staying with us, which is well above the industry average. That combined with the fourth cylinder on the car, which is taking profitable actions to overcome the headwind of spread compression. That includes controlling our expenses and managing in-force margin improvement, that results in an expense ratio that has declined 100 basis points over the previous year.

How does that translate into earnings? Dennis shared we would talk about the waterfall. The first two columns in the waterfall represents the impact net flows is having on our business. In fact, over the last 12 months, we've seen $1 billion in net flows, and that's representative of seven quarters of consecutive positive net flows for the business. In order for those net flows to fall to the bottom line, we have to offset the spread compression headwind we have, and we do that almost completely through the actions that we take on the management side from an expense and in-force management perspective.

As a result, we expect annual earnings growth in the 5% to 8% range. When I think about growing sales in the Retirement business, we're growing sales in our target markets faster than the industry average, in an industry that is growing at a fairly rapid rate. So, what are our target markets? We focused on the small and mid-401(k) market, the 403(b), our healthcare market, and the government market. Why? They're the fastest growing markets with the best margins in the industry. And as you can see from the right side of this chart, we are growing faster than the industry in those fast-growing markets.

And our model is resonating in particular more recently, as Will mentioned, in the 401(k) market, in that small and mid-401(k) space. Why? There's a significant opportunity there as those employers are looking for their employees to achieve better retirement outcomes into the future, and the opportunity is great in terms of the number of businesses that are seeking what we offer. And we have the ability to leverage and take advantage of that through our powerful distribution franchise. This allows us to take advantage of where the market is going. One of the top reasons that employers give today for why they choose a new retirement provider is, they want to ensure that their employees have sufficient retirement savings and lifetime income, and this need is multi-generational, it's not unique to just the boomers or the millennials, it's across all generations.

In fact, if I think about the boomers, they need to save more and convert that into retirement income. The millennials, on the other hand, they're very likely to have one or two of what we think of as the traditional three-legged retirement stool by the time they get to retirement. It is absolutely imperative that they have access to the best retirement plan that will produce the best outcomes for them, and the need for driving outcomes is driving growth in industry and driving growth faster in RPS, because of our proven ability to deliver on those outcomes.

As we focus on these target markets, you can see that it's delivered a strong growth rate over the past five years. And I mentioned earlier, an accelerated growth rate in 2017 at returns of 12% or better, as Dennis noted in his opening. What are the drivers of our success on the sales front? I'll lump them into two buckets. Lincoln's historical strength, we're leveraging products and distribution. On the distribution front, in the mid-large space, we are successfully targeting higher volume plan segments. And as a result, we have four times as many plans in that space in 2017 than the prior year. We have also improved our productivity across both segments, small and mid-large, with productivity up 51%.

On the product side, you've heard Will talk about this briefly. We introduced the new product mid-last year in the small market and that particular product is one of the most competitive in its space and that it's flexible, transparent and level fee, and has driven a 36% increase in sales in that market. And, again, as Will noted, has helped us to not only retain, but expand our shelf space with our product distribution partners.

And finally, we're leveraging innovations in new and different ways, specifically digital innovation, as we think about our opportunities going forward. And that innovation is part of what's driving outcomes, driving those outcomes is also driving us 58% increase in proposals year-over-year.

So, now, I'll spend just a moment on what are some of those innovations that we see that we put into the marketplace that are driving real results and real outcomes. First, let me say that, we didn't do digital in a vacuum. We did digital with our high-touch model in mind and using it to facilitate the combination of high-touch and high-tech to truly deliver a better outcome than if you use one or the other, and more importantly, we can measure it and prove it. And that's what separates us from our competitors and is driving our results. Two of the innovations at the top, you've heard about Click2Meet, and Dennis has spoken about Click-2-Contribute, those two innovations have combined to deliver $140 million in additional savings for Americans, which is $140 million in additional annual deposits for Lincoln.

We're also continuing on that digital front. Our omni-channel engagement, what does that mean? It means engaging with participants, when they want, how they want, in a way that is personalized and relevant. Why is that so important? Because we know when we do that, people will take action. And, in fact, we just piloted this approach in the fall with the save-more campaign, and again, drove an additional $25 million in additional savings and additional deposits for Lincoln. So, it's clearly working.

One of the last things I'll mention and it's not on the page. The digital innovation continues. We didn't stop, but before you see on the page, in September we rolled out the Apple Watch, giving us one more and more way to connect with the customers that we serve. And the digital innovation combined with our high-touch model will continue to be the hallmark of what we offer to the marketplace. Why? These investments are geared towards driving engagement with our participants.

Retirement savers like most consumers demand more today and they want to be able to engage with a plan, when they want and how they want. And it's proven that our model drives engagement and that drives results. On this page, you see that those who are fully engaged, meaning, they take advantage of our high-touch model and our digital capabilities, contribute 51% more to their retirement savings.

On the right-hand side – I've touched on sales, recurring deposits. On the right-hand side, let me touch briefly on retention, the third component of our growth strategy. We are driving significant improvement in our retention, in fact, record rates this year of 2.9% from a termination perspective, nearly half the industry average. And, again, related to all the investments and the service model we've been speaking about. Our recurring deposits and retention are driving net flows and account values in record numbers for the Retirement business.

I mentioned the trailing 12 months of $1.3 billion, more than doubled 2016. But more importantly, we're seeing consistency in net flows. Seven consecutive quarters of positive flows and more than $100 million in net flows over each of the last four quarters. That is combined with strong equity markets is driving record account values for the business. But in order for that growth to drop to the bottom line, it's imperative that we continue our profitable actions and our expense discipline. There are two components controlling our expenses and managing gross margin improvement. On the expense discipline side, we're focused on investing in digital initiatives and streamlining processes through re-engineering so that we can reduce that per participant or unit cost and have a more competitive proposition in the market.

On the in-force management side, we continue to work that we've done for the last several years around interest credited rate, lower GMIRs and fees. On the pricing side, we remain disciplined in our pricing approach and a piece of that is bringing on new business with a GMIR of 1%. All of those actions have combined to move the percentage of our business at 1% from 7% in 2012, up to 24% in 2016.

So, in closing, this is a line to be in the Retirement business specifically at Lincoln. Why? Declining expenses, record sales, record retention, record net flows, all leading to record account values of $65 billion. This is a result of executing on a focused strategy that is driving results and has us positioned for long-term growth. Thank you.

And with that, I welcome Will Fuller to the stage.

Will H. Fuller

President-Lincoln Financial Group Annuity Solutions, Lincoln Financial Distributors & Lincoln Financial Network, Lincoln National Corp.

All right. So, bringing it home, saving the best for last. Annuity franchise at Lincoln. This is a terrific business for Lincoln. We have the best franchise in the industry and we're going to give you the very specific proof points today that help support that convention, and that do support that convention. What makes this a great franchise, what makes it a great business? Well, you seek the benefits of the asset management business, fees on assets, the ability for capital market returns to push average assets higher, which will differentiate [indiscernible] (02:11:59) overlay and that guaranteed overlay brings benefits like sticky assets that stay around for a long time, like differentiated value propositions in the marketplace, like the ability to protect in charge discreet fees for the value of that guarantee that we've been able to do very effectively at Lincoln. And this is a guaranteed overlay that at Lincoln we manage very well, have a track record frankly that is differentiated from peers. And it's differentiated from peers, because we started this business from day one and we've managed it to a very specific formula. That strategy of consistent market presence that I talked about earlier, the discipline product pricing, ensuring that we set reasonable assumptions from the beginning, hedge readiness before selling a single dollar of guarantees, and then leading with that strength of the distribution in LFD that you've heard about today.

The formula works, the proof is in the performance and few companies have been able to get all of these pieces to come together day-in, day-out the way that Lincoln has. So, today I'm going to start, as everyone else has, with that waterfall chart that shows you a look-forward of our view from an earnings standpoint. Then, I'll turn our attention and provide you some proof points and importantly some new information that you've asked for as it relates to our high quality book of business that we believe will be beneficial to you. And then, I'm going to end by turning to the marketplace, giving you a sense of what we see in terms of opportunities, what are our actions in particular to continue to have the improvement in sales that we had been seeing.

So, let's start with the waterfall. What this slide tells you is what [indiscernible] (02:14:04) that in the short-term we expect the annuity business to generate earnings growth in the 4% to 6% range. While our sales are at the lower end of – lower levels that we're experiencing, the lower end of this range. So what's driving that 4% to 6% earnings growth, is the capital markets lever, which here we're assuming a reasonable equity market assumption of 6% to 8%.

While sales are lower, we continue to focus as you move to the left, on our strong bottom line management, building margin, improving expense efficiency, and that's contributing to our growth. And as we keep moving to the left and we'd look at our outflows, when you run a retail annuity business, one aspect of managing that business is that your customers or policyholders are going to take their income benefits, they're going to take withdrawals, there are going to be some lapses, you see that in the in-force chart as our outflows. And our outflows have been very steady at the midpoint of this range. So, with – as sales improve from the lower end of the range to the upper end of the range over the long-term, we see the annuity business being able to contribute earnings growth above the short-term range that we're showing you here.

So in summary, 4% to 6% in the short-term, and as sales improve, opportunity for upside longer term.

Now, let's talk about the financial results from the annuity business. Very [audio gap] (02:15:51) financial results and you see it in dollars of earnings, 12% earnings growth, with very limited volatility. And as you move to the right, you see it in the source of the 12% earnings growth, half of the growth coming from capital markets with fund returns being above and elevated, as we've seen since 2012. You see the other half coming similarly from net flows in this period as well as margin improvement.

You see the strong returns, 20% returns even when you factor in hedge results. And I want to remind everyone that these are returns that reflect the way we capitalize in this business. We capitalize this business to a greater of approach CTE-98 or floor. You've heard Randy say this many times in the past, that we believe that CTE-98 is the right measure. It is a deepen the tail risk measure and this is where we believe the risk of VA guarantees exists and the floor concept ensures that we maintain a minimal level of capital and strong levels of capital even in times where you have strong capital markets.

So, consistent results, impressive results, and capitalized in a prudent way. And it's a low risk book too. It's a low risk book. The top of this chart shows you the 45% of our assets are in higher-quality fixed annuity assets and variable annuities without living benefits.

Second, the living benefit book has an exceptionally low NAR. Our net amount of risk is below 0.6%, impressive and also even more impressive when you compare to the industry average, which is 6% to 7%. How do we get the low NAR? It's that strategy of consistent market presence. That's what leads to a lower risk book. We sell similar amounts each year over an extended period of time. And the result you get is what you see here. This is some new information for you. We think it's insightful, because it allows you to see what the $114 billion VA living benefit book today based on issue year sold. And what this slide tells you, if there's no single year that has a disproportionate risk to the others.

