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Lincoln National Corp. (LNC)

Q2 2026 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Hello and thank you for standing by. My name is Regina and I will be your conference operator today. At this time, I'd like to welcome everyone to the Lincoln Financial Second Quarter 2026 earnings webcast and conference call. All lines have been placed on mute to prevent any background noise. After the speakers' remarks, there will be a question and answer session. [Operator Instructions] I'd now like to turn the conference over to John Muething, Head of Investor Relations. Please go ahead.

John Muething

Vice President-Financial Planning & Analysis & Head of Investor Relations, Lincoln National Corp.

Thank you. Good morning, everyone, and welcome to our Second Quarter Earnings Call. We appreciate your interest in Lincoln. Our quarterly earnings press release, earnings supplement and statistical supplement can all be found on the Investor Relations page of our website, www.lincolnfinancial.com.

These documents include reconciliations of the non-GAAP measures used on today's call, including adjusted income from operations and adjusted income from operations available to common stockholders, or adjusted operating income to their most comparable GAAP measures. Before we begin, I want to remind you that any statements made during today's call regarding expectations, future actions, trends in our businesses, prospective services or products, future performance or financial results including those relating to deposits, expenses, income from operations, free cash flow or free cash flow, conversion ratios, share repurchases, liquidity and capital resources, as well as any statements relating to the closing of the GUL reinsurance transaction announced this morning and the expected timing thereof, and the expected impact of the transaction on our risk profile, RBC ratio, and free cash flow are forward looking statements under the Private Securities Litigation Reform Act of 1995. These forward looking statements involve risks and uncertainties that could cause our actual results to differ materially from our current expectations. These risks and uncertainties include those described in the cautionary statement disclosures in our earnings release issued earlier this morning, as well as those detailed in our 2025 Annual Report on Form 10-K, most recent Quarterly Reports on Form 10-Q, and from time to time in our filings with the SEC. These forward-looking statements are made only as of today, and we undertake no obligation to correct or update any of them to reflect events or circumstances that occur after today. In addition, please note that the reporting of risk based capital or RBC measures is not intended for the purpose of ranking any insurance company or for use in connection with any marketing, advertising or promotional activities.

Presenting this morning, are Ellen Cooper, Chairman, President and CEO, and Chris Neczypor, Chief Financial Officer. After their prepared remarks, we'll address your questions. Let me now turn the call over to Ellen. Ellen.

Ellen Gail Cooper

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

Thank you, John, and good morning, everyone. Thank you for joining our call today. This morning, alongside our second quarter results, we announced an agreement with Talcott to reinsure approximately $6 billion of our legacy Life reserves. The transaction marks one more important milestone in shifting the liability mix and enhancing the ongoing durability of enterprise free cash flow. Reaching this agreement in a quarter that added to our track record of solid operating results speaks to the financial and operating strength we have built and our ability to execute consistently. Chris will take you through the details shortly. This transaction reflects the deliberate strategy we've been delivering over the past several years.

From the outset, we laid out a clear path to build a strong balance sheet, optimize our operating model, and drive more profitable, durable growth across our businesses. Since then, we have followed through on each of these priorities. We have grown earnings, improved the quality of those earnings, increased free cash flow and built a more resilient, better positioned company. With the business performing well and our capital position strengthened there was one remaining priority to address.

This quarter we pre-funded the repurchase and/or redemption of half of the preferred stock that becomes callable next year, bringing greater certainty to our capital plans. Together with the growth in holding company cash net of pre funding, we are entering a new phase with greater flexibility to advance our capital priorities while investing in the long term growth of the business. As I reflect on what we've accomplished, I'm deeply grateful for the dedication, resilience, and commitment our team has demonstrated every step of the way. Every day, they make a difference in the financial lives of more than 17 million customers, helping them plan, protect and prepare for their future.

Together, we've built a better Lincoln, one with a stronger foundation, a better business mix, and growing earnings and free cash flow. While our work is never complete, I believe we have reached an important inflection point in our journey. That progress has expanded our opportunities and flexibility, positioning us to create greater value for our shareholders in the years ahead. Against that backdrop, our second quarter results demonstrate the consistent execution that has brought us to this point.

Adjusted operating income increased 3% year over year, marking our eighth consecutive quarter of year over year growth. Just as importantly, each of our four businesses advanced its strategy this quarter, and together they are building toward a more balanced, higher quality and more predictable earnings profile. In Group Protection earnings were among the highest in the segment's history, even as they moderated from a record one year ago. In Annuities, earnings remain solid as spread based products again represented about two thirds of sales. Life insurance produced a good quarter supported by favorable mortality, while sales increased meaningfully year over year. And in Retirement Plan Services, earnings grew at a double digit rate, driven by favorable markets and spread expansion as the strategic realignment of the business is in its early stages. Taken together, these results demonstrate that the strategic choices we have made are producing a more balanced earnings profile and creating multiple pathways for future growth.

I will now take a few minutes to discuss each of our businesses in more detail, starting with annuities. As a holistic annuity provider our competitive advantage lies in the breadth of our product portfolio and the depth of our distribution relationships. We offer a full range of solutions across RILA, fixed and variable annuities with and without living benefits, allowing us to meet customers' needs across a wide range of market environments. Our strategy is straightforward, grow where we can differentiate beyond price, achieve target returns, and steadily expand the spread based earnings power of the business.

Total annuity sales were $3.5 billion in the quarter, with spread based products representing 63% of sales as we shift toward a less market sensitive business. RILA sales rose 10% year over year, a more measured increase than we generated in the first quarter, as we prioritize profitability over volume in a competitive market. We remain selective and disciplined, concentrating on the sources of growth where our distinctive capabilities complement customer needs and our return objectives. Fixed annuity sales were lower this quarter but that does not change our view of the potential ahead. We believe this product category offers the longest runway for growth within our annuity business with capacity to extend our competitive position over time. The investments we've made in our platform, including through our partnership with Bain Capital, broaden our toolkit and position us to meaningfully increase fixed annuity sales over the remainder of the year.

