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PRESENTATION

Jennifer Childe - *CNO Financial Group, Inc. - VP of IR*

Good morning, everyone. We're going to get started now. For those who don't know me, my name is Jennifer Childe. I'm the VP of Investor Relations for CNO. We'd like to welcome you to our 2020 investor conference. We'd also like to welcome those joining us on the webcast. And we are streaming live.

Materials for today's presentation are available on our website at cnoinc.com. We're also offering the opportunity to e-mail any questions that you may have to us at ir@cnoinc.com. For those in the room, there should be WiFi password information on the table.

And with that, I'm going to read a few forward-looking statements. This morning's presentation is available in the Investors section of our website and was filed in a Form 8-K this morning along with our revised fourth quarter 2019 financial supplement.

Let me remind you that any forward-looking statements we make today are subject to a number of factors, which may cause actual results to be materially different than those contemplated by the forward-looking statements.

Today's presentation contains a number of non-GAAP measures, which should not be considered as substitutes for the most directly comparable GAAP measures. You'll find a reconciliation of the non-GAAP measures to the corresponding GAAP measures in the appendix.

On the screen is today's presentation and today's agenda.

With that, I'll turn it over to Gary Bhojwani, CEO.

Gary Chandru Bhojwani - *CNO Financial Group, Inc. - CEO & Director*

All right. Thanks, Jennifer. I appreciate that. We've got a handful of our -- members of our management team here. And I'm really grateful for all the hard work they've done. And also want to thank all of you that are here with us today. For those of you that've been involved with or following the stock for a while, thank you for your continued support and interest. We really appreciate it. For those of you that are new to the story, we think we have a pretty compelling story to tell, and we hope after today's presentation, you'll agree. Before I begin the formal part of my presentation, I really wanted to start this morning with a joke.

And so I Googled Wall Street jokes. And I didn't find any I could tell in this setting. Let's just say that. So I was trying to think about how I wanted to open. And I had a conversation with my dad last night. And oftentimes, when we're thinking about our business and how I explain our business, I really think about my dad.

First-generation immigrant, middle class, did everything the way you're supposed to do in terms of the American dream: following the rules, paying taxes, owning a home and so on. And I was talking to him a little bit. And part of what happened. We got to ring the bell yesterday, which I kind of screwed up, that's a different story. But my kid sent that video to my dad. So he did the whole dad thing. If he could have put the video up on his refrigerator, he would have. Anyway, so we were talking, and I was explaining to him what's going on, on Wall Street and the biggest point drop and all this other stuff. And without missing a beat, without missing a beat, he said, so what's the big deal? Isn't that why you guys do what you do? Isn't the very thing you're supposed to do is make a difference in that setting and make it so that people like me that are your clients don't have to worry about that? And by the way, don't ever forget, it's still the greatest country in the world. There's still more opportunity in this country than anywhere else. And with that, I was like, you know what, it's so true. At its core, the business that we do, we help middle class people, and we make sure they don't have to think about things like that. Now does that mean we're blind to what's going on? Of course, not. We live in the real world, but I think it's important to put it in context. We still have tremendous opportunity in this country. And the very thing that we do is help people navigate the challenges we're seeing over the last few days, and probably will see for some time to come.

So in terms of today, what do we want to do? I think there's really 3 things that I hope happen today. First, we'd like you to have a deeper appreciation for our business and really understand what makes us tick, how it is we position ourselves in the market, what those competitive advantages are and why they're sustainable.

The second thing we want to do is help you understand our roadmap. Now I will tell all the analysts upfront. I'm sure that we don't provide as much guidance as you like, but I would also let you know ahead of time, I'll cut to the chase here and try not to steal too much of Paul's thunder. We're materially increasing the amount of guidance we do provide. And one of the things we're doing is sharing with you that our 2020 plan -- and there are other guidance we're providing.

But our 2020 plan calls for us to grow earnings per share by 9% to 11%. And again, Paul will share with you much more detailed guidance in other areas. But we want you to understand that roadmap. We want you to understand how we're going to grow top line and earnings per share and why that's sustainable. Because we really think we've got something here that is indeed sustainable.

And then finally, of course, we hope that you walk away with an improved recognition of what an attractive investment opportunity this is. We think when you think about the market that we serve and how we serve it, that there's something unique here, and there really is an investment opportunity that's unparalleled. So what are the key messages in my capacity as CEO that I want to share? The first thing I want to do is make sure that you have an understanding of how we distribute our products. The distribution diversity is one of the key things that attracted me to CNO when I joined the company in 2016. When you look at our captive distribution force, so the agents that represent only our products. We have in excess of 5,000 agents that represent only our products. And I think a lot of people don't realize that makes us 1 of the 5 largest captive distribution forces in the country. Think about that for a moment.

Second thing, we have a very successful direct-to-consumer business in the form of Colonial Penn. And when you look at the number of contacts that we have at the consumer level, whether it's web chats or phone calls or what have you, it's actually 1 of the 5 largest direct-to-consumer financial services businesses when you look at the consumer touch points. I don't think most of the market understands that.

And then we've got an incredibly fast-growing worksite business with a really unique collection of assets that really enable us to serve that market very differently.

The second key message I want you to have is that we're trying to get in front of what we see as changing consumer behaviors. If you think about the way you buy anything, whether it's socks or airline tickets, your behavior has changed. And one of the things that really captured my attention when Amazon launched -- it's been a couple of years now, when they launched the ability to order something on Amazon, have it delivered to your home and then go return it to Kohl's without any packaging. And by the way, Kohl's has no formal ownership relationship with Amazon. Think about what they did there in terms of adapting to a consumer behavior. Consumers today, whether they talk to you on the phone, research it on the web, order it on the web or want to engage with you face-to-face, they expect that experience to be seamless. We announced the transformation of the organization, where we're moving from 3 companies to 2 divisions. And really the driver behind that thinking was how do we bring these disparate assets we have -- and again, we'll talk more about this later today. How do we bring those assets together to really get in front of what is a changing consumer behavior? A consumer is not going to tolerate. You have to call 1-800 Colonial Penn for this. You have to deal with the banker's agent only for that, and you have to look online for only this. They want that experience to be seamless. Now it's still evolving in financial services. Financial services are behind other industries, but it's clear that the expectation of the consumers is changing, and we think we're uniquely positioned to do that.

Third thing I want you to understand. We intend to remain focused on the middle income market. There are different definitions of middle income, but these are hard-working people. These are people that typically have a net worth of $500,000 or less. We intend to stay focused there. And in particular, the products that we manufacture are simple, safe and profitable. Now I've put LTC and annuities in parentheses here. We obviously sell a lot of different types of products. And Karen, our Chief Actuary is going to speak to those products, but she's going to go much deeper than we historically have, specifically on LTC and annuities. That's where we get the most questions, and frankly, that's where we think the market understands us the least. We think we have an opportunity to tell a very clear story about why those 2 products, in particular, are simple, safe and profitable.

Fourth, I want you to have an appreciation for our investment portfolio. It's balanced. It's built to sustain the low-for-long environment, and Eric is going to walk you through why we think we're in a very good place. And frankly, why we think some of the concerns about volatility are misplaced. But he'll walk you through that in detail.

The fifth thing, fifth key message I want to deliver. Set aside CNO for a moment. Consider any business you want, whether you're making shoes or selling insurance. If you think about cutting expenses, growing sales, navigating material changes to net investment income and in this case, pressures for net investment income to come down and growing earnings. I think it's a very simple statement to say you can't do all 4 of those things. You can't cut expense, grow sales, face off against the net investment income headwind and drive higher earnings. It's not possible to do all 4 at the same time. We've taken a very deliberate approach about moving from cleaning up the company to pivoting to growth and now to driving earnings. But in my view, in a very simplistic way, it's not possible to do all of those things at once. They had to be sequenced in a certain order. There's a logic to the order we use, and I believe we're extremely well positioned now to drive that EPS growth as well as other things that we'll talk more about.

The sixth and final thing, key message, I want to deliver. When I became CEO a little over 2 years ago, I made a decision that I didn't want to provide specific guidance to buybacks. I believe that, that ties the hands of management. But somewhere along the lines that decision not to provide guidance got interpreted as a decision not to do buybacks, and that's just wrong. We returned $319 million to shareholders when you look at buybacks and dividends in 2019. That is the most we've returned in over 4 years. It represents roughly 9% of our share count that we bought back. So a very significant commitment to deploying capital in a reasonable and shareholder-friendly way. And we want to give you some comfort as to why you should continue to believe us when we say we will be good stewards of your capital.

I also want to share with you some thoughts on ESG. This is obviously a fast-developing field in the world of public companies. For us, this is something that comes naturally. And again, I'll draw you back to where I started my remarks this morning. Helping people is what we do. So this is part of our DNA to do the right thing, to make sure that we continue to invest in our communities and our associates. We've received quite a bit of recognition over the last couple of years for our wellness and diversity rankings. We have a track record of investing in a very prudent way. Eric and his team do a very good job of making sure we're not investing in inappropriate things. And we remain dedicated to promoting ethical and responsible business practices. And again, we do all these things not because of some political stuff, but it's core to the business that we do. So you'll hear from a number of members of the management team. Thankfully for all of you, the person who does the least talking is me. And so what I would like to do next is introduce our Chief Marketing Officer, Rocco Tarasi. Rocco?

Rocco Francis Tarasi - *CNO Financial Group, Inc. - CMO*

Good morning. Rocco Tarasi, Chief Marketing Officer. I'm excited to be here with you today. I have 3 main takeaways for you.

First, we have tremendous opportunity in our market, and we are uniquely positioned to help them meet their needs. I'll give you some statistics about our market in a minute. Second, we use many different methods to access our market, and our brands and channels have largely operated in silos. I'll show you some of the marketing methods we use today.

Third, our transformation into 2 divisions is eliminating barriers and creating more opportunities for us to grow, and I'll talk about some of those opportunities. We are focused on providing health and wealth solutions to middle-income Americans. At every stage of life, the nature of their needs changes and the opportunity for our solutions continues to grow.

I'll briefly walk you through needs -- the needs of middle-income Americans at different stages and highlight how we help them in each of those stages. Our customers that are tightrope walkers are in the workforce and challenged with high out-of-pocket medical expenses. Unemployment is at its lowest point in 50 years. And employers are using benefits as a recruitment and retention tool. More than 2/3 of employers cite rising medical cost as a reason for them to add voluntary worksite benefits. And the market for voluntary worksite sales is projected to continue to grow. We have the products that employers want to provide to their employees. As our customers get a little older, they are setting the stage for their upcoming retirement. But for many, they're sandwiched between caring for children and caring for parents, while at the same time trying to save for their retirement. It's no wonder that nearly half of all households have no savings for retirement. Financial advisory services help people plan for secure retirement, while balancing the competing demands on their finances. And as a result, our financial advisory services is a fast-growing part of our business.

For our comfortable in-retirement customers, we provide health and wealth solutions. The number of people turning 65 will increase by 33% over the next 10 years. And demand for Medicare solutions will continue to grow. We will continue to sell both our Medicare supplement plan and third-party Medicare advantage plans.

Now after the Medicare decision, the conversation turns to the risk of outliving one's finances. People are living longer than they may have planned, and they need secure, guaranteed income for life. Our annuity solutions provide a simple solution to ensure that our customers don't outlive their finances, and demand for annuities continues to grow. Some of our customers are anxious in retirement and concerned with a potential need for costly long-term care services and for good reason. 70% of those turning 65 will need long-term care services in their lifetime. Yet, 79% of people don't have long-term care savings. The need for solutions to cover growing long-term care costs is greater than ever, and we have both stand-alone and hybrid products to meet those needs. On the life insurance side, there's a similar story. An estimated 70% of Americans are either uninsured or underinsured. With the help of our multichannel distribution, we offer life insurance options to help ensure that they get covered.

Now that you have a sense of our target market and how we're positioned to meet their needs, let's talk about how we access this market. If you watch The Price is Right or Let's Make A Deal, you almost certainly saw one of these commercials. Colonial Penn ran over 200,000 of these spots in the last year, which generate inbound calls into our telesales center. But we've really only used television to promote the Colonial Penn brand and really only for our life insurance product. We have an opportunity to use this marketing channel to promote more of our products and more of our brands.

If you turned 65 in the last year, odds are that you were contacted by Bankers Life to talk about your Medicare needs. Direct mail is one of our primary advertising channels for those turning 65. But we have opportunities to use direct mail for other products and other brands as well as the partner direct mail with other marketing strategies for multitouch engagement.

If you live in a rural community or on a farm, you might have received a knock on your door from an agent of PMA when they visited your town. PMA is a wholly owned subsidiary of Washington National, focused primarily on supplemental health sales to the farm and rural markets. We visited over 1 million households in rural communities in the last 12 months. And we have an opportunity to leverage our full product portfolio to help with their other health and wealth needs.