And of note, if you look at 2007, our year of highest NAR, that year of highest NAR is actually lower than some of our peer's entire books of business. So, it's a low risk book too.

So, I've shown you impressive returns. I've shown you impressive earnings. I've shown you a very impressive low risk book. Now, I'm showing you that it's more profitable too.

Oliver Wyman developed this chart by reviewing the top 20 selling variable [audio gap] (02:19:16) benefit products easily consistent set of assumptions. The middle line that splits the chart in two represents average profitability for the industry and in the size of the bubble signifies volume of sales. And what the slide tells you is that our VA living benefit profitability is higher than industry. But what it also tells you is that we sell more volume in times of higher profitability and vice versa, lower volume at lower levels of profitability. Demonstration of the discipline that we have as a product manufacturing organization and the effectiveness of distribution to be able to be a market leader on our terms.

Now, I'm going to highlight another terrific story for the Lincoln and that is our assumptions. So many companies have had significant negative results associated with unlocking. And our annual reviews continue to validate the steadiness of our balance sheet. We take assumption settings seriously. It's one of the key parts of that formula of setting reasonable assumptions from the beginning. And here on the right, you see our history, our unlocking history. What you see are pluses and minuses that add up to minimal impacts each year. And over this period of time, summing to $200 million of positive unlocking to net income, which is reflecting operating and not operating results.

In 2012, you'll see a methodology change, the installation of predictive analytics that we developed with Oliver Wyman and towers I believe, and so you see this offsetting impact on lapses in utilization as we stall that methodology sums near to zero. And then from that period of time, you see results have been modest at that individual assumption level. What do we put in there? We reflected what we learned about the different factors that affect lapses in utilization; factors in a level like whether the product is in the money or out of the money, attained age, tax status of the account, gender, and that is reflected and we – in addition, we installed a 1% lapse floor.

On the left, you see that our actual experience is in line with expectations, and like last year, we've updated the stress scenarios for each assumption, and as you can see, in each of the individual assumptions, the stress scenario impacts would be manageable. So, from a pricing to hedging, which you know is an industry-leading strength of Lincoln, and Randy will cover it in his remarks, an assumption setting, our strategy for managing our book of business is sound and the proof is in the performance.

Now, as a management team, there's another benefit to having a high-quality book. [audio gap] (02:22:45) benefit is that we can come to work every single day entirely focused on sticking to that successful formula and entirely focused on achieving our growth objectives, not being distracted with in-force challenges. And so, let's turn to the marketplace and how Lincoln as a management team, we view the marketplace and how we will chart our course forward.

First, total industry sales have been actually quite stable when you consider the headwinds that is faced in the annuity industry, in total sales. As you look under the service, what you do see is shifts in the mix of products based on customer preferences. You've seen a decline in VA living benefit sales and you've seen a tilt more to VAs without living benefits and the fixed sales offsetting that decline with each growing in the 10% to 15% range.

And if you think about Lincoln's performance, we've been right in there with industry and living benefits, but the timing of these impacts have been different. We outperformed industry in the 2012 to 2015 era, at a time when, again, where sales went to very high levels as competitors left. Those were very profitable years for annuity business. Go back to the profitability chart, you would have seen large bubbles, and they'd have been high on that chart. And then, as our sales were formed lower than industry in the years of 2015 and 2016, you would see that in the profitability chart as smaller bubbles, but down lower on the profitability chart, equaling out to about the same decline as industry.

We put our pedal, our foot on the pedal for VAs without living benefits in the shift and on guarantees and you see that reflected by performing better than industry. And we've not participated in the fixed indexed annuity space. We've not participated in that growth. It's been a space that we have viewed more opportunistically. And of course, that view has changed and shifted.

At the bottom of the page, let's talk about industry outlook. LIMRA, which is our industry group that does data and analytical projections, have projected the annuity industry to be down this year as it is, and rebounding in 2018. And the decline is attributed to the disruption related to DOL, the decline is attributable to lower interest rates that are affecting the fixed annuity business, and the rebound is attributable to the improvements in the DOL rule and the added benefit of rising rates, which allow the product value proposition to be improved. I want to go back one slide. Yeah. Thank you.

Now, adding to the tailwinds of an improvement in DOL, [indiscernible] (02:26:04) are the broader demographics, you see this here on the right, you see $42 trillion in the hands of retirees, growing and doubling from now to 2030. If we simply as an industry maintain annuity share of these investible assets, which today is $3 trillion, it would mean that the annuity AUM doubles to $6 trillion in this timeframe. And when you consider the compelling guarantees that annuities offer, there is an opportunity to even grow our share, our wallet share of investible assets.

So, how do we intend to do that as a company? We intend to focus on that historical playbook that's successful at Lincoln, of product actions, marry with distribution actions and our strategy is twofold. First, extend our market share and take share in our core products. We're going to continue to push on the non-living benefit line, which we've had success in over the industry. And what you're seeing this year and you'll continue to see is extending our market share in VA living benefits.

Today, we go to market with three unique living benefit designs and our patented i4LIFE income, which is what makes us the leader in non-qualified accounts. Both of those initiatives are underway and we're encouraged with their sales improvement.

Second, we're going to penetrate markets that we aren't in and take share. And this is all about product expansion that we've been very active in for the better part of the last year. In fact, we noted in the earnings call that in the third quarter, 20% of our sales in the third quarter came from new products that we've launched this year. Q4 sales, as I said earlier, continued to be strong, I think Dennis actually mentioned, continued to be strong in the fourth quarter; notably the sales improvement is broad based. It's broad-based across our product line; it's broad-based across our channels. So we are very encouraged with the progress that we're making in sales.

And today, we have the broadest portfolio of solutions that our Lincoln annuity business has ever had, and we aren't done. What are we doing to build out the portfolio even more? Well, next year, we'll be expanding into – and entering the already successful Indexed VA market or structured product market. I think, the industry is settling in on a terminology for this and calling it Indexed VA and that's how you'll hear Lincoln refer to it. We plan to have this out in the second quarter of next year. We plan to launch this very forcibly with our strategic partners. We plan to take share.

Second, we've made a commitment to expanding our fixed indexed annuity portfolio. We're doing it with select strategic partners, where we have a strong distribution value proposition, and that's how you can expect Lincoln's going to go to market in the fixed index annuity. We're going to go in with a strong product, where we have strong distribution and the combination is valuable to the producer and finishing up where I started. The progress that we're seeing so far, coupled with these additional actions that we're taking, is where sales contribute longer term to the future earnings growth ranges of Lincoln.

So, in closing, it is a terrific business. The annuity business, and we have a terrific franchise. You see our book of business generating strong earnings and returns, developed from that book. You see our strategy leading to an exceptionally low risk book, particularly compared to peers. You see our discipline in our assumption story, which is a great one. And you see our discipline in writing profitable business. We've got a clear path to growth. We're excited about where we are on that path and the marketplace is responding well to our actions.

So, let me stop there. Chris, you have 21 seconds left on the clock, which is probably enough time for me to invite Brian Kroll to the stage. Brian is the Leader of the Annuity business and annuity manufacturer and has been for some years, he's going to join me on stage for Q&A along with Randy, Mike and Jamie. Thank you.

QUESTION AND ANSWER SECTION

Christopher A. Giovanni
Senior Vice President & Head-Investor Relations, Lincoln National Corp.

A

Readjusting the living room for one minute, and then we'll maybe start at the back with Sean.

Randal J. Freitag
Executive Vice President, Chief Financial Officer & Head of Individual Life, Lincoln National Corp.

A

[indiscernible] (02:31:30) fall back.

Michael J. Burns
Senior Vice President, Head of Life Solutions, Lincoln Financial Group, Lincoln National Corp.

A

[indiscernible] (02:31:33).

Will H. Fuller
President-Lincoln Financial Group Annuity Solutions, Lincoln Financial Distributors & Lincoln Financial Network, Lincoln National Corp.

A

No back to the stage. So, we don't...

Sean Dargan
Analyst, Wells Fargo Securities LLC

Q

Thanks. This is Sean Dargan from Wells Fargo Securities. Will or Brian, I'm just wondering, if some proposed tax changes will mean anything to the flow reinsurance agreement and your ability to grow fixed index annuities as much as you're hoping, I think, unaffiliated offshore reinsurance is not impacted, but is there anything with the excise tax or anything in your counterparties willingness to do business that might impact your ambitions?

Will H. Fuller
President-Lincoln Financial Group Annuity Solutions, Lincoln Financial Distributors & Lincoln Financial Network, Lincoln National Corp.

A

The first thing to say is to reiterate Dennis' point, which is everything with tax proposals, so preliminary, and it can change. Second is, the reinsurance arrangement with a theme was really about what we both bring to the table. We bring a very strong distribution network, the banks and broker dealers, they bring what they bring and their advantage. And so, we are in our – not going to get into details of our arrangement, but we've applied that very selectively to not the whole fixed indexed annuity product line, but really just the products that we sell without an income rider inside the bank and the broker dealer marketplace.

In a scenario, where you have those that are paying no tax because they are offshore, that would mean that the competitive landscape would seem to come back more towards us, and you wouldn't have the need, the competitiveness in the fixed indexed annuity marketplace could perhaps normalize a little bit, not having that advantage for a few business models, but again, it's so early to tell.

Sean Dargan
Analyst, Wells Fargo Securities LLC

Q

Okay. Thanks. And a follow-up for Mike. I think, you mentioned something interesting regarding selling low face value term sales digitally to millennials and, I think, that makes sense, but how will you manage channel conflict with your external distribution partners, if that's the future of Term Life sales?

Michael J. Burns
Senior Vice President, Head of Life Solutions, Lincoln Financial Group, Lincoln National Corp.

A

I'll let Will lay in. I'll start off by saying that, even as we think about the lower face market, I think, it's still going to require, initially, as we're thinking about it, some form of intermediary. And so, there's different intermediaries out there that have access to that market. So, from our standpoint, as I think about it, really our focus, my focus, my team's focus is really on driving an effective efficient value proposition in terms of the underwriting capabilities, being easy to do business with and a large part of being effective in that marketplace certainly in the near term is having the right level of connectivity with some of the larger distributors that do have access to these markets. So, Will?

Will H. Fuller
President-Lincoln Financial Group Annuity Solutions, Lincoln Financial Distributors & Lincoln Financial Network, Lincoln National Corp.