As we've said previously, with fixed annuity flows now fully retained, we expect fixed annuity account values to rise this year, supporting future earnings and cash flow. Variable annuity sales met our expectations as volumes normalized from the elevated levels we saw in 2025. Within that, sales of variable annuities without living benefit guarantees rose more than 60% year over year and for the first time exceeded those with guarantees. This is a capital efficient part of our business that generates attractive earnings and cash flow without the guarantee and an area where we see room for expansion. Across the portfolio we are intentional about how to grow. As spread based products scale we expect them to contribute a larger share of earnings and free cash flow.

Now turning to Life Insurance. We have been deliberately reshaping the earnings profile of this business. We have improved the performance of the in-force portfolio, while shifting new business toward expanding segments and products that meet our long term objectives. Just as importantly, we have enhanced our value proposition by investing in the technology, underwriting and distribution footprint needed to compete and grow over the long term. Those efforts produced results again this quarter. Life earnings increased year over year, driven by favorable mortality, partially offset by lower alternative investment returns. Total Life sales increased nearly 80% year-over-year, with core Life sales up 18% to $103 million, led by MoneyGuard and VUL with limited guarantees. Executive benefits also performed well supported by one large case. As we've noted, sales of this product can vary from quarter to quarter based on the timing and size of individual cases. The Life business is moving in the direction we intended. We are seeing the benefits of the actions we've taken across the in-force block while the new business we're writing advances our strategic priorities. Together, those actions are building a durable foundation for future earnings and free cash flow.

Turning to Group Protection. Our targeted segment strategy shapes how we compete across the local, regional and national markets. We tailor how we serve each customer segment with dedicated distribution, underwriting, technology and service models built around the distinct needs of each market while emphasizing the areas with the most attractive long term returns. In keeping with that strategy, we are deepening our presence in the local market segment and supplemental health products which are the fastest growing. That emphasis is showing up in our results.

Overall, premium growth was 2.5% year over year and concentrated in the areas we have prioritized. Supplemental Health premium rose 28% year over year and now represents 7% of our in-force premium, up from 5% a year ago, consistent with the outlook we shared at the beginning of the year. Local market premium again increased more than 3%, supported by our tailored operating model and deep local market relationships. This reflects focused execution, pricing rigor across both new business and renewals, and expansion into higher return markets and products. Sales declined from last year's record second quarter but were solid and we held firm on our pricing discipline throughout.

Our efforts are concentrated on the segments and products with the greatest long term opportunity, along with the margins that have set our performance apart. We are also modernizing the business. This includes advancing our claims platform, expanding the use of AI and automation across underwriting and claims, and enhancing the digital tools available for brokers, employers and employees. Together, these initiatives improve responsiveness, simplify the customer experience, and reinforce our position. Today, Group Protection contributes more to Lincoln's earnings than it did just a few years ago, and the momentum behind it gives us confidence it will become an increasingly meaningful part of Lincoln's higher quality earnings profile.

Now turning to Retirement Plan Services. We are applying the same disciplined framework that has guided our strategy across Lincoln, making deliberate choices that improve the profitability of the business. While this work is earlier in its evolution than in some of our other businesses, we have organized the business around distinct market segments with products, distribution and service models designed for the unique needs of each segment. RPS earnings increased year over year and total deposits also grew, driven by steady demand for our retirement solutions. Net flows remain negative, primarily due to the planned transition of several large cases that don't meet our profitability objectives. These actions support the direction we have established for the business and our objective of improving its overall economic profile.

As we execute, we will build on our strengths while emphasizing opportunities with more favorable economics. The work is still in its early stages, but we believe it will steadily improve the profile of the business and its contribution to Lincoln's earnings growth. In closing, the actions we have taken over the past several years have reshaped Lincoln into a stronger, more diversified company with greater financial flexibility. Every one of our businesses now has room to accelerate earnings and grow free cash flow. We have reached an important inflection point. The next chapter is no longer about repositioning Lincoln. It is about building on what we have created, making disciplined, deliberate choices that expand our businesses and improve the quality and durability of our earnings. Lincoln today is a fundamentally different company than it was four years ago, and what matters most is what that now enables us to achieve. We will be defined not by the journey behind us, but by the opportunities ahead and the value we create from here. With that, let me turn the call over to Chris.

Christopher M. Neczypor

Chief Financial Officer & Executive Vice President, Lincoln National Corp.

Thank you, Ellen, and good morning, everyone. This quarter marked another significant step forward for Lincoln with three key milestones. First, we delivered our eighth consecutive quarter of adjusted operating earnings growth with each of our businesses showing progress in their transformation. Second, we signed an agreement to reinsure another $5.8 billion of our legacy life reserves, another significant step forward in the journey to improve that business and restore enterprise free cash flow. And third, we pre-funded the repurchase and/or redemption of half of the preferred stock that becomes callable next year, while at the same time growing our holding company cash net of pre-funding to over $900 million, positioning us earlier than expected to now have the flexibility to deploy holding company capital more freely as we move forward.

I'll walk through each of these three milestones in more detail and we'll start with the operating results for the quarter. This morning, we reported second quarter adjusted operating income available to common stockholders of $439 million, 3% growth compared to a year ago. EPS was $2.24 per diluted share, slightly lower than 2Q 2025 due to the incremental share count from last year's Bain transaction.

There were no significant items in the quarter. However, our Alternative Investments portfolio delivered an annualized return of approximately 5% in the quarter, below our 10% annualized target, representing $43 million after tax of below target income from that portfolio. On a net income available to common stockholders basis, we reported income of $1.3 billion, or $6.72 per diluted share. As in prior quarters, the difference between GAAP net income and adjusted operating income was driven primarily by the change in market risk benefits, which was favorable this quarter given higher equity markets and higher interest rates. Our hedge program, which explicitly targets capital, again performed in line with our expectations.