If you work at a company with between 100 and 5,000 employees, and you've purchased insurance through your employer via an online enrollment website, it's possible that you use technology provided by Web Benefits Design, a company that joined the CNO family in 2019. Web Benefits Design has provided a leading digital enrollment solution to over 500 groups, representing over 300,000 individuals.

While we've been distributing our supplemental health products through this platform, we have an opportunity to use this platform for more of our broad product portfolio.

And then there're the digital channels. If you're on social media, and you're in our target market, you may have seen any one of these or other videos that we've created to generate customer interest and we'll play one video for you.

(presentation)

We're expanding development of these types of videos to use them across all of our brands and through all of our channels.

So as you've seen, we engage with customers in multiple ways, direct mail, TV advertising, home visits, worksite technology, digital advertising. The combination of our middle-income focus, our broad product portfolio, our diverse marketing activities and our multiple distribution methods make us uniquely positioned to service this market.

As a result of these marketing activities, we have direct contact with over 10 million people a year, and that's excluding hundreds and hundreds of millions of other digital impressions.

Of those 10 million contacts, we generated over 2.5 million sales opportunities. And of those 2.5 million sales opportunities, we sold over 400,000 policies a year. But our marketing activities to generate contacts, opportunities and sales have largely been siloed within our individual brands. With our transformation, we are breaking down those barriers and improving every stage of this sales process.

Let's start with the top of the funnel, generating customer interest. Here are several ways that we will increase our contacts. First, our transformation has eliminated separate marketing budgets and sales goals for each of our brands, allowing us to better optimize where we spend our next marketing dollar.

Second, we'll expand our content marketing capabilities. The Bankers Life Center for a Secure Retirement has been our research arm, leading annual studies on retirement, including on your tables, a 2019 study that earned us the front of the USA Today, the graphic on the front of the cover the USA Today. We plan to remodel the Center for a Secure Retirement into a stand-alone thought leader property to engage with prospects and customers across all of our brands.

Third, we'll leverage our digital learnings from certain of our brands. For example, in 2019, we invested in web chat on our Colonial Penn website. We're going to expand web chat across all of our properties and use the same inside sales and support team to support that chat across all of our brands.

Now out of these contacts, we were able to generate over 2.5 million sales opportunities. You can't have a sale without a sales opportunity: face-to-face appointment, telephone call, direct mail application, the start of an online application. Here's how we'll create more sales opportunities.

First, we'll continue to develop intelligent lead routing to route leads to the next best channel. Second, telesales and field agents will work together on booking appointments and for collaborative post appointment follow-up. And third, our transformation allows us to more easily market multiple products across all of our different marketing channels. From our opportunities, we sold over 400,000 policies last year.

To increase conversion of our opportunities to sales is a simple formula. First, do we have the products that people want to buy? We have a broad product portfolio today. We'll continue our annual investment in building new products but now with the focus on reaching total top line sales, not individual brand-specific sales goals.

Second, can consumers purchase products the way they want to? A key part of our transformation is to take our broad product portfolio and make sure that as many of our products can be sold in as many of our channels as practical.

Third, do we provide a great buying experience? We'll improve the application process, provide tools, education, support across all of our channels to empower our customers to buy when, how and where they want.

Finally, let me leave you with a summary. We've generated nearly $4 billion in annual collective premium from our current siloed sales and marketing activities, siloed within our brands. There are tremendous opportunities as you've seen to improve each stage of our sales funnel. The transformation we've recently announced will help to unlock many of those opportunities. We will be marketing more of our products through more of our channels. We are changing today how we route leads to the next best sales channel. We're making new product development decisions with a total top line sales goal, not individual brand top line sales goals. We'll engage prospects across different channels to provide them with a buying channel of their choice.

And lastly, we're already leveraging our telesales team, which previously only focused on the Colonial Penn brand to support sales across all of our other brands.

With that, I'm pleased to bring up our next speaker, President of the Consumer Division, Scott Goldberg.

Scott Louis Goldberg - *CNO Financial Group, Inc. - President of Consumer Division*

Okay. Click, there we are. Okay. Good morning, and thank you for your interest in CNO. I have the privilege of overseeing our consumer division and grateful to have this opportunity to tell you a little bit about our business.

There's 3 conclusions that I want you to take away today. First, as Gary mentioned, we're a top distributor of health and wealth protection products to the middle market. We sell through 3 channels, and 2 out of the 3 channels are top 5 in their space. Second conclusion. We've spent the last several years, and I talked about it the last time that I was here and presenting at an Investor Day, making investments to modernize our infrastructure. We put together a series of initiatives and programs to stimulate growth. And it's been very satisfying to see the consistent growth that we've had over the last several years. I'm going to take you through that. You're going to see some of the product margins when Karen, our Chief Actuary speaks, and you're going to see some financials when Paul speaks. But from a top line perspective, we've had growth across agents, premium, assets and fees.

And third, as has been alluded to a couple of times now, we are evolving. I want to tell you a little bit about our vision going forward. And that is we're making this transition now, from being a multichannel distributor to something that I call an integrated delivery model, where prospects and clients move or are moved across channels to optimize their experience and the interaction. This is really powerful. We think we have an opportunity here to create a sales and service model that's going to resemble the insurance model of the future for insurance distribution. And we like our chances. So before I get into all that, let me just talk a little bit about our products, our channels. And then I want to tell you a little bit more about some of the success we've had with our largest source of premium, our exclusive agents.

So I'll start with products. Our product set is unique in that it spans both health and wealth solutions and even more unique in that compared to peers, we take a very different approach. We take a market-focused approach to thinking about products. What you'll find when you look across the industry, is that most do the opposite. They start by taking a product approach, and then they look for a market to serve. Now not everything that we sell is proprietary. We manufacture certain products where we believe we can achieve strong product margins, and we have the ability to compete. And then we source other products from third parties, where we can capture fees and boost our ROE.

Let me talk about channels. Within this division, we have 3 channels, and Rocco talked a little bit about them as well. The first is our -- we go direct. Now we do that principally through our Colonial Penn brand, which, as Gary mentioned, is a top 5 D2C program and a nationally recognized brand. We sell through independents, and I'll talk a little bit more about that. And then, of course, we sell through exclusive agents. And we do that through 2 agencies. The consumer division of PMA USA, and then, of course, through Bankers Life. And Bankers Life is a top 5 career agency. So what I want to do in the spirit of, kind of, where we're headed under this new model in the consumer division, I want to step away for a moment from thinking about these around brands. And let's just look at these by channel. So I'll start with direct-to-consumer. Today, we go to market through 4 different ways. And about half of it is direct response TV. And I think we're really good at it. So half through TV, and the other half will come through mail, the web and telesales. Now we get it. Today, we're principally marketing low-face, guarantee-issue, whole-life insurance to lower-income consumers, who are looking for a simple vehicle for planning for their final expenses. That's what we're doing today. But by the way, this past year, we did $80 million of new premium through that channel. That's a high watermark for that program. We think we got a lot of opportunity here. An opportunity to expand through simplified-issue health products. Think things like supplemental health products like critical illness, cancer products and such. We've had a lot of success, and I'll talk more about that. And also think about Medicare advantage, which is growing direct-to-consumer. We also think we have an opportunity to expand upmarket to capture higher premium sales, whether we do it through the Colonial Penn brand or through one of our other brands.

Independent agents. Today, we market through field marketing organizations and more and more through telesales centers. Now what's happened in the marketplace, as you've seen the growth of individual health products, individual major medical plans as well as the proliferation of high-deductible health plans, there's just been a growing need for products that pay lump sums and can fill in these gaps. And we've had great success working with telesales centers who are selling ACA plans and similar plans. So that market now, it's modest today, $20 million. But a lot of opportunity to grow, and we think we have the products that are most in demand. So there's an opportunity to expand our number of partners in some of these fast-growing channels like telesales. And then there's an opportunity to work more closely with our distribution to develop custom products to do integrated marketing and have a much tighter relationship.

And then, of course, our exclusive agents. This is the largest way that we reach the market today and most recognizably, under our Bankers Life brand. We go to market through face-to-face sales. And we're doing this across thousands of counties. We reach rural markets through PMA. We reach suburban and urban markets largely through Bankers Life. Now what's really interesting, I want to tell you about some of the things that's happened with Bankers Life over the last several years, and I'll go into this in a little more detail over the next few slides.

Bankers Life, life and health agents now partner with a financial adviser. They work in teams, often with the financial adviser as the captain of the team. And then together, they can provide expert advice and one-stop shopping to consumers, particularly those who are transitioning out of the workforce, having to navigate Medicare for the first time, trying to figure out what to do with their 401(k). Right? People roll over their 401(k) to an IRA, and suddenly, they are their own Chief Investment Officer. And they're looking for ways to turn their savings into secure retirement income. So here, our opportunity is really straight ahead to continue doing what's been successful for us, particularly over the last 3 to 5 years, which is to grow our rank of advisers and assets under management and then continuing to sharpen our focus on the upper end of the market where we can capture higher premium sales, sell multiple products and then have an opportunity to render our financial planning services, which is a big growing part of our proposition. When you look at our exclusive distribution, and I think that's really the word for controlled distribution, exclusive distribution. We have nearly 6,000 licensed agents that get up every day thinking only about our products. Now at the core of it are 475 field managers that have nearly 12 years of average service. Gary said this would be difficult to replicate, I think almost impossible to replicate.

We have in PMA this traveling group of agents, 425 or so agents that are traveling from county to county, accessing rural households that'd be very difficult to penetrate in any other way. And again, a field force that would be almost impossible to replicate. 4,700 local agents operating in communities all around the country that correspond to this map. You can see where we have outlets, sales offices, 260 different sales offices. And then, of course, our telesales agents. 250 telesales agents located in Pennsylvania, in Indiana and a large group that are virtual with lots of opportunity to grow. But it's not just the size of our dedicated agent force that I think is important. It's just also the decentralized nature. The fact that they are in the communities and that -- within the communities of our clients. And because we're able to get in their communities and develop these local relationships, we have an opportunity to build loyalty and rapport, cross-sell, upsell, render our financial planning services in a way that many other models cannot do. And I think that this last part about being able to provide financial planning services is particularly important when you look at what's going on in the middle market. This isn't talked about as much as it should be. We'll talk about the growth in the number of Medicare beneficiaries. But look at what's happened to U.S.-qualified retirement assets over the last 25 years or so. Go back to 1995, there were $3 trillion in IRAs and defined contribution plans. Look at where we are now. Over $16 trillion in personal retirement accounts.

And then, even more interestingly, when you look at the assets in which these IRAs are invested, so now take the $8.8 trillion, and let's expand it out with the chart on the right. What you see here is that very little of this money is invested in secure products. I mean, frankly, it's still invested in the same instruments that people were investing in when they're working, mutual funds, listed securities. And only the tiniest portion are in fixed-interest annuities and fixed-indexed annuities that actually can provide predictable income and are truly safe for people who are transitioning into retirement and where they can't lose their account balance. There is a tremendous opportunity for us to work with clients as they're transitioning out of the workforce into Medicare and then thinking about how to reposition their IRA. And this is largely what we do today when we're selling our annuities. So just a huge opportunity to help people here. And it feeds into the way that we go to market. I think that we're uniquely equipped to go-to-market in a way that you won't find other carriers or distribution organizations equipped to do so. And it just goes back to our products and our exclusive distribution. So this diagram is a good way to think about how we develop a relationship and have a conversation with clients. We generally start at the bottom of this pyramid, talking about their most urgent need, which is medical expenses.

Now this might be helping them fill-in gaps in their major medical plan, or this might be navigating Medicare. But then as we build rapport, as trust builds, and we identify they have greater assets to protect, we're able to move up this pyramid: looking at things like assisted care, which is kind of broadly the way that we talk about our long-term care and short-term care solutions; perhaps, looking at things like final expenses. But as they have greater assets -- and we find this all across what we call the middle market. Individuals who have more assets than you would otherwise believe, and no matter what amount of assets they have, need to protect and think about structuring those assets towards income. We're able to provide those solutions. That might be in the form of universal life insurance or indexed UL. That might be in the form of an indexed annuity, or that might be in the form of an investment management service that we provide through our RIA. In other words, we often begin with a health insurance transaction, and then we're able to pivot to a financial planning discussion. And it's just a really powerful model that we don't think others are able to do.

It's only been a few years now since we launched our broker-dealer and our RIA. But it has already had an outsized impact on our productivity, our recruiting and our culture. And I want to talk about these. Today, almost 1/3 of our veteran agents are registered to sell securities. That's 13% of our total agent force, but it means that we have one adviser for every 6 insurance agents. That allows them to work very effectively in teams. And if you look at what's happened. Agent commissions by product, they tend to veer more towards financial products as agents age in our system. You can see this from their first year to their second year. And then veteran agents who have been with us 3 or more years begin to derive a higher and higher portion of their income from financial products. In fact, agents who become registered to sell securities end up making over twice as much income as agents who do not.