A

Yeah. The only thing I would add is, this has not been a market we've been able to enter and participate in, in particular because the higher end market carries with a higher cost, you needed the efficiency of this innovation to enter this market, that's one point.

Second, we make our platforms available to all of our strategic partners. And so, we see actually some of our traditional strategic partners to Mike's point wanting access to our lower face, wanting access the Term Life sale, and then it also allows us to partner with new strategic partners that we wouldn't have as clients, because they didn't participate in our core business of high-end life. So, it's – I don't view this as a channel conflict more than I view it as the ability for Lincoln to participate in a new consumer segment, and it is a – is the requirement to be able to participate in that segment successfully.

Christopher A. Giovanni
Senior Vice President & Head-Investor Relations, Lincoln National Corp.

A

So, we'll go here to Tom and then next to Alex up front.

Thomas Gallagher
Analyst, Evercore Group LLC

Q

Tom Gallagher, Evercore. Randy, just I had a question on Life Insurance. Curious, if you have a view on why you think your block is held up so much better than a lot of others in the industry. I mean, we've seen significant charges by a number of competitors in Individual Life over the last several years. Now, the one thing that really stands out is different to me, for you, is that you maintained a presence in the market in a lot of those years that everyone pulled back. Is it – is that what's driving the difference do you think? Is it that the last seven, eight years you've remained much bigger in the market and that's more profitable versus the back book or what – any thoughts on that?

Randal J. Freitag
Executive Vice President, Chief Financial Officer & Head of Individual Life, Lincoln National Corp.

A

I think, there are so many aspects, so many reasons behind the answer. And I can only speak to our experience. I can't speak to what others may have experienced, whatever they have experienced. But it's all of the things that you've heard us talk about over the years. It starts with a quality portfolio. A portfolio that is where risk is embedded in the design process, a portfolio where the assumptions that go into the pricing of that product, the assumptions that go into establishment of that product, into our valuation system, are thought through and we end up starting at an appropriate place.

I've said before that charges are more than even [ph] being (02:37:33) about the experiences, but where you start from an assumption standpoint and I just think that where we've started, once again not an every single assumption, but in total has tended to be, at the end of the day, a reasonable spot when you think about how our experience has rolled out. I think, we benefit from the significant base of experience we have. So, the scale gives us a very clear view into what is going on in the industry. We only have to look at our own book to really understand what experience we should expect. I think, we benefit from having made some smart decisions to access outside expertise when needed. We regularly bring in outside experts.

So, I think, it's all of those things that have really put us where we are today, which is, as you mentioned, we've really had very minimal charges, whether that's on a GAAP basis and, in fact, on a statutory basis, we've got no charges at all, and I'll talk about a little bit about that when I get into the finance section. So, it's all those things, Tom, it's all the things that we've talked about over the years that have created our experience in the Life business, that's the experience we've had across all of our businesses and I think it's for the same reason across all of our businesses also.

Thomas Gallagher
Analyst, Evercore Group LLC

Q

And just a follow-up. Is there a considerable difference in returns of vintages if you look back at, say, the early to mid-2000s or even before that, is that much less profitable than the products you've put on the books in the last five to seven years?

Randal J. Freitag
Executive Vice President, Chief Financial Officer & Head of Individual Life, Lincoln National Corp.

A

Tom, I've never looked at it that way, but I think undoubtedly, if you look at some of the business that we sold in a much higher interest rate environment, we talked about the spread compression we experienced in the Life business and it's that business that is experiencing that spread compression. So. I'm going to [ph] imagine (02:39:29) that relative to our expectations, the returns on those book of business have not rolled out like we would have thought.

As Mike mentioned, what we've done over the last few years completely re-pricing our book puts us in a place today where the returns we expect that we're getting that business we sell today and over the last few years is well in excess of our targeted returns. So, yeah, I'm sure there's different returns if you look across vintages with older business that was priced in a very different environment, probably earning less than the business we're selling today. But, I think, it's all about wrapping it up the totality of everything. The scale, the diversity we get from the entirety of our book that really differentiates us.

Christopher A. Giovanni
Senior Vice President & Head-Investor Relations, Lincoln National Corp.

A

We'll go, Alex and then Nigel.

Alex Scott
Analyst, Goldman Sachs & Co. LLC

Q

It's Alex Scott from Goldman Sachs. I had a question on the expense improvement in Life Insurance specifically. I guess, just thinking about the revenue between the flows and the spread compression is relatively neutral. So, a lot of the targeted growth comes from expense improvement. Just wondering if you could elaborate on some of the things that would be done to achieve that and if you see that sort of near-term or is that something that's sort of deeper into the digitization strategy?

Randal J. Freitag
Executive Vice President, Chief Financial Officer & Head of Individual Life, Lincoln National Corp.
A

Mike, I'm sure, can add to this, but it's looking backwards. It's been about things like automated underwriting. It's been about things like electronic delivery, a lot of the paper-based forms that we used to send by the good old U.S. mail service. So, I think, it's all of those things looking backwards. It's good – it's been about automation of many processes, looking at our call centers, figuring out ways to improve the effectiveness about how we answer calls.

Looking forward, I think, it's a combination of the implementation of digital technologies embedded in the digitization initiative that Dennis talked about, and also it's just good old fashioned expense management. You know, we have a budgeting process that links expenses directly with revenues. Expenses are designed in the very fabric of our budgeting process to grow at a slower rate than revenues, so that we can ensure that we create expense leverage over time. So, I think, it's all of those things. Mike, I don't know if you'd have anything to add.

Michael J. Burns
Senior Vice President, Head of Life Solutions, Lincoln Financial Group, Lincoln National Corp.
A

No. I think, you captured it. I mean, I think, the two broad areas inside the underwriting and new business, we've certainly gotten a lot more efficient, effective and cost-effective. And then, inside the servicing, just whether it's technology or workforce management, all of those things have really driven effective expense management.

Alex Scott
Analyst, Goldman Sachs & Co. LLC
Q

And then, one more on the Annuities business, with some of the peers collapsing captives, and the tax bill potentially affecting offshore reinsurance, I mean, is there anything that changes around your strategy there and the durability of that structure?

Randal J. Freitag
Executive Vice President, Chief Financial Officer & Head of Individual Life, Lincoln National Corp.
A

No. Once again, our approach in using LNBAR to bring together our hedge program into one central place, it's not a captive, it's an insurance company. It happens to be an insurance company, it's something like it, but it's not a captive of Lincoln Life, so it actually doesn't get wrapped up in all those discussions.

But at the end of the day, the philosophy we used to manage LNBAR is no different than the philosophy we use to manage the rest of our company, we talk about all the time. If we were to bring that business back into [ph] L&L (02:43:09), if you look over the years, would have had very little impact and, obviously, most years it would have actually been an increase, I think, there is one year, it would have been a small single-digit decrease.

So, that approach that Will talked about capitalizing that entity at a CET98 level with a floor is really over time served us very well, and leads us to say that there is no pressure from anybody either by the structure of what the NAIC might do or because of pressures around other capitalization, I think, there's just none of that, that exists for us in our Annuity business.

Christopher A. Giovanni
Senior Vice President & Head-Investor Relations, Lincoln National Corp.
A

We'll go with Nigel and then Ryan.

Nigel P. Dally
Analyst, Morgan Stanley & Co. LLC

Q

Nigel Dally from Morgan Stanley. Just a bit of a follow-on from that question. Oliver Wyman being working with the NAIC on these new proposals, I was hoping, if you can update as to where you stand with [indiscernible] (02:44:02) potential impact that it may have on how you look at the Annuity business going forward?

Will H. Fuller
President-Lincoln Financial Group Annuity Solutions, Lincoln Financial Distributors & Lincoln Financial Network, Lincoln National Corp.

A

I'm sorry, Nigel. I couldn't – we couldn't understand the question.

Nigel P. Dally
Analyst, Morgan Stanley & Co. LLC

Q

Sure. The Oliver Wyman proposals that they're working with on the NAIC.

Randal J. Freitag
Executive Vice President, Chief Financial Officer & Head of Individual Life, Lincoln National Corp.

A

Okay.

Nigel P. Dally
Analyst, Morgan Stanley & Co. LLC

Q

Just where you stand with that process and the impact that it has on Lincoln?

Randal J. Freitag
Executive Vice President, Chief Financial Officer & Head of Individual Life, Lincoln National Corp.

A

Once again, we're in the – coming to the end of what has a [indiscernible] (02:44:31). So, the quantitative impact study, a whole group of companies, I think, there's 12 or 13 of us have provided data. The NAIC is partnering with Oliver Wyman to analyze all that data. I think, by the end of the year, they should have some sort of analysis [indiscernible] (02:44:48).

As we said before, I think, we're still some time off before the implementation of a final proposal. But we continue to feel very good about the direction the NAIC is moving. Why do we feel good? Because they are moving statutory, reserving a capitalization to be more economic than it is today. And any movement in that direction is a movement to how we hedge the risk on these products and that's a good thing. So we feel good about it. That doesn't mean each and every thing that they do is going to be a positive. There are some aspects that I'm sure will be a negative if you looked at it on that basis alone. But in total, what they're doing makes a lot of sense. We're active participants and partners and working with the regulators to come up with a good solution and we feel good about where it's going.

Nigel P. Dally
Analyst, Morgan Stanley & Co. LLC

Q

Thanks.

Christopher A. Giovanni
Senior Vice President & Head-Investor Relations, Lincoln National Corp.

A

Ryan and then Jay.

Ryan Krueger
Analyst, Keefe, Bruyette & Woods, Inc.

Q

Thanks. Ryan Krueger, KBW. First for Will, I had a question on annuity flow. Can you give us some updated thoughts on the timing of when you think you may be able to get back to the positive flow from that business?

Will H. Fuller
President-Lincoln Financial Group Annuity Solutions, Lincoln Financial Distributors & Lincoln Financial Network, Lincoln National Corp.

A

Yeah, Dennis mentioned this in the last quarter call, in that – we think it's going to – and it's just a matter of math that when you see the equity markets be elevated in their performance than when we started this, that the dollars of outflows are higher. So we think that timing of when we get back to positive net flows is likely not going to happen in the early 2018, but it doesn't diminish that, we are on the right path and we will get back to them, it might just take us a little bit longer.

Ryan Krueger
Analyst, Keefe, Bruyette & Woods, Inc.

Q

Got it. And then, on indexed annuities – I guess fixed indexed annuities, what's gotten you more comfortable expanding into that product line relative to the last few years?

Brian Kroll
Senior Vice President, Head of Annuity Solutions, Lincoln National Corp.

