Voya Financial

December 8, 2020
11:40 AM EST

Yaron Kinar: Good morning, everybody. I'm Yaron Kinar, Goldman Sach's insurance analyst. And I'm very happy and pleased to have Voya's Chairman and CEO, Rod Martin; and CFO, Michael Smith with us today. I'm going to open up with questions. We'll dive right into the Q&A. But as a reminder to the audience, if you have any questions, there is a button at the bottom or a box at the bottom of your screen. And if you have any questions, please send them over our way.

With that, let's start with a high-level question. What have been some of the key messages that you've been sharing with investors as you approach year end?

Rodney Martin: I'm happy to start. And again, good morning. And good morning, everyone. Look, a natural question that we've had and a message we've shared is where we are with the life transaction. And I'm pleased to say that we are operationally and financially ready to close the life transaction. We expect the regulatory decision on the 17th of December. And as we've previously communicated, we would expect to close on January 4th, the first business day of 2021. But we've made great progress on that front, and that's been naturally a key focus of ours, and a key question from investors.

In terms of our ongoing business, some themes, in retirement we're expecting, as we've previously discussed, $1 billion to $2 billion in full-service net flows. We've added over 400,000 new participants this year. And again, in a COVID year, we feel very good about the picture there. In investment management, we expect to continue to exceed our 2% to 4% organic growth. We've had over $12 billion of flows this year, which is counter to some others in the industry. And in employee benefits, we've experienced continued strong success there. And I think part of that is our workplace-focused model. So it's really a B2B model. And it's grown very nicely. The renewal season has progressed as we've expected, and that business continues to be our fastest-growing business and one of our best-preforming businesses.

Yaron Kinar: Mike, anything you want to add?

Michael Smith: Maybe just to talk a little bit about the operating environment, right? I mean it's a been a

challenging year, right, with the pandemic and moving to virtual. But I think we've done that seamlessly. And so part of what we've been talking about is where we see that work environment evolving to. And a real focus on our part of thinking about this less from a -- what can we do to reduce floor space, how can we change our lease profile, and very much thinking about it in terms of talent; both in terms of attraction and retention, and creating a better work environment throughout while they're here. And then we think that will be beneficial to the culture, as well as ultimately our overall success. Yes, there will be real estate changes. Yes, that will create some opportunities. But we're really thinking about it more from that standpoint. So working well, made the adjustment quickly, really interested and intrigued by the opportunities ahead.

Yaron Kinar: Got it. So you touched on the life sale. Once that's completed, the company's gone through a lot of transformation, right, in terms of rightsizing the business and really getting into more of a workplace and financial institution focused platform. Once that life deal is done, is there white space that you're looking to fill?

Rodney Martin: I think it's a great question. And again, I'd point out two parts, that we're very pleased in kind of the from-to journey, from what we inherited from ING Group to what we've chosen to lean into, again workplace and financial institution, is complete and behind us. 2021 will be the first full year that we will not be focused on those activities, the de-risking activities, and fully focused on our go-forward picture built around this platform. So at the heart of your question, I think you're going to see us leaning in even more to the workplace and the financial institution focus, on both organically, potentially inorganically capabilities that can enhance that growth and supplement that growth. But it will be fundamentally built around that.

And Yaron, as you know, we're two years into our three-year plan. We will be having an Investor Day in the second half of 2021, which will lay out our '22, '23, and '24 plan. Mike Smith, Mike Katz and our business leaders; we've been working all year long, as we would in any normal year, in the ideation around that. And I'm very pleased with the progress that has been made, and we're anxious to share that at the appropriate point. But it will be an extension of where we are. And I love the fact that all of our energy is forward-looking. Our capital will never be stronger. Our liquidity position will never be stronger. And we'll get into the sources and uses of all that I'm sure in the course of this conversation.

Yaron Kinar: Right. And maybe we can also touch on kind of how to think of income statement and balance sheet sensitivity once the life book is sold?

Rodney Martin: Mike, do you want to start?

