CORPORATE PARTICIPANTS

Albert S. Copersino  
Vice President & Head-Investor Relations, Lincoln National Corp.

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

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

OTHER PARTICIPANTS

Andrew Kligerman  
Analyst, Credit Suisse Securities (USA) LLC

Thomas Gallagher  
Analyst, Evercore ISI

Erik Bass  
Analyst, Autonomous Research LLP

Suneet Kamath  
Analyst, Citigroup Global Markets, Inc.

Jimmy S. Bhullar  
Analyst, JPMorgan Securities LLC

MANAGEMENT DISCUSSION SECTION

Operator: Good morning and thank you for joining Lincoln Financial Group's Fourth Quarter 2020 Earnings Conference Call. At this time, all lines are in a listen-only mode. Later, we will announce the opportunity for questions and instructions will be given at that time. [Operator Instructions]

I would now like to turn the conference over to the Vice President of Investor Relations Al Copersino. Please go ahead, sir.

Albert S. Copersino  
Vice President & Head-Investor Relations, Lincoln National Corp.

Thank you, Catherine. Good morning and welcome to Lincoln Financial's fourth quarter earnings call. Before we begin, I have an important reminder. Any comments made during the call regarding future expectations, deposits, expenses, income from operations, share repurchases, and liquidity and capital resources are forward-looking statements under the Private Securities Litigation Reform Act of 1995. These forward-looking statements involve risks and uncertainties that could cause actual results to differ materially from current expectations.

These risks and uncertainties include those described in the cautionary statement disclosures in our earnings release issued yesterday, as well as those detailed in our 2019 Annual Report on Form 10-K, most recent quarterly reports on Form 10-Q, and from time to time, in our other filings with the SEC. These forward-looking statements are made only as of today. And we undertake no obligation to update or revise any of them, to reflect events or circumstances that occur after this date.

We appreciate your participation today and invite you to visit Lincoln's website, www.lincolnfinancial.com, where you can find our press release and statistical supplement, which include full reconciliations to the non-GAAP
measures used on this call, including adjusted return on equity and adjusted income from operations, or adjusted operating income to the most comparable GAAP measures.

Presenting on today's call are Dennis Glass, President and Chief Executive Officer; and Randy Freitag, Chief Financial Officer and Head of Individual Life. After their prepared remarks, we will move to the question-and-answer portion of the call.

I would now like to turn the call over to Dennis.

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

Thank you, Al. Good morning everyone. During 2020, Lincoln responded well to the immediate health, economic, and capital market challenges. We also took steps to add new products, and build distribution, improve cost effectiveness, and strengthen the balance sheet.

Fourth quarter earnings were affected by elevated pandemic-related claims in our life and group businesses, which was partially offset by another quarter of strong returns from our alternative investment portfolio.

Given this year's circumstances, we saw quite a bit of variability in earnings. When normalizing for several items in 2020, the largest of which where charges from our third quarter annual review and pandemic-related claims, we view our EPS for the year at approximately $9.30, and ROE, excluding AOCI, at 13%. Based on our current views, we are poised to deliver 8% to 10% EPS growth off this level over the long-term.

Focus items during the year included three initiatives: one, executing our reprice shift and add new product strategy; two, achieving expense savings while improving the customer experience; and, three, maintaining a strong balance sheet and maximizing our financial flexibility.

Let me touch on each of these. First, with our reprice shift and add new product strategy, our aggressive and disciplined repricing actions targeted achieving appropriate returns on capital. As we exited the fourth quarter, we generated at least a 12% return on new business in our current portfolio based on the forward curve across all our businesses.

As expected, sales decreased in most businesses with growth expected to re-emerge over the course of the year based on the shift and add new components of our strategy. Also, several competitors followed our repricing actions, making our repriced products more competitive as we enter 2021.

We are introducing eight new products during the first half of this year that will increase consumer choice and expand our customer value propositions. These actions will further strengthen our product portfolio, enable us to participate in more market segments, and increase sales opportunities. Combining our product breadth and distribution capabilities is part of our historic playbook that we will continue to execute on to drive top line growth.

Second, on our efforts to increase efficiency while improving the customer experience. Expense management is a key priority. We are focused on actions that will further increase productivity across our manufacturing and distribution organizations and also enhance the customer and partner experience.

Accelerated implementation and acceptance of digital tools is part of the reason we see the potential for further expense savings opportunities. As an example, during the fourth quarter, 99% of life policies were delivered electronically, nearly triple the prior year quarter.
Successes like this, combined with our overall expense management capability, are enabling us to start another meaningful expense savings program. We'll update you later this year as the project plan is finalized and we size the opportunities.

Third, on the balance sheet. We have successfully focused on protecting and further improving the balance sheet. Our RBC ratio and cash at the holding company have increased and remain above our targets. We also increased our financial flexibility through capital actions, including adding contingent capital and extending debt maturities out until September 2023.

