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ING U.S., Inc. (VOYA)

Q4 2013 Earnings Call

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CORPORATE PARTICIPANTS

Darin Arita
Senior Vice President, Investor Relations, ING U.S., Inc.

Rodney O. Martin
Chairman & Chief Executive Officer, ING U.S., Inc.

Alain M. Karaoglan
Chief Operating Officer, Director & Executive VP, ING U.S., Inc.

Ewout L. Steenbergen
Chief Financial Officer & Executive Vice President, ING U.S., Inc.

OTHER PARTICIPANTS

Nigel Dally
Analyst, Morgan Stanley & Co. LLC

Erik J. Bass
Analyst, Citigroup Global Markets Inc. (Broker)

Mark Finkelstein
Analyst, Evercore Partners (Securities)

Ryan Krueger
Analyst, Dowling & Partners

Steven D. Schwartz
Analyst, Raymond James & Associates, Inc.

Yaron J. Kinar
Analyst, Deutsche Bank Securities, Inc.

Eric N. Berg
Analyst, RBC Capital Markets LLC

Christopher A. Giovanni
Analyst, Goldman Sachs & Co.

MANAGEMENT DISCUSSION SECTION

Operator: Good morning and welcome to the ING U.S. Fourth Quarter 2013 Earnings Conference Call. All participants will be in a listen-only mode. [Operator Instructions] After today's presentation, there'll be an opportunity to ask questions. [Operator Instructions] Participants are limited to one question and one follow-up. Please note this event is being recorded.

I would now like to turn the conference over to Darin Arita, Senior Vice President, Investor Relations. Please go ahead.

Darin Arita
Senior Vice President, Investor Relations, ING U.S., Inc.

Thank you, Emily, and good morning, everyone. Welcome to ING U.S.' fourth quarter 2013 conference call. A slide presentation for this call is available on our website at investors.ing.us or via the webcast.

Turning to slide two, on today's call, we will be making forward-looking statements. Except with respect to historical information, statements made in this conference call constitute forward-looking statements within the meaning of federal securities laws, including statements relating to trends in the company's operations and financial results and the business and the products of the company and its subsidiaries.

ING U.S.' actual results may differ materially from the results anticipated in the forward-looking statements as a result of risks and uncertainties including those from time-to-time in ING U.S.' filings with the US Securities and Exchange Commission.

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ING U.S. specifically disclaims any obligation to update or revise any forward-looking statements whether as a result of new information, future developments or otherwise. Slide two also notes that the call today includes non-GAAP financial measures. In particular, all references on this call to ROE, return on equity, ROC, return on capital or other measures containing those terms are to Ongoing Business adjusted operating return on equity or Ongoing Business adjusted operating return on capital as applicable, which are each non-GAAP financial measures. An explanation of how we calculate these and other non-GAAP financial measures and the reasons we believe they are useful can be found in the Quarterly Investor Supplement available on our website at investors.ing.us. Reconciliations to the most directly comparable GAAP measures are included in the press release and the Quarterly Investor Supplement.

Joining me this morning on the call are Rod Martin, Chairman and Chief Executive Officer of ING U.S.; Alain Karaoglan, Chief Operating Officer; and Ewout Steenbergen, Chief Financial Officer. After their prepared remarks, we will take your questions.

With that, let's turn to slide three and I will turn the call over to Rod.

Rodney O. Martin

Chairman & Chief Executive Officer, ING U.S., Inc.

Thank you, Darin, and good morning everyone. As Chairman and CEO, I'm always challenging our people to be forward looking. However, there are distinctive moments that deserve a look back and 2013 held a number of those moments.

Before we discuss our solid fourth quarter and full year results, I want to take a few minutes to reflect on some of our major accomplishments in 2013. As you can see on slide four, 2013 was a year of extraordinary transformation and value creation. First and foremost, we conducted an initial public offering of VOYA stock in May and a secondary offering in October, which reduced ING Group's ownership stake to approximately 57%.

For US IPOs larger than $1 billion, ING U.S. had the second best performance in 2013. Only Twitter's IPO outperformed ING U.S. And while we're pleased with the first seven months' performance, we remain deeply committed to executing our plan and adhering to our financial discipline.

Second, we completed our recapitalization plan by accessing the capital markets with our compelling transformation story on five separate occasions. And we did this while maintaining an RBC ratio well above our target of 425% for 14 straight quarters, including a 504% RBC ratio as of year-end 2013.

Third, we introduced Voya Financial, our new brand, which is a derivative of the word voyage and symbolizes a journey that all Americans are on to become retirement ready. And as you've recently learned, ING U.S. will officially change its name to Voya Financial on April 7, making this our final earnings presentation utilizing the ING brand. We're excited to transition to Voya Financial. However, we'll continue to move in a deliberate manner to ensure a seamless transition for our customers, clients and distribution partners.

And fourth, behind the strength of our Retirement Solutions, Investment Management and Insurance Solutions business, we cast our vision to be America's Retirement Company. ING U.S. is dedicated to helping Americans become financially and emotionally ready for retirement. And this vision guides our efforts to provide our customers and clients with quality asset accumulation, protection and distribution products and services plus guidance and advice. We're proud of these accomplishments, yet, we also recognize there's considerable work

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ahead of us. We will continue to aggressively pursue long term transformation and value creation for all stakeholders as we make focused investments in the growth of our business.

On slide five, let me highlight our year-end financial results. We achieved total after tax earnings of $198 million or $0.75 per diluted share for the fourth quarter, and $825 million or $3.27 per diluted share for the full year. We generated net income available to common shareholders of $548 million for the fourth quarter and $601 million for the full year. In the fourth quarter, Ongoing Business pre-tax adjusted operating earnings grew to $324 million, and for the full year 2013, Ongoing Business pre-tax adjusted operating earnings grew to $1.2 billion.

