CORPORATE PARTICIPANTS

Alex Scott
Analyst, Goldman Sachs & Co. LLC

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

MANAGEMENT DISCUSSION SECTION

Alex Scott
Analyst, Goldman Sachs & Co. LLC

All right, we'll go ahead and get started. We're very happy to have Lincoln National CEO, Dennis Glass, with us today. Lincoln is in the business of annuities, life insurance, group protection, retirement here in the U.S. Dennis has been with the firm as CEO since 2007.

In terms of the format today, we're going to be doing a fireside chat. I'll save a little bit of time in the end just to open it up to questions.

So, with that, I'd like to say, thank you very much for being here, Dennis.

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

We're delighted. Thank you for inviting us and always like to attend the Goldman Conference.

Alex Scott
Analyst, Goldman Sachs & Co. LLC

Appreciate it.
QUESTION AND ANSWER SECTION

Alex Scott
Analyst, Goldman Sachs & Co. LLC

Q

So, maybe start with the annuity business. Can you discuss the index linked annuity product that's planned to be launched during 2018 and the size of the opportunity you see in the market?

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

A

Yeah. The market size on that by other competitors right now is about $6 billion and that can get bigger. It's kind of an interesting product. The way it works is that it's an indexed annuity crediting rate put on a variable annuity chassis. And the importance of putting on a variable annuity chassis is that you can let the customer take a little bit downside risk, in other words, break the buck a little bit. So, maybe, you'd set the minimum guarantee of principal at 90% of what the customer puts in. But the opportunity then is to increase the participation rate on the indexed crediting factor. And so, it's a spreading of risk, a little more risk taken by the customer and a little bit more opportunity for upside for the customer that contrast to a fixed indexed annuity where there is – you can't break the buck just by law. So, it's a good product and it's attractive in the marketplace.

And importantly, we always talk about the significance of our distribution channels. It's sold in channels where we are already selling. So, good product, consumer acceptance, another way to provide value in channels that we operate in.

Alex Scott
Analyst, Goldman Sachs & Co. LLC

Q

Got it. And I guess just on the planned expansion of the wholesalers, in annuity specifically, can you talk around some of the timing, how you would expect that to unfold during 2018 and how it sort of flow through to sales?

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

A

Well, it's hard to predict how it'll flow through to sales, but let me talk about the strategy. We're increasing the wholesaler sales force, I think, about by 15%, about 30 people. Most of that is going to be supporting product expansion in the bank channel, so I think, two-thirds of that [ph] 30% (02:55), and that's typically what we do with wholesaling. We get extra shelf space or we get another product and oftentimes that's associated with the expansion of the wholesaler force. So, again, I don't think you can – I can't tell you that's worth x million dollars of sales, but I can tell you it's a positive opportunity for us.

And just sort of on the other side, when sales are down in VA or any product channel, sometimes you have a reduction in your sales force. So, the fact that we're going up, the fact that we're selling a broader product line in existing channels calls for wholesaler expansion, sort of our playbook.

Alex Scott
Analyst, Goldman Sachs & Co. LLC

Q

And maybe on the DOL, the fiduciary review kind of going on, how do you see it playing out with the harmonization just between DOL, SEC, NAIC, Annuity Suitability Working Group, et cetera?
Dennis R. Glass  
*President, Chief Executive Officer & Director, Lincoln National Corp.*  

Yeah. We're at the front end, now that the second phase of the DOL has been delayed until July 1, 2019. And so, one of the key opportunities is just what you're talking about is to get more of a harmonization among the key regulators. And you mentioned them, the SEC, FINRA, the Department of Labor and the state regulators. And each of those groups or the leaders of each of those groups have made positive statements about trying to get to a harmonized standard. So, we're encouraged by that. We, certainly, will continue to work for that to happen.

Obviously, having multiple different rules on a single product doesn't make sense. So, if you have variable annuity that's looked over by the SEC, it's looked over by the DOL, it's looked over by the state regulators and they don't have the same sort of view on – or harmonized best interest standard, that gets complicated. So, anything that can happen among those regulators to harmonize, and again, repeat what I said, seems to be the direction – positive direction that we're hearing from each of those groups.

Alex Scott  
*Analyst, Goldman Sachs & Co. LLC*  

Got it. And as some of the Life Insurance products have been repriced for principal-based reserving, I think, in certain cases, it's changed pricing a bit, just an update to sort of the reserving methodology. When we think about the Annuities business and some of the things that are going on with the NAIC changing the VA capital framework, do you see any need to reprice with those products?