The investment portfolio has benefited from derisking actions and various government support programs. As a result, credit losses and downgrades have been less than expectations at the onset of the pandemic.

Looking forward, capital generation will face some near-term headwinds from elevated COVID-related claims. However, given our strong balance sheet and overall free cash flow generation, we remain in the market repurchasing our shares during the first quarter. Additionally, we have put more energy and resources into potential risk transfer deals with a goal of enhancing capital deployment.

Lastly, before shifting to segment results, it is important to note that since our last conference call in early November, we have seen a number of favorable developments, including the rollout of COVID-19 vaccinations, further gains in the equity markets and an increase in interest rates, and continuing economic stimulus. All of these bode well for Lincoln over time.

As I just noted, our underlying earnings are firmly intact, and we are positioned for growth as COVID impacts diminish. Many medical experts forecast that COVID-19 deaths will peak in the first quarter and recede over the course of the year. When mortality claims ultimately return to normal levels, we see earnings momentum building in the second half of this year and into 2022.

Now, turning to the business segments. Starting with Annuities, where we successfully leveraged our unique manufacturing and distribution capabilities. We expanded our shelf space, and the number of producers selling Lincoln's indexed variable annuity products doubled in 2020, which helped cement our leadership position in the IVA marketplace, which is the fastest-growing segment of the annuity market.

In total, IVA sales were $5 billion for the year. Asset protection products like IVA are resonating with consumers and producers. This is contributing to our sales shifts toward variable annuities without living benefits. These sales represented more than two-thirds of total VA sales in 2020. Based on our in-force, VAs without living benefits and other non-guaranteed products represent 47% and of total annuity account values.

Growth in asset protection sales, combined with continued market demand for guaranteed living benefits led to positive annual variable annuity net flows for the first time since 2015. As expected, total annuity sales were down as we de-emphasized fixed annuity sales due to return challenges in the current environment. In 2021, we expect continued benefit from our high quality in-force book of business that generates consistent capital and strong returns.

We project sales begin the year consistent with the $2.5 billion run rate we have produced in recent quarters and build over the course of the year as we benefit from our 2020 product introductions as well as products we plan to add this year. Our new products create additional consumer value propositions and expand on our already broad product portfolio.
In Retirement Plan Services, our digitally focused model, where high-tech enables high-touch, continues to differentiate us in a virtual environment. While economic and pandemic-related uncertainty weighed on most businesses this year, strong performance from our sales and retention teams drove a 6% increase in total deposits, including growth in both first year sales and recurring deposits, along with our sixth consecutive year of positive net flows.

Notably, some of the headwinds we have seen from employers reducing or eliminating matching contributions and workforce reductions have receded, with recurring deposits up slightly year-over-year in the fourth quarter compared to a decline in the third quarter. Overall, it was a strong quarter and year for the retirement business, and we expect momentum to continue as we are well-positioned to compete in our target markets.

Near-term, we see further opportunities with YourPath, our alternative to target-date funds, and longer term we see significant potential from key provisions in the SECURE Act that facilitate providing protected income solutions to working Americans and multiple employer programs that address access to worksite retirement plans.

Within the Life Insurance business, our focus in 2020 was on repricing and product innovation, with an eye on introducing new solutions during the first half of 2021. Given repricing actions, combined with record sales in the prior year quarter, sales declined year-over-year, and we expect sales to remain at similar levels until our new products are introduced. These new products offer consumers more choice and alternative value propositions, positioning us for long-term sales growth at attractive returns.

While we continue offering guaranteed solutions, our product portfolio expansion leverages separate accounts as the investment engine, providing non-guaranteed upside benefit potential for our consumers. Examples of these new products include our MoneyGuard and VUL solutions. As always, we will couple this expanded product portfolio with the strongest distribution platform in the industry, positioning us well in 2021 and beyond.

Lastly, on Group Protection, sales in our seasonally strongest quarter increased over the prior year period due to timing of when cases closed. While for the full year, sales declined 6% as gains in disability were more than offset by decreases in life and dental.

Strong persistency of 87%, up 350 basis points in 2020, more than offset the lower sales, which led to a 4% increase in premiums for the full year. Importantly, the contraction in premiums we experienced at the onset of the pandemic is stabilizing and quote activity has resumed, both of which are positive for premium growth.

Even adjusting for the pandemic, margins were below target. We are taking action. And based on focused pricing enhancements we began in 2020 along with expense initiatives, we expect continuous margin improvement over time, building towards our 7% target.

Briefly on investment results. As I mentioned earlier, our investment portfolio has performed well through this volatile period for capital markets, highlighting sound portfolio construction and the high-quality nature of our portfolio. We manage credit risk defensively with proactive derisking, as well as adjusting our new money allocation to higher-rated assets that match our liabilities at attractive yields.