Our Ongoing Business adjusted operating return on equity improved to 10.3% in 2013, a 200 basis point improvement from our 2012 result of 8.3%. We're pleased with the improvement of our ROE in 2013 and that each business made a contribution to that progress. Our ROE improvement exceeded our planned average of 110 basis points of improvement per year. It's important to acknowledge that 2013 benefited from some items that may not repeat in 2014 and in a moment, Alain will provide more detail on the drivers of the ROE improvement and these notable items. We remained committed to improving our Ongoing Business adjusted operating ROE to 12% to 13% by 2016.

Turning to the Closed Block Variable Annuity segment, as you know, our hedging program is designed to protect regulatory and rating agency capital from market volatility. In our 2013 Closed Block Variable Annuity result, while varying from quarter-to-quarter performed in line with our expectations. In addition, several of our key risk metrics showed steady improvements throughout the year due in part to favorable market conditions.

As we move to slide six, you'll see how the ING U.S. franchise continues to leverage its leadership positions in attractive market segments to deliver diverse earnings. As I just mentioned, in 2013, we delivered $1.2 billion in Ongoing Business pre-tax adjusted operating earnings. Approximately 74% of those earnings came from Retirement Solutions and Investment Management.

Retirement and Investment Management achieved positive net flows for the fourth quarter. In addition, annuities generated its second consecutive quarter of positive net flows for fixed indexed annuities. The remaining 26% of earnings came from our Insurance Solutions business. We've made steady progress in our transformation of our Individual Life business.

Term sales are at comfortable levels and we saw encouraging sales results with our indexed Life product portfolio, which are focused on both asset accumulation and asset protection. Employee Benefits sales results were also strong for the quarter.

Across all of our businesses, our assets under management and administration grew to a record $511 billion, up from $461 billion at the end of 2012. Overall, we remain confident that our premier franchise is well positioned in the right markets to generate steady growth.

And as we move to slide seven, you'll see the ROE improvement I referenced earlier. Our Ongoing Business adjusted operating ROE for the full year 2013 was 10.3%, up 200 basis points from 2012. And we're encouraged by the ROE improvement and our progress towards our objective of 12% to 13% by 2016. Our ROE plan is designed to generate steady improvement and we remain committed to that plan.

I will now turn it over to Alain for more details about our ROE and ROC improvement program.

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Alain M. Karaoglan
Chief Operating Officer, Director & Executive VP, ING U.S., Inc.

Thank you, Rod, and good morning, everyone. As Rod noted, in 2013, we made very strong progress towards achieving our long-term targets. And this morning, I will provide further detail on some of the drivers of our performance in 2013.

Turning to slide nine, as you know, when we discussed each of our business segments we focused on return on capital instead of return on equity since we do not allocate debt to each of our businesses. And our Ongoing Business return on capital improved 140 basis points to 8.6%, up from 7.2% in 2012. We are making very solid progress towards our 2016 target of 10% to 11%. And by continuing to execute on our more than 30 margin, growth and capital initiatives, we were able to significantly improve both our return on equity and our return on capital.

More specifically, the year-over-year return on capital improvement was due to several key drivers, many of which were outlined in the plan that we shared with you prior to our initial public offering. For example, each of our ongoing businesses contributed to the year-over-year return on capital growth. We earned higher fee-based margins, we managed our administrative expenses, we continued to focus on profitable growth including shifting to less capital-intensive products and we earned higher investment spreads.

On slide 10, you can see how our margin, growth and capital initiatives each contributed to the return on capital improvement. First, our margin initiatives, as we expected, were the primary driver contributing 112 basis points of improvement. Initiatives here include re-pricing actions, the run-off of less-profitable assets and aligning costs with lower levels of sales in certain capital-intensive products. Also in 2013, we achieved approximately $30 million in cost savings as part of our plan to realize $100 million in cost savings by 2016.

In addition, as Rod mentioned, there also were several notable items that contributed 42 basis points to margin improvement in excess of what we'd have considered our normalized run rate. And these included limited partnership income, pre-payment fee income and record-keeping change orders. Second, our growth initiatives contributed 39 basis points to the improvement. This partially reflects higher fee-based margins on assets under management and under administration, which was due in part to positive net flows from Retirement and Investment Management and our mutual fund custodial business.

Third, our capital initiatives contributed 40 basis points. This includes reinsurance actions and progress with shifting the composition of our product portfolio to be less capital-intensive. And finally, the headwinds of low interest rates negatively impacted the return on capital growth by 44 basis points. While the impact of low interest rates was factored in into our plan, the increase in rates during the last half of 2013 should mitigate some of the expected impact going forward through 2016.

Now let's look at how the execution of our initiatives is benefiting each of our ongoing businesses and let's begin on slide 11 with Retirement, which improved its return on capital to 8.9% up 170 basis points from 7.2% in 2012. Adjusted for the notable items I mentioned earlier, Retirement's return on capital was 8.5%, 130 basis points improvement over 2012. We are benefiting from the actions that we've taken to improve margins. For example, crediting rate actions reduced rates by 7 basis points in 2013 compared to – with 2012, bringing 90% of policies to the guaranteed minimum interest rates. We also had a 12% improvement in Full Service deposits with an associated improvement in Internal Rates of Return above our 12% IRR target.

In addition to growth, we are also focused on capital initiatives in Retirement and in the fourth quarter, we implemented a capital efficient solution for a block of deferred annuities. Finally, I would also note that we

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remained focused on risk adjusted returns. For example, in January of this year, we completed a transaction that will help meet stable value reserve requirements in an adverse economic condition.

Moving to slide 12, annuities improved its return on capital to 7.3%, that's up 140 basis points from 5.9% in 2012. Adjusted for the notable items, annuities return on capital was 6.8%, a 90 basis points improvement over 2012.

In annuities, we are improving margins through the run-off of the annual reset and multi-year guarantee product. We also grew our fee-based mutual fund IRA custodial product which had a 30% increase in net flows over 2012 to $599 million.