Now turning to the segments beginning with Group Protection. Group delivered operating income of $147 million compared with a record $173 million a year ago. The margin was 10.4%, down 210 basis points from the prior year quarter. Excluding the $15 million related to the annual experience refund on one state's paid family leave program in the prior year quarter, earnings declined $11 million as favorability in Life was more than offset by modest normalization and disability results. Our Group business continues to operate within our expected margin range with the impacts of the past three years repricing and strategic growth and higher margin segments and markets contributing to earnings while the disability environment continues to slightly moderate towards our longer term expectations.

On a product basis, the life loss ratio this quarter was approximately 62%, improving roughly 500 basis points from a year ago as low incidence levels continue to support favorable mortality. While mortality experience can vary from quarter to quarter the favorable trends we've observed over the past several quarters continue to provide a supportive backdrop for the business alongside the benefits of disciplined pricing actions. The disability loss ratio was 71.9% this quarter compared to a loss ratio of 64.2% a year ago. As I noted earlier, the prior year quarter included roughly $15 million tied to the annual experience refund on one state's paid family leave program which we now accrue quarterly. Excluding that item, the disability loss ratio increased approximately 500 basis points from the prior year quarter, reflecting a comparison against the exceptionally favorable long term disability results we experienced in the second quarter of 2025.

As you know, disability results have benefited from favorable experience over the past couple of years. While the disability loss ratio remains favorable relative to historical levels, we have seen modest normalization from these historically strong results which we expect to be reflected in year over year comparisons over the periods ahead. Looking ahead to the remainder of the year, we expect many of the trends in the first half of the year to continue. Group Life mortality should remain favorable while disability results are expected to reflect a broadly similar year over year headwind to what we experienced year to date, as the benefit from particularly strong 2025 experience continues to moderate. Overall, Group continues to perform well, and we expect to deliver a full year margin within our targeted range of 8% to 9%, supported by the underlying strength of the business.

Now to Annuities, which reported operating income of $287 million. Sequentially, earnings improved $12 million, reflecting market appreciation, higher spread income, the non-recurrence of the unfavorable tax item we discussed last quarter, and an additional fee day partially offset by continued variable annuity outflows. On a year over year basis operating income was flat as higher average account balances and continued growth and spread income were largely offset by the reallocation of net investment income on our index credit hedging collateral to non-operating income which we implemented earlier this year. Average account balances net of reinsurance were approximately $179 billion, up 12% from a year ago. Spread based products accounted for approximately 31% of total account balances, compared with 28% a year ago.

Turning to flows, total net outflows were approximately $2.9 billion, driven by traditional variable annuities. Traditional variable annuity net outflows were about $2.7 billion. With the pace of outflows consistent with recent quarters and in line with our expectations. The higher dollar amount reflects larger account balances following strong equity markets over the past year.

As we look toward the third quarter, higher starting account balances, an additional fee day, and continued spread income growth should support additional earnings growth. Overall, we are seeing early benefits from the shift toward spread based products, and we see meaningful opportunity to build on that progress over time.

Turning to Retirement Plan Services, which delivered operating income of $49 million, up 32% from $37 million a year ago driven by higher equity markets supporting average account balances and spread expansion. Base spreads were 119 basis points, up 20 basis points year over year, driven primarily by a higher earned rate as we continue deploying new money at yields above our portfolio yield. Average account balances grew approximately 15% year over year to $128 billion, supported by equity market performance over the past year. Net outflows were approximately $2.4 billion in the quarter driven by three large planned sponsored terminations, none of which met our profitability thresholds.

As we have said throughout the past year, we are prioritizing the profitability of the business we retain over volume, even when that produces elevated outflows in a given quarter. We remain focused on disciplined pricing and improving the profitability of the business we retain. While we experienced elevated outflows this quarter they support a higher quality, more profitable earnings base over time and are consistent with the disciplined, returns focused approach at the center of how we are realigning this business. The disciplined pricing on the business we retain and the meaningful spread expansion we delivered this quarter build on the results we achieved in the first quarter and are continued evidence that this approach is taking hold. Together with the operating leverage from a higher quality mix, spread expansion and stable value, and the potential for a more efficient cost structure, Retirement Plan Services is well positioned to deliver durable earnings growth over time. We are still early in this work, but the progress is real and we remain focused on continuing to execute in the quarters ahead.

Finally, turning to Life Insurance, which delivered operating income of $57 million, an improvement of $25 million from $32 million a year ago. The improvement was driven by favorable mortality and the continued benefit of our fourth quarter captive consolidation, an approximately $10 million year over year tailwind that continues into the third quarter before the comparison normalizes, partially offset by lower alternative investment returns. Mortality was a significant contributor this quarter with broad based favorability across both frequency and severity and among the most favorable results we have seen in some time.

That favorability extended across the portfolio, including continued favorable experience in our term business, consistent with the broader improvement we continue to see in US mortality trends. Mortality favorability of this magnitude will not recur every quarter. That said, we have now seen favorable experience for the better part of the past year and a half. And while quarterly results will always vary, that longer track record has been encouraging and remains supportive of the underlying trajectory of the business.

Turning to alternative investments, which was the primary offset this quarter. Alternatives generated an annualized return of 4.9% versus our 10% target, representing an approximately $39 million headwind in the quarter to the Life business. As we have discussed previously, the majority of our alternatives portfolio supports our Life business, and that is by design, as they are a natural fit for the long duration profile of this business. Over time, that allocation is a meaningful source of risk adjusted return that supports the economics of the business. While quarterly results can fluctuate as was evident this quarter, we remain confident that the portfolio will deliver returns consistent with our long term target.