As a result of these actions, the credit quality of the portfolio is in line with pre-pandemic levels. Additionally, the alternatives investment portfolio performed well in the quarter and for the full year generated an 11% annual return, slightly above our long-term target.
In closing, I am very pleased with how Lincoln responded to this year’s unique challenges, including product outcomes that further differentiate us in the marketplace. Importantly, I want to recognize our employees for their extraordinary efforts and unwavering commitment last year.

We entered 2021 well positioned and a stronger franchise. Sales momentum should build over the course of the year at attractive returns as we benefit from new product introductions. Our digital tools and capabilities have never been stronger, which will enable us to further enhance the customer experience and improve productivity.

We have a durable balance sheet with a high-quality investment portfolio and strong free cash flow generation and capital ratios. The underlying earnings power of our businesses are intact. And as I said earlier, we are poised to deliver 8% to 10% growth over the long term even in the current low interest rate environment. As a result, I am optimistic about our ability to drive shareholder value.

I will now turn the call over to Randy.

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

Thank you, Dennis. Last night, we reported fourth quarter adjusted operating income of $346 million or $1.78 per share. There were no notable items within the current or prior year quarter. However, this quarter's result was impacted by a number of items.

First, pandemic-related claims reduced earnings by approximately $187 million or $0.96 per share. This included a $174-million mortality impact and $13 million from disability claims. Second, results benefited from strong performance in the alternatives investment portfolio relative to our targeted annual return of 10%, boosting earnings by $73 million or $0.38 per share.

Third, there was unfavorable expense variability of $28 million or $0.13 per share in the Other Operations segment, related mostly to elevated deferred compensation costs resulting from the increase in Lincoln share price last quarter. Finally, there was $20 million or $0.10 per share of favorable amortization levels in Life Insurance, which was largely offset by seasonal unfavorability in Group Protection.

Net income totaled $143 million or $0.74 per share as improvements in credit spreads drove a $240-million loss in variable annuity non-performance risk. Outside of this non-economic item, credit experience was excellent. And the variable annuity hedge program performed exceptionally well with 100% effectiveness in the quarter.

Moving to the performance of key financial metrics compared to the prior year quarter. Adjusted operating revenue increased 3%, with operating revenue growth in each of our four business segments. Average account values increased 9%.

Total G&A expenses, net of amounts capitalized, decreased 1% or 7% when excluding unfavorable expense variability in Other Operations. The 1% decline combined with operating revenue growth led to 60-basis point improvement in the expense ratio. And book value per share, excluding AOCI, stands at $71.59, an all-time high.

Now turning to segment results, starting with Annuities. Operating income for the quarter was $289 million compared to $269 million in the prior year quarter. The increase was primarily due to higher account values, driven by growth in the equity markets. Average account values of $151 billion increased 9% year-over-year and 5% on a sequential basis. Additionally, end-of-period account values exceeded average values by 4%, providing a tailwind into the first quarter.
Base spreads, excluding variable investment income, were up 8 basis points from the year ago quarter, driven by active management of crediting rates and some quarterly noise. G&A expenses, net of amounts capitalized, increased 5% for the full year and quarter, leading to a 60-basis point improvement in the expense ratio for the quarter. G&A expenses rose sequentially due to typical fourth quarter seasonality.

Return metrics remained healthy in the quarter, with return on assets coming in at 77 basis points and return on equity at 21.4%. Risk metrics on the VA book continue to demonstrate the quality of the business as the net amount at risk fell to 70 basis points of account value for living benefits and to 34 basis points for death benefits.

Continuing a theme that has been in place for well over a decade, 2020 was another excellent year for the Annuities business. Earnings grew in line with account values. And excluding the unlocking, return on equity was very strong, coming in at 21%. Looking into 2021, we expect more of the same.

Retirement Plan Services reported operating income of $49 million compared to $47 million in the prior year quarter as favorable alternative investment performance, expense management and higher average account values more than offset spread compression.

Positive flows combined with favorable equity markets drove average account values up 10% over the prior year quarter. G&A expenses, net of amounts capitalized, were flat compared to the prior year quarter and down 5% for the full year, driving a 140-basis point improvement in the expense ratio in 2020.

Base spreads, excluding variable investment income, compressed 28 basis points versus the prior year quarter. Spread compression was above normal, primarily due to lower yields on floating rate securities where the crediting rate on the matched liability adjusts less quickly. We expect this to moderate and return to our more typical 10-basis point to 15-basis point range in 2021.

The retirement business ended the year with strong results, including a 23-basis point ROA in the quarter, with momentum in sales and expense management serving as positive drivers going forward.

Turning to Life Insurance. We reported operating income of $144 million compared to $179 million in the prior year quarter. This quarter's results included $113 million of pandemic-related mortality, partly offset by $53 million of favorable alternative investment experience and the favorable amortization I noted upfront.