So what's happened here is we've really strengthened the value proposition of being a producer in our system by setting up our broker-dealer and RIA and being able to pivot towards this financial planning discussion. And let's just face it, there is just a certain amount of natural appeal in transitioning from being an insurance sales agent to being a financial adviser. And what we've been able to do is now translate this into recruiting. So if you look at the chart on the left, what you'll see is, we've been able to take down the number of new agents that we need to recruit each year to grow our sales and to grow our agent force. Now some of this has come because we've been able to put together what we call our PRP program.

In 2016, we started something that we call our personal referral program, PRPs. And what it does is it matches the high potential producer candidates that are referred to us by an existing producer and provides performance-based incentives for first year income support. Now the referring producer gets to serve as a mentor, and they get rewarded based on the early success of their PRP. Today, PRPs are our fastest-growing and best source of new recruits. And the benefits that we're seeing in productivity and retention are greatly outweighing the rather modest cost of this program. And you can see that even in the chart in the middle. The retention of a PRP is over 3x what had -- an Internet recruit, which had been the primary source of recruiting that we've relied on. So as we brought on more PRPs, as they've had higher retention and productivity, we've been able to reduce the number of new contracted agents and yet grow our producing agent force. This is a formula that we had not unlocked previously but now is a big track for us to run on. And you can see not only are we growing the number of producing agents, but their productivity has gone up as the amount of premium per producer has gone up year after year. We have a lot of runway here. The translation of all this from a top line perspective, we've been able to grow new annualized premium, new annuity collections, third-party revenues, annuity account value and client assets in brokerage, which, assets in brokerage often become the source of future insurance sales. So we're demonstrating really nice growth. I'm really pleased with the initiatives that we put in place and kind of where we are today from where we were able to address this group in this forum a few years ago. And now with demonstrated growth and a lot of momentum behind us, I believe, we're really set up nicely for where we go next. So let me talk about that.

We announced this transformation. Before the transformation, we operated separate companies -- separate operating companies. And they were formed to serve what I'll call a traditional consumer. In that a traditional consumer, you segment the consumers according to their purchase preferences and then traditional marketing said, you aligned products and marketing with a specific channel to serve that consumer. And that might have been direct or people who wanted to buy through an agent and so forth.

Today, with the transformation that was announced, we're structured to serve a modern consumer. What I mean by that is a consumer who wants a customer experience that gives them access to a menu of products and provides them the ability to move seamlessly across channels as a way to optimize the interaction. This is how we're structured today, and it unlocks all sorts of opportunities. We have an opportunity to deliver, what I'll call, an integrated experience. What do I mean by this? I mean, in this new model, we might engage with consumers digitally. After all, that's how many of us begin to engage with products and services that we want in our lives. These consumers might be motivated to research a product, or they might go online and hit the buy button. More likely, they might begin a web chat session with one of our telesales agents, or they might pick up the phone and call one of them. But whether they buy a product or don't buy a product direct, we have the opportunity to now pair them up with a local agent. And this is really powerful. Because, again, that is where we build trust and rapport, loyalty, find the best opportunities to upsell, cross-sell. And then, in many cases, render our financial planning services, which often begin with that face-to-face interaction. We think that this type of model, and I call it a hybrid sales and service model, hybrid because it blends virtual with local.

We really believe that, that is the model that's going to win in the future, particularly in our market. And we think we're really set up to do so. You just look at what's already running through this model today, 2 million leads, 500,000 new applications and we issued 400,000 policies out of that. And it's 2.5 million policy holders that we have the opportunity now to move across channels to maximize the opportunity. I think we bring a lot of scale to it just today.

When you look across providers we just don't see anyone else who is equipped as we are to serve the marketplace in terms of product, in terms of investment management services, in terms of having exclusive distribution. We check all the boxes. So it's going to take a basket of capabilities to win in the future. We understand that. But again, we think that we're ahead of the game in most of these. As pointed out earlier, we generate 2 million leads but we have the ability to transact with consumers in such a variety of ways, digitally, through voice authorization, electronic applications that agents can access via mobile and so forth. And we can provide service digitally through telesupport, through a local agent. And then in cases where we have overlapping capabilities because we're now bringing these operating companies together, we have an opportunity to select the best-of-breed capability as we rebuild this model for the future.

So I'm going to wrap it up. I'm going to leave it here and just a few additional messages as we look ahead. We're focusing now on ways that we can leverage our products and brands across channels in new ways. Rocco referred to some of this. We're going to be focusing on ways that we can engage and capture consumers to deliver this integrated channel experience that I talked about. And then, of course, particularly with our local agents, we're going to be driving more and more of these relationships towards holistic retirement planning, where we've had demonstrated success in growing premium, assets and fees. Thank you.

And now it's my pleasure to bring up Mike Heard, our President of the Worksite Division.

Michael D. Heard - *CNO Financial Group, Inc. - President of Worksite Division*

Thanks, Scott. Well done. Great overview. Thanks to all of you for your interest in CNO. I'd love to talk now about kind of the final piece of the transformation we've talked about, and that's the Worksite Division. And if you listened to what Scott talked about there, it was largely a collection of some of our more mature assets, from a distribution perspective, that we're now piecing together and kind of creating a 2 plus 2 equals 5 with those particular distribution channels. The Worksite Division actually comes from a history of being kind of an incubator inside of the Washington National Insurance Company, where it was kind of a hobby, run by an individual company trying to capture some worksite market share over the years. And we've made some investments and we've continued our focus on this worksite market. And now it is becoming a piece, a division now in a critical place to access middle-income Americas where they work. So what I'd like to do today as we talk about the Worksite Division is first talk about some of the macro drivers. Now Rocco did a great job, kind of laying out the playing field for us across both Consumer and Worksite Divisions. I'd like to go into just a couple more quick specifics in terms of small business, and what we like about the small business worksite market. We'll talk about those tailwinds and kind of how we fit in there geographically, and what our environment looks like, and where we see some opportunity.

Then talk about 4 key assets that we have at CNO that we think gives us an opportunity to leverage and capture some more market share. And then lastly, just show you the proven formula, how we've grown over the last 2 to 3 years, the success we've had and why we think we can continue to take advantage of those tailwinds and mix them with the assets. So that's the way we'll go. And then I think when we're done, Scott, Rocco or Gary I think we're up here for a little question-and-answer on the talk show set here, and so we'll go through that.

So first, let's talk about the employer and the employee needs. So when we talk about tailwinds here, you know all the statistics in terms of what's going on in the employment economy. It's becoming very competitive, and specifically for small employers. You have them looking for ways to attract new employees, retain new employees, deal with multigenerational employees. And so voluntary benefits become something very flexible for these small employers, especially because in most cases, little to no cost to those employers to be able to offer those benefits. So a clear need there.

Now when you look to the employee side, our customer, the ones who are writing the checks, also pretty important because things like high deductible health plans, all the gaps that Scott talked about that we try to deal with consumers who are buying individual health plans have some of those same gaps on the employment side. The advantage in the worksite environment is we can bring a little knowledge about what's going on with those small employers and be able to smartly supplement what those employers are doing. So we feel really good about the consumer pull, if you will, of the worksite approach.

So I want to talk now about tailwinds in our existing market. And so before we even talk about plays we run for growth, there are some things that we really like about what we're doing right now that we've been growing double-digit over the last 6 quarters. First is small groups are creating jobs. This is not anything new. This has been happening over the last 10 to 11 years. A similar profile when you talk about small employers creating 74% of the jobs in the employment economy and representing almost 78% of current employment. And the voluntary worksite market itself serving these small businesses has grown 4% in 2018.

Now you say, how do you do well there? And how can you continue to grow in that market? Or have you maxed out? One key advantage for us is our geography. And when you look at the geography at the bottom, our base started in these green states, and we have grown the last 2 to 3 years in 16 states, marked in blue up here on the map. And so that's where we've grown, about 45% of our new group sales has come from these expansion states. So we've had really good success there. 40% growth in those states since 2017.

But what excites me, even more, is the yellow states up here because those are places where we've done the work in the past to get the product ready to go. And now we just have to bring distribution to the table and experience more growth. What I really like about this piece of the strategy and what really has me confident about it, it's just running the plays that we already run. It's nothing new; it's nothing fancy. It's just doing it in new places. So that's what we like about what we're currently doing.

Now, where else can we go to grow? Another thought that we have, if you look at the addressable worksite market at $2.2 billion -- we've pulled out some of where we don't play, like products that we don't offer right now and don't have a desire to manufacture right now. We see about a $2.2 billion addressable market. And if you just add with this second bar up here, employer sizes from 1,000 to 2,500, you have almost a 50% increase in addressable market. And we've amassed now some assets. Web Benefits Design is a key acquisition for us that we think allows us to scooch higher a little bit in terms of market, and gives us a 50% increase, over $3 billion addressable market.

And when you look on the right and say, well, it's going to be too crowded there, how can you manage that many larger accounts? We actually don't do a lot over 500 lives. Our sweet spot has been in the 100-life range. And so we've got a lot of room to grow over on the right side of the graph here. And when -- if you kind of run some of your numbers and look at a 2% to 3% penetration on that $900 million, you can kind of get a sense of what we might be able to achieve in terms of sales growth.

So how can we be successful with those tailwinds? Four key assets that we'd like to talk about, and it's a pretty similar story tell to what Scott did. First is, I'll talk briefly about the product portfolio. Karen and Paul are going to talk more about the financials and the specifics of those products when they're up here after we do a question-and-answer and a break. I'd like to talk about diverse distribution because we have the same dynamics as the consumer division, a number of different ways to access the market.

And then using that distribution, we found a way to build an enrollment capability, our own enrollment firm, and so I wanted to spend a brief moment and explain that to you and how that's taking independent and wholly-owned distribution, putting them together. And then the last piece that we've probably been most active on is the technology element of this. The Web Benefits Design acquisition was a piece of this, some of the other work that we do, tools to help our field agents. And so I want to walk you through that quickly as well. First is the broad product portfolio. We have strong voluntary products. We have broad national coverage. There's very few places where those products aren't positioned now. And now it's just getting distribution resources in place. As I talked earlier, we have over 25,000 groups under management right now so we have some experience dealing with groups. We also have some value-added service offerings to help people with things other than just their financial needs. We have relationships with the American Cancer Society, some other third-party vendors that bring some services to bear at claim time to help people navigate, whether it be a cancer diagnosis, heart attack, those kinds of issues.

And then also, when you reflect on what you've seen in some of the earnings, the loss ratios in particular on these supplemental health products have run favorable for us and in our guided range. So that we're also feeling really good about the kind of business that we're putting on the books through the worksite. So move to that next asset. If you think of my 4 boxes from the previous page, this is the distribution piece. We also have the wholly owned and independent mix here. About 86% comes from the wholly owned distribution. And this is that Worksite Division of that PMA U.S.A. Scott referenced the consumer side of that PMA U.S.A., where those agents are the traveling agents that work in the rural areas. This is the worksite piece of the PMA U.S.A. agency, about 450 folks around the country working with small employers. And then we have access to a number of independent partners and they help us sometimes in some geographies where we're not as strong with wholly owned, and they have some different approaches and relationships as well.

One of -- our expertise, again, I want to reemphasize, is in those smaller groups, less than 1,000 lives. We go a little bit bigger and have been successful in the public sector. They tend to behave like collections of smaller groups, even though there's a kind of a master group, whether it be a school superintendent or accounting executive. But the public sector works well for us in an emerging practice for us now. And unions is another place where we seem to be successful. I want to talk about the embedded enrollment firm, at what we call the Washington National Enrollment Solutions. And this was that third element of the assets and how we're putting things together. I thought maybe just like a case example or a story on how does this thing work versus just running you through a process chart or how we came up with some brilliant idea. We have a couple of partners in Wyoming -- in Cheyenne, Wyoming. Very successful there. And they occasionally run into groups outside of Wyoming and they contacted us a couple of years ago and said they had a 100-life group in Pennsylvania. But they're in Wyoming, and they started to do the math and said, well, we've got to fly a couple of people to Pennsylvania, and then we're going to have to stay in a hotel for a week and eat meals and then have our administrative cost as well. They did the math and said, we're not going to sell that group. We can't enroll that group. It doesn't make any sense from a cost perspective. In comes our wholly owned distribution who has people in Pennsylvania and said, we could do that enrollment for you. You found the group; we can do the enrollment for you. So we get those 2 groups together. The commissions are split and everybody wins. We have new customers, our distribution partners have a new relationship with a group and everybody wins.