Looking ahead to the third quarter, two dynamics are worth noting. First, on mortality, while we would ordinarily expect a seasonal improvement from the second quarter to the third, this quarter's favorability was greater than that typical seasonal uplift. Second, we expect alternative investment returns to recover and be at or above our target in the third quarter. Taken together, we'd expect to see earnings in line sequentially. Beyond the near-term, we remain focused on building the durable earnings power of the Life business and improving its overall economic profile.

Turning to expenses. Second quarter G&A expenses, net of amounts capitalized, were $604 million, up approximately 5% year over year. The increase reflects continued investment tied to specific actions across our businesses. The investment in our claims platform and Group Protection, the cost of retaining and servicing a larger share of our fixed annuity business, and investments in our retirement plan services operations. Each of these support a better experience for our customers and a more efficient platform over time, and expense discipline remains a strategic priority as we advance our transformation.

Turning to investments. Our high quality and broadly diversified portfolio remains tightly aligned with our liability profile and is positioned to perform well across a range of economic scenarios. 97% of the portfolio is rated investment grade, with below investment grade holdings near historic lows. The portfolio is broadly diversified across asset classes, industries and issuers, with a granularity and limited single name concentration that come from years of disciplined credit selection. It also reflects the deliberate work we have done across the general account to improve quality and diversification over time, and the portfolio delivered positive net rating migrations in the quarter.

Together, that quality and diversification are central to how we manage risk in the portfolio. We have also continued to enhance our sourcing and execution capabilities, which allows us to be more deliberate in how we optimize the general account. Over the past several quarters, we have executed a targeted shift in our asset mix toward high quality assets and structured strategies, adding incremental yield within our overall risk appetite while preserving the credit quality of the portfolio. These efforts support our spread based growth initiatives and remain an important part of our broader strategy to enhance returns and product competitiveness.

On the alternatives, returns were below our target this quarter at approximately 4.9% annualized, reflecting softer performance across parts of the portfolio. Based on the visibility we have into our public and venture capital positions, together with the market recovery through the second quarter, we would expect alternative returns to improve meaningfully in the third quarter and to run at or above our target. As always, the quarterly range of outcomes is wide and alternative returns are difficult to predict, but what we have seen to date gives us confidence in a rebound. The breadth and diversification of the portfolio continue to support our confidence in its ability to meet our return objectives over time. Stepping back our portfolio across asset classes remains strong. We maintain a robust asset allocation framework with rigorous stress testing and a measured, diversified approach to managing the general account, grounded in a consistent and disciplined risk framework. We remain very comfortable with the portfolio.

Now let's turn to the transaction we announced this morning, which represents another deliberate step in the multi-year work we have done to shift our liability mix and improve the quality of our free cash flow. This morning, we announced that we have entered into an agreement to reinsure a legacy block of guaranteed universal life business to a subsidiary of Talcott Financial Group. Under the agreement, we will cede approximately $5.8 billion of our in-force guaranteed universal life statutory reserves, roughly 37% of our remaining guaranteed universal life block, along with approximately $500 million of funding agreement business.

Together with our 2023 transaction with Fortitude Re, approximately 60% of our total in-force guaranteed universal life will now be reinsured upon the closing of the transaction. The transaction is structured partly as coinsurance with funds withheld and partly as modified coinsurance with robust counterparty protections, including over collateralization and investment guidelines aligned with our risk management framework. We will retain administration, recordkeeping, and claims management for these policies, and there is no change to our commitments to policyholders or distribution partners. The rationale is straightforward, guaranteed universal life is among the most capital intensive, long tailed parts of our in-force, and this transaction meaningfully reduces our exposure to long term mortality. Lapse and interest rate risk on an all-in basis, transaction will have a statutory capital impact of approximately $200 million, or roughly 10 RBC percentage points.

As we have said previously, we intend to fund that impact from a portion of the remaining proceeds from last year's Bain Capital transaction. Even after giving effect to the transaction, we expect to remain meaningfully above our 420% RBC ratio buffer. Going forward, we expect the transaction to increase our ongoing annual free cash flow by approximately $30 million to $40 million a year. From a GAAP perspective, the transaction is expected to reduce net income through amortization of the deferred loss, but we do not expect a material change to our adjusted operating income. Given that reinsurance of exited blocks has become a more significant part of our results beginning in the fourth quarter, aligned with the expected closing of the deal, we intend to refine our definition of adjusted operating income to exclude the amortization of deferred gains and losses on business exited through reinsurance, providing a cleaner view of our ongoing operating performance while aligning the operating result with the underlying economics. The transaction is subject to regulatory approval, and subject to those approvals, we expect the transaction to close in the fourth quarter.

Lastly, turning to capital, where we continue to operate from a position of strength, further reinforced by the progress we made during the quarter. Our estimated RBC ratio remains well above our 400% target, and the 20 point buffer we hold on top of it, and we maintained our leverage ratio at roughly 25% in line with our long term target. At the same time, we continue to build excess cash at the holding company. Holding company cash net of pre-funding ended the quarter at approximately $900 million, an increase of roughly $100 million from the first quarter and well above our historical operating range. Underpinning the build were strong remittances from our operating subsidiaries at $310 million in the quarter, bringing year to date subsidiary remittances to $580 million and tracking in line with our full year expectations.

We also took advantage of an attractive market backdrop to issue $500 million of hybrid securities, creating increased certainty as we look ahead to the repurchase and/or redemption of our outstanding preferred stock. Taken together with the continued build of excess cash at the holding company, we are now well positioned to address the preferred securities, which in turn allows for increased capital flexibility going forward and an ability to turn to other capital priorities, including share repurchases.

In closing, let me just say how proud I am of the team. We set out three-and-a-half years ago with a mission to restore our capital base, de-risk the balance sheet, improve our operating model, and strategically realign our businesses for profitable growth. While the momentum has been building with each successive quarter, this quarter marks an important milestone for Lincoln, with continued progress across our four businesses, another in a series of transactions to meaningfully shift our liability profile, and the ability to now expand our capital priorities toward a more complete mix of options to generate shareholder value. With that, Ellen and I would be happy to take your questions.