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

Alex, there's a couple of moving parts. Specific answer to your question is, at this point, we don't see significant repricing driven by the captive issue and the other things that are going on, but there's a couple of pieces that we're watching. As a general matter, the NAIC is going in a positive direction on captives with VA. And so, we are encouraged by that. But, again, I'll qualify that by saying there's one or two things out there that could change. But, even with that, I just don't see a big repricing effort as a result of the captive work that's being done by the NAIC.

Alex Scott  
*Analyst, Goldman Sachs & Co. LLC*  

And then turning to Life Insurance, some of the guaranteed universal life sales have declined in recent years, but the MoneyGuard product has really picked up most of the slack with term life as well. Can you just discuss the hybrid LTC market, do you think there's still room for growth there? And what's sort of the strategy with the planned increase in wholesalers and how you'd expect it to kind of play there as well?

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

Yeah. So, the hybrid LTC life product is going to be continued to be driven by the demographics in the United States. So, we all know the numbers, 10,000 people turn 65 every year, a large portion of those people need some type of LTC protection, and so that market is just going to get bigger and bigger.

What we're also seeing is that financial advisors, to an increasing extent, are seeing the need for that product and so are more likely to show it these days and maybe so in the past. So, the demographics, the need for the...
product, financial advisors getting more comfortable with the product, I think they are all powerful tailwinds to make the LTC market a strong and robust market as we go forward.

Alex Scott  
Analyst, Goldman Sachs & Co. LLC

And maybe shifting gears to tax quickly, just with the House bill or the Senate bill now out there, do you have any updated views you can provide on the impact of the tax?

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

I've been spending a lot of time with other CEOs on the Hill, so I'm sort of talked out on taxes in general, because there's been so much of ongoing change. So, let me give you some specific answer to that question. Let me start by saying nobody knows what the final bill is going to be, and therefore anything I'd say in the next couple of minutes is got to be qualified by it's an ongoing process, big changes keep occurring and so, I don't know, but if I just narrowly focus on the Senate bill that was passed on Friday, so that's the bill and the provisions in that bill will retain in the final rewrite, a couple of things.

There's two issues for most companies and then an industry issue that I'll talk in a bit. The two issues are first, do your cash tax payments change over the 10-year period? So, that's different than your effective tax rate, your cash tax payments change. And based on what was passed Friday by the Senate, Lincoln's tax cash payments would go up moderately over the 10 years, but we don't see that increase as affecting our current capital deployment plans. So, a little bit up on cash tax, but not affecting us, our capital deployment in material way. So, that's the tax cash piece of it.

The next piece of it is what happens to GAAP operating income and GAAP operating income per share. Again, based on the Senate bill, we expect to see a moderate accretion as a result of the bill. So, we think our tax rate will go down somewhat. I'm not going to try to quantify that other than somewhat, little bit up in terms of accretion. So, I think that's a positive outcome. Again, if you don't mind me qualifying this, that's the Senate bill passed on Friday, more things are going to change. So, that could change as well.

So, slight increase in cash tax payments, manageable, doesn't change our view on our capital deployment plans and some modest accretion on the GAAP operating income per share side.

Now, there is a third issue that we all have to pay attention to. When I say we all, I mean, broadly speaking the insurance industry and a lot of my counterparts and our competitors have talked about this, but that's the effect of the change in the tax rate on RBC. And as a general matter, if the tax rate goes down, if you get less, if you have a loss and you have less taxable benefit versus where you are today, that'll have an effect on the RBC ratio. And so, the magnitude that people have come out with that, I don't know what it is, for the industry in general, but there is downward pressure on RBC.

I think, a couple of things, let me talk about that for a minute, I think a couple of things. One, because it's an industry issue, if it goes down, I think there will be a recalibration in part about what's a good RBC ratio. So, if it goes down, but it goes down for everybody, it's just relative to what's Lincoln's versus PRU and so on and so forth. And that RBC actually is sort of just mostly important as a relative measure of different companies’ capital strength. So I think, there might be a recalibration.

Lincoln and I suspect most companies, but let me just limit it to Lincoln, we do our stress testing around the objective not so much of RBC, but around the objective of maintaining our ratings. And so, probably the more
important question than the recalibration because of the downward drift for the industry in the RBC is how the rating agencies sort of measure the impact of these bills. They haven't really come out and talked about it, but they have their own capital models, they have their own capital – investment loss models and so, it's different than the RBC.