And so that's what our enrollment -- that spawned this idea to say, wow, we should, like, package that up and make that a program. And that's where we came up with Washington National Enrollment Solutions. Another thing that we do, we have a number of partners who like to open groups, build relationships, but don't have the time to go back and do what we call re-service groups. And so our wholly owned distribution will go in, visit with those groups and do reenrollments at an annual or whatever basis that we see as necessary.

We've seen almost $2 million last year, and we launched it in the middle of the year. And this is something now that we market. We created a brand, and we're super excited about this Enrollment Solutions, really gives us an enrollment capability. Last piece is technology. The exciting fun part to talk about: Web Benefits Design. When we talk about technology, you can't talk about technology without talking about Web Benefits Design. A best-in-class software, offer a full solution to allow clients to manage their employee benefits, including their insurance programs. So that's something we like about that. We're also really excited about the management team and the expertise that they bring to the table on small business and HR practices because that's who they're talking with every day, employers and employees. So that kind of brings us closer to the customer. And then another thing that's super exciting about Web Benefits Design is they move very quickly from a technology perspective, not the slow insurance company, mainframe kind of approach. Kind of joke with Bethany Schenk, she's here today, the CEO of Web Benefits Design.

And when we talk about products taking a year to get implemented, and she said, we don't do anything that doesn't take a pay period, pretty much to get things implemented. And so we're really excited about bringing that kind of approach into the business. The other thing that Web Benefits Design offers then for CNO is a door opening-opportunity for our agents. So now to be able to not just talk about voluntary benefits products. But to be able to talk about a technology solution as well all of a sudden can prolong a conversation and eventually lead to increased sales.

We also like the -- once you have a tie to it, like a ben admin platform. We like the persistency dynamics of that because people would have to leave the product and the platform. So we like that. Also a very compelling offer for benefit brokers. So obviously, when you're working with benefit brokers, oftentimes, they are in the seat of providing these kinds of solutions, so we can support brokers with this kind of technology solution to make them look good for their employers.

Then the other thing, to be honest with you, even just from a plain old leads perspective, Web Benefits Design right now has 500-ish clients and less than half of them offer voluntary benefits right now. So that's a whole bunch of doors to knock on, just with our -- within the family company. And then lastly, to me, what is most compelling -- and we talk about this a lot and how can we continue to take this out into the market. Is this uncommon mix now all in one place of in-person enrollment, telephonic enrollment and online enrollment. All in one place, all with one company. And so that's something that I think provides tremendous opportunity for us in the future because we're not trying to navigate multiple companies or saying we're only going to play in one lane.

So why would we think that we could take these assets with these tailwinds and do anything with it? Actually, I wanted to share the strong track record, something that a lot of people have been hard at work on over the last few years and actually the last 10 years in terms of building this practice from infancy to where it is now. First is the agent growth, you can see the folks that do our recruiting. We've grown 14% last year, 16% over the last couple of years. So we continue to grow the agent count. One of the neat dynamics about recruiting into a worksite model is you're actually -- you're hiring commission sales folks, but you're giving them a place to work.

So you hire them, you train them and say, I want you to go to this car dealer on Monday, and that's where you're going to work for the week. And you're going to do enrollments versus asking them to go knock on a bunch of doors or just give them a set of leads and say, good luck to you, we'll see you in a couple of weeks. Geographic expansion, I talked about as well. Geographic expansion, last year -- as I mentioned, 45% of our new groups coming from those new geographies. We did over $5 million in new sales just in states that we added over the last couple of years. New product launches, we continue to keep it fresh. We had 2 key new product initiatives. First was our worksite universal life, our life insurance has delivered 20% growth in 2019 coming off of 2018, where we grew 42%. So you see that hockey stick in life insurance. We've changed our mortality risk from 15% to 23% in the last 2 years. And so we like that risk mix as well, health and adding the mortality risk.

Another launch that we did was a hospital indemnity product, which is becoming very popular right now, especially with more high deductible health plans growing. We launched that right at the end of the fourth quarter of '18, and in 2019 sold $6.5 million in that product alone. So we're very encouraged by those results. I talked on the -- a couple of slides ago about the Enrollment Solutions, and we've seen a couple of million dollars come out of that program as well. I think that's a key area of growth for us as we move forward. And then lastly, the Web Benefits Design has been successful to date. We're really happy about the integration progress, the organic performance of the business and now revenue synergies is where we're headed next year in 2020, which I think will give us another leap in terms of performance.

So you see the results on the bottom, 16% CAGR over the last couple of years. We grew 14% '18 to '19. And again, just some terrific momentum here that we really think we have a lot of things in place here to continue. So looking ahead, here's the -- so here's the strategy first. We want to continue that small group momentum, and I talked to you about doing the same things in new geographies, growing that agent count, kind of sticking to our knitting, if you will, in these small employer groups.

And so we're going to keep doing that. That's where we've been growing double-digit already. We'll do that through agent count. We'll do that through geography. The second place we want to go then is let's start moving upsize a little bit, but not get crazy, but move upsize. We think there's opportunity there. And we started to put together the assets that we think give us a right to win now in some of those larger groups that we didn't have 3 to 4 years ago. And then lastly, is just supporting this growth with additional product development and technology that applies to both. We still think we need to keep the products fresh, and we're always looking for new ideas and ways to go on the technology front. And we're super happy to have Web Benefits Design with us to help us chart that course for our technology future. So we see Worksite as a tremendous opportunity to grow CNO. I think the need is clear. I think the customer and employer need is there, and I think this is a critical way to reach middle-income America's -- middle-income Americans where they work. It's a great place. One of the things I love about the worksite model is that people are already thinking about these issues at work. When you're doing enrollment, you're thinking about your health care, you're thinking about your life insurance. And so to talk about supplemental health and life insurance at the same time, I kind -- we kind of joke in the division that people are in the mood to talk about these things, so let's just go ahead and continue the conversation then, instead of trying to cold call and get them to talk about these issues with you.

So we'll continue this momentum, take advantage of those assets and hopefully start to move up the spectrum a little bit. So I do thank you for allowing me to share some thoughts on the worksite division. I don't want you to take away that we're the immature division. We're just -- it's a younger division growing in. And we're going -- Scott, we're going to catch that Consumer division someday. So what I wanted to do is invite Gary, Rocco, Scott back up here, and I think we're going to do some Q&A now. So thank you for your time.

QUESTIONS AND ANSWERS

Jennifer Childe - *CNO Financial Group, Inc. - VP of IR*

Okay, we've got a mic in the back and a mic here. Any questions?

Randolph Binner - *B. Riley FBR, Inc., Research Division - Analyst*

Randy Binner from B. Riley FBR. I appreciate all the presentation on all the sales initiatives. I guess, my question is, what should we focus on to track your success across these initiatives? Is there 2 or 3 important areas, whether it's fees, NAP? What's your benchmark for success here, given the variety of different sales?

Gary Chandru Bhojwani - *CNO Financial Group, Inc. - CEO & Director*

I'm going to -- I'll make a general comment, and then I'll invite some specific responses. So Randy, first of all, thanks for being here. Thanks for the question. Paul is going to walk you through some areas where we're giving financial guidance. But maybe to be responsive to your question, what I'd like to do is ask my colleagues. I think the best way for you all to think about the business and these initiatives is really, first, to think about them across Worksite and Consumer. Those are the 2 divisions. That's the way we're going to the market. Those are the 2 customer types that we serve.

And then within Consumer, and within Worksite, there's 1 or 2 things the operating leaders are really focusing on. Some of which are, I would argue, leading indicators, and some of which are just progress against initiatives. So I'll let each of them comment on that. Scott, maybe we start with you to comment?

Scott Louis Goldberg - *CNO Financial Group, Inc. - President of Consumer Division*

Yes, sure. So we've been providing a growth scorecard each quarter. I don't think it changes. It's -- when I think about the Consumer Division, what we're trying to do. Obviously, we're trying to bring these channels together in a way that works for the consumer interaction. But I think that there's less -- we're going to optimize this economically, right? Sometimes it's going to make sense to have that sale happen D2C and sometimes it's going to make sense for that sale to happen with an agent.

So I think at least for the time being, I'd spend -- be less concerned about which channel is making the sale, and just step back and look at the top line metrics, at least as it pertains to the Consumer Division, which is we want to collect assets. We're doing that into our own annuities or into brokerage. We think if it goes into brokerage, it eventually comes into our annuities. So: assets; of course, premium; and then fees; and the fourth one is producing agent count. I mean, yes, over time, this could shift, and we could say, okay, we're doing more of this virtually and the local agent becomes less important. Tell you what, I don't think we're going to see that over the next planning horizon. Reality is, a lot of the real sales are still made face-to-face. D2C is a way to engage people, maybe make a smaller sale, maybe begin to bring them in. But I think producing agent count is still going to be one of the metrics that you want to pay attention to.

So it's the things that I showed on the chart, it's premium, assets, fees and agents.

Gary Chandru Bhojwani - *CNO Financial Group, Inc. - CEO & Director*

Mike, do you want to -- from a Worksite perspective?

Michael D. Heard - *CNO Financial Group, Inc. - President of Worksite Division*

Sure, Randy. Not a huge addition there. New annualized premium and then the net revenue at Web Benefits Design are the 2 things I look at, principally, for how we're doing. And then there's some other secondary metrics that we might look at to make sure it's the right risk profile. So looking at product mix and some of those other things. But those top level key indicators: NAP, fee revenue at WBD.

Gary Chandru Bhojwani - *CNO Financial Group, Inc. - CEO & Director*

Rocco, anything you want to add?

Rocco Francis Tarasi - *CNO Financial Group, Inc. - CMO*

The only thing I'd add is -- it is not going to be publically disclosed. But certainly, internally when you look at sales funnel, we are tracking contacts, opportunities, sales, as I shared. And occasionally, I think we'll have stories to tell about initiatives that have driven change there.

Erik James Bass - *Autonomous Research LLP - Partner of US Life Insurance*

Okay, Erik Bass with Autonomous. Can you talk a bit about the producer reaction to the announcement of the changes? And do people see the benefits? Or is there any concern about -- sort of internally about losing some leads that they used to have exclusive access to?

Scott Louis Goldberg - *CNO Financial Group, Inc. - President of Consumer Division*

Erik, I'll take that one. So we've been on a bit of a roadshow in the last few weeks talking about this transformation to our various groups, our PMA, annual sales celebration, and what we call our National Managers Meeting at Bankers Life. And I'll tell you that both have had really good reactions to this as probably folks who are listening to this call.

At PMA, which is obviously the smaller outfit, the story has been about us being able to bring resources of the organization to their programs. They've been a little bit subscale. And they've had to manage on their own P&L. And as you can imagine, there are certain things that you look at from a CBA perspective that don't get funded. Now we have the ability to take resources and investments that were made at Bankers Life and immediately bring them over to that organization, whether they're recruiting programs or other types of support, et cetera.

At Bankers Life, what we told the leadership is the biggest challenge in financial services and in insurance, probably in any business, is customer acquisition. How do you begin to engage that customer? And frankly, one of the channels that is the way most of us begin to engage with products and services, which is getting online and looking at things digitally, had been separated into the Colonial Penn operating company. Now we're able to bring that right into the division and just have much greater opportunity sharing as Rocco puts it. And so they're excited by that. Are they concerned that all of a sudden, these products are all going to move direct and they're going to be out of business? These guys have been doing this for a while. They're not concerned with that. Because as we know, those consumer behaviors that, even though they're changing, they're still changing somewhat gradually. It still is to some degree a product that is sold, not bought. And the products that are moving online the quickest, things like low face policies or simplified issue products, isn't where producers want to make their money.

They want to sell the more sophisticated products that are higher face, higher premium. They want to get financial planning clients where they have recurring fees. So they see this symbiotic relationship that can happen between the channels.

Erik James Bass - *Autonomous Research LLP - Partner of US Life Insurance*

And then one other question. Are there more products that you want to manufacture internally? Or is more of your focus, if you're adding to the product suite, to be doing it through third party partnerships. Is it broadly across the businesses?

Gary Chandru Bhojwani - *CNO Financial Group, Inc. - CEO & Director*

Yes. I think there too, I did invite both Mike and Scott to comment. Again, thinking about both of our consumer types. Mike, do you want to?

Michael D. Heard - *CNO Financial Group, Inc. - President of Worksite Division*

Yes, Erik, maybe I'll start. There's a handful of worksite products that we don't have, disability, vision and dental are some examples. Third-party is where we look right now. We'd have to get ourselves pretty comfortable to get into those product lines, get ourselves comfortable that we might have a right to win. Inorganic options are also a way to kind of accelerate getting into some of those products. But in the meantime, we don't run into any obstacles not having those products. Often other producers might bring those to the table. And when they do, we do have some third-party options to access them.