Underlying earnings drivers continue to show growth, with average account values up 6% and average life insurance in-force up 9% over the prior year. For the full year, outside of the pandemic, mortality was in line with our annual expectations.

G&A expenses, net of amounts capitalized, decreased 13% from the prior year quarter, leading to a 140-basis point improvement in the expense ratio. Base spreads declined 25 basis points compared to the prior year quarter due to a previously noted noneconomic change in our crediting rate methodology. We expect base spreads to return to our more typical 5-basis point to 10-basis point rate of decline in 2021.

Looking forward to the first quarter, we continue to expect headwinds from the pandemic. Over in the coming months, the worst should be behind us and key Life Insurance earnings growth drivers remain strong.

Group Protection reported a loss from operations of $42 million compared to operating earnings of $54 million in the prior year quarter, with the decrease driven mainly by pandemic-related claims.
Group earnings were impacted by a number of items during the quarter, including $74 million of claims related to the pandemic, $15 million to $20 million of seasonally higher fourth quarter disability claims and expenses, and a slowdown in social security approvals that negatively impacted results by $8 million, partly offset by $5 million of favorable alternative investment experience.

The reported total loss ratio was 87.8% in the quarter, up 4.6 points sequentially. This was driven in part by an increase in pandemic-related mortality and hospitalizations, which resulted in elevated claims including $39 million of direct COVID-19 mortality, $13 million of direct COVID-19 disability, and $22 million of excess mortality.

Excluding pandemic-related claims from both periods, the total loss ratio was 78.9%, up 3 percentage points sequentially as improvement in group life and dental were more than offset by an increase in the disability loss ratio. The sequential increase in the disability loss ratio was driven by typical fourth quarter seasonality as well as the previously mentioned slowdown in social security approvals.

G&A expenses, net of amounts capitalized, decreased 6% from the prior year quarter and 5% for the full year. Excluding the pandemic and other items I mentioned, the earnings of the business were below our expectations. However, as Dennis mentioned, we are confident that the actions we have been taking will over time get us to our targeted margin.

Turning to capital and capital management, we ended the year with $10.3 billion of statutory surplus and an RBC ratio of 452%, which includes 23 percentage points from our non-economic goodwill associated with the Liberty acquisition that we expect will go away at the end of 2021.

Cash at the holding company stands at $754 million, above our $450 million target as we have pre-funded our $300 million 2022 debt maturity. Additionally, we added a $500 million contingent capital facility earlier this year. This combination of strong life company capitalization, cash at the holding company, pre-funding of debt maturities until 2023, and new sources of contingent capital puts us in a stronger, more diversified position than we were a year ago.

We resumed buybacks in the fourth quarter and deployed $50 million towards share repurchases. As a result of our confidence in our capital position, we plan to increase our buyback to $100 million in the first quarter. And we’ll provide additional updates on our next earnings conference call.

To conclude, this year’s result included a large impact from COVID-19, and we continue to expect headwinds from the pandemic in the near term. Looking past that, we see strong underlying earnings and solid drivers of EPS growth, including record end-of-period account values, a strong record of expense discipline across the company, the ability to grow sales looking forward, pandemic-related headwinds that we believe will decline over 2021, and a robust capital position, providing us an ability to increase the pace of capital deployment. And as a result, we reiterate our plan to grow EPS at an 8% to 10% rate over the long term.

With that, let me turn the call back over to Al.
QUESTION AND ANSWER SECTION

Albert S. Copersino
Vice President & Head-Investor Relations, Lincoln National Corp.

Thank you, Dennis and Randy. We will now begin the question-and-answer portion of the call. As a reminder, we ask that you please limit yourself to one question and one follow-up, and then re-queue if you have additional questions. With that, let me turn the call over to Catherine to begin Q&A.

Operator: Thank you. [Operator Instructions] Our first question comes from Andrew Kligerman with Credit Suisse. Your line is open.

Andrew Kligerman
Analyst, Credit Suisse Securities (USA) LLC

Hey. Good morning, everyone. I wanted to focus on the individual life segment. And starting off with sales in the quarter, and I understand you repriced many of your life products. But interest rates really aren’t a big factor with term life. And per our producer survey, there was an expectation in the fourth quarter for mid-single digit sales growth, whereas your term sales were off 17%. So, I’m wondering, did you reprice the term product and why might you think it kind of dropped off in sales?

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

Andrew, this is Randy. Well, thanks for the question. Andrew, I’m going to get to that question, but Al, let me know this morning that there were a number of questions concerning a report that you recently republished on Lincoln. And so let me take this opportunity though, hopefully, clear up some of the confusion that I think has been created by that report. So, let me make just a few points on that before I get to your sales – your term sales specific question.