A

Well, I would say that it's really a matter of customer preference. And when we look at our product development, we're really trying to meet customer needs. The indexed annuity business is a good business that fulfills a need for clients to have gathered assets, and they're now at a point where they want to protect those assets. Our product development efforts are looking to expand our presence in that space, and take advantage of the change in the consumer preferences.

Will H. Fuller
President-Lincoln Financial Group Annuity Solutions, Lincoln Financial Distributors & Lincoln Financial Network, Lincoln National Corp.

A

One thing I'd add is that, yeah, this is a business that we've looked at for a long time and we focused in on the consumer friendly side of the business, particularly in areas, where you had a broker dealer. So there's a higher level of compliance and suitability. These are shorter serener charges, lower commissions and more – and more value for the consumer. There was an element of the fixed indexed annuities that longer durations, high commission, the consumer value was really for the producer. And I think what we've seen is that evolve in a shift. We've seen the industry come in a little more tighter, where we've been all along in these consumer friendly options, perhaps that's been accelerated by the emphasis of DOL best interest. We view that favorably.

Second is, we see certain broker/dealers that haven't had as much interest in fixed indexed annuities in the past start to become more interested. And it's expensive to build the distribution network to the broker/dealer and the bank community that we have. And so there's a greater ability for us to participate in this market. That's very competitive from a pricing standpoint. We have to do it on our terms.

Ryan Krueger
Analyst, Keefe, Bruyette & Woods, Inc.

Q

Thank you.

Jay Gelb
Analyst, Barclays Capital, Inc.

Q

Thank you. Jay Gelb from Barclays. First, I had a question on the variable annuity flow potential. I mean, based on my numbers, it looks like Lincoln would need to generate around $12 billion in variable annuity sales in 2018 to generate positive flows for the year. I mean that would be almost double from 2017, so can you tell us how reasonable that expectation might be?

Brian Kroll
Senior Vice President, Head of Annuity Solutions, Lincoln National Corp.

A

Sure. I mean the $12 billion number is in the right range. I think what – and it is higher than we had anticipated because of the stronger compounded growth that we've seen in our block. I think, what we have heard Will say a little bit earlier is that while we may not get to positive net flows early in 2018, we would expect to get there later in the year maybe not for the entire year, but it will really depend on the sales momentum. We're seeing a lot of really positive activity in the fourth quarter here. And we've got a lot of product actions that we are taking that Will covered in the presentation that we feel really good about our opportunity to grow sales.

Will H. Fuller
President-Lincoln Financial Group Annuity Solutions, Lincoln Financial Distributors & Lincoln Financial Network, Lincoln National Corp.

A

Yeah. And it's not going to take a double in our sales to get there. It's a healthy sales increase somewhere about 30%, 25%, 30% in that range, but not a double.

Jay Gelb
Analyst, Barclays Capital, Inc.

Q

That's helpful. Thank you.

Will H. Fuller
President-Lincoln Financial Group Annuity Solutions, Lincoln Financial Distributors & Lincoln Financial Network, Lincoln National Corp.

A

Thank you.

Jay Gelb
Analyst, Barclays Capital, Inc.

Q

Could you also give us a little bit of perspective on the indexed variable annuity product? First, what is it? And second, why would a customer be interested in buying that product?

Will H. Fuller
President-Lincoln Financial Group Annuity Solutions, Lincoln Financial Distributors & Lincoln Financial Network, Lincoln National Corp.

A

Yeah. So, let me take a stab at it, and then Brian can follow on. It is a new value proposition for the annuity business. And the value proposition for the consumer is protection against the downturn or protection against negative investment performance. And so, the way to think of it is that, it is a buffer.

And let me just give you an example. A client would be protected from the first 10% decline in an S&P 500 index. First 10%, they'd be protected, they would not be protected on declines beyond 10%. So if the S&P 500 was down 12%, they'd have a total decline of 2%. And in return, they'd have higher upside in that index, higher than they would have had with a fixed indexed annuity. So it really plays because right in between I think VA and fixed annuity for those that want some protection, but also want to have a greater upside than what a fixed indexed annuity would allow.

Brian Kroll
Senior Vice President, Head of Annuity Solutions, Lincoln National Corp.

A

Yeah. No, I think Will described it well, it's a growing market. There are very few participants in it today. It's sold in distribution channels, where we have very strong presence and sold primarily in the bank distribution, where we're very strong. Think about the $7 billion in that marketplace last year. It looks like this year will be stronger than that. We're seeing other participants come in. Again, as I said earlier, it's a customer preference that we're seeing in the marketplace and it's a place where we can expand, and grow share in that – take share actually in that segment.

Will H. Fuller
President-Lincoln Financial Group Annuity Solutions, Lincoln Financial Distributors & Lincoln Financial Network, Lincoln National Corp.

A

Yeah. And so if you kind of think about the annuity value propositions, pretty exciting, you've got income protection which comes through the guarantee limit benefit rider, then you got two versions of asset protection; fixed indexed annuities provide guarantee of principal, indexed VAs provide a buffer guarantee for market downfalls. So, pretty interesting and compelling differences in the value proposition which should over time allow the market to expand.

Christopher A. Giovanni
Senior Vice President & Head-Investor Relations, Lincoln National Corp.

A

We'll take one last question here from Eric before lunch.

Erik Bass
Partner, Autonomous Research

Q

Thank you. Erik Bass from Autonomous Research. So on the Individual Life, you commented about the very strong profitability on new business that you're seeing. I was hoping you could give a little bit more color on what's allowed you to boost profitability? And I guess are we seeing any competitors that have pulled back, sort of reengaged in the market given the improvement in the profitability of new products?

Christopher A. Giovanni
Senior Vice President & Head-Investor Relations, Lincoln National Corp.

A

You've got that, Mike?

Michael J. Burns
Senior Vice President, Head of Life Solutions, Lincoln Financial Group, Lincoln National Corp.

A

Yeah. I'll take it. And, Randy, if you want to add, feel free to. I think that as the market has changed and you saw that slide where a lot of carriers have pulled out, it has since, in many respects, in some of our markets, become a much less crowded space. I would point to variable life as an example of that, where the competitive landscape is a lot less crowded. So that would be one factor. I also think that just the natural cycle of carriers, re-pricing products has changed the competitive landscape. And so, I would expect that the whole industry probably is seeing better returns, but certainly I know for a fact that we're getting solid returns on our new business.

And so, I think it's those factors as well as the fact of the matter is that in our markets that we are in, we are selective. And so, we're not necessarily going to be the most competitive in certain aspects of the markets, but when you put the entirety of our portfolio, combining the variable with the indexed, with products like guaranteed universal life, they all produce a nice complementary balance and again that's where the wholesaling force of what Will and his team really have and the ability to drive sales in areas, where we would like to get business and get business on our terms. And I think that all of that has led to the general overall lift in returns on our new business.

Erik Bass
Partner, Autonomous Research

Q

Thanks. And then I noticed on your MoneyGuard slide where you listed the competitors, all of the major competitors are mutual. Is there a reason that you think that other public companies haven't been more active in the linked benefit space?

Michael J. Burns
Senior Vice President, Head of Life Solutions, Lincoln Financial Group, Lincoln National Corp.

A

There have been a few who have tried, there have been a few who have tried, but beyond that, I think it's probably more coincidental than anything else.

Randal J. Freitag
Executive Vice President, Chief Financial Officer & Head of Individual Life, Lincoln National Corp.

A

It's a tremendous amount of investment to create that platform. When you think about the investment like it is made in that distribution force, which is a definite differentiator and the investment we've made over 25 years, I think when a public company faced with the pressures of growing earnings thinks about that sort of investment, it becomes more difficult. I think that's a contributing factor. I have no doubt when you look at the attractiveness of that marketplace that you will see companies come in that way. But we have a significant head start, Erik, and we think we'll take a lot of advantage of that head start.

Erik Bass
Partner, Autonomous Research

Q

Great.

Christopher A. Giovanni
Senior Vice President & Head-Investor Relations, Lincoln National Corp.

So, now we're going to take a break here for lunch. Back of the room, lunch will be served. We'll do about 40 minutes, and then we'll be back to finish up the day. So, thank you, all.

[Break] (02:55:55-03:38:51)

Unverified Participant

Ladies and gentlemen, please welcome back your host, Chris Giovanni.

Christopher A. Giovanni
Senior Vice President & Head-Investor Relations, Lincoln National Corp.

Great. So, we're going to wrap up here, we're going to go with Ellen Cooper on Investments, Randy will finish up in finance. We'll bring it at the end and do a Q&A session. So look forward to finishing up here this afternoon. Ellen?

Ellen Cooper

Chief Investment Officer & Executive VP, Lincoln National Corp.

Take another step little slowly. So, good afternoon, everybody. And I am here to talk to you about the general account investment portfolio. So you've heard lines of business this morning and most importantly, as we think about the investment portfolio, it starts with our liabilities. And as you know, and as we've talked to you in the past, we have a very disciplined asset liability management and overall risk management framework.

So, in my remarks, this afternoon, there are three themes that I want to really highlight for you. The first is our unique multi-manager framework. We are differentiated in the U.S. Life Insurance Company peer group. In that, we are the only large life insurer that primarily utilizes external managers to manage the assets on our behalf. And I'm going to talk to you about how that model actually work, and I'm going to talk to you about why we do it and the benefits, very powerful benefits that we are experiencing from it.

The second thing I'm going to talk to you about is our execution around proactive investment strategies and what we're doing to mitigate managing through the low yield environment. And I'm also going to demonstrate to you that our spread compression does continue to moderate. And finally, the third theme and a pillar of our risk management is, I'm going to talk to you about our effective and diligent portfolio construction and our active risk management, and how they are improving our overall investment flexibility.

So with that, let's start by looking at how our multi-manager framework actually works. So this for us is a powerful model, and it is much more than just throwing asset management mandates over a wall. It starts with building an infrastructure here at Lincoln. It was an experienced team that is deep and seasoned and investment professionals, and then giving them and building alongside them a structure and a process to be able to have external managers manage assets on our behalf.

So, for example, we have built very robust risk management and reporting capabilities to be able to track what our managers are doing in real time. This way, we can be tracking how they're managing our assets over the course of the day at a very granular level. So, when we think about this operational model, there are really five key steps that I want to talk to you about. The first, which is owned by Lincoln is setting investment strategy. And Dennis mentioned this this morning. When we set investment strategy, we think about first of all our objective, which of course is to maximize net investment income, while we're trying to minimize the amount of credit losses that we'll take.