Also supporting our growth efforts going forward will be the new strategic distribution partnership we formed with Allstate. This agreement combines our fixed annuity product expertise with Allstate's broad reach and it enables us to help more Americans meet their need for guaranteed income retirement. It also ensures proper alignment of focus on customers, distributors and investors.

Moving to slide 13, the operating margin for Investment Management increased to 27.7%, up from 24.6% in 2012, unlike our other ongoing businesses, there were no notable items in 2013. And excluding results from Investment Capital, the operating margin improved to 24.7% from 18.4% in 2012. As you know, we focused on operating margin for Investment Management instead of return of capital since this is not a capital intensive business. And one of our key initiatives for margin improvement is to leverage our strong investment performance and we have positive results to show here as well.

As of year-end 2013, 93% of fixed income assets outperformed their benchmark on a five year basis. This is a very strong testament to the great work of our Investment Team. In addition, 84% of equity assets outperformed their benchmark on a five year basis. Likewise, we are pleased with the strong sales performance this year, which helped us grow our third party assets under management by $19 billion in 2013. And what 2013 has clearly highlighted is the scalability of our Investment Management business and our ability to generate revenue that will meaningfully drop to the bottom line.

Turning to slide 14, Individual Life improved its return on capital to 4.9%, up 60 basis points from 4.3% in 2012. Adjusted for the notable item, Individual Life's return on capital was 4.5%. During 2013, we continue to align costs with our new level of sales. In addition, we furthered our capital initiatives in part by shifting our business mix to indexed products, which accounted for 40% of sales in the fourth quarter of 2013 compared with 26% in the fourth quarter of 2012. And moving forward, we will continue to shift our business mix with a view towards improving margin.

Turning to slide 15, the return on capital of Employee Benefits grew to 18.8%, that's up 190 basis points from 16.9% in 2012. Adjusted for the notable items, Employee Benefits' return on capital was 18.1%. Employee Benefits continue to perform well in 2013 as we focused on improving margins in the business and in both the fourth quarter and full year 2013, loss ratios for Group Life and Stop Loss were within or better than our expected ranges.

We continue to invest in Stop Loss sales force training related to prospect identification and information collection. This investment in training has enabled and will continue to enable us to improve our momentum for Stop Loss while maintaining solid risk selection and underwriting.

Finally, in Voluntary benefits sales grew 11% in 2013 compared with 2012 driven by our critical illness, accident and hospital indemnity products. In conclusion, we made significant products with improving returns in 2013.

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Moving forward, we will continue to execute on our margin, growth and capital initiatives with a focus on achieving our longer term return on equity and return on capital targets.

The result of our first year as a publicly traded company combined with the improved interest rate and equity markets has increased our confidence in our ability to reach our targets.

Now, let me turn it over to Ewout who will cover our financial results in more detail.

Ewout L. Steenbergen

Chief Financial Officer & Executive Vice President, ING U.S., Inc.

Thank you, Alain. Good morning, everyone. I will highlight some of our key financial metrics for the fourth quarter and the full year 2013. Slide 17. I will walk you through this quarter's reconciliation from Ongoing Business adjusted operating earnings to net income. All information presented here is on an after-tax basis.

Starting on the left side. The Ongoing Business adjusted operating earnings were $210 million. After positive DAC/VOBA unlocking and the additional gain from the Lehman Recovery, the Ongoing Business operating earnings were $229 million. Including Corporate segment losses of $29 million which is mostly interest expense and an operating loss of $2 million from the Closed Block Institutional Spread Products and other Closed Blocks, we had operating earnings of $198 million in the quarter.

The $2 million operating loss in the Closed Block Institutional Spread Products reflects the recognition of pre-payment fees on the early termination of certain funding agreements. As we look to 2014, we expect operating earnings in the range of $5 million to $10 million for the full year from this Closed Block and this number can fluctuate quarterly.

Then moving to below-the-line items, our Closed Block Variable Annuity segment had a loss of $147 million. This was driven by $177 million in non-performance risk, reflecting a further improvement in our own credit spreads.

In addition to $69 million in net realized gains this quarter, we also had a gain of $263 million in our actuarial pension and post retirement plans, $44 million in losses in other items and $209 million attributable to the difference between the assumed 35% tax rate and our actual tax rate of close to zero. And this brings our total net income available to common shareholders to $548 million.

Then slide 18. We conducted our annual actuarial review of our pension and post-retirement plans during the fourth quarter. As a result, we recorded $405 million in pre-tax actuarial gains driven by the combination of an approximate 90 basis points increase in the discount rate, and strong investment returns in the pension plan assets.

Our funding needs have also declined. We now expect our 2014 cash contribution to be approximately $30 million and that is roughly 40% lower than our cash contribution in 2013. It's worth noting that we use a fair value methodology to account for our pension plan. This approach recognizes non-operating gains and losses in the current period, rather than amortizing them over a multi-year timeframe. This does lead to more volatile results to the bottom line, and we consider this an appropriate trade-off.

Then slide 19. We are managing our business as you know on the basis of three main drivers of operating revenues, beginning with underwriting gains, we saw a decline driven by favorable mortality in Individual Life in the third quarter of 2013, and this was partially offset by sequentially better mortality results in Group Life. Investment spread and other investment income increased during the fourth quarter, benefiting from higher

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prepayment and limited partnership income, and this was partially offset by lower core investment income, which was moderated by crediting rate actions we have taken.

Finally, we continue to see a nice increase in fee-based margins, mostly in Retirement and Investment Management, and these were driven by positive net flows and a strong equity market appreciation in the quarter.

Slide 20, you can see the strong Ongoing Business adjusted operating earnings, we achieved in part by managing our expenses. The 17% year-over-year improvement in Ongoing Business adjusted operating earnings was achieved despite lower investment income, stemming from approximately $600 million lower capital in the ongoing business.

On the expense side, we have managed to hold our expense growth flat year-over-year. Active cost reductions that we have implemented will offset the higher variable expenses related to higher sales and other higher volume effects from some of our businesses during the quarter.