Andrew Kligerman
Analyst, Credit Suisse Securities (USA) LLC

He just told you about it this morning. Wow, it's been a long time.

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

...created – that has been created by that report. So, let me make just a few points on that before I get to your sales – your term sales specific question.

Andrew Kligerman
Analyst, Credit Suisse Securities (USA) LLC

Sure.

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

First, just a belief that we face a sizable charge in our life business as we’ve only taken $500 million of charges since 2011, and the report represents that this is too small a portion of our reserves versus charges that our peers have taken. Unfortunately, from my standpoint, I must correct the estimate of prior charges by noting that we’ve
actually taken charges of nearly $1 billion since 2011 including charges for mortality, which you can find in our SEC filings.

Those mortality charges have been focused on resolving many of the industry issues that are referenced. And the end result is that as we sit here today, we have mortality assumptions covering our business that are aligned with our credible experience and reflect the latest industry data on future mortality expectations.

So, in short, I'd say we're very comfortable with all our assumptions, including those pertaining to mortality. I think that additionally I'd just say because I've seen this news try to be used in other areas. Using peers as the sole data point in deriving expectations for Lincoln is really a blunt estimate approach. I think that really ignores the fact that every year our assumptions are trued up for experience and go through a significant amount of internal and external audit review. So that's the first, I think, confusion that I want to clear up.

The second thing is really just broadly on the adequacy of reserves. As it pertains to the GAAP, just to remind everybody, 95% of our life reserves are governed by FAS 97. And they've been reviewed and updated every single year. When you turn to the small amount of business that we have that is governed by FAS 60, we review those – sufficiency of those reserves every year. And without getting into specifics, I'll note that there's a significant amount of sufficiency.

When you turn the lens to statutory reserves, our cash flow testing results indicate an overall sufficiency of $14 billion at the end of 2019. And additionally, [indiscernible] (00:35:21) with rates having increased somewhat, but I note that we now expect little to no impact from cash flow testing subtests at the end of 2021. So, that's the second item I wanted to clear up some confusion on.

The third is on this discussion around the potential for large price increases on reinsurance and/or recaptures. We've discussed this extensively. I think we've discussed this more than any other company out there, actually. And in fact, we noted at our 2019 Investor Day that this issue is part of a $250 million annual headwind that was embedded in our earnings.

As we sit here today, we've reached resolutions covering 70% of our ceded face amounts. And I note that an additional 20% represents recent reinsurance treaties that are meeting all parties' expectations for that remaining 10%. For that remaining small 10%, we've accounted for likely outcomes as part of our assumption setting process. So, I really think we're in pretty good shape there.

The fourth item really digs into one of the reinsurers specifically, so it relates to Scottish Re. It's – that 3%, it's a small piece of our YRT reinsurance. It's included in that 10% that I noted as remaining. And I'd also point out that we did take charges on both GAAP and STAT in 2020 to account for likely outcomes that might come from Scottish.

So on this – and I know it wasn't a specific question you asked, but I really think there were some confusion that I wanted to clear up. So, just let me wrap-up by saying that these represent the facts from Lincoln, facts that we've really talked about over the years, and we'll gladly discuss any of these issues further at any one of the many meetings that we do with investors and analysts over the course of the year. So with that, hopefully, that clears up that confusion that I believe was put into the marketplace.

So let me get around to your question on life sales broadly and terms specifically. I think the term market itself is one where it's a price-sensitive market. So a little movements here, a little movements there by companies will
push sales up and down. I think broadly speaking in terms, we have continued to increase our position in that marketplace.

Our share of the term market has continued to grow, I think, driven by our digitally focused ability to both issue and deliver policies, our automated underwriting capabilities, especially for policies under $1 million. So, I think we're very happy with where we're positioned. We did make some small pricing tweaks here in the first quarter that I think will have a favorable impact.

Broadly on life sales, what you saw in the fourth quarter was what we believe is a trough. I think we, at Lincoln, believe that when it came to repricing products that really needed to be repriced, given the environment, specifically low rates, we think we moved first on MoneyGuard. We moved first on other products. And I think that negatively impacted our level of sales. I do think that others followed. And so you saw a little bit of fire sale going on at some of our peers in the fourth quarter, and that probably negatively impacted our level of sales a little bit.

I think the real key to life and what we're really excited about is the work we did over 2020 to create whole new value props, especially in the MoneyGuard space and in the variable space. Those products we'd be rolling out here in the fourth quarter – in the first quarter, excuse me, of 2021, we'd expect sales of those products to – as usual, things start a little slow, but we'd expect them to ramp up over the course of the year.

But I think those are products that really speak to the environment, right? You're using the separate accounts as the driver of value. You're shifting some risk to the consumer when doing that and away from Lincoln, and you're shifting products away from products that are negatively impacted by interest rates. So, Andrew, that's what I broadly say about life sales and specifically about term.