And in addition, we set broad risk guidelines, so as examples of those, some of the keys are managing within our ALM guidelines, and managing within the risk asset guidelines that we set for ourselves. We then go a level deeper. And the second operational step is around portfolio construction, and we own this at Lincoln as well. And this is really next level down, where we think about, how we're going to invest across various asset classes, and how we're going to invest within asset classes and that gets as granular as looking inside an industry sector, looking at individual position sizes, looking at geographic limit, and really distilling it down.

And then from there, we think about the canvas of best managers for the job. And we go out and we select those managers, and the managers are [indiscernible] (03:43:28) good at investing assets in those asset classes, but it goes well beyond that, because these managers also have to be able to manage general account insurance assets. They have to understand book yield orientation. We are not total return based. They have to be able to comply with our high touch collaborative model and be willing to communicate with us multiple times during the day. And so once we hire a manager, the manager is then responsible for selecting the individual securities that fit within that particular mandate.

And then the fifth step, which is really critical, is around risk management. Every manager that we hire that's on our platform and is our partner is responsible for risk management, of course, of their individual mandate as well as portfolio construction within their own individual mandates. But we at Lincoln have built a robust process with an experienced team, where we holistically then evaluate and are constantly monitoring and managing the overall risk management of the investment portfolio. So that's some insight into operationally how this works, and we find this model to be really powerful.

So, let's talk about why do we do this. So, there are several key benefits that I want to talk to you about and they really start with maximizing our flexibility. So as I mentioned, we go out and we find the best managers, and what we have seen in our experience is that even though there are great managers out there, not every manager is actually good at everything. And so this enables us to pick the best manager for that particular asset class. And so as a result of that, we continue to diversify our managers. We now have 11 managers on our platform, many of which have multiple mandates on our framework.

We also favor certain asset classes where there is really scarce supply. For example, investment grade privates, and I'll touch on this more later. And in that particular asset class, in order to continue to invest in as much as we would like to have, we have found managers that actually have unique sourcing capabilities. And those unique sourcing capabilities in order to be able to get that filled, we go out and we hire another manager. And they don't overlap with each other, so we get really nice diversification, again another benefit.

The third area is that we also effectively get extension of our team by hiring these managers. So, they have their own deep research teams. They're working alongside of us, and we now have a broader team.

And finally, we also have the benefit of multiple manager views. And I often say to my team that this is kind of like going to the doctor for a second opinion, because there's a lot of art to having an individual view in a credit or in a sector. And so we have the benefit of hearing that from multiple experts and then our experienced team really synthesizing this information.

And I think so far the best proof point that we've had around how this works, really has to do with how we manage through the energy sell-off that we saw about 18 months ago. So, you'll recall that about 18 months ago, we saw oil prices fall to below $30. And at that time, what we did was we went to our managers, and we had them create a framework where they were running on a regular basis, stress scenarios, very stressful scenarios to look at those particular issuers in the portfolio that could potentially see significant credit deteriorations, if there was to be a very prolonged energy sell-off. And then what we did was we took that information, we pulled it all together, we prioritized and we executed on a de-risking plan. Now, this was purely a de-risking plan. As a matter of fact, we really have had very minimal impairments over energy exposure.

But I'm pleased to tell you that we reduced our energy exposure as a percentage of invested assets from 10% to 6.7% today, and our stress scenario losses are reduced by 70%. Again, I think this is a demonstration of the power of this model. And as if that wasn't enough, we have an additional add-on benefit, which we didn't anticipate when we originally built this out, and that is that we've been able to use the power of our balance sheet to negotiate lower fees. And so this year in particular, the base fees for our core fixed income have reduced by 25%, and that now enables us to have all-in investment management fees that are 40% lower than the peer group, again compelling, the model works, and it's cost effective.

So, as I mentioned in my upfront remarks, liabilities is where we start. And ALM is part of everything that we do. And we manage our ALM within tight guidelines at the line of business levels, and in aggregate for all of Lincoln as well. So you can see on the left hand side of the chart, that all of our lines of business, as well as old Lincoln is well within [indiscernible] (03:49:21). And as you've heard us talk about repeatedly, we are tilting away from long-term guarantees. And that's having effect on the investment portfolio. And so some of what we're starting to see is the shift away from some of the longer duration assets and more into purchase needs that are shorter. And this is also giving us several benefits.

So, the first benefit is a broader asset class mix. So examples of that, more access and exposure to structured credit. The ability to invest in public fixed income in names of issuers that are typically shorter duration, again, bringing broader diversification. It also gives us more capacity to invest in illiquid strategies such as commercial mortgage loans and private debt. And in all of those cases, we are seeing and benefiting from enhanced spread opportunities.

So, let's move to theme two. It was around proactive investment strategies, and I want to start first with highlighting our strong new money yields. And so we looked historically through time since 2012, and what we see is that on average, we have produced a new money spread that is 60 basis points over the Investment Grade Corporate Index. And even as we look to 2017, what we see is that although credit spreads have come down, and they've tightened pretty considerably this year, so you can see that the Investment Grade Corporate Spread Index is 120 basis points over the 10-year Treasury on average in 2017. We have continued to invest new money 60 basis points over that.

And so 2017, so far, year-to-date, we've invested at 180 basis points over the average 10-year Treasury. And if you look to the right, we show you the diversified mix of how that money's being invested. So, the first 12% of that 180 basis points is coming from what we're referring to as ALM, and that's reflecting the fact that when we match our liabilities, we're slightly longer than the maturity of the 10-year Treasury. Roughly 50%, 48% is coming from investment grade corporate spreads, and the remaining 40% is coming from diversified sources of new money. And most notably, corporate private debt, as well as commercial mortgage loans, two strategies that I'm going to highlight in more detail on the next few slides.

So, let's talk about private corporate debt, first of all. This class that we have been investing in at Lincoln for decades. It's one that we like very much, and you'll see year-over-year that we've increased our new money purchases by 40%. We also are able to have the benefit of 35 basis points to 45 basis points of incremental spread over comparable public corporates. Now, why have we increased by 40%? Well, we have really two main reasons. The first is increased capacity. So, I mentioned that we've been shifting to more needs at shorter duration, private corporates tend to be shorter, and so we have more capacity to be doing more.

And the second reason has to do with increased sourcing. So, I mentioned that we can go and add more managers to be able to do more, and if you look at the bar charts, the red bars year-over-year is a place where I can really highlight this for you. The red bar is increasing from 2016 to 2017, and the reason is that we've added more managers, and so we're able to get more.

And so looking over at the right-hand side, I also wanted to share with you the total private portfolio holdings. So, we have $14 billion, it's 14% of the total general account portfolio, and there are two areas here that I want to focus on that are both around risk management. The first is related to credit risk. And so, historically, private corporates have much lower losses and that's really as a result of the fact that there's better downside protection. As a matter of fact, our historical – since 2012 – losses have averaged 10 basis points per year. And that by the way, we went back and we've looked at Moody's defaults just general publics for the same credit quality mix, and we see that the public comparable was at 40 basis points. So our loss rate was 25% of the overall public rate.

The second area I want to highlight for you around risk management is the focus on portfolio construction. And you can see on the bottom of this chart, the building of a well-diversified portfolio. As a matter of fact, private corporate debt and the industry sectors here are also a good diversifier to public corporates corporate, as we see new names in the portfolio relative to publics and we also see different industries. So for example, one-third of the existing portfolio is actually invested in project finance and in infrastructure debt, areas that we also think are just overall good investments, and also provide really good diversification for the portfolio. And finally, more than 90% of this portfolio is investment grade.

So the next strategy I want to hit on is commercial mortgage loans. And one of the things that is unique for us about commercial mortgage loans is that this is one of the places where we have our own internal team. Our internal team has been in place for decades. They have a long track record of excellent portfolio performance, and we continue to really like the space and find attractive opportunities here and have been strategically growing this portfolio.

Coincidentally, we also find that we are able to achieve 35 basis points to 45 basis points of incremental spread over public corporates. And we also have a low average annual loss rate of 11% (sic) [11 bps] (03:56:14) per year since 2012. We've grown the portfolio. It stands at 10% of invested assets today, and we have plans to continue to grow the portfolio such that it will be 12% by the end of 2019.

We also focus here on portfolio construction and diversification. Our commercial mortgage loan portfolio has 1,300 loans in it. It's a $10 billion portfolio. The average loan size is a little bit short of $8 million. That means there is significant diversification. It's also incredibly high quality. So, you may know that the NAIC has risk-based capital standards, and the highest standard for risk-based capital in commercial mortgage loan space is called the CM1. And the CM1 starts with a debt service coverage ratio of 1.5 times, and anything higher than 1.5 times gets a CM1. Our average debt service cover is 2.2 times, significantly higher than that 1.5 times. And finally, our loan to value average percentage is only 50%.

Now, I think the story gets even more powerful when you look at the middle of the slide. And that's showing you that we have a higher yield and we have higher quality than our peer group, 4.5% commercial mortgage loan average yield, and CM1 of 86% compared to the peer group at 61%.

Now, any time, I want to talk about commercial mortgage loans, we have to talk about retail because it's in the news almost every single day. So, what I want to say about retail is that, the first thing is, it's not going away. The second thing I want to say is that, we do recognize that there is a secular shift and a change in retail that is occurring. And we're going to see – we're seeing and we're going to continue to see a shift in more omni-channel distribution and a shift to smaller stores. But I'm also here to tell you that our portfolio is positioned accordingly. So when we look across our retail formats, the majority of our portfolio is already positioned in smaller retail formats. And in addition, we have a lower overall allocation to retail as a percentage of the CMO portfolio as our peers.

And one additional strategy that I have to highlight is our alternative strategy. And here – and we've talked about this with you for some time. Some years ago, we talked about our desire to grow this portfolio. In 2012, it was $900 million, and it's grown at a 10% CAGR. And today, it stands at $1.4 billion. We also told you at our last Investor Day that we were going to reduce the hedge funds. It had been one-third of the overall alternatives portfolio. And we told you, we were going to reduce it to 20% and that's exactly what we did.

So, the hedge fund portfolio is 20% of the overall alts, as we have continued to grow the overall alternatives portfolio. Here, just like every other place, inside of our portfolio, we also focus on risk management. And a way to think about risk management in alternatives is to build a highly diversified portfolio. And so we demonstrate that to you in the middle of the slide. The top shows that we're well diversified as it relates to sub-strategy; and the bottom shows you that inside of the private equity portfolio, we're well diversified by industry. And something else is – I talked about are robust analytics and reporting, we have built systems that enable us to look underneath of each of our funds and see all of the individual investments that are inside of there. And so we're able to see and monitor that we have 1,500 individual investments inside of our private equity portfolio and able to manage that and measure it accordingly.