QUESTION AND ANSWER SECTION

Operator: We will now begin the question and answer session. [Operator Instructions] Our first question will come from the line of Wes Carmichael with Wells Fargo. Please go ahead.

Wes Carmichael
Analyst, Wells Fargo

Q

Hey. Good morning. Thank you. So clearly some positive developments from a capital flexibility perspective. Ellen, you mentioned Lincoln's entered a new phase. You've pre funded some of the prefs. The reinsurance transaction's coming together. So I just wanted to see, Chris, you mentioned buybacks, but I just wanted to see if you could provide more insight on, on what you're planning for a resumption of the repurchases. Is that 2026? Or anything on timing would be great.

Christopher M. Neczypor
Chief Financial Officer & Executive Vice President, Lincoln National Corp.

A

Sure. Good morning Wes. Good question. And you're right. It was a really good quarter for Lincoln, especially on the capital front where a number of milestones, are important to understand. I think if you step back, you think about the priorities that we've talked about over the past couple of years. We are largely complete and ahead of schedule. So if you think about it, the first thing that we talked about was rebuilding RBC back to the $400 million level and then holding a buffer on top of that. We largely, executed on that with the Fortitude deal and the LFN deal. We also talked about bringing our leverage ratio back down from, call it, north of 30% to the 25% level. We did that last year and it continues to hold.

We talked about being able to fully retain our fixed annuity sales and allocating capital to continue to deal with the legacy life block. We've largely done that mostly through the combination of the Bain transaction last year and standing up the Bermuda entity in 2024. And then, frankly, we've talked a lot about growing our ongoing capital generation. So improving the free cash flow conversion. And you saw with last year, in the fourth quarter that we had gone from the 30% a couple years ago, up to almost 50%. And this year remains supportive of that trend in terms of growth.

So the last piece has really been about being in a position to deal with the preferred. We've been very clear that this is an expensive security for us. And from a capital priority perspective we want to be well positioned to redeem or repurchase that security, as we've mentioned, and that's $1 billion as you know. And so with this quarter we're now for the first time, able to say that we're well positioned to handle it. We issued the $500 million of hybrid. You can see the cash continuing to build at the holding company. So it feels really good to be able to say, with all the different capital priorities, that we've set out over the past couple of years, we're now in a position where we can pivot to other opportunities that are available to us.

So if you think about where we are today, there's about $1.8 billion of capital at the holding company, $400 million of that is for the senior note pre-funded that comes due in December, $500 million from the hybrid will be put towards the preferred. So, that leaves about $900 million of available capital. And recall, we tend to hold around $500 million of a liquidity buffer. So call it $400 million of excess. If you think about the first half of the year, the cash at the holding company built by call it $250 million. And as you know, we think about the second half, look at the guidance that we gave in, with the outlook, in fourth quarter, we would expect that number to be relatively similar.

So you can do the math and understand sort of where we will be as it relates to what we'll do with that excess capital. There's a number of different options. We could obviously retain more of a buffer. There is the other $500 million of the preferred, and then most accretively would be share repurchases. So at the end of the day we're not announcing anything as it relates to timing today. As you would imagine, our normal cadence for capital decisions involves reporting our earnings quarterly and then meeting with our board thereafter. And any decisions for the next quarter would be confirmed subsequently. But what I can tell you is that we do have an outstanding repurchase authorization. It's obviously been dormant the past few years, and our board has recently reconfirmed that program, which is a good sign. But beyond that, we don't have anything else to add at the moment.

Wes Carmichael
Analyst, Wells Fargo

Q

Okay. Thanks, Chris. That's all helpful. Just, I just wanted to come back to on the transaction and the redefinition of operating earnings regarding the reinsurance deal. Did I get that right that you don't expect adjusted earnings to change going forward, or is, like after the re-definition or should we think about earnings actually going higher if you exclude those deferred losses.

Christopher M. Neczypor
Chief Financial Officer & Executive Vice President, Lincoln National Corp.

A

Yeah. So that's a good question, Wes. What I would say is as it relates to this transaction in particular the impact of the deferred loss, obviously won't have any impact on operating income when we make the accounting policy. What we realized was we were a little bit of an outlier as it relates to the way the industry treats those transactions. And frankly, when you think about the underlying economics, getting GAAP to be as close as we can is important from an operating income perspective. So that's really what drove the thinking. And then to your point we have done a number of other deals. And so there is some businesses that would have a deferred loss, some that would have a deferred gain. And so we're going through all of that in anticipation of closing the deal in the fourth quarter. And when we do we'll obviously give you the pro formas and lay everything out for you.

Wes Carmichael
Analyst, Wells Fargo

Q

All right. Thank you.

Operator: Before we take the next question, I'd like to remind everyone to please limit your initial questions to one and one follow-up. Our next question will come from the line of Ryan Krueger with KBW. Please go ahead.

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

Q

Hey, thanks. Good morning. I guess first, I just wanted to confirm what you were saying on how to think about Life Insurance earnings for the third quarter. Are you saying the $57 million of reported earnings is a reasonable expectation for the third quarter, or did you mean the $97 million with normalized alts?

Christopher M. Neczypor
Chief Financial Officer & Executive Vice President, Lincoln National Corp.

A

No. The reported for this quarter should get you to within some range, Ryan, how you would think about the third quarter, and that's before accounting for or adjusting for any favorable mortality trends that might continue. All we're doing is resetting the baseline for the very favorable mortality that we had this quarter, as well as the underperformance in alts. So when you, normally if you think about the seasonality in that business, as you know it's very seasonal, 2Q tends to be your baseline. And then third quarter and fourth quarter tend to be better.