Slide 21, I will quickly give you some color on the underlying performance in each of our Ongoing Businesses. Retirement achieved another quarter of positive net flows. We saw $363 million in the quarter based on sales that are priced at or above our 12% target return level. We generated positive net flows in our full service corporate markets and in our stable value products.

In slide 22, our Annuities business has continued to generate positive net flows into our Select Advantage mutual fund custodial product, where we earned attractive margins. We also saw a second consecutive quarter of positive net flows for our fixed indexed annuities. Strong distribution momentum, helped by the rising rate environment, contributed to this positive result. At the same time, we saw a continuation of the outflow of low and negative margin products such as the Annual Reset and the Multi-Year Guaranteed Annuities. These outflows also helped in reducing the capital held for this business, thereby improving the return on capital.

Slide 23. We saw a solid commercial performance in Investment Management where net flows were $1.3 billion excluding variable annuity outflows. The strong flows were led by [ph] senior loans (0:26:47), CLOs and alternatives, and those are all higher fee asset categories. We did not have any non-ING U.S. sub-advisor replacements during the quarter. As we have previously indicated, these flows tend to vary quarter-to-quarter.

At the bottom of the chart, you will see that the Closed Block Variable Annuity outflows for the funds that are managed by Investment Management were $651 million. Including the Variable Annuity Outflows, Investment Management net flows were $646 million.

In slide 24, this slide shows that we continue to execute on our strategy to shift our Individual Life business to less capital intensive products. In conjunction with the sales shift, we have right-sized our expenses relative to the new scale of the Individual Life business. Looking ahead, we're focused on growing our indexed Universal Life business.

In slide 25, Employee Benefits total sales were up year-over-year. As this chart illustrates, sales in this business are lumpy with the majority of sales occurring in the January and July renewal periods. To date, we have been encouraged by our efforts to drive Stop Loss sales while maintaining our underwriting discipline.

For the quarter, our Group Life loss ratio was 72% while our Stop Loss loss ratio was 78.4%. For the full year, the loss ratios for both Group Life and Stop Loss were within or better than our targeted range of 77% to 80%.

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Then turning to slide 26, in the Closed Block Variable Annuity, our hedge program largely offset the change in statutory reserve liability as a consequence of equity market movements during the quarter. Our hedge program for the Closed Block Variable Annuity continues to perform well in protecting regulatory and rating agency capital from market movements.

The estimated available resources for the Closed Block Variable Annuity segment are $4.1 billion and the net amount at risk for the living benefits declined by roughly $900 million during the quarter to $2.2 billion and that is now lower than the estimated $2.4 billion in statutory reserves for the living benefits. The net outflows were $1.1 billion for the quarter which translates to a 10.2% annualized net outflow as a percentage of the beginning of period assets.

Then at the bottom of this page, you see the new sensitivity tables for the end of the fourth quarter for both regulatory capital as well as GAAP earnings, for equity market movements and interest rate movements. We will provide an update to our 50-year cash flow scenarios that we originally provided during the IPO Road Show no later than our first quarter 2014 earnings call.

And then finally, slide 27, you can see that our combined estimated risk-based capital ratio at the end of the fourth quarter was very strong at 504%. The RBC ratio improved relative to the third quarter, primarily reflecting statutory pre-tax income earned during the quarter, and a reduction in risk-based capital due to the update of the NAIC factors.

The re-domestication of our re-insurance subsidiary, Security Life of Denver International, in December, had no effect on the overall capital position of ING U.S., the CBVA book, the reported combined RBC ratio, or our holding company cash level. Given our strong capital position, we get many inquiries about when we might provide an update on our capital return plans.

I would like to remind everyone that our plan is to finalize our statutory reporting at the end of the month, conduct an assessment of our capital position and our long term operating plan, review it with our Board and report back to investors at the latest, during our first quarter 2014 earnings call.

As you can see on the right-hand side of the slide, the debt-to-capital ratio at the end of the fourth quarter further declined and is now 23.5%, slightly better than our target of 25%. In the Appendix section, we have added a slide highlighting the seasonality we experienced in our business. This should give some improved insight into our business trends. For example, we have lower performance fees and higher FICA payroll taxes in the first quarter. As a reminder, we benefited from pre-payment and limited partnership income in the full year 2013 and it also helped in the fourth quarter.

In summary, we delivered strong financial results both this quarter and for the full year as we continue to focus on increasing margins, running off less profitable businesses, strengthening our balance sheet, generating free cash flows, and protecting regulatory and rating agency capital for the Closed Block Variable Annuity.

And with that, let me turn it back to the operator, Emily, so we can take your questions.

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QUESTION AND ANSWER SECTION

Operator: We'll now begin the question-and-answer session. [Operator Instructions] Our first question is from Nigel Daly of Morgan Stanley. Please go ahead.

Nigel Dally
Analyst, Morgan Stanley & Co. LLC

Q

Great, thank you. First question just on capital, in trying to assess the amount of excess capital, we know that for 425% is your target. But in looking at the amount of capital potentially available for buybacks, would you be looking at maintaining some sort of buffer above that? Or are there any things with regard to getting dividends out of the subsidiaries that we should be aware of? I'm just trying to get some sort of appreciation as to how much of the excess capital is really readily deployable for buybacks and dividends.

Ewout L. Steenbergen
Chief Financial Officer & Executive Vice President, ING U.S., Inc.

A

Nigel, good morning. This is Ewout. If we look at the RBC level of 405%, that translates into approximately $1.1 billion of excess capital above the 425% level. A part of that is available in terms of ordinary dividends. So we expect approximately $800 million to be available in ordinary dividend and we will have some other consideration to be made. We have some holding company expenses during the year. We have to think about some buffers, some recapitalization and rebalancing of capital between entities and then we have to determine what is available in terms of excess capital. It is simply too early to give you a number at this point in time because we still have to go through that exercise and we first have to close our statutory financial statements, which we will do at the end of this month.