And then, finally, we are very proud of the performance and we really think that it speaks for itself. The annualized performance of our alternatives portfolio at 10.6%, that's 170 basis points over the peer group.

So, [indiscernible] (04:01:00) many of your favorite slides, and for those of you that haven't been with us before, I want to spend a few minutes walking through this with you. And this is a slide that talks about our fixed income portfolio yield decline and its continuation to moderate. So at the top, we show you what the answer is, and we all know that we've been living through this low yield environment.

From 2012 through now, on average, we've experienced spread compressions of 16 basis points per year. But I also want you to know that as we look forward for the next three years from 2018 to 2020, we expect that spread compressions to be cut in half to 8 basis points per year.

And when we get to 2021 to 2025, we expect that spread compression to actually be fairly small at minus 2 basis points. So let me show you why. So let's go back to 2012 to 2017. And if you can look at the slide, the solid blue line is showing your actual new money yield, which averaged by the way at 4.1% over that time period. The blue bar up at the top is showing you the average portfolio run-off yield, which was 6.2% with 200 basis point differential. And by the way, the portfolio was running off at a pace of 9% per year. And so you can see in the red bars, the significant decline in the portfolio yield over this period of time. But as we look to 2018 to 2020, what we see is that if we assume again a 4% new money yield, which we think is a fair assumption, the run-off portfolio is at 5.2%. That differential is shrinking.

And we see that the portfolio yield spread compression therefore is 8 basis points per year. And looking even further out, again assuming a 4% new money yield, the average run-off of the portfolio is only a little bit over that, at 4.1%. And by the way, the portfolio run-off also slows down during this entire projection period to 5% per year. So not as much pressure coming from those runoff portfolio. So again, we really do have evidence that the portfolio yield spread compression will continue to moderate even though we're managing through in a low yield environment.

Total portfolio, little more than $100 billion of general account assets. I've touched on this point multiple times, well diversified portfolio, across asset classes, across sectors and across issuers.

High credit quality, below investment grade assets stand at 4.3%, that's almost a 200 basis point reduction from 2012. And finally, as we think about our effective portfolio construction, there are a couple of quick points that I want to make. The first is that, we have lower concentration, lower credit concentration relative to our peers. The second is when BlackRock went through their annual peer analysis and really consistent with that, they're showing that in a stress projected scenario analysis that we would experience a lower amount of credit tail off than our peer group.

And finally, when we look across all of our risk assets, which include below investment grade bonds, schedule VA assets which include alternatives, and other assets such as equity real estates and mortgages that are in foreclosure, we see that we have significantly lower risk assets as a percentage of total assets, and as a percentage in capital and surplus. We're about 33% less than the peer group.

So in conclusion, we have a unique multi-manager investment framework. We believe that the benefits of that are really compelling and we have the add-on benefit of seeing fees that are 40% lower than the peer group. The second is our proactive investment strategies. We demonstrated to you, our private corporate debt and commercial mortgage loans are achieving 35 basis points to 45 basis points over comparable public credit.

And in addition, our alternatives portfolio, which has had strong performance is achieving at 170 basis points over the peers. Our portfolio yield spread compression, yes, it's been difficult managing through the low yield environment, but we expect that to be cut in half over the next couple of years and down to 2 basis points starting in 2021. And finally, as it relates to effective portfolio construction, we see that we have lower credit concentration, we see that we have lower projected [ph] tail (04:06:13) credit loss versus the peer group and we have lower risk assets.

And with that, I'm going to hand it over to Randy to finish off the day.

Randal J. Freitag

Executive Vice President, Chief Financial Officer & Head of Individual Life, Lincoln National Corp.

Thank you, Ellen. We've made it, the final presentation. Thank you all for coming today. I hope you've enjoyed the venue. We greatly appreciate you making the trip here to Philly. There are a lot of factors that went into Chris' thoughts when he was thinking about the venue, a couple that come to mind. Lincoln Financial Investor Day and Lincoln Financial Field, that makes a lot of sense, a lot of. But even more importantly, when Chris would do surveys after prior Investor Day meetings, he gets comments back like great Investor Day, I learned a lot, people did a great job of presenting, but you know what, when I went to the bathroom, I had to wait in line, there you go. 27 stalls in the men's restroom, and an equally spacious women's bathroom, I'm sure.

You know why this comes at the end of the day. It comes at the end of the day because there is nothing more than an aggregation of everything you've heard before, whether it was Dennis talking about our strategy, whether it was Will talking about what differentiates us from a distribution standpoint, whether it was his discussion about what is undoubtedly the highest quality annuity book in the industry, whether it was Dick talking about the tremendous job they've done rebuilding the group business and our expectations for that great business looking forward, whether it was Mike and myself talking about areas for growth in the Life business, or Jamie talking about the tremendous momentum she's built up in the Retirement business, or whether it was Ellen talking about our high-quality investment portfolio.

All of those things, when you put them all together or what it has generated, the consistently strong and differentiated results, which I'm going to talk about today, results that we believe that are repeatable when you look forward, based upon the drivers discussed by our business leaders today.

I'm going to spend some time drilling into our financial performance. I'm going to talk about capital generation and deployment, and what it means to strike the right balance when it comes to investing in businesses and returning capital to shareholders. And finally, I'll touch on those key risk management programs, which differentiate us in the marketplace.

Before I get into what will contribute to our future success, let's talk about the last five years, a tremendous period of performance. Results have been strong, not only on an absolute basis, but on a relative basis, I would argue even stronger. Performance starts with the top line. I can guarantee you over a five-year period, if you can't grow the top line, you are going to have a very difficult time growing the bottom line. We have. We've grown our top line in a mid-single digit rate. And we've been able to leverage our scale to drive expense leverage in addition to that operating revenue growth. And when you combine top line growth with expense management, you get a very predictable outcome. You get bottom line earnings growth and that's what we've seen, bottom line earnings that have grown 4% a year for the last five years, bottom line earnings that we've been able to leverage with capital deployment into EPS growth of 11%, very strong results, the results that have been underestimated by the marketplace.

It's just a fact that when we sat down with investors over the last five years. The questions we get, it's not that they're all like this, but on average, the questions come tinged with a bit of pessimism behind them. That's a pessimism which tends to overestimate things like the impact of low interest rates on Lincoln. That's a tinge of pessimism which tends to underestimate our ability to respond to those sort of things, but the reality is so much different than those tinges of pessimism.

In fact, we have far exceeded consensus estimates time after time after time, while our peer companies have underperformed those very same expectations. Believe me, we have all operate in the exact same environment. Lincoln isn't over here in some parallel universe. It's the same for all of us. We've over performed, they've underperformed. That's resulted in an EPS CAGR nearly twice that of our peers. That is performance. In my opinion, it's been this way for a long time. The most reliable way to value an insurance company is by looking at two factors; the book value of a company; and the return that it delivers on that book value. On just those two basis, it is so easy to see why we have outperformed over the last five years.

Book value, we've grown it at 10% a year, well above the rest of the industry. Not only that, we've done it with far less volatility. It's just the fact that our lowest year book value growth exceeds the average for the rest of the industry. That's outperformance. Strong book value growth, coupled with strong ROE growth. In fact, we've grown ROE again. Not only we outperformed the industry by over 300% over the last five years, we've grown ROE another 60 basis points this year. That is the period and the history of outperformance that we're very proud of.

So, that's the story of what we've done. How we've been able to close some of the valuation gap that existed five years ago. Let's flip the story now and let's talk about what we can do when you look forward. Hopefully, you're all familiar with this chart. Chris created it a few years ago. We've used it over and over and over. In fact, today, we decided to take this whole concept a little deeper. We showed it for each of our businesses. And this slide here is nothing more than the addition of all four of those businesses, with a little dial up of share repurchase added in, and what do you get? You get this.

Now, over any given period, you're obviously going to have pluses and minuses in some of these different towers of growth. In fact, over the last five years, we've been able to leverage a seriously undervalued share price to more than double our contribution from share buybacks. You could really see that all the other drivers are largely within their targeted range. Now, looking forward, we still expect to be in that 8% to 10% range, but we do expect to be at the lower-end of that range. And this is really all about that full story.

We're in the process of rebuilding annuity flows, but over the next few years, we're still going to be a little below our long-term average, and that means from an expected standpoint, we'd expect to be at the lower end of that 8% to 10% range. You should also be rest assured that to the extent something deviates from the numbers you see here, we will do everything we can to adjust, take actions to offset any potential negative impacts.

Our digital initiative is a great example of us taking action. Yeah, absolutely interest rates are low for spread compression it must have been on 20 different slides today. Absolutely, it's a fact. And if you only focus on that one thing, you would have missed 90% of the story. You would have missed the fact that we don't stop there, we do what we can to overcome headwinds. You don't expect management teams to stop that walls, you expect them to climb over walls. The digital initiative is our next ladder to get over that wall.

Our expected impacts from this program have not changed. A net investment of roughly $40 million over the next couple of years 2017/2018, a neutral impact as we move into 2019, and ultimately $90 million to a $150 million of benefits from this program.

These digital technologies are powerful, powerful tools. It's so much different than it was a decade ago. When if you wanted to improve customer experience, what you do? You went out and hired more people; you increased your expense base. These tools completely change that whole paradigm. They allow you to both improve the customer experience and do it at a lower cost. And, in fact, that's where the majority of the benefits will come, from the implementation of technologies across the organization.

So, we will get some from other approaches, for instance, there are a number of companies that have already grown some of these capabilities and we would look to source some things we do today, some of these outside parties to leverage the benefits they've already captured.

[indiscernible] (04:17:18) the fact that I just beat up on some of my competitors, I would like to argue, [indiscernible] (04:47:59) subjective view, but the life insurance industry is undervalued today. I think we trade far too close to where we've traded during times of stress, as opposed to where we've traded in times like before the financial crisis. I told you it's a subjective opinion. Just moving up to the midpoint of these two points, would imply one full PE point for the industry. I think it's justified based upon the performance.

I talked to earlier about my view for how to best value an insurance company. So, once you pull outside of that industry, let's talk about Lincoln. When you plot the book value and ROE for our industry, you get a pretty tight regression line. And to me one thing stands out, Lincoln is still below that line. I think we deserve to move up to that line. A simple movement to that line implies a share price of a $90.

One question we often get, why don't you return more capital to shareholders, why do you increase your free cash flow conversion target from 50% to 55%. I'll remind you, we have done that in the past; we use to be 45% to 50%. Look, we could certainly do that. You could have shut off new business, you'll have as much free cash flow as you can possibly imagine, we'd be virtually swimming in this stuff, but that would not be the right answer.