Scott Louis Goldberg - *CNO Financial Group, Inc. - President of Consumer Division*

Yes. So I started the company 15 years ago. And every product that we distributed was something that we manufactured. And that's how most carriers think about the world. If they don't manufacture it, they don't participate in it. We said, hey, we have an opportunity to leverage our distribution, which many players don't, and certain products, we just either don't feel we're well situated to compete in because maybe they have a network of providers as for instance, with things like Medicare advantage, or there are certain products where we just don't like the risk. Mike pointed to disability, that's kind of a classic product that invites a lot of long tail risk. So generally speaking, we can make a higher margin if we manufacture the product. You have a greater part of the supply chain if you're a manufacturer and a distributor. So we're going to look to manufacture things first. But if we don't like the returns. We don't like the margins. We don't think that we have the capabilities to compete, being able to source the product and sell it through our distribution, gives us a great way to generate fees and boost our ROE.

And I think that, that's a weapon that a lot of other carriers can't deploy because they don't have exclusive distribution. So I think it's going to be a mix. We generally look to manufacture first, but certain products are going to fall into the sourcing category.

Gary Chandru Bhojwani - *CNO Financial Group, Inc. - CEO & Director*

Yes, I just -- I want to add to the comments both these guys made. So first of all I, of course, agree with everything they said. But I want to tie together the last 2 questions because I think it's -- perhaps it's helpful. From my perspective, I want us to stay focused on the middle-income market. And whatever is going to get us into those households, whatever they need, whatever opens that door, I'm interested in talking about. Now if we get into that middle-income household through the worksite because they're at work and they've enrolled on a Web Benefits platform, and they're buying a Washington National Product, great.

If we get into that household because they want Med advantage, which we don't manufacture but a Bankers Life agent goes and talk to that consumer with the Humana Medicare advantage product, and that gets us in the door, and then we can talk to them about annuities in Life? Great.

I'm far less concerned about whether or not we manufacture it. I don't have this proprietary view. I completely agree with what Scott said. If it meets our return threshold, if it makes sense to us, if we've got the expertise, we should do it. Because we'll get more of the margin. We get the distribution and the manufacturing margin. But there is not this sense of ownership that we have to build it, and you see that in our fee income. You can see what's happening with the fee income. Actually, you haven't seen it yet, Paul will show it to you. It's going up very nicely so it will make the point.

But what I really want to do, I wanted to tie the last question together with that. If you think about what we've done with the transformation, really, it comes down to a couple of messages. First, if you're one of our distribution partners, either that's captive or independent, with this change, previously, you might have had access to 1 or 2 products. Over time, you will have access to many, many more products. So whether you're a telesales agent or you're a PMA agent, you will now get access to more products. That's a good news story.

The other thing if you're, say, a Bankers Life agent who's already had a pretty broad product portfolio, you will now get a chance to access leads or get into households that previously weren't shared either as much or as quickly. So that person that calls in on 1-800-Colonial Penn? We will be pushing those leads to our other platforms. So when you think about the combination of those 2 questions and data points, we're going out via the transformation and telling people, you will either get access to more leads or you will get access to more products. And by the way, as we continue to evolve, we don't necessarily limit ourselves to having to manufacture. We're open to building strategic partnerships, whether it's with a Humana or somebody else.

So we will continue down that path. And can I give you a guide, this one we'll manufacture and this one we won't? I can't. I can tell you that we will bring the same discipline that we have to everything else. And you'll see that with -- when Karen and Paul present, you'll see the profit profiles and the margin profiles of the products. And frankly, I think some of you will be surprised. And we will bring that same discipline to that decision process.

Taylor Alexander Scott - *Goldman Sachs Group Inc., Research Division - Equity Analyst*

It's Alex Scott from Goldman Sachs. First question I had was on just your online sales. And I guess, we've all become a bit more familiar with some of these online agent models over the last year. So I was just interested in hearing whether the kind of growth that they're seeing is something that you could see? I mean, are you going after the same kind of online leads that they are? Or I mean, has that gotten competitive to the point where it's not profitable to maybe go after some of those online leads? Or is that an opportunity that you have in front of you?

Gary Chandru Bhojwani - *CNO Financial Group, Inc. - CEO & Director*

I think the bulk of that has been in the Consumer channel, so I'd invite Scott to comment first. And then there's been obviously some online activity even in Worksite, so Mike, I'll ask you to supplement that.

Scott Louis Goldberg - *CNO Financial Group, Inc. - President of Consumer Division*

Yes. It's been really hard to miss what's happening in the marketplace. There's obviously been some big transactions that have happened, particularly in the kind of health space. And we've looked at some of those properties. And our conclusion is that this is a growing and attractive space. There's no doubt about it. We've competed -- specifically, we look at something like Medicare advantage.

We're a big player today, but we do it face-to-face. We think there's an opportunity for us to borrow some of the things that some of these other outfits have been doing and bring it into CNO. We have all the capabilities. And I'd say, if you're looking for where we're going to point our machine next that's a pretty good bet. The -- what's happened in the -- particularly in the Medicare advantage space is there's just been a lot of growth overall. When we talk to our carrier partners. We are one of, if not the leading distributor that looks like we do.

We've been primarily focused in the Colonial Penn brand on the Life side. So we've seen what those -- what other companies have done. And we look at that and we say, you know what, that's an opportunity, and we think we can play and we think we have all the capabilities. And we think that we can -- this is evolving quickly, and we think we can get there.

Gary Chandru Bhojwani - *CNO Financial Group, Inc. - CEO & Director*

Scott, why don't you explain a little bit the thesis and the approach behind GenHealthy?

Scott Louis Goldberg - *CNO Financial Group, Inc. - President of Consumer Division*

So we've been very quiet about a couple of pilots that we've done because they're not material to our results. But there is one thing that we've done that's out in the marketplace, and I'll talk about it now. It's a program that we launched called GenHealthy, and you can go to genhealthy.com and you can take a look at it. And what this is, it's the notion that can we use direct-to-consumer marketing and data analytics to identify individuals who are likely already receiving Medicare benefits, are already outside of their guaranteed open enrollment period. And can we offer them a value proposition where they can receive the same standardized benefits that they're receiving today but at a lower price? And the reason we're able to do that, and we think we can make that offering is because, a, we're able to identify people who already have a healthier profile; and b, they're already outside of their open enrollment period, and therefore, we can underwrite them. And you put those 2 things together, you can offer rates that are kind of below prevailing rates in the marketplace.

So we launched that online property, and we're beginning to drive traffic to it through social media and direct mail and other sort of means. And we think that that's kind of just one line in the water that sort of is in the vein of some of these new ways to approach the market. I'd say, if you look at where we'll be over the next 12 to 24 months, I expect us to have a handful of properties like that in the marketplace that use some combination of data analytics and direct-to-consumer to go after some of these pockets in the market that we haven't been able to exploit quite as well through a broad field force approach.

Taylor Alexander Scott - *Goldman Sachs Group Inc., Research Division - Equity Analyst*

A follow-up question I had, I guess, maybe a little more geared towards the Worksite side. I'd just be interested to hear about if you feel that the Web Benefits Design platform and some of the things that you've done give you a big enough capability now, where there's no obstacles for you to be able to really execute on this. I mean, we've heard about bigger players that offer a full suite that are trying to go downmarket. I think the supplemental voluntary products are a big focus, but then again, you're focused in the small end of the market. So do you have the platform capabilities to be able to execute? And are you seeing the competitive pressures coming down?

Michael D. Heard - *CNO Financial Group, Inc. - President of Worksite Division*

Yes. Yes, great question. We do feel some of that competitive pressure coming down, but I'm not sure coming down kind of as far as where we are. And I think one of our advantages is being small and coming up. And when I look at the way we face-to-face enroll right now, we kind of have that variable cost model that would allow us to go into groups of 50 and 100 that bigger companies, using enrollment firms paying salaried enrollers, aren't going to touch anything under 100 to 200 lives, regardless of the technology unless they can get in there with a pure technology play. And now with Web Benefits Design, we think we can go head-to-head there because it is a comprehensive benefit admin solution.

I think we're unique in having that mix and at least a little far ahead, but definitely a fair point that bigger companies could be coming at us. I feel like, in this case, we have a head start.

Daniel Basch Bergman - *Citigroup Inc, Research Division - VP*

Dan Bergman with Citi. Just regarding the geographic expansion initiative at the worksite, is there any way you could help us frame where we are, kind of what inning we're in on that initiative? And maybe any thoughts around the pace of the lift you'd expect in 2020 relative to the nice uplift we saw in 2019?

Michael D. Heard - *CNO Financial Group, Inc. - President of Worksite Division*

Sure. I'd probably put us kind of fifth or sixth inning in terms of geographic expansion. You saw that we kind of painted the bottom half of the country, and then we've kind of got the East Coast covered. We still have work in the Pacific Northwest and kind of the north plains. And then New England is another place that's particularly unpenetrated for us. And so now it's just a matter of -- you got to have your recruiting machine going or you've got to get independent partners in those places to be able to make some hay. But I would say, fifth, sixth inning, so still a lot of baseball to be played, but we've also established.

Jennifer Childe - *CNO Financial Group, Inc. - VP of IR*

We have time for about one more question before the break. Okay. We're going to take about a 15-minute break.

(Break)

PRESENTATION

Jennifer Childe - *CNO Financial Group, Inc. - VP of IR*

Okay. We're going to get started with the second half of the presentations. I'd like to introduce our Chief Actuary, Karen DeToro. Karen?

Karen Jeannine DeToro - *CNO Financial Group, Inc. - Chief Actuary*

All right. Thank you, Jennifer. Good morning. How's everybody doing this morning? Good. All right. Great. I'm very excited to be here today to talk to you about our product portfolio. So there are 3 key insights that I want you to take away from this presentation. So the first, we have a broad and balanced product portfolio. Second, we have targeted product designs that meet middle-income consumers' needs and enable us to generate profits. And third, we have disciplined and prudent product management. So let's jump in with that first point. We have a broad and balanced product portfolio. In the product space, we're a specialist serving the middle market. We have a well-balanced portfolio of products and a broader portfolio than many of our competitors. We don't just lean in on health or annuities or life. We play across the board to offer the products that are most important to our target markets. This breadth allows us the flexibility to pivot as circumstances change. We not only have these products on the shelf, we're actively marketing and servicing them. This ensures that we retain the muscle memory to pivot if we need to. The insurance margin chart shows you that each of our product lines carries its own weight. Our distribution of insurance margin tracks closely with the distribution of collected premium. Another important benefit that this product portfolio provides is diversification of risk and some natural hedges in the portfolio. The high-low balls on this chart represent the degree of risk present in each of our products. So for some risks, we may have more or less risk present in the portfolio. But for other risks like mortality, there are actually natural offsets in the portfolio. So for example, increases in overall population mortality help us on annuities, and they may hurt us on life insurance and vice versa. So our balanced portfolio provides a competitive advantage through this diversification benefit. And later on, I'll go into more detail on how we manage some of the specific risks on some of these products.

So now I want to turn to my second key takeaway. We have targeted product designs that directly address the most critical needs of Middle America and enable us to generate profits. I'm going to touch briefly on our life and health business, and then I'm going to turn to annuities and long-term care. As Gary mentioned, that's where we get most of our questions. In life and health, we offer a standard set of protection-oriented products that are attractive to the middle market. These products are reasonably simple for consumers to understand, and they deliver a solid and stable margins. Note that we don't offer variable life or variable UL. Those are registered products, and they give consumers direct exposure to the equity markets.

Now I'm happy to answer any questions you have about our life and health products during the Q&A. But the main takeaway here is that our collective premiums and our insurance margins are stable. So now I'd like to spend a few minutes talking about our annuities. We offer both fixed indexed and fixed interest annuities, although like most other annuity writers, we see most of our sales shifting towards the indexed products. Those products represented 96% of our annuity sales in 2019. So the main difference between fixed indexed and fixed interest annuities is how interest is credited. The premiums that we receive are invested in the same assets backing our annuities, but the fixed indexed product offers consumers access to returns that are indexed to the S&P 500. We declare the participation rate at the beginning of each contract year, but we won't know what the actual performance is until we get to the end of that year, and we see how the S&P 500 performed. The returns are floored at 0. So the customer knows that their account value can never go down. The fixed interest product has a credited rate that's based on our expected earned rate and our general account portfolio, less the spread. The credited rate is also declared each year, but it's known in advance. So the customer will know exactly what they're going to earn on their money. The fixed interest return is also floored at 0 or higher, depending on the specific guarantee in the contract. And I'll point out, also, here that we do not offer variable annuities, those are registered securities. We feel like fixed index is a better fit for our market, as I'll show on the next slide. So our fixed indexed annuities are targeted to our market because they offer a middle path for consumers who want the potential for upside by investing in the market, but without the risk that comes with it. So the graph on this slide shows illustrative performance from a period of July of 2008 to July of 2018. So the blue line shows how $100,000 invested in the S&P 500 in July of 2008, would have performed over that 10-year period. And you can see, it's generally good performance once you get past those early negative years. The gray line shows how the same amount would accumulate at a fixed rate that's similar to what we're offering on our fixed interest annuities today. And remember, that this is based on the rate we earn on our general account assets less the spread. And then finally, the orange line shows how that same amount would accumulate at the participation rate that we're currently offering on our fixed indexed annuities. Now note that that's not the actual participation rate we offered over that historical period. That's why this graph is illustrative. Remember that we reset that participation rate every year, so it would have varied over this historical period. But I think that this graph gives you a good picture of why customers like the returns that we offer on our fixed index product. They don't have to worry about losing value in periods where the index underperforms, as in the early years of this graph. They get the potential for a higher return relative to the fixed return, and their principal is guaranteed. So for our target market, they're willing to give up some of that upside in exchange for the downside protection that we offer. And so by offering what I call this middle way, we not only meet customer needs but we manage our own exposure by passing through some of the equity risks to our customers floored at 0. And I'll talk in a little bit about how we manage that portion of the risk using hedges.