So as we stated before, we will come back to you at the latest when we announce our first quarter earnings early May with a precise detail on our excess capital and our return plans.

Nigel Dally
Analyst, Morgan Stanley & Co. LLC

Q

Okay. That's very helpful. Just a couple of...

Rodney O. Martin
Chairman & Chief Executive Officer, ING U.S., Inc.

A

Just to clarify one number that Ewout spoke about, it's 504% and then everything else followed.

Nigel Dally
Analyst, Morgan Stanley & Co. LLC

Q

Right. Right. Then just a couple of quick numbers questions. Closed Block ISP, I understand results were negatively impacted by a prepayment penalty. Can you quantify the impact there? Then on alternatives, clearly solid quarter but looking forward, can you discuss what you would consider to be a normalized return on those investments?

Ewout L. Steenbergen
Chief Financial Officer & Executive Vice President, ING U.S., Inc.

A

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Nigel, the answer on your first question is the amount for the prepayment penalty that was in relation to an early termination of some FHLB funding was $13.9 million.

Nigel Dally
Analyst, Morgan Stanley & Co. LLC

Q

Okay.

Ewout L. Steenbergen
Chief Financial Officer & Executive Vice President, ING U.S., Inc.

A

And then in relation to our normalized alternative investment income, the assumption, long-term assumption we use is 9%.

Nigel Dally
Analyst, Morgan Stanley & Co. LLC

Q

Okay. Perfect. Thanks very much.

Operator: Our next question is from Erik Bass of Citigroup. Please go ahead.

Erik J. Bass
Analyst, Citigroup Global Markets Inc. (Broker)

Q

Hi. Thank you. I guess one question on the captive consolidation. I appreciate that there's no meaningful impacts to RBC or capital. But are there any tax implications particularly around the usage of the deferred tax assets?

Ewout L. Steenbergen
Chief Financial Officer & Executive Vice President, ING U.S., Inc.

A

Erik, good morning. The short answer is, as a side effect of the re-domestication, there might be some tax benefits. Let me elaborate a bit on that. The deferred tax assets in relation to Security Life of Denver International so far were held offshore, and we could not use onshore income to offset and to use those DTAs.

Now, SLDI is part of the onshore entities. There might be a possibility to use those DTAs in the future. As you know, the tax position of the company is very complicated and we have to take into account many assumptions and judgments. So, we don't know exactly how much we could use in the future, but there might be a benefit of the re-domestication as a side effect.

Erik J. Bass
Analyst, Citigroup Global Markets Inc. (Broker)

Q

Okay. Thank you. And then, I guess, on Investment Management flows, and clearly it's still positive but the pace has slowed from earlier on the year. Can you just talk a little bit about the flow dynamics you're seeing? And also, I mean, do you still see additional opportunities for sub-advisory replacements going forward?

Alain M. Karaoglan
Chief Operating Officer, Director & Executive VP, ING U.S., Inc.

A

Yes. So – Eric, thank you, it's Alain. The flows are in line with our expectations. If you think about the areas that were generating these flows are our senior bank loan team, alternatives with prices of equity and an alternative fund and equity were the areas that generated flows. So depending on market conditions, these areas are either of interest to investors or not and they will generate additional flows.

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In terms of the sub-advisor replacement, we do have additional opportunities going forward. As I mentioned earlier, our performance both in fixed income and in equity is very strong and it compares very well to the market and to other players. And as long as that's the case that will provide us with additional opportunities for sub-advisor replacement going forward that will be beneficial to our clients.

Erik J. Bass
Analyst, Citigroup Global Markets Inc. (Broker)

Q

Okay, thank you.

Operator: Our next question is from Mark Finkelstein of Evercore. Please go ahead.

Mark Finkelstein
Analyst, Evercore Partners (Securities)

Q

Hi. Good morning. My first question relates back to capital, if you just look at the fourth quarter, rough calculation is somewhere in the [ph] 450 to 475 (0:38:38) of stat capital generation and I know you identified some specific items that influenced that. Can you just walk through what those were, I assumed some was from the [ph] MIB (0:38:50), but can you just walk through what those kind of abnormal capital generation items were?

Ewout L. Steenbergen
Chief Financial Officer & Executive Vice President, ING U.S., Inc.

A

Mark, maybe if I may – I ask to clarify the question, do you refer to the RBC ratio movements and the capital development there?

Mark Finkelstein
Analyst, Evercore Partners (Securities)

Q

Yes.

Ewout L. Steenbergen
Chief Financial Officer & Executive Vice President, ING U.S., Inc.

A

Or do you mean the capital on a GAAP basis?

Mark Finkelstein
Analyst, Evercore Partners (Securities)

Q

No, no, no, statutory.

Ewout L. Steenbergen
Chief Financial Officer & Executive Vice President, ING U.S., Inc.

A

Okay. So if you look at the improvement of the RBC ratio during the quarter, we saw a change in total adjusted capital of $164 million. And that was mostly driven by the pre-tax statutory income.

At the same time, we saw a reduction of the RBC requirements of $370 million and that is at the 425% level. And that is reflecting changes in the NAIC factors with respect to commercial mortgages, RMBS and CMBS, but mostly commercial mortgages NAIC factor update. So, you could say approximately 25 RBC points is coming from those factor updates.

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Mark Finkelstein
Analyst, Evercore Partners (Securities)

Q

Okay. That's very helpful. And then my follow-up question relates to the statutory variable annuity – Closed Block Variable Annuity, $4.1 billion of kind of capital resources, $2.2 billion of living benefit reserves. Can you just walk through what represents the difference between those? I know last quarter you had $800 million of death benefit reserves and some asset adequacy reserves. Is there a way of framing out how those numbers have changed and, perhaps, how much is true capital?

Ewout L. Steenbergen
Chief Financial Officer & Executive Vice President, ING U.S., Inc.