The right answer is about striking the right balance between both investing in your businesses and returning capital to shareholders. Well, some companies have grown their earnings a little faster rate than Lincoln, a few of them, well, a few of them may have taken their share count down a little more than Lincoln. While we're not quite in a league of one, we are in a league of two. Only two of us, one of those being Lincoln, have outperformed the industry on both of those metrics. Those are great results. So, let's focus on this little bit more, free cash flow generation, free cash flow deployment.

You know what we target, 50% to 55%, because I mentioned, that's come up over time, driven by the fact that we've had a tilt away from longer-duration products or capital-intensive products. We continue to see that as a good proxy.

Looking forward, what has it resulted in. And I'm going to update the numbers on the slide. $4.5 billion of share buybacks to the third quarter this year, a 29% CAGR in our dividend over six years, most recently increasing our dividend 14% for 2018. That's a total of $5.6 billion of deployment; a pretty impressive figure, that wasn't exactly zero of your models, if you went back to the end of 2011.

Now, you could probably deliver these results in a couple of different ways. You could [indiscernible] (04:21:39) the balance sheet, you could take down RBC, you could add leverage, that would be one way to create deployable capital. We've chosen the other way. The good old fashioned way. We've generated free cash flow for each and every dollar of it.

In fact, what you see over the last five years is an RBC ratio that is unchanged, right around 500%. You've seen capital that has grown right in line with the risk of this company. You see leverage that has actually come down $300 million over those five years. And you see us continuing to hold capital above our long-term target at the holding company. That's a tremendous story about creating free cash flow and one we would expect to continue going forward at the rate of 50% to 55% as I mentioned. And as I mentioned earlier, at the end of the day, this isn't about choosing either or this is about striking the right balance between investing in very attractive businesses, and returning capital to shareholders.

So, let's finish up by switching over here and talk about a couple of risk management programs, ALM, which is what we used to, be a key component of managing interest rate risk. We talked about interest rates over and over, over the years, and every time the punch line has been the same, really not a big deal when it comes to the balance sheet, a little bit of a headwind when it comes to growing earnings.

And mainly I'll reiterate that point, but first I thought, I'd focus on exactly what we have said over the years and what the exact outcome has been, compare those two. Let's start with the statutory balance sheet, statutory reserves, what have we said. We have pointed to significant asset adequacy. We've pointed to the fact that we didn't believe we would ever need to strengthen reserves, with the small exception of if interest rates dropped to very low levels, around 1%, we talked about a little bit of potential strengthening, because of some of the sub tests inside the cash flow testing, $350 million, compared to our over $9 million of capital. What's happened? This much, zero reserve strengthening exactly what we said, exactly what we have said all along.

Next, the GAAP balance sheet, and here the only real area of focus has been on the long-term interest rate assumption, embedded in our models. We've been very consistent. We have said it over and over and over again. If we lower this assumption 50 basis points, it will have an impact of $125 million. We've done it three times. Each time the impact has been within steady distance of a $125 million. And it would be again if we had to do it again; exactly what we said.

By the way I feel pretty good about where we stand from an interest rate assumption standpoint right now. We're having a 10-year assumption, a little below $375 million. That's above where we are today, but I think it's a reasonable estimate of the future And we've told you once again what the impact would be, would we have to change that.

So the long-term earned rate has been a very powerful story. It's just one of the many assumptions we use inside of the assumption setting process. And in fact, as Will mentioned for the annuity business, if you look at Lincoln's results when it comes to unlocking our assumptions over the years, even including the fact that we've lowered this assumption three times in total, the impact on our results over six year is minuscule, sum total of $95 million, like $60 million a year if you want to do a little math.

Lastly, spread compression. This has really been the item we've talked about, the fact that we invest below our portfolio yield, Ellen just discussed it as part of her discussion. We've made a few points when we've talked about this. Yes, it's real, but we consider our earnings, what's happened? We've grown earnings. There are actions we can take. What's happened? We've taken actions, the digital initiative I talked about, this headwind will abate. The impact today is half what it was five years ago. And as Ellen pointed out, we expect it to continue to decline looking forward.

So, we continue to feel very good about our ability to operate in the low interest rate environment. Don't let me kid you, I would love for interest rates to go up, it would allow us to present the more competitive product for consumers, a more compelling value story. But we can continue to operate. Our products have been priced for this environment and we're ready to go.

So quickly our latest thoughts, as we've shown over the day, new business returns are very strong and been priced for this interest rate environment. Spread compression continues to abate and we have significant reserve adequacy, $12 billion, if you want to know the most recent number. We continue to have small impacts in a very low interest rate environment, 10-year treasury around 1%, $350 million, there it is, zero change, that's what you've heard now for five straight years.

Finally, let me talk about value embedded in our available annuity book. We'll talk about what differentiates our book, and you can see it on this page. I know it's difficult for you guys to compare book to business, we've tried to do it by showing you net amount of risk. Here we went out and we found people's disclosures around their cash flows. We tried to use assumptions that are consistent with what other companies are using, happens to be that we've used separate account return assumption of 5%, interest rates fall in the forward curve, and the stress scenario we looked at, equity markets down 30%, and interest rates consistent with that.

So we tried to get comparable results. And what you can see, whether you're talking about a baseline, whether you're talking about a stress case, our book over-performs. It's extremely profitable in the baseline world. It's very profitable even in a stress world, and all the things we talk about. The high-quality risk profile of this book of business, the quality of our hedge program really emerges in that stress event, when we really outperform any of our peers. That's all about product design, and that's all about the things Will talked about.

So, wrapping it up, [indiscernible] (04:29:25) long-term value for shareholders. We continue to believe we were an undervalued asset, an asset that will continue to deliver strong, stable and sustainable financial results. We're going to continue to appropriately balance investment in our businesses and capital return to shareholders. And lastly, we will never forget about risk management. We will never forget about the critical importance it plays in our success.

With that, I think we're going to invite the whole team up here, and hopefully the stage doesn't collapse on us. And we're going to take questions. So thank you.

Dennis R. Glass

President, Chief Executive Officer & Director, Lincoln National Corp.

Am I on? I'm on. Randy that was terrific. Everybody has done a terrific job today, I think the numbers speak for themselves. What I can tell you is that you've been able to see much of our management team, but there's several others here today that support and contribute as much as the people that you've seen today for our long-term success. So, I'd like to mention each one of them my direct reports and have them stand for a second.

I'll start off with Lisa Buckingham, Lisa, If you could stand up please. Lisa Buckingham is both our Head of HR and she is also our Chief Marketing Officer and Communications. She has just been named HR Executive of The Year, which is very prestigious. Congratulations to you.

I got to have a list, because the last time I did this I forgot Randy if you can believe that. Ken Solon, Ken would you stand up please? Ken has been with us for a long time. He runs our [indiscernible] (04:31:30) overall and supports a lot of the things I think you've heard talk about today.

Raj Chakraborty, hard to name to pronounce. He's our Chief Digital Officer and of course you've heard all of the digital activities that we have underway. And then not last or least, so however that goes, Kirkland Hicks, our General Counsel; Kirkland, thank you.

So, tremendously effective management team, very experienced in the life insurance industry. And nothing happens at Lincoln unless each of us do our job successfully, and that's all 9,000 employees, and so I'm happy to introduce at least the addition of my senior management team.

Thank you very much guys and ladies.

Christopher A. Giovanni
Senior Vice President & Head-Investor Relations, Lincoln National Corp.

So we have about 25 minutes for those that are going to stay for the toward the end, they'll be guys in the back, for those that are catching the shuttle back to the train station, we'll try and keep it as close to 2 o'clock as we can. So, let's get started. We'll start in the back here with Suneet.

QUESTION AND ANSWER SECTION

Suneet Kamath
Analyst, Citigroup Global Markets, Inc. (Broker)

Q

Thanks, Chris. Suneet Kamath from Citi. Just on ROE, Dennis or Randy, can you just tell us where you think the ROE is headed? Over the next couple of years, it seems like we've been traveling in the 12% range, maybe a little bit north of that. Do you think we can get to 13% over the next couple of years?

Randal J. Freitag
Executive Vice President, Chief Financial Officer & Head of Individual Life, Lincoln National Corp.

A

Suneet, we don't give guidance, so we can't get specific. I can only point out that we have been improving ROE every time. As I mentioned, we've outperformed the industry. We've increased that again this year. And then the other key point I would make is that the products that we're selling today are very, very profitable returns at or above the ROE that we're getting on the overall book of business, that's in each and every business.

So, when you factor that in, you've got that natural tug up from the addition of new products. We have to overcome the tug down from interest rate headwinds, but we've talked about how we do that with things like the digital initiative. So, we're doing the things we need to do to grow ROE, but once, again, we don't get specific around our own guidance.

Suneet Kamath
Analyst, Citigroup Global Markets, Inc. (Broker)

Q

And then, my follow up was just, I guess, Dennis, in your prepared remarks, you'd made a comment about some trapped capital in the balance sheet that could be available for M&A that you wouldn't use for buyback, and then maybe Randy would get into that and I don't think that he did, maybe I missed it, but could you go into that a little bit of detail?

Randal J. Freitag
Executive Vice President, Chief Financial Officer & Head of Individual Life, Lincoln National Corp.

A

Yes, Suneet. If you look at our statutory capital position, little over $9 billion. I'd estimate that there is somewhere between $500 million and $750 million of capital that we could put to use in the context of M&A, that we could not put to use in the context of share buybacks. Why is that? It's from a rating agency standpoint, when you're buying something, you're buying a stream of cash flows that's much different than sending capital out of the organization. One is seen as at least holding the strength of the company neutral, while the other is, is taking strength out of the organization. And we are a ratings driven industry, ratings are very important to us here at Lincoln. We're AA company. We'd expect to continue to be that.

The other area I'd talk about is the fact that, as I pointed out, we've taken leverage down $300 million over the last five years, to the point where our leverage ratios are well below where I think they need to be. Our coverage ratios have more than doubled over the last five years. So, I do think we have room to add some leverage as part of capital that we would deploy as part of M&A. I would estimate that in the range of $500 million.

So, you've got those two items, $1 billion, $2.25 billion. When you combine with our ability to generate free cash flow, you know, we've been putting a tremendous amount of capital to work each and every quarter, I went over it as part of my discussion. So, when you combine all those elements together, we feel very comfortable in our ability to deal with M&A up to roughly $2 billion.

Christopher A. Giovanni
Senior Vice President & Head-Investor Relations, Lincoln National Corp.

A

Tom and then Eric.