And first quarter obviously tends to be the worst of the four quarters given the dynamic with mortality. So all we're saying is just keep in mind that mortality was very favorable this quarter. And so when you think about the seasonality adjustment that you would normally make for third quarter, you have to adjust for all those things. So, hopefully that helps. We can go through the math more if you'd like.

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

Q

No, that makes sense. Got it. I mean, just as a follow up is on mortality trends. [ph] Dave, (00:40:06) you mentioned a year and a half of favorable mortality. I guess as you analyze your experience that, are you seeing anything that you think might suggest this could, maybe some portion of this could become more permanent, or is it do you just feel like it's too early to tell right now.

Christopher M. Neczypor
Chief Financial Officer & Executive Vice President, Lincoln National Corp.

A

So these are very long term trends, as you know. And I think when you go back and you look five out of the last six quarters have been very favorable for mortality. It's mostly been in the term block, although the UL block has had as much positive quarters as it has negative, which is a really good sign as it relates to the health of that block in relation to mortality. I think when you look at the overall trends and you look at general US mortality trends that's, we're not alone. And frankly if you look at our results in our Group business, those have also been favorable.

So we'll see what it means about the long term. But if you go back especially prior to Covid, the industry was dealing with mortality, unfavorability off and on for years. And so I just think it's a really good sign that we've had a number of different drivers. We've had, like I said, five out of the last six quarters being positive. And so it just speaks to the go forward health of that business, which is not to say that you can't get surprised by severity in any given quarter, right. Especially in the UL block. If you have a handful of $20 million claims in a given quarter relative to your expectation, you can certainly have it go the other way. But underneath the surface, the mortality trends are encouraging.

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

Q

Thank you.

Operator: Thank you. Our next question will come from the line of Tom Gallagher with Evercore ISI. Please go ahead.

Thomas Gallagher
Analyst, Evercore ISI

Q

Hey. Good morning. The first just to follow up on the amortization of deferred gains or losses. Chris, today, is that a positive or negative, when we think about your earnings.

Christopher M. Neczypor
Chief Financial Officer & Executive Vice President, Lincoln National Corp.

A

So it depends which business, Tom. But in aggregate I would say it's a net negative.

Thomas Gallagher
Analyst, Evercore ISI

Q

Got you. So that, if we were to just pro forma that on your current earnings, putting that below the line would actually lift your operating earnings, all things equal.

Christopher M. Neczypor
Chief Financial Officer & Executive Vice President, Lincoln National Corp.

A

All things equal. But again it's going to depend on which segment. There's, we've done obviously a number of deals that have impacted the Life business. We've done some fixed annuity blocks, although a lot of that was a while ago. And so the liabilities have run off to a degree. So, yeah, I, in aggregate, that's certainly the case, Tom. But it's going to be very business by business specific.

Thomas Gallagher
Analyst, Evercore ISI

Q

Got you. And then my follow up is just on Group Protection. Results continue to look good there. The, I guess some peers had PFML related elevated claims. Curious if you also saw that if you peel back the onion on your underlying group disability results and maybe just tell us, and I heard your forward comments, Chris, about what, how you expect disability to remain a bit elevated. But I guess is there a, also a PFML elevated claims issue that you would expect to reprice or you could see some improvement? Just wanted to understand kind of underlying on the disability claims what's happening. Thanks.

Christopher M. Neczypor
Chief Financial Officer & Executive Vice President, Lincoln National Corp.

A

Sure. Yeah. So disability, there's always a lot of moving pieces. So let's just unpack it. Within disability obviously you have LTD and then STD. You also have within each of those you're looking at your incidence, you're looking at your severity resolutions. And then against all of that you're comparing to the prior quarter and any volatility that may have occurred there. So there's a lot of different dynamics when you're looking year over year. What I would say if you take each of those, STD, which includes PFML is a little bit pressured. But relative to first quarter the PFML headwind is much less severe. When we look at the first quarter, impact to disability loss ratio from PFML, it was probably about 100 basis points. In this quarter it was like less than 20 basis points. And so the dynamic is as the new states come online, and by the way, we've learned from prior experience, because this year there was three new states that came online.

But we've dealt with this in the past and have had fairly arduous results in the short term. So I think we have a good process. But essentially with that first quarter you're looking at the claims that are coming in and you're putting up extra reserves. So when you get into second quarter, the headwind just becomes a lot less, and it's really the first quarter dynamic that is the most impacted. As it relates to the product overall, look I would say it's obviously not margin accretive, but it is good for the customer. And over time is something that we're happy to have as part of the book. But the very simple answer to your question on PFML is that was really a first quarter dynamic for us. Not as much go forward.

So big picture then for LTD. Look, I think I would reiterate what I've said the past couple of quarters, which is you are seeing some normalization in results. It's modest and measured and in line with what we expect. In any given quarter, you're going to get volatility and severity. And, when you think about the resolutions, I think it was third quarter of last year where we had both volatility as well as the real start of normalization from a recovery perspective.

The normalization is going to continue but just keep in mind these are still really good results. So net net, when you step back I think our view is we'll do sort of that 8% to 9% all in margin for the year for Group. Third quarter the trends should continue. We'll see what happens with volatility in any given quarter. But also just keep in mind when you look at the third quarter of last year, the reported loss ratio has the assumption review in it. And so you have to back out the very favorable assumption, positive that obviously will influence that loss ratio.

We gave the numbers at the time, but I think it's important with all the moving pieces that you just have the right baseline.

Ellen Gail Cooper
Chairman, President & Chief Executive Officer, Lincoln National Corp.
A

And, Tom...

Thomas Gallagher
Analyst, Evercore ISI
Q

Got you.