Michael Smith: Sure. Yaron, so bottom line is in the short run, while eliminating the life transaction I think takes off a significant amount of tail risk and sort of the volatility that comes from mortality. It's not going to have a particularly profound impact on equity market sensitivity. That remains where it's been for a long time. Our earnings will move $4 million to $5 million for every 1% change in the S&P. We did give interest rate guidance that was pro forma for the life transaction back earlier this year, which was that a 100-basis point drop would product a $10 million impact this year and incremental $25 million in '21, and then another $25 million in '22 if it stayed at that new level, right?

So it would be an acceleration of the compression of spreads. But the life business was a relatively small contributor to that over the short run because of the length of the assets and the length of the liabilities.

Yaron Kinar: Got it. Okay. So Rod, you'd said that we're probably going to get into uses of capital. So here we go. So I think you expect to release about a $1.5 billion of capital when the life deal closes. I think you've talked about $600 million to $800 million that you plan to use to de-lever the balance sheet. I think you've then updated that to maybe coming at the lower end, because of where spreads were. So maybe the first question would be, we have seen some credit spread tightening. So has your thinking around that $600 million to $800 million number changed at all?

Rodney Martin: Mike, why don't you start with the credit piece, and then we'll go into the second part of that?

Michael Smith: Yeah. So the short answer is not really. While the credit spreads have continued to tighten, there's been a little bit of a move up in the underlying curve, right? So net-net it's not meaningfully different. And I think we gave a range for a reason, which is it's going to move around a bit. But look, the way to think about this is at close, there will be somewhere in the neighborhood of a billion-dollar gain on the assets that we sell to the trusts that will support the reinsurance portion of the transaction. That will offset a loss that we've already booked on the portions of the business that we'll sell. And so that gets us to a net impact of the transaction of somewhere around zero to 500. That restores our leverage to a place that is below our target. Then as you go forward and presuming we buy back shares, we'll have to continue to buy back debt to kind of keep the leverage ratio where we want it. And we're targeting -- I think we've said 600 to 800 of total debt repurchase, assuming everything gets applied to-- or the balance gets applied to the share repurchases.

I'd only point out that those numbers were calculated on the basis of returning us to the leverage at the time we announced the transaction, and that was actually meaningfully below the target of 30. That was at 27 and change. So there is a little wiggle room there, and we'll certainly do it as we make our way through the uses of capital, and maintain -- the key is that we'll be focused on maintaining a leverage ratio below 30.

Yaron Kinar: Okay. Maybe on that, so the company is becoming a more and more capital-light company through these deals. So why is the debt leverage target a below-30 target? Why can't that go up as you become less capital intensive and more capital generative?

Michael Smith: Well, it can, and actually it has, right? So if we go back to before the annuity transaction, we were at 25%, right? So one of the key changes we made as a consequence of selling the VA business was recognizing that we could take a bit more risk. We already increased up to a 30%. Over time, to the extent that our business mix continues to shift toward more fee-oriented, less long-term promise oriented, I think there's an opportunity for us to look at that. But that is more of an evolutionary step. It's not something that happens in rapid succession. In working with the agencies over the years, they are very comfortable with changes that burn in over time. They're not very comfortable with sort of lots of quick stairsteps. And I think our business still needs solid ratings to be successful in a

commercial sense. Our ratings matter. We do make long-term promises in the fixed account on the retirement side. We do offer protection. And the customers and distribution pay attention to that, not to mention wanting to continue to have a credit rating that is supportive of being able to raise funds when we need it at attractive rates.

Yaron Kinar: Got it. And then I guess the other aspect of capital deployment, and I'm just looking at my screen here, questions coming in from the audience on buybacks. What are your thoughts around buybacks? When should investors expect to see maybe your resumption of the buyback program? How do you prioritize buybacks versus other uses of capital?