Andrew Kligerman
Analyst, Credit Suisse Securities (USA) LLC

Okay. And then I guess just for my follow-up question, I think I'll just reframe from it because we're absolutely, there's no confusion on our part with this. Number one, the term insurance under FAS 60 does get marked. So that could be – does not get marked. So that could be a real issue.

Number two, with regard to the assumption reviews, it absolutely came out to $500 million. There could have been other stuff. And then thirdly, in terms of looking over a 10-year period and saying don't look at your comps and you didn't mention the statutory numbers over 10 years, which was widely different from you versus all of your peers. I mean, the earnings were just outsized. So, I think over a 10-year period, given that we don't have the data, this blunt indication is quite a jump out given Lincoln's exposure.

And then thirdly, you mentioned that you recaptured most of the business. And the points of our research were that the companies that did recapture were anti selected against because the reinsurers had outsized information and ultimately recapturing the business and not leaving it with the reinsurers over the long-haul should be problematic.

With regard to Scottish, I get that it's small relative to everything else. But over $12 million in force on an absolute basis reinsured with a company that's in rehab and could experience severe problems, that's a lot of money on a stand-alone basis. So, I'll just leave it at that, but there's absolutely no confusion on our end. And I appreciate your feedback.
Andrew, let me say just a couple of thoughts. One, I own these financial statements. I can add, and you can add up to $500 million – I'm telling you, factually, it's $1 billion. So, I own the financial statements. I looked at the numbers, it's $1 billion. So, you can continue to say its $500 million, but just let me say, you're wrong, period, end of story on that topic.

Once again, on this whole concept of FAS 60, it's 5% of our reserves. Significant amount of sufficiency in reserves. We really don't expect any issue when it comes to LDTI around that small component of our business once again.

So I'm just going beg to differ. In terms of the STAT earnings concept, I mean, if you look at our STAT earnings over those years, and by the way, my numbers are a little different than yours. It's not materially different. They represent just a fraction of GAAP reserves, which is what you would expect, right? It's roughly 40% to 50% of GAAP reserve. That's what you would expect – our GAAP earnings, excuse me. It's what you'd expect that there is strain in issuing business, and we're one of the leading writers of life insurance.

So the results, to me, look right in line with what I would expect on Scottish. I noted at the end, we did put up impacts in our financial statements in 2020 for potential impacts from anything that happens there. So yes, I hope that answers.

Andrew, you are – as with any analyst, you are – it's your job to go and assess companies and you're open to come up with any opinion you want. I'm just trying to correct some of the confusion created by some points in there that I just don't think are correct, and I tried to give the facts from Lincoln's side. So I appreciate your thoughts, and thanks, Andrew.

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Andrew Kligerman  
Analyst, Credit Suisse Securities (USA) LLC

No, I appreciate it on my end as well. I mean, again, term life is $600 billion, $700 billion in-force. It's a lot of money. We'll see how it plays out, but I appreciate the feedback.

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

It's interesting on this whole concept of post-level term. I'm not really sure who your experts are. Let me tell you, we work with every leading reinsurer in America, and there's a huge amount of really interesting research done by some of the biggest reinsurers around what's called post-level term optimization. So, yeah, I'm not sure who your industry expert is, but you might want to ask them those questions because there's a lot of very interesting research around optimizing post-level term results. Well, thank you.

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Andrew Kligerman  
Analyst, Credit Suisse Securities (USA) LLC

We did and there were multiple concerns.

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

Thanks, Andrew.

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Operator: Thank you. Our next question comes from Tom Gallagher with Evercore. Your line is open.
Thomas Gallagher  
Analyst, Evercore ISI

Thanks. That's a tough question to follow, so I'll - mine will probably be a little more benign. So Dennis, I'd like to just follow-up on what you're thinking on risk transfer? Are you thinking just from a product standpoint more likely on fixed annuities, life insurance or variable annuities based on the work you've done so far? And based on kind of the work you've done so far, are you anticipating a sizable transaction or something more modest?

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

Tom, thanks for the question. Let me start by saying that just when I look at the market for risk transfer, it's pretty active. And it's active across a couple of spectrums. And not only is it active, but more capital is coming into the industry from players that haven't been in the industry before. So overall, it's a pretty active market.

In terms of kind of activity, it includes block transactions, Lincoln has done one as you know. It includes strategic transactions that have been going on, asset management companies, and there's been some flow transactions. And again, as you know, we have done those in the past both on our fixed annuity portfolio and our variable annuity portfolio. So, active market, Lincoln has participated in all dimensions of it over the past, and we'll keep looking at each of those components.

In terms of sizing, I think we'll have to wait and see on that. It sort of hard to - what's big and what's small. But we'll be looking at meaningful transactions, I guess, is the way I would respond to it. So, I'm quite encouraged that there will be opportunities at the time we've transacted in the past for Lincoln.