Thomas Gallagher
Analyst, Evercore Group LLC

Q

Tom Gallagher, Evercore. Dennis, just back on the comments you made earlier about the tax reform. You thought it would be, call it roughly neutral overall based on your understanding of it. One of the other parts of the proposal looks like it's going to accelerate cash tax payments for the industry, even if over time it was neutral. Is that a correct interpretation? And is it possible that this is going to be negative from a free cash flow standpoint in terms of near-term?

Dennis R. Glass
President, Chief Executive Officer & Director, Lincoln National Corp.

A

Tom, there's no way to answer that given where we are in the process. The interplay is really between there is a couple of things at work here, one is cash tax payments, and to your point, when do they increase or decrease as a result of whatever comes to pass. So, we're watching that. And the other one is, what does it do to your net income and your effective tax rate. So, we're very – the industry is very focused on those two questions. And again, working to the best of our ability to have a good outcome in the final bill.

Thomas Gallagher
Analyst, Evercore Group LLC

Q

And I guess...

Randal J. Freitag
Executive Vice President, Chief Financial Officer & Head of Individual Life, Lincoln National Corp.

A

But, Tom, and as I talked about just remind you that, I think the direct words I used as part of my presentation, we see 50% to 55% as a reasonable proxy looking forward.

Thomas Gallagher
Analyst, Evercore Group LLC

Q

And Randy, have you even with – I'm sure you've looked at some preliminary estimate based on the range of outcomes that are out there and there's nothing that you'd seen that would cause you to go below 50%, based on -I assume that, that when you're saying 50% to 55%, that assume some [indiscernible] (04:37:55)?

Dennis R. Glass
President, Chief Executive Officer & Director, Lincoln National Corp.

A

Tom, we have to be very carefully here, this stuff is in flight. In my early comments, I said these are impressions that I've gathered from conversations with key players, but that I wanted to keep our comments at a very high level. So, there's just simply no way to – there's no ability for us to dig any deeper than sort of combat the notion that there's someone out there that's trying to do harm to the life insurance industry in general.

And, again, I want to qualify the heck out of this, because it is changing by the hour, not necessarily by the hour for the life insurance industry, but just in the last 48 hours, this has nothing to do with us, but all of a sudden the ACA has got back in the mix. So, no detailed responses to these questions can be made at this time.

Suneet Kamath
Analyst, Citigroup Global Markets, Inc. (Broker)

Q

Fair enough. Thanks.

Christopher A. Giovanni
Senior Vice President & Head-Investor Relations, Lincoln National Corp.

A

Erik.

Erik Bass
Partner, Autonomous Research

Q

It's Erik Bass with Autonomous Research. So, you've highlighted the strong sales growth and across a number of products. I'm just wondering if you could comment sort of on the level of capital deployed for new business this year versus – and kind of the recent trend? And then as you think about the cash generation for 2018, should we expect it to go back to sort of that 50% to 55% range from being sort of 60% to 65% this year?

Randal J. Freitag
Executive Vice President, Chief Financial Officer & Head of Individual Life, Lincoln National Corp.

A

Yeah, Erik, yes, absolutely 50% to 55% is our expectation, what we would tell you to think about as you look forward. In terms of what we invest in new business, the number hasn't changed much. We're investing a little less in the annuity business today, because sales are down, but we expect those sales to grow back. And the Life business has seen its sales grown, even though we've brought the capital intensivity of that business down, I'd estimate that we put about a $1 billion of capital to work behind new business each and every year.

Christopher A. Giovanni
Senior Vice President & Head-Investor Relations, Lincoln National Corp.

A

Front here to Mark and then next to Alex.

Mark Dwelle
Analyst, RBC Capital Markets LLC

Q

Mark Dwelle, RBC Capital Markets. Is there a level of market interest rate that you guys target? And a level which you would think the consumer would then become more energized towards annuity products?

Will H. Fuller
President-Lincoln Financial Group Annuity Solutions, Lincoln Financial Distributors & Lincoln Financial Network, Lincoln National Corp.

A

I guess, I'll take a stab at that. Maybe the best way to take a stab is to say, just with small movements in income payouts, we've seen the marketplace respond. So, in January, when we saw just north of the 20% increase in sales, we introduced a 25 basis point increase in the payout rate. So, I laid it out there to show that I think the marketplace is absolutely paying attention to small impacts. And as we do make these improvements, you are seeing them get the necessary response in sales and demand.

So, I'll make that comment from a demand perspective and Brian I'm sure will have a perspective around sustainability of the annuity business from rates perspective.

Brian Kroll
Senior Vice President, Head of Annuity Solutions, Lincoln National Corp.

A

Yeah. No, I think that's exactly right. And as interest rates come up, it makes it easier for us to improve the customer value proposition, and we have found that relatively small moves have been effective.

Mark Dwelle
Analyst, RBC Capital Markets LLC

Q

But there's not sort of a magic number like 10-year, gets to 3% and you'll see it take off or 3.50% or 4% or whatever?

Brian Kroll
Senior Vice President, Head of Annuity Solutions, Lincoln National Corp.

A

My belief is it'll be incremental on the way up.

Christopher A. Giovanni
Senior Vice President & Head-Investor Relations, Lincoln National Corp.

A

Alex?

Alex Scott
Analyst, Goldman Sachs & Co. LLC

Q

Hi, Alex Scott, Goldman Sachs. I was just interested in hearing your thoughts about the impact of potential changes from the FASB Board's accounting that they're considering. And just if you would change anything about the way you manage the business, and whether it be annuities or life insurance?

Randal J. Freitag
Executive Vice President, Chief Financial Officer & Head of Individual Life, Lincoln National Corp.
A

Yeah, we're following along. We've provided our comments all along the way. I'll give you our view – our company's view on this proposal. We favor some aspects. Think it makes a lot of sense to unlock assumptions on traditional products. We do it on interest sensitive products.

Some of the other changes don't make a lot of sense. For instance, amortizing DAC over a fixed period of time at a level rate. It's nearly the dumbest thing I've ever heard of in my life, if you want to know my exact opinion. I mean, the benefit of coming up with a DAC schedule that my 12-year-old could create, is far swamped by the fact that you would have income statements with less meaning than you have today, that's a pretty bad tradeoff.

So we've argued against some of those things. I think some of the things they talk about from a fair value standpoint, around some of the withdrawal benefits. It's too hard to really understand where exactly they're going to say for sure. I think we will continue to focus our management of these products on the economics of these products, whatever occurs, and we'll continue to be active participants in the discussion that is going on.

Christopher A. Giovanni
Senior Vice President & Head-Investor Relations, Lincoln National Corp.
A

Jimmy and then Humphrey.

Jamminder Singh Bhullar
Analyst, JPMorgan Securities LLC
Q

Hi, Jimmy Bhullar from JPMorgan. Your leverage as you stated has gone down over the last several years. What do you feel is an appropriate level? And I think you implied that you would go up and leverage if there was an M&A opportunity, but would you do it otherwise? And, like, if you don't see – if you don't see an M&A opportunity, would you consider going up a little bit on leverage just provide that to other purposes?

Randal J. Freitag
Executive Vice President, Chief Financial Officer & Head of Individual Life, Lincoln National Corp.
A

You know, Jimmy, we look at things like leverage ratios, coverage ratios, every agency has different metrics. We're below leverage ratio targets by a couple of points, when you think about S&P, which is the agency that focuses on that particular target. And we're above where we need to be when it comes to coverage ratios, which is Moody's key metric there. So, you know, we're better than we need to be, by the book, by the ratings book, and that's why as I talked about, I think we have a little bit of capacity, should it come to us, having the need to use them, leverage as part of something like M&A.

Christopher A. Giovanni
Senior Vice President & Head-Investor Relations, Lincoln National Corp.
A

Humphrey?

Humphrey Hung Fai Lee
Analyst, Dowling & Partners Securities LLC
Q

Humphrey Lee from Dowling & Partners. Just a couple of housekeeping questions for Randy. I understand you mentioned that you don't want to provide guidance on ROE, but I think in the past, you talked about on a normal business environment, you can expect kind of 20 to 30 basis point of ROE improvement over time per year. Is that still the right way to think about that?

Randal J. Freitag
Executive Vice President, Chief Financial Officer & Head of Individual Life, Lincoln National Corp.

A

I don't remember ever saying that, Humphrey. I think you're putting words in my mouth. All I have ever said is exactly what I said. We're earning. We have to earn our ROE every time and we continue to sell business with a strong return profile that should hopefully tug that up over time. And we have some headwinds that we need to overcome and we're doing that with actions, like the digital initiatives. That's probably the exact same answer I just gave about five minutes ago. But that's all I've ever said, Humphrey, and that's I think all you'll get me to say.

Humphrey Hung Fai Lee
Analyst, Dowling & Partners Securities LLC

Q

And then on the SGUL subtest, I think in the past you show if rates were to be 50 basis points, then it will be $700 million of impacts, is that still applicable?

Randal J. Freitag
Executive Vice President, Chief Financial Officer & Head of Individual Life, Lincoln National Corp.

A

Yeah. Humphrey, all that we show you today is, if they are 1%, I mean I don't have a reason to think they've changed substantially, but what we've showed is the 10-year at 1%. Are you really that skeptical about the world or are you thinking that 10-year, it's going to be 50 basis points up, where are you Humphrey?

Humphrey Hung Fai Lee
Analyst, Dowling & Partners Securities LLC

Q

No, I just wanted...

Randal J. Freitag
Executive Vice President, Chief Financial Officer & Head of Individual Life, Lincoln National Corp.

A

You and me, you need to get optimistic.

Humphrey Hung Fai Lee
Analyst, Dowling & Partners Securities LLC

Q

No, just want to hear that from your mouth.

Randal J. Freitag
Executive Vice President, Chief Financial Officer & Head of Individual Life, Lincoln National Corp.

A

You got that, to be in the pessimism, I talked about it.

Humphrey Hung Fai Lee
Analyst, Dowling & Partners Securities LLC

Q

Just want to give you an opportunity to clear the message?

Randal J. Freitag
Executive Vice President, Chief Financial Officer & Head of Individual Life, Lincoln National Corp.

A

Thanks, Humphrey.

Christopher A. Giovanni
Senior Vice President & Head-Investor Relations, Lincoln National Corp.

Q

Any further questions?

Christopher A. Giovanni

Senior Vice President & Head-Investor Relations, Lincoln National Corp.

Okay. All right. Well, we truly appreciate you guys making the trip down to Philadelphia. Hopefully, you got a lot out of it and I look forward to touching base with you guys at the end of the year. Thanks.