So, the more important issue I think for the industry and Lincoln is how do the rating agencies react to this change, don't know the answer to that. But even if there was some pressure to increase capital because of this issue, the rating agencies would incorporate that over time. I mean, even during the crisis, if your capital levels went below what their models, where they give you 10 years to work it out.

And then just back to will there actually be a change in RBC? That's not 100% clear because it's a sort of locked in factor by the NAIC in the model. And so, they would have to change their model assumptions. So, just be aware that there could be some downward pressure and there's a lot of different players. So, it remains to be seen.

Alex Scott
Analyst, Goldman Sachs & Co. LLC

Okay. That's very helpful. Let's, maybe, moving on to the digital initiatives, fair amount of focus on sort of how that could translate to some expend-saves over time. Could you also kind of help us think about how it could contribute to the underwriting process, the margin kind of embedded in new value and maybe some of the products that would impact?

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

So, at the highest level, the idea of investing in digital for Lincoln is because we think that the customer service experience is being set not by our competitors, as it has been in the past, but by the born digital companies. So, if you're accustomed to interacting with Uber or Amazon or Airbnb, so easy to conduct business, you're going to want the same – have that same kind of experience with all your providers of services and products. And so, our goal is to move up the scale, and digital has a lot to do with that in terms of the customer experience. So, we're pretty excited about that.

Now, in the digital program, there's many dimensions to it. And just to list a few, cost reduction comes from the utilization of optical character recognition and robotics on manual processes. So, now when papers come in and you have people reading them and then taking the data off of the paper and then incorporating into, say, an administrative system, that can be done using optical character recognitions, a machine reads the paper rather than the person and then robotics can be used to enter it into the system. So, that's a very powerful cost reduction, and while you're improving the overall customer experience. So, we're working on that.

And then, sort of dropping down to your specific question, Alex, yes, there will be digital initiatives inside underwriting. I think, there's a lot going on in underwriting, reaching out into the social networks to get data that otherwise you'd have to get through a doctor's report, that's happening. There's automated underwriting that makes it more cost-effective to do products that have narrower margins such as term products, that's in place and we're doing that. So, there's quite a bit.

I think, it's hard to isolate digital as a component of dramatically reducing the margins there. But when you add everything that's automated, automated underwriting, digitization, which would be sort of from app to issue, there is no manual participation in that, and we have some products that do that already. So, all of these things help
with the margins on particularly term insurance, so that's where our first focus has been because we see that as a big opportunity moving into sort of the millennial market.

So, in general, it's positive, but there's so many pieces to it, it's hard to say that digitization all in of itself is going to have a big, big impact, but it's a very powerful opportunity for Lincoln and others who take advantage of sort of this whole digital world.

Alex Scott  
Analyst, Goldman Sachs & Co. LLC

So, one of the positives that I came away from the Investor Day with was just around the impact of margin improvement that you're expecting, and I think the digital initiative was I think supposed to be neutral as we kind of look into 2018. What are some of the other things that can kind of help drive margin improvement, I guess, before we start seeing the digital initiative start to flow through?

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

Yeah. So, I think, the way we’ve characterized this as I think we have isolated about $50 million investment in digital over the next couple of years. The actual number will be a little bit higher, but there will be benefits from digitization, the other programs that lower our overall G&A cost. So, I think, we’re sort of talking about $50 million a year, $40 million a year. So – and that $40 million is a net number as we get – every year, we’re going to get some improvement in expenses. So, that’s a positive we’ve isolated.

Lincoln has always been a company that focuses on, I think, effectively on expense management. It really starts with the basic requirements of the business units and the staff areas, the corporate staff areas, as you enter into the budgeting process. And that fundamental requirement is your costs have to go down 2% about more or grow 2% less than your revenues do. So, if your revenues are growing at 8%, your cost can only grow at 6%. So, just sort of embedded in the day-to-day management of the company, we would see margin improvement because of that requirement.

And then, you do special deep dives where you think you can get even more from that, the digital more than just that 2%. And so, examples of that would include, so separate from digitization, our Retirement business cost have historically been a little bit higher than the industry. We’ve got a very powerful program to bring those costs down, some from digital, just some of them from process improvement, separate from digital. So, that would be an example.

So, on the investment cost side, I think we’ve talked about this, but we’ve reduced the fees that we pay our money managers on the general account, which has generated a pretty significant reduction in our general account management fees. I think it’s in the neighborhood of $20 million, I think we’ve talked about that.