Rodney Martin: Well, I'll begin, and Mike and I have -- look, a very fair question and we've talked about this regularly through the course of the year. So let's go back to the beginning of the year. As we turned the calendar going into '20, we had communicated our intention for '20 was to buy back approximately a billion dollars of shares. In the first quarter we did $436 million, so a little -- and by the way, if you look at the $6.4 billion that we've done, in '18 and '19 it was approximately a billion dollars. Our intention going into '20 was approximately a billion dollars. And that was done pretty ratably as we went through the year. And that philosophy really hasn't changed in terms of prospective. So what we've said all along is we're paying attention to the broad macro environment, the election, the stimulus, COVID, and the life transaction.

And although there has been progress on many but not all of those fronts, we certainly in closing the life transaction, the election behind us, hopefully clarity on stimulus; beyond having the discussed election and understanding what those implications are, COVID is still very real, although as Mike shared with you, all trending well within the parameters we laid out. But we are paying a heck of a lot of attention, as we think everyone should be, to what happens in the next four or five or six months. We're very encouraged about having a vaccine. But that certainly is a second half of '21 picture more than a first half of '21. So that said, I think one should look at a resumption of buybacks as we go into the year in a manner similar to what we have talked about previously. We are intending on the fourth quarter call, Mike -- and maybe I'll throw it to you, to update on a number of factors, including that. And why don't you share that and certainly as we've talked, we will have an Investor Day in the second half of the year where we'll lay out some longer-term guidance at that point. Mike?

Michael Smith: Yeah. To the question of future guidance which is certainly pertinent to the question of share repurchase, our expectation is that we'll be in a position on the fourth quarter call to give a sense for how '21 is looking from an earnings standpoint, as well as to lay out at least a range of what we might see from a share repurchase in the year. That all depends a little bit on what happens between then and now. If we get a really strong curveball somehow economically or we see significant deterioration in the ratings environment or something like that. But right now I don't see that happening. That seems like more of a -- that would be very much closer to an anomaly than an expectation. So that's where we're headed, as we think we'll have a pretty good ability to give everyone a sense of where we see the year coming in.

Yaron Kinar: Got it. Maybe kind of taking one step back, we talked about the deleveraging at the Hold Co. How should we think about that being the RBC target? So I think it's been at 400%. Now with the life insurance business again, with that deal closing, is there room to

further lower that number?

Rodney Martin: So Mike, maybe you start, but go back -- and where it was, where we moved, and what our thinking was? Because there has, again, been a migration of this. Mike?

Michael Smith: Yeah. This will be kind of a replay of the answer on that leverage ratio, right, except for different facts, right? So we did lower the RBC target as a consequence of annuity transaction from 425 to 400. And I think we've been there now for a couple of years. I think that's a comfortable place for us to be at current ratings levels. In the day-to-day management of it, it's not quite as simple as just the RBC. One of the rating agencies has a proprietary capital formula, which doesn't necessarily mirror the RBC. So I think we have to manage all of that together. And we also need to see our how business mix is going to evolve, right? I think again, to the extent that we continue to shift away from insurance-type risk and particularly the more capital-heavy -- although relatively speaking we're capital-light -- we still have some interest rate guarantees and some long-term fixed account guarantees that do have a consequence there.

But as we shift to more fee-oriented, I think there's an opportunity for us to look at that. But that again is probably not a '20 or a '21 item, at least not the way we're thinking about it.

Yaron Kinar: Okay. Then maybe one more at the kind of consolidated level, and then hopefully we can jump into some of the segments as well. So my last one on consolidated, hopefully, though don't hold me to it. Stranded costs, so I think you talk about $130 million to $140 million of stranded costs once the life deal closes, which you were looking to offset through cost savings. I guess I just want to confirm that those cost savings are not part of the $250 million that you've already achieved, that those would be new cost savings that you're looking at, right?

Rodney Martin: That's correct, 100% correct.

Yaron Kinar: Okay. And do you have any estimate as to by when you would be able to achieve those additional cost savings?