Our fixed indexed annuities are also targeted to our market because they are clearer and simpler than the products offered by other writers in the market. We offer simple clear products that they can understand and that we can manage effectively. So I'm showing here a comparison of our guaranteed lifetime income annuity, or GLIA, to another annuity writer's product. And this annuity writer was the second highest seller of annuities, fixed interest -- or fixed indexed annuities in the third quarter of 2019. This is one of the representative products from their suite. We offer our customers a choice between 1 fixed and 1 indexed option. Our indexed option is a simple monthly averaging of the S&P 500, and returns are credited on an annual basis. This other company has 9 indexed options for customers to choose between. And frankly, we see companies out there that offer 20 or more indexed options within a single contract. For customers, choosing between so many options is confusing. And for the companies that offer these, they have to put in place expensive hedging programs to manage such a broad offering of indexes.

Second, we don't offer any complicated bonuses. Other companies may offer bonus structures that kick in at different points of the contract. They're hard for customers to understand. They tend to look really good in sales illustrations, but there's no guarantee that they'll actually materialize. Now we offer a participation rate on the S&P 500. Other companies may have a more attractive looking participation rate, but they may also apply caps. What that means is that if the index over-performs beyond what the cap is, they're not going to credit that to the customer. Or they may take a spread, so they haircut the indexed return before applying the participation rate. The point here is that you cannot just look at participation rate when you're looking across this competitive space.

We don't charge our customers for our guaranteed lifetime withdrawal benefit, whereas some other annuity writers assess fees for this annually. This is important because what it means for our customers is that their account value can never go down. It's floored at 0 and we don't take charges out. So they have the security of knowing that, that account value will not go down from year-to-year.

And then finally, some companies extend the period that customers have to wait before they can take advantage of that GLWB benefit. We allow our customers to access it after one year. So hopefully, I've made it clear how we think our annuities are a better fit for our market. But this market fit isn't just good for our customers, it's good for us. Scott talked earlier about the fact that our Bankers agents sell these products at the kitchen table. They form relationships with their clients. So generally, career agency business tend to have lower voluntary rental rates than business sold through other channels. Also, our agents can only sell our product. So they're not looking to turn customers by moving them to another company. And the customers who tend to buy this product, they're not chasing rate in the market. They're not being courted by the bigger players. They're looking for a product that will give them stability, and so they tend to be stickier with us. So another important point is that our fixed index annuities generate profits. And so let me explain how we make money on annuities. When we receive premium from our customers, we invest it in our fixed asset portfolio. We take what we earn, we subtract out the spread and the remainder becomes what we credit to our contract holders. For fixed interest annuities, we credit that interest directly. For fixed indexed annuities, we use that credited portion to buy options on the S&P 500. And I'll talk more in a minute about how those hedges work. So the spread is our primary source of earnings. It covers our benefits and expenses, and the remainder is our profit. So the charts here show where our spread has been trending recently. The chart on the left is for fixed indexed annuities, and the chart on the right is for fixed interest annuities. The bars show the account value as of 12/31/18 and 12/31/19, and the line show where our margins were as a percent of account value at those dates. So you can see that we're able to maintain healthy spreads on these products even as interest rates have come down.

So now let's turn to long-term care. We offer a long-term care product that is targeted to our market. And we offer a product that is less risky in several important ways that differentiate us in the market. The business we're currently selling is predominantly short-term care. We have eliminated or reduced the benefits that drive the greatest risk in this market. So as you can see from the graphs on the right, only 2% of our in-force policies have a lifetime benefit period, and 94% of our in-force policies have a benefit period of 4 years or less. On our 2019 sales, 92% of policies have a benefit period of one year or less and we've eliminated all benefit periods greater than 3 years. We offer a reimbursement benefit, not an indemnity benefit. So we only pay for costs that are actually incurred by our customers. That reimbursement is subject to a daily limit. For most of the policies that we sold in 2019, the maximum limit that our customers could choose was $250. On average, most are at about $150 of daily benefit. Almost all of our contracts are now sold without an inflation benefit. Most other LTC writers are still offering a 5% compound inflation benefit. Long-term care products may have a restoration of benefits feature. What that means is that the full benefit amount is restored, if the customer goes without care for a period of at least 180 days. And benefits can be restored, even if they've already used their maximum benefit period. We offer a onetime restoration of benefits. But some companies are still offering repeated restoration of benefits, some offer unlimited restoration of benefits over the life of contract.

So finally, 25% of our sales are reinsured by RGA. And we believe we could reinsure more of this business if we wanted to. But we like the profit patterns on it. So we're comfortable retaining 75% of the business. But what's important about our relationship with RGA is that it does serve to limit some of our exposure. But it also provides affirmation that our underwriting is appropriate, our assumptions are reasonable and the product is profitable.

So this less risky product also happens to be a good fit for our target market's needs. You might wonder, if we could still be competitive with a product where we've eliminated some of the richest and riskiest features. But here's the thing, by rightsizing our products and streamlining features, we've actually created a product that better fits the needs of our target market. Our market needs a product they can afford. They can't afford a Cadillac product that will cover every potential future care scenario. So they need to prioritize the short-term care needs that are the biggest concern for them. 50% of all long-term care claims are for a period of less than one year. And the average length of stay in a nursing home for those who are discharged from a nursing home is 9 months. We know that 75% of future retirees don't have long-term care coverage, and that's primarily due to affordability. So by eliminating the richest and the riskiest features from our product offerings, we're able to offer them a product that meets their needs at a price that they can afford.

So our success at reaching this market and managing our financial outcomes is clear from our track record. We have stable collected premiums and stable insurance margins, as shown on the chart here. And we have levers that enable us to continue to manage the risk on this block, as I'll talk about in a couple of slides. So the last takeaway that I want to leave you with is that we have disciplined and prudent product management. And so to illustrate this, I'll again talk about our annuities and long-term care. Disciplined management of fixed annuities means active management of credited rates. I spoke earlier about how we set the credited rates. We earn a rate, we take off a spread, and the rest is what we credit. Every month, we review what we're earning in on our portfolio. And we set the credited rate for the coming year for all contracts with an anniversary in that month. So generally speaking, as earned rates move, our credited rates move in tandem. Now all of our annuities offer a guaranteed floor of some kind. The floor is either at or above 0, depending on what's guaranteed in the contract. When credited rates reach the guaranteed rate, we will begin to experience some spread compression. And that means that we can't keep the full amount of the spread that we had planned to. But a lower earned spread does not necessarily mean that we are losing money. It just means we're earning less than we planned to.

So we often get asked where we are in relation to these guarantees and how much room we have to maneuver in setting our credited rates. The charts at the bottom of this slide show where our current rates are in relation to guarantees. And while some credited rates are currently at guarantees, particularly on the fixed interest portfolio, we still have room to lower credited rates on 76% of our account value. And again, remember that just because we're at guarantees, it doesn't mean that we're losing money on those blocks.

So disciplined management of fixed indexed annuities also requires prudent hedging of the index crediting strategy that we offer to the customer. So as we discussed early on fixed indexed annuities, we don't just pass the credited right to the customer. We use that credited amount to buy hedges on the indexed crediting strategy that we're offering to them. And so the price of those options in the market is what dictates our participation rate. We manage our fixed indexed annuities by fully hedging the index crediting strategy that we offer to the customer. Some companies only partially hedge their fixed indexed annuities. So what they do is they take that credited amount, they use part of it to buy options and they drop the rest of it into profit. That gives them potentially more profits in some periods, but it also creates risk. We are 100% hedged on our liabilities. And as you can see on the graph, that tight matching of assets and liabilities shows that our hedge program is extremely effective. Although the underlying economics are volatile, what matters is that the match remains tight.

So next, I'd like to turn back to long-term care. I spoke earlier about how our product designs serve to limit some of our risks, even as they meet our customers' most pressing needs. I'd like to talk about some of the other actions we take to ensure that we have prudent management of this portfolio. So disciplined management of long-term care means knowing when to derisk your portfolio. In 2018, we entered into a reinsurance agreement with Wilton Re that significantly derisked our portfolio by transferring some of our oldest and riskiest blocks. You can see on the charts that we offloaded almost $3 billion of net GAAP liability as measured at 12/31/2017. On the right, you can see that the block we transferred to Wilton Re had a reserve margin of 3% of net GAAP liability at 12/31/2017. You can also see that the block we retained, which currently has a net GAAP liability of $2.4 billion as of 12/31/19 is sustainable and healthy in total. Our reserve margin on this block has grown from $234 million at 12/31/17 to $255 million at 12/31/19 in spite of interest rate headwinds.

All right. So this is where management of long-term care also means prudent reserving and active management of operations. So the first point I'll make here is that our reserves are calculated using prudent assumptions informed by historical experience. We don't assume morbidity improvement. Other carriers sometimes do, and it can be overly optimistic. We include some portion of rate increases that we filed for but that we haven't yet received. Other companies may include rate increases that they haven't even filed for and that they may not have actuarial justification for. Also in our 2019 testing, we set what we believe is a prudent ultimate new money rate, which was at a 4% 10-year treasury. Second, the economics of our block growth is strong. As I showed on the prior page, although we use prudent assumptions, our 2019 loss recognition testing margin increased to $255 million or 11% of net GAAP liabilities. We have never taken loss recognition testing charges on our open block. Third, we have actively managed the experience on this block by taking rate increases. We've taken rate increases, when warranted, over the 20-plus years that we've been managing this business. Over the last 10 years, we've had 2 rounds of rate increases in 2010 and 2015. On average, we ask for 20% rate increases and we receive 10%.

Finally, we actively monitor our operational processes around long-term care. Our reinsurance agreement with RGA ensures that we maintain appropriate underwriting discipline. We leverage outside key experts, like LTCG, to help us manage our claims and help us understand best practices in that area. And finally, we actively monitor our internal processes around claims, fraud and terminations.

So as we look ahead to 2020, we'll continue to maintain these same themes in the management of our portfolio. With the shift from 3 segments to 2 divisions, we'll be looking to maintain balanced product portfolios in the Consumer and Worksite divisions. We're continuing to develop and launch new targeted product designs that are good for our customers and enable us to generate profits. And we'll continue to maintain our disciplined and prudent management as we evolve our accounting and reporting in response to the GAAP requirements under long-duration targeted improvements.

And so with that, I'd like to turn things over to our Chief Investment Officer, Eric Johnson.

Eric Ronald Johnson - *CNO Financial Group, Inc. - CIO*

All right. Good morning, everybody. And why don't we just jump right into it. We have a lot of information to share with each other. Like everyone else, I get 3 key takeaways. Key -- number one, we're managing through the low-rate environment, I think, very adequately. One thing we're not doing is compromising on what counts for the long term. And what that means is that in the future, risk level we have in the portfolio may go up, and it may go down. But it will only go up when we're being adequately compensated for that, and it's good for the company, we have the capital to support it and it's good for the shareholder. I don't think that condition exists today. Second key point, our general account is in very solid shape, and it turns out quite predictable income. Third key takeaway, I think we're extremely well positioned for the uncertainty of the times and the turn of the cycle. Stepping back from the 3 key takeaways, in the big picture of things, when everyone leaves here today, I really don't want you to talk so much about interest rates and spreads and things like that. Really focus on all the good things Mike and Scott and Gary are doing to really build the sales machine of the future. That's the real story of today. But what I want you to go away with today is confidence that we've got the money in the right place to make the future happen for the company.