And then, we’re also negotiating with our mutual fund companies inside of our separate accounts. And there, we’ve – sort of a revenue increase, we increased the revenues from our administrative fees that provided us more income, it’s not a cost reduction, [ph] much of it's got (21:14) more income. We're negotiating the fees with each one of our mutual fund partners, trying to get those down a little bit, that will create some opportunity. So, I'm speaking about the ongoing, you start with 2% improvement, and then you deep dive where there's obvious opportunity to even do more.
Alex Scott  
Analyst, Goldman Sachs & Co. LLC

Okay. And on the Group Protection, the expansion in the supplemental and voluntary products, is this expected to come more from participation rates within existing groups? I know there are also some product launches mentioned with critical illness, I think, in 2018, and could there be an M&A element to sort of further expansion in this business?

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

So, let's talk about product. Yes, we continue to emphasize increasing our opportunity with employees or employee-paid products sort of in the traditional sense of just buy-ups. So if your employer provides you $10,000 a year in life insurance, you can buy-up and maybe get $15,000. And so, that's the typical way in the past that you have benefited from the employer-paid side.

Over the last five or seven years, we've added new products, critical illness, so other sort of severe cancer insurance and things like that. In that respect and we've talked about the administrative platform changes that we're making. Sometime in 2018, the platforms will permit us to offer more critical illness products and accident products and we see that as a very positive lift to the top line in the employer-paid side. So, administrative changes help, trying to penetrate more existing customers and, of course, as you add new customers, you get new employees and keeps going up.

Alex Scott  
Analyst, Goldman Sachs & Co. LLC

Okay. So, when we think about the Group Protection business, you guys are developing some of your products here, you're kind of hitting some of the margins that you've laid out as targets, is the need to kind of go to M&A to achieve scale and so forth less necessary at this point?

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

Well, I would say that we're at scale in the market segments that we are focusing on. And so, there's no need to do from a scale perspective and the ability to produce this 5% to 7% margin range that we're talking about. There's no need to do M&A to achieve those sort of organic growth and margin improvements.

But separate from that, we've had a goal sort of at the corporate level to increase our profits coming from non-capital market earnings drivers. So, non-equity market, non-interest rates, and that's really mortality and morbidity because we already are so big in the mortality business that really our first choice is to expand that source of earnings by doing some type of a Group acquisition. We're in no hurry, but over time, if we could achieve something on the Group side from an M&A perspective, I'd like to see that happen.

Alex Scott  
Analyst, Goldman Sachs & Co. LLC

Sure. One of the things in the U.S. Treasury report that they put out on Asset Management and Insurance Regulation, there is a recommendation there, I guess, to make group annuity sort of guaranteed income benefits a greater portion of the menu that's available to 401(k) investors. I was wondering if you had any thoughts or kind of view that as potential growth areas you look at your Retirement business?
Dennis R. Glass  
President, Chief Executive Officer & Director, Lincoln National Corp.

We have a couple of products that provide guaranteed income inside of 401(k)s. They haven't taken off, they've been in there for two or three years. And so, in the DOL, there's this one provision that sort of puts the burden of measuring the solvency of the insurers that provide that protection on the shoulders of the plan administrators, and they're really not rating agencies and so, corporate America 401(k) departments. So, I think, to get any real traction on guaranteed lifetime income inside of 401(k)s, so that impediment has to be removed, then I think it probably is on the list of the things that DOL would give consideration to removing.

So, the answer is, maybe a group variable annuity contract, it may be another chassis, but the most important thing is, I believe Americans ought to have access to guaranteed lifetime income within their own existing 401(k) plans or [ph] 403(b) (26:45) and so forth.

Alex Scott  
Analyst, Goldman Sachs & Co. LLC

And this one, I guess, just on capital. An item more companies are grappling with is just the value proposition or share repurchases versus other opportunistic uses of capital. Can you provide some commentary around what drove the decision at Lincoln to reduce the targeted cash flows as a percent of GAAP operating earnings sort of the cash flow?

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

Yeah. Alex, I think, let's get on the same page because I think it's the other way. We have not reduced our targets for share repurchase. As a matter of fact, we've increased them. So, historically, we provided a range of 45% to 50% of GAAP net operating income as what's available for discretionaries capital, share buybacks, increases in dividends and so forth. We then moved that up to 50% to 55%, so we actually increased the target.