A

Mark, the $4.1 billion is build up by the following components. $2.4 billion is the statutory reserve, the living benefit as we already stated. Then we have $500 million, which are the death benefit reserves. There are approximately $400 million cash flow testing reserves. And then the other $800 million is unassigned. So, those are additional assets we have available above the statutory reserves and the cash flow testing reserves.

So, that is the composition of the $4.1 billion. We have currently no letters of credit outstanding on this block anymore.

Mark Finkelstein
Analyst, Evercore Partners (Securities)

Q

Okay. So, the cash flow testing reserves went down roughly $400 million sequentially?

Ewout L. Steenbergen
Chief Financial Officer & Executive Vice President, ING U.S., Inc.

A

Yes. I think I probably haven't specifically spiked out the cash flow testing reserves last time, so it's hard to comment on that right now, Mark.

Mark Finkelstein
Analyst, Evercore Partners (Securities)

Q

Okay. All right. Thank you.

Operator: Our next question is from Ryan Krueger of Dowling & Partners. Please go ahead.

Ryan Krueger
Analyst, Dowling & Partners

Q

Hey, good morning. I had a question on Individual Life. You took out a fair amount of expenses in 2013. Just thinking about the trajectory of ROC improvement going forward, is the main thought that the improvement will just come from writing new business with better returns? Or do you also think you can do more things to improve the in-force returns there as well?

Rodney O. Martin
Chairman & Chief Executive Officer, ING U.S., Inc.

A

Ryan, good morning it's Rod.

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Ryan Krueger
Analyst, Dowling & Partners

Q

Good morning.

Rodney O. Martin
Chairman & Chief Executive Officer, ING U.S., Inc.

A

Two components to the answer. So first, we think we're at a run rate basis for new business that is roughly in the $100 million to $125 million base as we project forward. And that's roughly $50 million in term of the balance in our indexed Universal Life portfolio and a little bit of Variable Life.

The other piece I'd remind you is we are not presently a tax payer, and that has an impact. And the second piece is we're going to continue to be very diligent on the focus on expenses go forward. So we took some very aggressive actions that we thought were appropriate by reducing the expenses over 13% in 2013. We think we're at the right level and we're going to continue to move forward.

The protection element and the asset accumulation element of our Life products is very important to our overall retirement readiness strategy. And so we're going to continue to move forward and keep you updated with the progress we're making.

Ryan Krueger
Analyst, Dowling & Partners

Q

Okay. Great. And then just a quick one. Can you say what the holding company liquidity was at the end of the year and how it compares to your target?

Ewout L. Steenbergen
Chief Financial Officer & Executive Vice President, ING U.S., Inc.

A

Holding company liquidity was approximately $600 million at the end of the year. And you know our target is a 24 months holding company needs in liquidity, which translates to approximately $450 million, so we're holding a little bit higher balances at the holding than our targets.

Ryan Krueger
Analyst, Dowling & Partners

Q

All right. Thank you.

Operator: Our next question is from Steven Schwartz of Raymond James & Associates. Please go ahead.

Steven D. Schwartz
Analyst, Raymond James & Associates, Inc.

Q

Hey. Good morning, everybody. Just a follow-up on Life, what did you guys think about mortality in the quarter? I know it was – you had very favorable mortality in 4Q 2012. I'm wondering what do you think about it into this quarter?

Rodney O. Martin
Chairman & Chief Executive Officer, ING U.S., Inc.

A

Hey, Steven. It's Rod.

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Steven D. Schwartz
Analyst, Raymond James & Associates, Inc.

Q

Hey, Rod.

Rodney O. Martin
Chairman & Chief Executive Officer, ING U.S., Inc.

A

On average, it was approximately 90%. So as we look over the last eight quarters, by way of example, it is roughly averaged that outcome. So it was within our average expectation for the quarter, which we were pleased with, and that's approximately what we would expect go-forward.

Steven D. Schwartz
Analyst, Raymond James & Associates, Inc.

Q

Okay, great. And then on the investment performance, I'm going to ask two quickies, on the investment performance, Alain, you referenced the five-year numbers. How does that look on one and three? Is there very much difference?

Alain M. Karaoglan
Chief Operating Officer, Director & Executive VP, ING U.S., Inc.

A

So on the fixed income side, this has constantly improved. And so I think last year, the number, if we had on the five-year program, have been significantly lower, so 94% is significantly up from that level.

Steven D. Schwartz
Analyst, Raymond James & Associates, Inc.

Q

Okay.

Alain M. Karaoglan
Chief Operating Officer, Director & Executive VP, ING U.S., Inc.

A

So you could see that the one year, three year and five years. On the equity side, the one year performance would be weaker than the five-year performance. A part of it is our investment philosophy. Our investment philosophy is research-driven, quality-driven, sustainable institutionalized process. And in market that are extremely positive, we will tend to outperform in these markets. As markets become more normal or subdued, the quality bias shows and the performance and we outperformed.

Steven D. Schwartz
Analyst, Raymond James & Associates, Inc.

Q

Okay. And then if I may, just one more, on the tax rate, the assumption is a 35% tax rate and I think the assumption always was that the DRD would go away. We have the two -year budget agreement, it seems unlikely to me that the DRD will go away. Is there any thought about to possibly changing that guidance and of course that would affect the value of the DTA as well?

Ewout L. Steenbergen
Chief Financial Officer & Executive Vice President, ING U.S., Inc.

A

If we look at the effective tax rate for the company that is mostly driven by the tax valuation allowances we have on our books. So what is happening is when we generate income, we're able to release on tax valuation allowances and driving the effective tax rate close to zero, and the other way around in case the company has an overall [ph] net and net (0:46:19) loss.

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There are other moving parts as you are mentioning, the DRD, some other tax credits, and other items. If you look at the effective tax rate for the quarter it was in fact minus 4%, so in fact we had a small tax benefit on an overall income level pre-tax for the company. And those differences in those few percentages, there you will find the effect of the DRD. So in other words, there's clearly a benefit of the DRD and if that continues it will benefit our effective tax rate. But the main driver between the 35% and zero is coming from the tax valuation allowances.