Rodney Martin: Yeah. Let me start and then -- I'm particularly proud of this, Mike. I'm proud of it, because Mike has led it. So it's easier for me to comment about that than perhaps Mike about Mike and Mike's team. But if we take a step back, we had previously announced in the prior program a number that -- and then we updated it to be $250 million. And we exceeded that number, and we exceeded it four months early. And so if you think about both the track record there, the methodology we used, and frankly the team that did that; reporting this team over. So to just repeat again, the $130 million to $140 million is in addition to what's been accomplished already. And the ideation for that is largely complete. The team is moving over, and I have a high level of confidence in our ability to execute that over roughly 18 months to 24 months, so a similar time period. And some of that, it largely comes in pretty ratably. Some of the IT things come in the latter part of it, but it's not a hockey stick by any stretch of the imagination. It comes in pretty consistently.

And part of that, we have ASA & TSA in say revenue, and that will fall off as it did with

the Venerable piece. And our objective is obviously to be neutral on this. So by the time that revenue is gone, that we've eliminated fully the $130 million to $140 million expense component. And again, the work and the thinking around this, we're not beginning to think about it starting January 4th. We're beginning to implement it. You can't implement it until the transaction closes. But we're implementing immediately, and thus it will be something that Mike and I will manage in the same way that we did the other. And frankly that was regularly very hands-on. So we had weekly meetings with the teams. There are multiple tracks to find this and execute against it. And I feel very, very good about what has been put together and how Mike and the team have led it.

Yaron Kinar: Got it. All right, so maybe a couple or a few questions on the segments themselves. If we start with retirement, in this COVID environment, we've seen a bit of a slowdown of recurring deposit growth in 2020 to I think we've got it as 3% to 6%. Do you expect there to be a catch-up opportunity in 2021 or maybe in 2022, as kind of the COVID environment hopefully relinquishes at some point and we go back to life as we once knew it? And with that, maybe we see targets that exceed that 10% to 12% range that you initially set?

Rodney Martin: So I think the shorter answer is yes, we see real room for improvement. But I really want to underscore something. This year is coming out in the 3% to 6% range. But I would just underscore for all the listeners and people participating, that's 3% to 6% positive. I mean if you think about the fact we've done $89 billion in deposits this year or will have, 13% participation growth, 6 million in defined contribution participants. I mean we've had a lot of growth in a very challenging year. And the gating factor will be the same thing that Mike talked about earlier on the pace of which the intersection of the vaccine, the burning off of as COVID goes through the winter and how those results are, and how that affects the economy. I mean we've given an update on the targets on the downside targets that we shared about that $300 million to $600 million. We updated that $300 million to $450 million at the end of 2Q, and that really hasn't changed.

We're trending on the lower end of that. Hopefully that continues in that way. But we are paying attention to what happens with COVID. And the reason that's important is as some further stimulus happens and we get through the election cycle and people see an end in sight with the vaccine, we think we'll get a more normal environment. It's really the pace of which we get there will affect again, I think the rate of which that we'll get back to that piece. And that's the hard part to predict. Do I think it's going to be positive for us? I do. Do I think it's going to be better than the low end of the range we are? I do. How fast and how far? It's going to be more macroeconomic dependent than Voya dependent at this point. But I think we've performed better than many, and I expect we will perform better than many prospectively.

Yaron Kinar: Okay. Then we've seen a lot of consolidation in the defined contribution retirement space. And I guess that brings me to two kind of opposing questions. One, do you think that that increases the emphasis on scale and the need to scale up for Voya, whether organically or inorganically? And then I have a follow-up.

Rodney Martin: So we've have seen a number of key transactions. If you go back two years, approximately two years, the Principal and Wells transaction, the most recent Empower and MassMutual transaction; so those are clearly different than what was happening

previously. We have been a scale player. We are a scale player. That isn't to say we wouldn't look at a book of business and add it. But we would do it through the economic lens that Mike and I have been talking about.

And the other thing that's happened, if you go back 10 years, and just in the 401(k) space, and we've used this statistic before. But it's really relevant. 10 years ago the top 10 players had 50% of the AUM in the 401(k) market. Today it's 75%. The majority of that has happened by the market choosing where it places its business. It hasn't been largely driven by M&A. Now this recent M&A changes that landscape a bit. But the market has been rationalizing itself through what are the four or five-plus players that are the long-term committed players that have all of the tools necessary to compete. And we have been a net beneficiary in a flight to quality over this period of time, simply by our focus and making sure we're staying as current as we can with the tools, the technology, and the infrastructure necessary to do so.