And this year, we've said that we might be above that 50% to 55%, I think predominantly because we always talk about the fact that when a particular line of business sales go down, that frees up capital. And so, capital that would have otherwise this year gone to support the variable annuity business is being used to buy shares back. And so, that's why we're above our 50% to 55%.

So, to summarize, we were at 45% to 50%, we moved to 50% to 55%. 50% to 55% is our ongoing target, and when there is opportunities, either – this shift in sales of guaranteed to non-guaranteed frees up capital, because the non-guaranteed products are more or less capital-intensive, so the 50% to 55% is a good number for everybody to use in their models. And as we did this year, maybe there is upside from that or event-specific reasons as we go down the road.

Alex Scott  
Analyst, Goldman Sachs & Co. LLC

Got it. And sorry for the mistake there. I guess, I was thinking more year-over-year, but I shouldn't have.

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

Yeah, that's okay.
Alex Scott  
Analyst, Goldman Sachs & Co. LLC  

So, now we got about five minutes left. I just wanted to make sure if there are any questions from the audience, we had an opportunity to ask them.

(indiscernible) (29:15)...

Alex Scott  
Analyst, Goldman Sachs & Co. LLC  

(ph) Is there a microphone (29:17)?

...the pension risk transfer business that some of your competitors are active in, how do you look at that business as a sort of mortality-driven business or maybe an investment management business? And how do you think of it as a potential opportunity for Lincoln?

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

That's a question that there are different views on. So, here's my view, and it'll be challenged by people who are in that business. But, I view it as a credit risk business, in order to make it work, you have to take excess credit risk. Now, certainly, there's some mortality and morbidity to it, but I think bottom line, it's a credit risk deal.

Now, having said that, there are companies that we compete with that have a much, or sort of historically have had more in-house sourcing capability to a PRU or a MET, they have these vast employee systems that raise middle market loans, or they raise – or they can source middle market loans, they can source private equities, they can source – or excuse me, less liquid assets in the middle market, they can source mortgage loans. And so, they have sort of a in-house capability to take incremental credit risk that, A, Lincoln would not have because we don't have that same in-house capability we do on the mortgage side.

So, bottom line is we only – I don't view that as a retail product and I view it as driven more by credit risk than by sort of the broader distribution, product breadth, risk management, [ph] and connectivity (31:05) that we do that I think makes our franchise more competitor-resistant, good business for some people, but not for Lincoln.

Dennis, within the Scott Amendment of the Senate tax bills we talked about before, it looks like the industry kind of got product neutral for most of what was put through from the bill there. Do you agree with that in general? And is there anything else that you might see that might be affecting a line of business more than others with at least what's expected there?

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

A
So, if I heard the question, is the Scott Amendment is what's in the Senate bill? So, when I talked about what's in the Senate bill, that's what I was referring to. There are two or three different spots that cross – that sort of raise revenues that cross business models. So, it doesn't seem to me that any particular line of business is materially benefited or materially hurt by what's in the Scott Amendment or what's in the finance. Maybe you'd make an argument that the Group business has a little bit of an advantage coming out of the Scott, not to the disadvantage of other people because the – some of these other factors that are the DAC tax and reserves, long-term guarantee products.

So, let me summarize. I think, it's fairly neutral across businesses in aggregate, which is not to say that there's not a company that could have a better or worse outcome depending on their specific business mix. But, generally, it's – and intentionally, on the part of the industry, because we've been advocating for a set of changes that we're just that mostly neutral across business lines, business models. This is so fast moving that anything can change at any hour. And so, it could turn out that one business model or the other is more dramatically affected, but that's not the case right now, to the best of my knowledge.

Alex Scott  
Analyst, Goldman Sachs & Co. LLC

Maybe I'll sneak in one last one. Can you provide any kind of update on just what you're seeing in terms of fourth quarter annuity sales as it relates to maybe the partnership with Athene? I think there was some commentary at the Investor Day of the Max 6 Select product and sort of gotten going.

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

Yeah. I think I'm going to look to Chris to make sure I don't misspeak, but I believe that at the IRB, we indicated that we're seeing strength across product, across individual annuity product lines and across channels from a sales perspective, and that has continued for the last couple of weeks. So, we're quite pleased that results are better than what we've been seeing. I'm not going to – we're really excited about fourth quarter sales without getting into more detail and consistent with what we said at the IRB.

Alex Scott  
Analyst, Goldman Sachs & Co. LLC

Okay. Very helpful. Thank you.

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

Thank you for being here, and if you're investors, we appreciate that very much, and if you're not, we hope you take a hard look.