Operator: And our next question is from Yaron Kinar of Deutsche Bank. Please go ahead.

Yaron J. Kinar
Analyst, Deutsche Bank Securities, Inc.

Q

Good morning, everybody. If we go back to the Life, the Individual Life business for a minute, it seems to be tracking maybe a little below what the target was, and I'm just curious, with the new management in place there, are there any changes to the strategic initiatives and the targets in the long term?

Rodney O. Martin
Chairman & Chief Executive Officer, ING U.S., Inc.

A

Yaron, it's Rod. Good morning. One of the benefits of the transition that we've done with Butch Britton and with Mike Smith is, I think, it demonstrates two things. One, the bench strength we had to draw on and, we're very pleased for that, and Mike's been with the organization, so he knows the strategy, the people and the organization well. That said, our fundamental strategy hasn't changed.

Shifting from where we were was a significant change, and it takes a period of time to work through as we've discussed in previous periods. We have been very aggressive at aligning expenses with the current run rate of sales. As I mentioned in one of the earlier questions, we'll continue to be vigilant about that go-forward. We've been very active, Butch, Mike, myself and others in communicating our strategy to our distribution platform, and I think it's being well received.

In terms of our focus being broadly on middle market term portfolio, in our indexed Universal Life portfolio for both asset accumulation and asset protection. So, I feel good about where we are. We've got a solid base to build on, and we'll continue to be vigilant. We're very mindful about where the returns are and what our objectives have been outlined, and we're going to work very, very vigilantly to continue to close that gap.

But I think the fundamental strategy, as we discussed in May, hasn't changed as we go forward. We're simply in the implementation mode of that.

Yaron J. Kinar
Analyst, Deutsche Bank Securities, Inc.

Q

Okay. And then in the Annuities business, do you have any sense or are you able to quantify the impact of the Allstate strategic partnership?

Alain M. Karaoglan
Chief Operating Officer, Director & Executive VP, ING U.S., Inc.

A

We – Yaron, as you might appreciate, we're not going to quantify the impact. But it's an important partnership. As we execute on that and develop our relationship and the relationship with the distribution of Allstate and the agents, and we would report results as they become more meaningful, we'll highlight them to you. But we're very

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excited about it. It hits our strategy on many front. It's a testament to our capabilities on the fixed annuity side, and also the way we would like to operate going forward.

So we're very excited about it. We're looking forward to the results. We're not willing at this stage to quantify it, but keep posted, we will update you of that over time.

Yaron J. Kinar
Analyst, Deutsche Bank Securities, Inc.

Q

Let me try maybe one other approach at it. Do you think it would – or can you operate any assessment whether it would be accretive to this year's earnings?

Alain M. Karaoglan
Chief Operating Officer, Director & Executive VP, ING U.S., Inc.

A

Yaron, excellent try. Thank you for trying.

Yaron J. Kinar
Analyst, Deutsche Bank Securities, Inc.

Q

Thank you.

Operator: Our next question is from Eric Berg of RBC Capital Markets. Please go ahead.

Eric N. Berg
Analyst, RBC Capital Markets LLC

Q

Thanks and good morning to everyone. I won't ask about the earnings from the Allstate business, but I would like to understand a little bit better than I do the philosophy behind the partnership. And by that I mean this, if you were withdrawing from or reducing your exposure to the MYGA business, the Multi-Year Guaranteed Annuity, and the Annual Reset, what is structurally different about the Allstate arrangement that makes it attractive, but your existing MYGA and Fixed Annuity business, a business that you're withdrawing from?

Rodney O. Martin
Chairman & Chief Executive Officer, ING U.S., Inc.

A

Eric, good morning.

Eric N. Berg
Analyst, RBC Capital Markets LLC

Q

Good morning, Rod.

Rodney O. Martin
Chairman & Chief Executive Officer, ING U.S., Inc.

A

The second part of your question in terms of what's fundamentally different, we are pricing this business consistent with the targets that we have outlined to you and to others. So we're able to price this, and I think it brings together the strength of our manufacturing capabilities and the strength of Allstate's distribution platform, 11,000 captivations and price that at or above our targeted returns.

And candidly the MYGA business as we've discussed in – when we did the Road Show and in subsequent periods, simply didn't meet those returns and that's why we're running that business off at faster rate as we can at this

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point in time. So, it really goes back to kind of the fundamental shift in culture in the company for when we started.

And we'd talked about a value-creation focus tied to the three metrics that we discussed, certainly with you and all others on the call. And as risk-adjusted return sales are at or above our targeted IRRs and distributable earnings and we are bullish about our distribution capability and our ability to partner with Allstate and we would certainly look for other like arrangements assuming they can meet or exceed our targeted returns.

And that's – it's no more or less complex than that.

Eric N. Berg
Analyst, RBC Capital Markets LLC — Q

Got it. My second and final question is aimed at even sharpening further, Rod, your comments about administrative expenses in Life. I don't think in the December quarter they changed all that much, relative to the year ago quarter or if there was progress, it appeared to me to be modest. When you say that as you look forward you will be vigilant about expenses, does that mean that they will go lower or does that mean that they will be controlled?

Rodney O. Martin
Chairman & Chief Executive Officer, ING U.S., Inc. — A

Good question, Eric. And I would say they'll be controlled. So most of the stuff that we put in motion was reflected before the fourth quarter, so that's an excellent observation and they certainly will be controlled. And we're really talking about the administrative expenses associated with the run rate of the new business levels. We're going to continue, as reflected in the slide that Ewout talked about in the early part of the deck, if you look at the aggregate expense level and particularly take into consideration, we grew our business, in total, from our three business segments. The aggregate expense level, in light of that, was still flat for the year. I think it shows that we've been very disciplined about controlling the expenses and it will be on a go-forward basis.