Ellen Gail Cooper
Chairman, President & Chief Executive Officer, Lincoln National Corp.
A

...just a couple of double clicks in addition into your PFML point and Chris's point around the fact that we have learned from, as these states come online. So, first of all, we don't sell PFML as a standalone. It's always as part of some other comprehensive benefit offering. But in addition, as they come online, repricing is just part of our overall standard process. So there's nothing new there. Again, we've learned along the way as we continue to implement PFML across these states that are coming online.

Thomas Gallagher
Analyst, Evercore ISI
Q

Okay. Thank you.

Operator: Our next question will come from the line of Suneet Kamath with Jefferies. Please go ahead.

Suneet Kamath
Analyst, Jefferies LLC
Q

Great. Thanks. Good morning. Just wanted to get some color on the $30 million to $40 million of incremental free cash flow that you expect from this deal. It just strikes me as a little bit low relative to the over $100 million that you got from the first deal. I just want to think about or just any color on kind of what's driving that. And when you say medium term, what do you what do you mean by that? Over what period of time? Thanks.

Christopher M. Neczypor
Chief Financial Officer & Executive Vice President, Lincoln National Corp.
A

So it's an annual number, Suneet, it's just, we're making the definitional point as it relates to the medium term outlook that we gave in fourth quarter. So that's all that means. We would expect an immediate benefit once the deal closes. I look at the deal and it's $6 billion of pure GUL. And the free cash flow uplift there is pretty good. I mean, we're spending $200 million of capital and we're getting $30 million to $40 million. That's a pretty good return.

I think, if you're comparing it to the Fortitude block there was a lot of different things in there, right. Because we had a couple of other blocks of business that we ceded alongside it. It was a bigger size of GUL. And if you think about the improvements we've made overall for the business over the past couple of years, all those things are going to influence it. So this is a much more straightforward block. But again, when I, you think about the fact that you're removing, call it 40% of the very capital intensive mortality risk, interest rate risk, [ph] lapse (00:48:58) risk, and it's costing you $200 million, which you funded with the Bain deal, and you're getting a $30 million to $40 million uplift in terms of free cash flow. It's a big positive for the company.

Suneet Kamath
Analyst, Jefferies LLC

Q

Okay, that makes sense. And then I guess, I think, Chris, you had made some comments about the subsidiary dividend outlook for the second half. I was just hoping you could just remind me of what that is. And you also mentioned a board authorization existing share repurchase authorization. If you could just comment on the size of that and when the board plans to meet next. Thanks.

Christopher M. Neczypor
Chief Financial Officer & Executive Vice President, Lincoln National Corp.

A

Sure, Suneet. So we meet with our board next week, as we always do following earnings. You can see the details of the existing program. I think it's in our queue. It's a $1.5 billion program, obviously dormant since 2022. I think there's over $700 million left on the authorization. And then to your question on remittances. I think what we said in the fourth quarter was that we would expect, call it $1.2 billion to $1.3 billion a year. So far in the first half, we did about $580 million. So you can sort of take the midpoint and subtract one from the other to get the expectation for the second half.

The thing that's worth remembering, Suneet, is we tend to take our dividends from our smaller subsidiaries in the second half. So the Bermuda sub, LNBAR, they are usually third quarter, fourth quarter dividends. And so there is some seasonality. You can't just take the remittances and divide it by four and think that that's the cadence. So I know you know that. But it's just worth reiterating.

Suneet Kamath
Analyst, Jefferies LLC

Q

Yes, makes sense. Okay. Thanks.

Operator: Our next question will come from the line of Joel Hurwitz with Dowling. Please go ahead.

Joel Robert Hurwitz
Analyst, Dowling & Partners Securities LLC

Q

Hey. Good morning. A couple on annuities. Ellen, in your prepared remarks, you remain bullish on growth in fixed annuities. Can you just talk about what you saw in the quarter that it resulted in the more subdued sales and what gives you confidence for a rebound in the second half of the year?

Ellen Gail Cooper
Chairman, President & Chief Executive Officer, Lincoln National Corp.

A

Absolutely. So first of all, if you just take a step back and some of my comments in the remarks upfront, we are a holistic annuity provider. And so along with our broad distribution, we are really one of the few carriers that is across all of the main product categories. And so, in terms of our distribution, we're able to take a solutions based consultative approach. And at the same time, we were being very intentional around how we are prioritizing profitability over volume in a very competitive market. And so this really enables us to stay flexible, so that we can lean into the areas where we overall see the greatest opportunity.

So we're not beholden to any particular segment in one particular moment in time. So when you look at our quarter and you look at the fact that we saw opportunity, first of all, in RILA, where our sales were up 10% year over year, we mentioned and we referenced that we saw opportunity in VA without GLB. Those sales were up 60% year over year. And then when it comes to fixed annuity, we also want to be clear that our conviction in terms of this opportunity remains unchanged. We see fixed and in particular FIA as our longest runway for growth. And some of the reasons why are that number one, we have spent over the last couple of years, while we have been working to rebuild the foundation, we've also built a foundation in terms of all the capability to be able to support us in fixed indexed annuities.

That includes unique crediting strategies, it includes differentiated product features. It includes our work with Bermuda, but it also includes our investment capabilities and in particular our partnership with Bain, which is really broadening our toolkit. Additionally, we have been working to expand on the shelves of distribution firms where we already had deep existing relationships, but we've been able to put our FIA product on the shelves in particular. And over the last call it 12 to 18 months, we've actually added the product onto nine firms where we had existing relationships, and we're starting to gain traction there as well. So you put all of that together and you put on top of that the fact that one of our objectives is to expand our spread based earnings power. And we really see a long runway, and in particular that our expectation is to meaningfully increase our FIA sales in the back half of the year.

Joel Robert Hurwitz
Analyst, Dowling & Partners Securities LLC

Q

Got it. That's helpful. And then just on the earnings power there, Chris, anything unusual you'd call out in annuities in the quarter? I guess I would have expected, or I expected, a bigger rebound in the ROA, just given the equity market recovery and the dynamics of like the extra fee day. I don't know if there's anything, it looks like net expenses might have been a little higher. But, anything you would call out there?