Do I think there will be other blocks of business that come to market? I do. The lens of which we will look at it is what Mike and I have already talked about. I think we'll continue to see opportunities for growth. Look, when these kind of transactions happen, and it doesn't matter what company; it's basically a stimulus package for the broker community to say, let's take a look at what happens. And certainly the acquiring company retains a healthy amount of the business. But there's a healthy amount of the business that simply these events cause a market opportunity for the advisor community to say, let's take a look. And that has been true for a long period of time. It is no less true at this point, and we're seeing that activity from these transactions happen now. It's a natural thing, and it will always be that way.

Mike, feel free to add.

Michael Smith: No. Look, I think that you said it well. The financial criteria we use to evaluate this is relative to other uses of capital, right? And that's share repurchase. Now that's been a fairly high hurdle over the last 6 to 9 months. Certainly with the recent pick-up in stock it's been lowered some. But it's still, I think, the right way to look at it from a shareholder perspective. We don't need to do a transaction to have scale. I think the success we've had in attracting clients over the last several years, I think the real success we've had this year in growing by the numbers that Rod mentioned. I think I'll speak to the fact that we are there. We have what we need. We're darn competitive and we expect to continue to be.

Yaron Kinar: So you've actually addressed my second question there. So maybe we move onto investment management. And why don't I start with the company's top priorities for investment management? What do you see those as being?

Rodney Martin: Christine and we have talked about three things. And I'm happy to answer. One is organic growth of 2% to 4%. And we continue to see that. And we expect the recurring deposit growth in '20 to meet or exceed that, and going on. The other part is the margin, getting back to the 30% to 32% margin, and we can speak of that. And then the increased emphasis on the specialty asset classes, we've got the good fortune of having a very good track record in this space on a 1, 3, 5, and 10-year basis. We understand the management of this. We started marketing, as we've discussed with many on the call, these capabilities to other insurance companies, 5-plus years ago. We're now doing business with over 40

different insurance organizations. In fact, this is one of the fastest-growing legs of our asset management business. And all of that is this is where our focus is going to be.

Now there has been many areas of this industry -- meaning the asset management business -- that's been consolidating. And that is disrupting the business and creating both teams and talent that are available in the market, and potentially capabilities that are available in some markets. So this would be an area that we would be willing to look at prospectively. We just added a small team, as an example. We talked about it quite recently, this G2 team out of London that adds a very unique capability with AI and ESG. And that's a small example, but that's the kind of thing that's an adjacency that we think is quite additive, and we would be open to that. And with the consolidation that's happening broadly in the asset management business, we think our culture, our environment, our long-term retirement orientation is appealing to a certain group from a talent perspective that we're quite excited about. Mike?

Michael Smith: I'd only point to just continuing to capitalize on the strong momentum we have, right? We got $10 billion plus of net inflows this year, which we think is certainly contra-trend. And I think it demonstrates the performance and the capabilities that we have, and the fact that there is a market need for that. So I think that's a great thing for us to be focused on.

Yaron Kinar: Okay. And then how should we think about the fixed income side of the investment management business? So the rates are still near historic lows. Yields generate like fixed income funds have compressed meaningfully. We could see further compression I guess as bonds mature or are called. So what shifts are you seeing from an investor appetite, as far as fixed income is concerned? And what are you doing to try to address these particular shifts (inaudible)?

Rodney Martin: Mike, do you want to start with that?

Michael Smith: Sure. Look, I think the shifts just play to our strengths, right? Is that the fixed income -- there will always be a need for fixed income investment, right? Folks are always going to be looking for the income, for the relative security, and the less volatility. And so what we have are things like private credit, mortgage capabilities, a really top-notch and longstanding CLO platform. Those are the kinds of things that are going to generate a higher yield. So that if you've got a low overall interest rate environment, but can generate consistent spread width, the strong risk management which I think we can demonstrate over the years; I think those are the kind of characteristics that are attracting the flows that I mentioned a few minutes ago. That's going to continue to be, I think, a real strength for us.