Eric N. Berg
Analyst, RBC Capital Markets LLC — Q

Thank you.

Operator: Our last question is from Chris Giovanni of Goldman Sachs. Please go ahead.

Christopher A. Giovanni
Analyst, Goldman Sachs & Co. — Q

Thanks so much. Good morning. I know a lot of focus around capital and timing of when you could deliver something, but could you just remind us kind of your key priorities in terms of rank order uses of capital?

Ewout L. Steenbergen
Chief Financial Officer & Executive Vice President, ING U.S., Inc. — A

Chris, good morning. This is Ewout. We have not determined in which way if we come to the conclusion that we have some excess capital during this quarter. We have not concluded in which way we would like to return that to shareholders. All the options are on the table. It can be an increase of our dividends. It can be share buybacks or other options. We will come to a conclusion on that over the next few weeks and try to get the approval from our Board for that proposal. But clearly, the driving factor behind our thinking and conclusion will be what is in the interest of our shareholders, the value maximizing outcome in terms of return of capital.

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Christopher A. Giovanni
Analyst, Goldman Sachs & Co.

Q

Okay. And then, I guess, around the ROE improvement that we saw in 2013, I guess, certainly better than, I think, what we, many and maybe even you guys have in your original assumptions. So, kind of wondering what this means for the 2016 target? Is it purely your ability to achieve this is maybe pulled forward some or is it maybe the pace of improvement starts to moderate a little bit from what we saw this year?

Rodney O. Martin
Chairman & Chief Executive Officer, ING U.S., Inc.

A

Chris, it's Rod. So, two-part answer. One is as you heard me say in the opening remarks and you certainly had heard from all three of us over a period. On average, we expect the ROE to improve 100 basis points to 110 basis points a year. We talked about some notable items that were – we benefited from and were being very consistently transparent in the discussion of that and the revealing of that both on this call and in the – in our communication.

If you make an assumption that macroeconomics continue, what we've – in the way that they have, what we said is we will – we're staying vigilant to these targets. If those factors enable us to accomplish our 2016 objective sooner of 12% to 13%, then we'll consider raising the targets at that time.

And I think I point to Prudential when they went through a similar path of laying out three or four-year targets hitting them, raising the targets, hitting them and so on and so forth. And that's certainly a model that we are wanting to follow.

We think just barely or not even a year into being a public company, we laid out a very aggressive plan. We feel very good about the pace of accomplishment. We're trying to be very clear about what has contributed to it in terms of what were notable. And we'll continue to communicate in that way go forward. But our eye is on accomplishing what we said. I'll reinforce that's a point in time number. That's not a ceiling and that will be based on market conditions at that point in time.

But we look forward to continue to make progress in 2014 and on – as we've discussed earlier on the call.

Christopher A. Giovanni
Analyst, Goldman Sachs & Co.

Q

Okay. Thanks. And last question, obviously the next kind of big – or one of the next big milestones is around the rebranding initiative. Can you talk again about just the expenses you guys are associating with that? And then how we should be thinking about that from a timing perspective?

Ewout L. Steenbergen
Chief Financial Officer & Executive Vice President, ING U.S., Inc.

A

This is Ewout. What we have earlier disclosed is that we will expect to incur expenses with respect to the operational rebranding of $50 million over 2014 and 2015. So, for both years combined, $50 million, and that relates to changes in our IT systems, that relates to changes with our legal entity names and other matters. It does not include an advertisement budget in terms of announcing to the markets the name change. [ph] That (0:58:02) advertisement budget has not been determined yet, so we don't have a number for you for the additional marketing expenses we have to do in a short period of time.

But in respect to the operational rebranding, it's that $50 million and that's still our best estimate as we speak.

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Christopher A. Giovanni
Analyst, Goldman Sachs & Co.

Q

Okay. Sorry and then one follow-up, the $50 million, is that in your ROC and ROE targets or not? And then, equally, is there marketing rebranding, whatever that number will be, is that embedded within your targets?

Ewout L. Steenbergen
Chief Financial Officer & Executive Vice President, ING U.S., Inc.

A

Those will show up as non-operating expenses. So, they will not be part of the ROE or ROC numbers.

Operator: And this concludes our question-and-answer session. I'd like to turn the conference call back over to Rod Martin for any closing remarks.

Rodney O. Martin
Chairman & Chief Executive Officer, ING U.S., Inc.

Emily, thank you. We're pleased with the results for the fourth quarter and the full year, and we're making steady progress with our transformation story. ING U.S. is a premier franchise with leading positions in attractive markets and we're investing in our growth.

We're continuing to execute on our ROE improvement plan, we will continue to build on our solid foundation which is based on the recapitalized and de-risked balance sheet. We have a lot of confidence as we head into 2014 based on our track record and continued focus on execution.

We have three solid businesses. We have quality products and services meeting our customer, clients' needs for asset accumulation, protection and distribution. We are an exciting new brand.

We have an experienced management team across the entire enterprise. A couple of weeks ago, we announced the retirement of our Insurance Solutions CEO, Butch Britton. Butch is a great leader, colleague and friend to all of us, he will be missed. Fortunately, we had a strong and experienced Life Insurance and Annuity veteran in Mike Smith in place to succeed Butch as the CEO of Insurance Solutions.

We're saying farewell to a strong leader, however, we're transitioning to someone as I mentioned moment ago, who also a very strongly understands ING U.S., our strategy and our people. It will be a seamless transition and our distribution partners and customers will benefit from that.

The same is true for Chet Ragavan, who has succeeded Mike Smith as our Chief Risk Officer. Chet has been with ING U.S. for more than six years. He has also joined our Executive Committee. And we're fortunate to have the bench strength to make these moves from within the organization.

With that, we'll conclude our call. Thank you and have a good day.

Operator: The conference is now concluded. Thank you for attending today's presentation. You may now disconnect.

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