Talking about rates. I remember when I first started working, the 10s were between 14% and 15%, yield to maturity. Prime rate was between 18% and 19%. Who even says prime rate anymore? So times have changed quite a lot. But one thing that hasn't changed is, if you're in the investment business, you learn how to fly the plane through all kinds of different market cycles and conditions and land it successfully. And we're going to do that here also. We have a very methodical process with a lot of folks with gray hair or at least hair. But one of the things that's cool about it is, it's largely about -- the machine we've got is, in many ways, largely about managing how yield and risk and credit interacts with the rest of the enterprise. We have a lot of resources and spend a lot of time and energy on risk planning and capital planning, strategic asset allocation and certainly, asset liability management, as Karen was just describing. And if you looked at the tenure of those folks on our team who are involved in all of the exercises, I'm the oldest one, probably, but not by that much actually.

Enough about me. Let's talk about the company. And certainly, the topic of the day is interest rates. And there's one inescapable, which is that as long as new money rates are below book yield, both book yield and net interest income will be pressured. That's the force of gravity. Let me give you some background on kind of the slope of the book yield line, which you see in front of you, which is the top line. And over the last couple of years, it's down roughly 35 to 40 cumulative basis points. Let me -- I can decompose that for you a little bit. Of that 35 to 40 basis points, 15 of them were the long-term care transaction that we did to reduce risk in the long-term care block. That's the largest factor. About 10 of them were a trade we did last year, which we call up-in-quality, which -- more on that later. And the rest of them, roughly 20 are just the run rate drip of low for longer, 3 or 4 basis points a quarter. So a way of thinking about this would be the following. If we turn our portfolio over actively at about 1% per quarter, and we get in roughly 2% of the portfolio per quarter in maturities, prepayments, repayments. That is up to around 3% of the portfolio coming in per quarter. And there's net new sales from all the things that Scott and Mike were describing. So it's 3% or 4% per quarter of the portfolio is coming in. If you take the delta between the new money rate and book yield, let's say, it's a 100 basis points, a 100 basis points times 3.5 is 3.5 basis points. That's roughly the delta in book yield quarter-over-quarter. It's actually a very simple formula. It's just gravity.

From a managerial perspective, keeping our voluntary turnover down to around 1% a quarter or 2% a quarter. Imagine a large room full of hyperactive investment professionals like yourselves, all sitting on their hands all day. That's basically the management task. And we've had turnover as much as 40% of our portfolio in a year when market conditions justified it. We've had it as low as 1% a quarter, last quarter. So we try to do what's good for the company, not what's fun for us. We manage according to the circumstances.

You can see on this chart, it's on your left-hand side, the onetime impacts on book yield from a long-term care transaction. You see the 15 basis points. And from what we're calling the up-in-quality trade which is, you see there the 9 basis points. But what the bigger picture of this page is that basically book yield times AUM creates core income and it trends very predictably. One question you might ask because certainly it's one question I asked myself is the up-in-quality trade, would I do that again? The answer is yes.

And I'll give you the reason. If we're foregoing roughly $10 million to $15 million in income a year, I view that in the nature of an insurance premium. And what we do know is that ultimately, the house will be on fire. And what I can tell you is that I think when that day comes, that $10 million or $15 million a year in foregone income will be viewed as a very, very -- the present value of that transaction, I think, will be very successful. It's good today, for example, to be basically half-weight energy, to be underweight airlines, underweight containers, underweight railroads, underweight auto, underweight metals and mining. More on that later.

Let's talk about variance. We have 2 sources, principal sources of variable income in our general account. The first one is, spoken broadly, from alternatives, which are nontraditional asset classes. Yet we have roughly $580 million AUM in that area, and I'll say some more about it later. If you look at the rolling 4-quarter average quarterly income there. It revolves around the low teens. But it has variance. It can be -- it's been as low as, over the last couple years, $5 million in a quarter. It's been as high as $18 million in a quarter. But the average is pretty clear. By the way, when we're planning for income for a year, we tend to use something around 8%. So it's pretty much always done better than what we've intended it to do. Although it does have some quarterly variance. The second area where we generate variable income is prepayments and calls. Now this is obviously involuntary. And what we do is receive it. We can't -- we don't manage it. Having said that, a good rule of thumb to think about would be 2 to 3 basis points per quarter. And that's an average. As you can see, you've got a big bar that says 10, a little bar that says 2. And the reality is if you stand too close to it, it's hard to see. But if you step back, you can see the normalization. And that's how we think about it when we plan it, and that might be a way for you to think about it when you model it.

One of the key messages I want you to take away today is that our core income, which is book value times AUM is consistently over 90% of our NII. It's very consistent. Secondly, that the noise in variable income, which I just described, has a much lower effect on NII than perhaps you think. 50% changes in variable income creates about a 3% change in NII. So don't focus on the 50% focus on the 3%, right? And that's a very -- it's quite transitory noise, although I do recognize that in terms of its effect on quarterly EPS, it leverages its way down the balance sheet. If you look at the area I boxed there in red, which was the second quarter of 2019. That had a sort of -- I'm calling that the harmonic convergence. It's was all good, pretty much everything worked the way you would ideally like it to. The up-in-quality trade was just getting done. So we were still earning all that income. We had a good quarter in alts, and prepays were a little bit over their norm as well. So it was a really good quarter. There'll be another one of those out ahead of us again, but it's not going to be like that every quarter. So if you're wondering why did income step down the second parts of the year, harmonic convergence doesn't last forever. You appreciate it and look forward to the next one.

We have a quite a traditional portfolio diversified by sector. We have very consistent key risk measures, which we track, probably about 25 of them on a monthly if not more frequent basis. And we're actually pretty consistent with our sector allocations. Although there is much more activity within the sectors than there is across the sectors. And what this tells you is that we're willing to be consistent, and we're willing to be boring as long as we can also be successful in generating the core income the company wants. And I think we're doing all those things.

Another area I get a fair number of questions about is in the structured securities area, particularly around the ABS space. This is roughly 1/4 of our portfolio, which is a little higher than many companies. 97% investment grade, it's a really good fit. Karen described the annuities, and how we've had good margins in that area, in part because we invest heavily in this space. Their credit duration matches up well with fixed income annuities. They have good non-binary outcomes. The market volatility is a lot less than many other fixed income spaces because they're shorter on the curve. They tend to have heavier coupons. They tend to have amortizing structures or prepayable structures, so you're getting cash back from day 1. I'll say, talk a little bit more about it later, I think, but it's a diverse mix of asset-backed securities, RMBS, CMBS and CLOs and some other specialized areas as well. We like it very much. We have a lot of skills in this area. In fact, I'd like to invest more in it, if the opportunities present themselves. We have a commercial mortgage portfolio, which -- this is an area where we like to be boring. We have very conservative underwriting standards. For example, we don't do any construction lending. We don't do any non-stabilized properties. We don't do any raw real estate lending. And we hit it right down the middle of the fairway. CLOs is an area people ask me about often, and here's what I will tell you, we operate with great caution in this area with a true eye to the downside. Our debt portfolio is A and better only, with a strong margin for safety. If you believe Moody's and S&P, which I think you can, no A or better CLO tranche has ever lost money. I don't think we'll be the first to test that maxim. Our equity portfolio, we think, is sized to our tolerance for risk. It's managed. We manage that, those CLOs. We tend to concede on the equity distributions to make sure what we have is high-quality collateral. This is an allocation we've reduced 40% over the last 3 years as the ARB has decreased. We'll tend to put them on when the ARB is producing mid-teens or higher returns. Down here where it is at 8%, 9%, 10% doesn't pay, so we don't do it. So we've actively managed this according to the company's need for return and eye on risk. And I'm very pleased with our results in this area.

I mentioned earlier in alternatives that we have roughly $580 million allocation. I used the term, I'd like to focus on strategies that pay rent. And what I mean by pay rent is, they're just making distributions. There's no J curve. They're making distributions from day 1. Core real estate, infrastructure and private credit are 3 good examples. And those are areas where we have large allocations, and it's produced fairly consistent, stable returns for the nature of this asset class. It's produced less in -- on the upside than stocks. But it has not experienced kind of downside velocity we've seen in stocks the last 2 days, and it pays a heavy current. As I described earlier, we model-in 8% as a run rate. And I think the current income on this portfolio, the carry is north of 8%. So I think we have a good reasonable view on it.

As I said earlier, we are pretty consistent in our attitude toward risk. And we have, over long periods of time, pretty stable key risk metrics, which we monitor very closely. We consider this in close linkage with enterprise capital strategy. And we try to be conscious of competing needs for capital or opportunities for capital around the organization. People often ask me, how do we think about possible allocation changes. We think about it all the time, but we think about it in this context. We don't think about it in isolation from the rest of the needs of the company. As Karen described to you earlier, one reason we've had good annuity results and done better in long-term care than people think we have a right to is, we have a very disciplined approach to asset liability management. I will tell you, we manage at a far higher degree of granularity than we report. For example, you think we have one general account, or you think we have 3 statutory entities. But from where I sit, we have roughly 17 portfolios, which are product portfolios within those entities, which we managed according to the needs of each of those independently. Now it all has to roll up into something that makes sense, but it has to make sense at the granular level as well.

And so let me say a word about low rates. Low rates have exerted a price, but it also -- that environment also has its benefits. The housing market benefits greatly. Commercial mortgage market benefits greatly. Custody credit benefits greatly. Emerging markets benefit greatly, and consumer credit generally benefits. All of those benefits mean there's less credit dilution. Less credit dilution helps offset lower NII. So -- and putting that all aside, we're sitting on close to $3 billion positive AOCI today. All of that is a benefit of having low interest rates. Having said that, NII helps feed the beast, and we like it very much, but I do want to mention that there are benefits to the climate we're in.

My last page is really around kind the macro theme, but it's hard to talk -- which is about quality assets and stable income. Hard to talk about anything, though, in the year 2020 without mentioning recent events in coronavirus, and how are we thinking about that? And it's a human tragedy of unknown dimension. And first, we're an insurance company. We want people to be well, stay well and get well, and we get paid to help them along that journey. And that certainly comes up ahead of investing money for sure. But having said that, most of the sectors that are most greatly exposed or so they say to the current circumstances are sectors that we're -- fortunately, we've been pretty light. We have a very, very small exposure to Asia. Asia and EM directly probably under $50 million. That includes China. Now someone's going to stand up and say, yes, but Chinese fixed income market has done great the last month because of what the government has been doing. True. We're pretty light commodities. We probably have about $120 million in metals and mining in total in the big diversified global names, which will be fine. In terms of autos, all we have is GM, and it's a small amount of that. Containers, we are not a huge investor in container securitizations. We only have less than $50 million. And in energy, as I mentioned earlier, we're probably about half weight. So whether it's by brains or luck, I think we're fairly well positioned for the circumstance we have to the extent we can understand the circumstance we have. I mean, there's a lot yet to be experienced. And the effect on the global economy and just on the local circumstances, we'll just have to wait and see.

So that's my prepared remarks. And then on that note, I'll turn it over to our cleanup hitter, which is our CFO, Paul McDonough.

Paul Harrington McDonough - *CNO Financial Group, Inc. - CFO & Executive VP*

Thank you, Eric. Good morning, everyone. I don't have a joke to start with. I'm sure those we manage you who know me expected me to start with a joke, but I don't have one. Thank you so much for being here. We really appreciate your interest and in most cases, your support of CNO over the years. We are, as I hope has been evident in all of our prepared remarks, we're proud of what we've accomplished in 2019. We are excited about the opportunity that we have to continue to serve our target market and, we think, create value for our shareholders. The focus of my prepared remarks are to provide hopefully some perspective, some insight into our 2019 financials and also provide some outlook, a bit more than we have provided in the past, maybe not quite as much as Gary alluded to in his earlier remarks. And in the process of proving that perspective and outlook, I'm hopeful that I'll leave you with 3 key takeaways that are summarized on this page. So the first point is, as we have established what we think are sustainable top line sales, we're now turning our attention to capturing operating efficiencies: i.e., actually reducing expenses year-over-year, which will offset the headwinds that Eric was just talking about from lower interest rates and will result in a better balance between sales growth and earnings growth.

The second point is that continued strong free cash flow and disciplined capital management will support the 9% to 11% earnings per share growth that Gary mentioned in his opening comments. And the third point is that our disciplined stewardship of the balance sheet will continue to optimize our assets and ultimately enhance shareholder value.

As I think most of you know, we are introducing today a new reporting framework. We posted on our Investor Relations website this morning, a new investor supplement that recharacterizes our '18 and '19 financials in this framework that's summarized in this chart. We also filed that new supplement in an 8-K, and with our first quarter 2020 reporting we'll be formally adopting this with our SEC filings.

So let me just walk you through this chart. These are the main components of operating earnings under the new framework. The first component is insurance product margin by major product lines, so life, health, annuities, long-term care. The second component is expenses that we allocate to insurance products in total, but that we don't allocate to the individual product lines. The third component is fee income; fourth, investment income not allocated to product lines, so not embedded in insurance product margin. And then lastly, expenses not allocated to product lines, largely truly corporate overhead. The sum of all those things is operating earnings. We do believe, and we hope that you'll find that this new framework will provide more transparency and more insight into the profitability of each of our products. You'll see that the -- each product contributes meaningfully to our earnings. I like the fact that it distinguishes -- this new framework distinguishes between different types of expenses, variable and fixed and corporate overhead; and different types of income, net investment income, that related to the assets, the fees, the insurance liabilities and the rest largely relating to our capital.