Christopher M. Neczypor
Chief Financial Officer & Executive Vice President, Lincoln National Corp.

A

Not in particular, Joel. There weren't any one time items or unusual items for the quarter for annuities. I think if you step back, there's a couple dynamics to understand. So I know you know this, but the ROA on VA is relatively stable. The account value is going to move up and down with markets. We and the industry have been in a net outflow position there for a while. And so I think the earnings power from VA is relatively straightforward depending on what happens with markets. I think the important thing to understand then as it relates to spread. So obviously on a year over year basis we're still dealing with two dynamics. The first is the op to non op where we moved some of the NII related to collateral for the hedging from operating income to non op. And so that is still a dynamic this quarter.

And then also as we exited the flow agreement you're retaining more of that acquisition expense near term. And then you get the spread income associated longer term. The last thing I would call out, when you think about ROA specifically for RILA you have to understand that the index credit piece of it is going to, especially in periods with large market moves but definitely over time, is going to increase the A without necessarily increasing the R, it's, by design, you're earning the, your spread income on the assets that you're purchasing. But if you think about it, the surrenders that we had this year from the 2020 vintage, the, for a $100,000 deposit the policyholder was receiving $170,000 in benefits. So it's a really good product for customers. It's a good product for Lincoln. But from a strict metric as it relates to ROA, it can be skewed sometimes, depending on what's happening with markets and the index credit and so forth.

So net net, the economics of the business continue to grow. In the short term you have some of the accounting noise which masks some of the underlying positives. The bottom line, however, is we're seeing growth in our spread based account value. We're seeing growth in spreads. And VA is going to move around with markets.

Joel Robert Hurwitz
Analyst, Dowling & Partners Securities LLC

Q

Got it. Thank you.

Operator: Thank you our final question will come from the line of Alex Scott with Barclays. Please go ahead.

Alex Scott
Analyst, Barclays Capital, Inc.

Q

Hey, thanks for taking it. Wanted to circle back on Group and just see if you could talk about competition in the space, what you'd anticipate heading into the end of the year just given some pretty favorable performance across group life and some of the other products.

Ellen Gail Cooper
Chairman, President & Chief Executive Officer, Lincoln National Corp.

A

Absolutely, Alex. So, as you would expect, the market remains competitive as really as it always is, but still completely rational. And so as we look at this and we look at the back half of the year, first of all, we believe that we are well positioned. We have, as you know, a targeted segment strategy across local, regional and national. We've got strong distribution relationships. We have strong retention in terms of continued business with employers. We've got broad expanding product coverage. And our lineup in particular, as we see voluntary supplemental health enables us to continue to grow expanded lines of coverage. So, and then importantly, also, we are continuing to invest in all the capabilities to support customer needs.

And we mentioned a number of them upfront. But all of that goes to persistency. It goes to new business as it relates to investing in the claims process, investing in underwriting, investing in digital capabilities. We really we see a healthy pipeline as we go into the second half of the year. We believe that we have all the capabilities and the right to continue to win there as well, and we'll continue to update you.

I think importantly, there are a couple of other things while we talk about Group that I just want to mention. We really see the fastest growing areas for us are in the supplemental health area and in local markets, and we see continued growth there. So I spiked out in in my comments supplemental health premium being up 28%. And also seeing local market premium growth up over 3% as well. As we look even at our second quarter sales, and we are comparing them to the highest second quarter sales result ever, but at $150 million of sales in the second quarter is also healthy. We also see continued momentum there. So, supplemental health represented 26% of the sales in the quarter. Local markets represented 37%. So as we continue to prioritize profitability and value over volume with a healthy pipeline into the second half, expect to continue to see us leaning into those segments and markets.

Alex Scott

Analyst, Barclays Capital, Inc.

Q

That's very helpful. Thanks. Maybe pivoting over to annuities. How are you thinking about unit costs and your ability to compete in the market? Obviously, there's [ph] two peers that (00:59:42) teamed up to generate more scale. Certainly you guys have some digital initiatives that are working on it just within your own firm. Can you do enough there? What do you anticipate you can do from a technology standpoint? And is it enough to be able to compete with some of these big peers?

Ellen Gail Cooper

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

A

Yeah. So, Alex, we believe that we will be able to continue to compete and perform extremely well. I mentioned earlier broad distribution, broad distribution strength, got relationships across all the organizations. We have holistic offerings. We oftentimes have distribution that is going across product, across solutions, et cetera. And we also mentioned upfront that we are making significant investments in particular in your question around technology and digital. So a great example of that is that we have a completely digital process as it relates to new business processing for some of our annuity segments. As it relates to overall financial producers and firms, we are oftentimes really a preferred provider because of our ability to handle new business in a fully automated way. So we're going to continue to develop the right products to be able to compete.

We're going to continue to invest in all the digital and technology. We believe that we can do that with significant operating leverage going forward and then broadening and deepening our distribution relationships. I think it's worth mentioning also that as it relates to distribution, a very significant portion of our wholesalers are long tenured. They've got deep relationships with financial producers. And at the same time, we've done all the investment that we need in terms of distribution platform to be able to offer training, online capabilities around product, support with illustrations, et cetera. So, really believe that we will compete well in these markets and that we have the scale that we need.

Alex Scott

Analyst, Barclays Capital, Inc.

Q

Great. Thank you.

Operator: That concludes the question and answer session. I'll hand the call back over to John for any closing comments.

John Muething

Vice President-Financial Planning & Analysis & Head of Investor Relations, Lincoln National Corp.

Thank you for joining us this morning. We're happy to address any follow up questions you have. Please email us at investorrelations@lfg.com.

Operator: This concludes today's meeting. Thank you again for joining. You may now

disconnect.