Thomas Gallagher  
Analyst, Evercore ISI

Okay. That's helpful, Dennis. The - just my follow-up question is, I know historically, Randy, you've converted GAAP to distributable free cash flow in the 50% to 55% level, I think. Given the product mix shift that Lincoln has gone through, and then - and I know now you're talking about some recovery in those sales, what kind - when we get to the other side of the pandemic, what kind of conversion do you think we're looking at? Are we likely to be back in that 55-ish range? Or do you expect it to be lower or higher?

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

Hey Tom, thanks for the question. I'm not going to update the range right now, but let me make a couple of points that hopefully help. If you look at the pricing actions that we've taken and the impacts that's had on, the capital we allocate to new business. If you think about sort of the mix of sales that we have today being a little less capital intensive, I think it's fair to say that the amount of capital that we allocate to new business is lower today than it was a couple of years ago. So I think, over time, that will definitely be a benefit.

Now, I think you have to look through 2021 here because I think the pandemic is going to be providing some negative impacts to distributable earnings for at least the first half of the year. But, yeah, I think over time when you think about how we're allocating capital, we're allocating less to new business. And I think that could have some positive benefits on distributable earnings over time. And we'll try to give more guidance later. Thanks, Tom.

Thomas Gallagher  
Analyst, Evercore ISI

Okay. Thanks.
Operator: Thank you. Our next question comes from Erik Bass with Autonomous Research. Your line is open.

Erik Bass

Analyst, Autonomous Research LLP

Hi. Thank you. Wanted to focus on the group business. And you noted that, I think even ex-COVID, group results were a bit below your expectations this quarter. So, I was hoping you could talk about where you're seeing the biggest variances. I think you also mentioned some planned actions to improve margins. So, hoping you could go into some more detail there.

Randal J. Freitag

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

Yeah, Erik. It's Randy. So if you look at the quarter, let's start with the quarter. We reported a loss of $42 million. And if you listen to my script, I spiked out items that totaled low-90s to mid-90s. If you sort of added that in, you'd be sort of at a normalized number of $50 million to $55 million in that 5% to 5.5% range, which if you look back to last year is kind of where we were last year. We exited 2019 in that 5% to 5.5% range.

What I think that the pandemic did was really sort of right shifted what is our belief, which is that when you start at the 5% to 5.5% level, we have clear vision on growing that to 7% over a planning cycle. And it's really driven by four big elements, really executing on fous things. It's pricing, it's expenses, it's claims management, and it's underwriting.

So we, inside of Lincoln, have a clear vision from going where we are today sort of in that 5.5% range towards that – to 7%, which is our ultimate target, as Dennis mentioned. And then I think COVID sort of caused it to be right shifted one year from where we were last year. So, that's how we think about the group business as we sit here today, Erik.

Erik Bass

Analyst, Autonomous Research LLP

Thank you. And then maybe just if you could go into a little bit more detail on the drivers of the increase in the group disability loss ratio and I think you mentioned some higher STD claims, some seasonality, as well as some social security impacts. So maybe if you could just dig into that a little bit more, please.

Randal J. Freitag

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

If you think about the quarter, we reported a disability loss ratio of 86.2%. And I spiked out two items specifically, COVID and social security slowdowns – social security approval slowdowns. If you add those two items together, that's roughly 4.5%.

And then when you think about the seasonality which we typically see in the fourth quarter, we saw this year in the fourth quarter, we saw last year in the fourth quarter, if you factor that in I think you'd get down to a range of 78.5% to 79%, and that compares to roughly 77.5% to 78% in the third quarter when you adjust for COVID.

So, I think we're a little above where we were. But underneath the noise that's being driven by COVID, social security approvals, et cetera, and then the seasonality, I think we're just a little worse than what our target would be. And I think that's really driven by one big factor, which is that we did lower our discount rate in the LTD business this year. That's had a little bit of a negative impact.
Now, the good point there is that we had clear insight early in the year that that was something we were going to do and so we’ve been putting it into price all year, all the bids we’ve put out, and all the – the nature of the group is a lot of those cases will hit on January 1, so I feel good that the price to cover that discount rate decrease is coming in the first quarter, which hopefully can put us back into the more normal range outside of any negative impacts that we might see from COVID.

Erik Bass  
*Analyst, Autonomous Research LLP*

Got it. Thank you. That's helpful.

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

Yes.

Operator: Thank you. Our next question comes from Suneet Kamath with Citi. Your line is open.