And so I would say that we should really be thought of as a fixed income and specialty player. I think that's -- we still have an equity capability. But I think where we're really leaning in is on those first two.

Yaron Kinar: Got it. Maybe one other hopefully quick one on the investment management side, so the 401(k) or the CARES Act; what are the trends you've been seeing in retirements funds post the CARES Act? Have you seen any increased appetite from investors to draw down on the time and savings, or for corporates to increase the suspension of matches post-COVID? Maybe you can talk about the momentum you're seeing there.

Rodney Martin: Mike, do you want to start, or--?

Michael Smith: No. I think obviously we were among the first, if not the first, offer and some additional support to those who were seeking loans or withdrawals by waiving fees. And so we saw some take-up of that. I think that was absolutely the right thing to do. It was not a particularly expensive thing for us. But it was a way to contribute to what was certainly at the time, it seemed like a potentially really difficult situation.

So we have seen withdrawals up. We have seen hardship withdrawals up. Actual overall withdrawals are a little bit down. And when I say up, that's from a pretty small base. So I think kind of the reality is that in crises like in the Great Financial Crisis and this, although different in characteristics, you didn't really see people tapping into their retirements funds in a way that affected us in a profound way, or even in a material way. I think it's good for the individual, and certainly there are folks that you can find anecdotal situations where it's very helpful. But it's not a meaningful needle mover for us in terms of the withdrawal activity.

Yaron Kinar: Got it.

Rodney Martin: I would add that just I think the other thing it's done, just broadly COVID and the virtual piece, it has caused people to think even more thoughtfully about their personal financial situation. Are they saving enough? Are they taking advantage of all the tools the employers are making available? We've actually -- Mike answered it very completely in terms of hardships are up over a very small base. We've also seen savings rate up for those that have that capability to do it and were not impacted in their particular job. So it's been an interesting year from that perspective. I think people are very much focused on their personal responsibility and taking full advantage of both with the tools and educational pieces, the programs that are made available by employers, and are they doing this at the right pace and cadence. So we've seen interesting activity there too.

Yaron Kinar: Got it. So I think we're almost out of time. I did want to close with a question about maybe the greatest opportunities and challenges that you're seeing as we head into 2021.

Rodney Martin: I think one of the pieces I'd start with, and Mike and I go back and forth, is the theme I'd love to leave with you all is if we had put in an envelope where we thought the year would end when we all went virtual in mid-March and what the results have proven to be; I'm sure we would have come up with a number much less than what we've produced. So the commercial growth that we've had, the numbers that Mike and I have shared on the recurring deposits and the participant growth, the ESG progress we've made, the workplace orientation, of Voya Cares program and the reception of that in marketplace; we feel really good about that going into next year. The other piece is we're done with the de-risking and the time and attention that takes. It's been executed very well from my point of view. And again, my compliments to Mike and team, broadly for leading that. But this is really all about trying to identify opportunities to further enable our organic growth, and adding capabilities to supplement that as we go forward.

As you've pointed out, we've got 85% to 95% free cash flow. We're a far more capital-light company. The majority of the tail risk has been eliminated. We've never had long-

term care exposure. It's a very different picture and a very different story, and one we're very proud of. But Mike, feel free to add.

Michael Smith: Not much to add, other than just I think we're really excited about where we are. We've taken some pretty big steps over the last few years to clean up the balance sheet and position us for what I think is some really intriguing and exciting opportunities. And so we're just anxious to get at it is all I'll say.

Yaron Kinar: Great. Well, Rod, Mike; thanks so much for joining us and for your time. Hopefully we get to host you in person next year.

Rodney Martin: Perfect.

Yaron Kinar: All right.

Michael Smith: Absolutely.

Yaron Kinar: Take care, everybody. Thank you.

Rodney Martin: Happy holidays, everybody. Thank you.