Suneet Kamath  
*Analyst, Citigroup Global Markets, Inc.*

Thanks. Good morning. I just want to circle back to the 8% to 10% long-term EPS growth you guys are talking about. I think, back in 2019, when you had your Investor Day, you talked about a 4 to 5-point impact, positive impact from, I guess, net new business. I know there's a lot in motion now with new products, but would it be fair to think about sort of 2021 as a transition year and then as you get into 2022 that you could get back to something like that 4 to 5 points from net new business?

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

Suneet, it's Dennis. The 8% to 10% growth sort of traditionally, as you point out, has 4% coming from sort of the new business versus the runoff of business, some amount of margin improvement. So, I think we get up to 5% from management actions, and we net out capital market, growth in equity markets offset by spread compression, 1 to 2 points, and then share buybacks. And all that adds up to 8% to 10%.

And so, over the long-term, that's our expectations. I think, in the near term, and we've demonstrated our success in accomplishing that, some of those bars are higher. Some of them are lower because of circumstances. So I think as we rebuild sales at 4%, for a little bit of time will be a little bit lower, but the expense saving bar and the margin improvement bar is going to be higher. So each of the bars can change given the circumstances that we find ourselves in, macroeconomic conditions, pandemics and so forth, but management, driving toward that 8% to 10%.

And to repeat what Randy and I have both said, we can see ourselves getting to that up to the $9.30. And again, how we get there might be a little bit different over the next 6 to 18 months, but we can get there.

Suneet Kamath  
*Analyst, Citigroup Global Markets, Inc.*

Got it. And then sort of related to the same chart, I think when you guys talked about expense reduction in the past you were looking to offset, I guess, the spread compression or at least that was one way to think about it. I
would imagine the spread compression impact today is probably worse than what it has been or what it was in 2019. Is that the goal of this new plan to try to offset that spread compression as we think about getting more information, I guess, maybe in 1Q?

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

Hey, Suneet. Randy. Yeah, I think when you think about spread compression, a while back we talked about a 2% to 3% range and we were at the low end of that sort of coming out of 2019. And then as rates dipped significantly the beginning of this year, we talked about how we might have moved a little above that.

I think where we sit today and as we look out over our planning horizon. I think we see it in that 2% to 3% range, probably in the upper half of that 2% to 3% range. Put I think we're back inside of that range, albeit a little higher than we were back in 2019.

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

Hello, Suneet. It's management's job when there's pressure – like there is from this sort of continuing spread compression but at a lower amount. It's our job to replace those earnings. And so, that's very much in our mind as we get into this next financial plan, as we move into the next couple years.

**Suneet Kamath**  
*Analyst, Citigroup Global Markets, Inc.*

Okay, thanks.

**Operator:** Thank you. Our next question comes from Jimmy Bhullar with JPMorgan, your line is open.

**Jimmy S. Bhullar**  
*Analyst, JPMorgan Securities LLC*

Hi, good morning. So first, just for Randy on changes in accounting LDTI coming up in a couple of years, do you have a better insight into how you're yield will be affected and if not, then when do you think you'll start sort of rolling out guidance or indications on what the impact might be?

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

Yeah, Jimmy, other than the comments I made a little earlier that we don't see a large impact from the FAS 60 component, I really don't have any insights that I can share with you today, Jimmy. I really think it's going to be 2022, maybe in that middle of 2022 range before we have numbers that we can really start sharing.

I think there's – if you go back to the FASB, there's a reason that they differed the implementation of LDTI here. It's because there's a lot of work. And that work was somewhat influenced by everybody shifting to the work from home environment. So, yeah, I think we're in that – somewhere in the 2022 area, we'll start sharing data with – we'll be able to start sharing data then.

**Jimmy S. Bhullar**  
*Analyst, JPMorgan Securities LLC*
And then just on your retirement business, your flows have been pretty good. And I think your business is holding up better than some of the 401(k) businesses, and it's just the makeup. If you could just talk about what you're seeing in terms of trends on deferrals on matching contributions. And I guess, talk about the customer segments that you're in and how susceptible or not as susceptible to the economy there.

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

I mentioned, Jimmy, some of the statistics on contribution rates early in the year and later in the year from employees and matches and so forth from employers, and that seems to be improving, has improved over the course of the year. The markets that we participate in are less susceptible in large part to the pandemic, education, health and government, a little bit more stable employment in those areas. So, yeah, we've had a good run here and we expect it to continue.

**Operator:** Thank you. That's all the time we have for questions. Management will follow-up with those in the queue later this afternoon. I would like to turn the call back over to Al Copersino for closing remarks.

**Albert S. Copersino**  
*Vice President & Head-Investor Relations, Lincoln National Corp.*

Well, thank you all for joining us this morning. As always, we're happy to take any follow-up questions that you have. You can e-mail us at investorrelations@lfg.com. Thank you all and have a great day.

**Operator:** Ladies and gentlemen, this concludes today's conference call. Thank you for participating. You may now disconnect. Everyone, have a great day. Speakers, please stand by.