So in addition to that, look at operating earnings. The new supplement in the new reporting will show top line sales growth for each of our products grouped by the Consumer Division and the Worksite Division. And as you can see here, and just echoing Scott's remarks and Mike's remarks, we've clearly established top line growth, which, again, which we think is both sustainable and profitable.

All right. So in the next few slides, I'm going to provide a little bit more information about each of the major components of operating earnings in this new framework. The first being insurance product margin, which you can see in the chart on the right, grew by 2.8% in '19 versus '18, reaching roughly $890 million. The components of insurance product margin, as defined are: policy income; net investment income allocated to product margin net of insurance policy benefits, amortization and nondeferred commissions; other nondeferred expenses such as advertising, particularly supporting our direct-to-consumer channel; and where applicable interest credited on our annuities. The way that we allocate net investment income to each product line is using the book yield of the actual investments that back the block of business applied to the average insurance liabilities for the block in each period. Notably, insurance product margin as defined here is not reduced by the expenses that we allocate to products in total, but not to the individual product lines. That's all I have to say about that.

The next item is fee income. As you can see here, as Gary and Scott alluded to, the income has grown at a very healthy clip from '19 to '18. I should point out that in the fourth quarter of '19 due to a change of assumptions in estimating lifetime revenue for revenues and expenses related to Med advantage, the fourth quarter '19 fee income was increased by about $6.5 million. But even net of that, a very healthy growth. As I think Scott and Gary alluded to in the Q&A, we like this source of income. Certainly, from an ROE perspective, but also from a tax perspective, as it's a source of non-Life income relative to our non-Life NOLs, which I'll touch on in a bit more detail on a later slide.

All right. This is the largest bucket, if you will, of expenses. So these are expenses that are not allocated to each of the product lines. They're largely fixed in nature. These are the -- it's the infrastructure supporting our businesses and it's the shared services that also support our businesses. And I would point out sort of 2 dynamics that are operating here that are captured in the blue boxes at the top. One is the fact that expenses are increasing, albeit at a decelerating rate, if you look at the chart on the left, which breaks '19 versus '18 into first half and second half. The reason that they've been increasing is that we have certain expenses that I would characterize as mandatory. So think of things like the cost associated with preparing to comply with long duration targeted improvements which the industry will adopt in Q1 of '22. It's extraordinarily expensive to do what you need to do to be prepared to adopt that new reporting. We feel good about where we are. We feel like we're ahead of the curve in being prepared, but we're spending a fair amount of money as is all of our peers. Second example of mandatory expenses are expenses associated with complying with the California Consumer Privacy Act, also very expensive in terms of compliance. The third example is everything that we're doing and the industry is doing generally to help manage cybersecurity threats. We spent close to $20 million in 2019 on just those 3 things alone as compared to less than $10 million in 2018. So that's certainly -- those kinds of things are certainly contributing to the increase in expenses.

The other thing that's adding expense are all the decisions that we've made to invest in growth. Scott spoke to this. Mike spoke to this. And we certainly think that those investments are paying for themselves, helping establish sustainable top line growth, which importantly is also profitable.

Having said that, as we've mentioned a few times this morning, we're now at a place where having established sustainable top line growth, we're turning our attention to reducing expenses. And you've seen a couple of examples of that in the last few months. In November, we issued a press release announcing a strategic technology partnership which will reduce expenses by about $20 million over the next 5 years. In January, we announced our new operating model, which we do believe will be truly transformative. We didn't adopt that model for expense reasons. We adopted it to adapt to what we think are changing consumer behaviors and expectations. But one of the things that we expect will happen, we know will happen, we've implemented this, really, already, is when we go from 3 segments to 2 divisions and simplify our structure, we take expense out. In total, we're taking out about $22 million of expense from our cost structure. We're reinvesting about half of that in the business. So a net savings of $11 million.

Beyond those 2 things that you've already seen, as we went through the 2020 planning process, we simply just tightened our belts. As we're going through the process and going around the table with the executive leadership group, everyone had to contribute. Beyond that, we've, I think, been thoughtful about identifying specific initiatives that would take cost out. And so we're actually expecting that expenses in '20 versus '19 will actually go down.

These are -- this is the last bucket of expenses. This is really -- it's really corporate overhead, not allocated not embedded in product margin, not allocated to products in total, things like public company expenses, board related costs, some portion of executive comp, that sort of thing, trending down, reflecting our expense management discipline.

All right, turning to investments. So in this new framework, there are 2 buckets of investment income. The bucket on the left is in investment income that's allocated to the insurance product margin. We've deliberately kept the scale on all 3 of these charts the same, which highlights the fact that the bucket in the middle, which is the net investment income not allocated to product, is tiny compared to the bucket on the left. The assets supporting net investment income allocated to insurance product margin are primarily fixed income with some -- a portion of our alternative investments, largely allocated to some of our longer duration products. The balance in the middle is mostly what Eric described as the variable components of income. So the lion's share of alts. Interestingly, and you could not have seen this in our old reporting, the net investment income allocated to insurance product margin actually increased year-over-year by about by about $14 million. And there are 2 dynamics happening there. One is the insurance liabilities actually increased by about $0.75 billion in '19 versus '18. And at the book yield on the portfolio in '19, that drove about $38 million of incremental NII.

Going the other way is the fact that book yield is declining based on the gravity that Eric described. And so the net investment income on the beginning portfolio was lower than what it produced in '19. And that went the other way, the net of those 2 things was the positive $14 million. On the other hand, the bucket in the middle went down by about $42 million, which is largely a reflection of the volatility that you're going to get in that space. And so that's ultimately the gravity that Eric was describing.

So putting that all together, I spoke to each one of the major components of operating earnings. You can see that in '19 versus '18, we had growth in insurance product margin, growth in fees, and that was offset by higher expenses and the headwinds from net investment income. If I think about what's our conclusion about that. As I mentioned at the outset, we're actually very proud of what we accomplished in '19. And notwithstanding this total dynamic, if you just think about the macro context, both in terms of lower interest rates and also in terms of where we have been in our journey, focusing very much on establishing sustainable top line growth and sort of during '19, pivoting to a more balanced sales and earnings picture.

Okay. Turning away from earnings and focusing on capital. I think as most of you know, we've been reevaluating our target capital, largely in the context of the very different risk profile of our business in the wake of the long-term care reinsurance transaction that Karen talked about. My thesis, when I joined the company in the second quarter of last year, and Gary was certainly pushing me in this direction, given the reduced profile that we ought to at least look at our target capital. And you would think that in the context of a lower risk profile that the target capital would go down. But we didn't want to make that kind of a decision without really being thoughtful and doing some analysis. So we've done that analysis and have concluded and have decided and are sharing with you today that our target capital inside the operating companies, we're reducing from what it had been, 400% to 425%, down to a new range of 375% to 400%. All else equal, that frees up about $125 million of capital. We, in arriving at that decision, certainly worked through the rating agency capital models to make sure that we, and each of the rating agencies were aligned on those models. There is some redundancy in each of those models relative to our current rating. We also used our own internal capital models to have an independent view of what would be appropriate in terms of target capital, largely shocking the balance sheet with stress tests and having an informed view of how much of a cushion we should have.

And lastly, we looked at peer companies and their publicly stated target capital. And from the standpoint of all of those things, concluded that this new target was appropriate. At the holding company level, we're not changing our previous target, which was minimum holding company liquidity of $150 million. That's about 2 years of interest expense and about a year of parent company expense. That seems an appropriate level. We're not changing that. We're continuing to target leverage, so debt to total capital of 22% to 25%. We're comfortably in that range and will remain so.

I think as all of you will recall, we refinanced a portion of our debt during '19. And so our debt capital is, we think, in a good position in the wake of that refinancing. And then lastly, we remain very committed to our investment-grade ratings. The company fought long and hard to get back to investment grade. We were upgraded by Moody's on the heels of the long-term care transaction in '18 and and by S&P and Fitch in the middle of '19, but largely also in reaction to that transaction. I should say that when we were reaching the decision to reduce the RBC target, we did talk to each of the rating agencies to try to make sure that we were aligned with them on that. We don't have a bright line answer from them because that's not how they operate. Bob Garofalo and [Erica Reynolds] are actually here. And so they could tell you themselves if we ask them that we don't have a bright line. But in the context of the discussion we have, in the context of redundancy in the models, in the context of what we think will be continued stable operating results, I'm very confident that this reduced capital doesn't have any adverse rating implications.

Free cash flow. So as mentioned on the previous earnings calls. For the full year 2019, we generated about $330 million of free cash flow on a gross basis and about $290 million at the holding company, net of the capital that was retained in the operating companies to support our organic growth. Relative to our operating income of $290 million that translates to free cash flow conversion of close to 100%, which I think is probably one of the more compelling aspects of our financial profile. We will continue to be disciplined and opportunistic in our approach to capital allocation.

Those of you who tuned into our earnings calls will be very familiar with the left side of this slide. Captured on the right side, in 2019, as Gary mentioned, we returned $319 million in capital to shareholders through a combination of ordinary quarterly dividends and a share repurchase. That's 13% of the market cap at the beginning of 2019. As Gary mentioned, the highest level of capital return since 2015. And over the last 3 years, we've returned over $700 million of capital to shareholders or 25% of our current market cap. In 2019, we also closed on the Web Benefit Design transaction that Mike talked a lot about, which certainly improved our market presence and capabilities in the worksite space.

As stewards of the balance sheet, we're always looking for ways to maximize the value of our assets. And as a great example of that: in 2019, no news, but I just wanted to emphasize the tax strategy that we adopted in the fourth quarter, which resulted in a reversal of the tax valuation allowance that we had to the tune of $194 million; which flowed through net investment income in the fourth quarter and increased our book value per share at year-end '19 by $1.29; contributing to a 13% growth in book value per share ex AOCI for the year. As of year-end '19, we had about $0.5 billion of life NOLs and about $2 billion of non-life NOLs with the combined economic value of just over $400 million using a discount rate of 10%, which equates to $2.71 per share, which I'm nearly certain is not fully reflected in our current stock price.

Also, as stewards of the balance sheet, we're, I think, appropriately conservative in setting assumptions and recording our liabilities. I think this is evident in the very modest impact on earnings in 2019 from the annual review of actuarial assumptions. Despite lower initial earned rates and reduced ultimate new money rates, we had no loss recognition triggered in our FAS 60 products, reflecting, I think, very healthy reserve margins in those products; and a modest $10 million of unlocking in our FAS 97 products.

I'll conclude now with our 2020 outlook, noting again that we've elected to provide some more guidance than we have historically, perhaps not as much as some would like. As we've said a number of times now, we expect earnings per share off of $1.80 base; significant items in 2019 to grow by 9% to 11% in 2020, obviously, benefiting from share repurchase. We expect earnings in absolute dollars to be flat to slightly up, with continued growth in sales, insurance product margin and fee income; a decrease in expenses, as I mentioned earlier; offset by continued headwinds from lower interest rates.

Based on net free cash flow at the holding company between $330 million and $380 million, we expect to have the capacity, not necessarily the commitment in the context of how we think about capital allocation, but the capacity to deploy $75 million in share repurchase per quarter, absent compelling alternatives. So that's it. Thank you very much for your attention. We look forward to another Q&A session. But first I'll ask Gary to come back to the stage.

Gary Chandru Bhojwani - *CNO Financial Group, Inc. - CEO & Director*

Thank you, Paul. All right. I am the final impediment between all of you and lunch, I guess, me and Q&A. So as I wrap this up, I want to begin by just, again, placing in context where we've been. If you look at the company and just step back a moment to think about some of the things we've done. The first thing that I want to ask you to remember, and I've said this a number of times on our earnings calls, please judge us by our actions. I think we have a story to tell, and I think we have a certain amount of credibility where we can say, we say what we do and then we do what we say. We try and keep it very simple. And if you look at what the company has been through prior to 2017 when we were really focused on the turnaround and de-risking the balance sheet and cleaning up various things, there were a number of things there that we did that I think were absolutely critical and really positioned us for the future. And then in 2017, roughly, we started to pivot towards growth. Now there were a couple of other things there that we did such as the LTC transaction during that period. But largely, we were really focused on getting that growth engine going again. And I think we've demonstrated that. Now we've had several quarters of consistent top line growth so we feel like now that we've built the growth momentum back -- we cleaned up the company. We've built the growth momentum. That's up and running, now is the opportunity for us to maximize profitability. And again, I think one might be tempted to say, well, why couldn't we do it all at the same time. And I go back to where I started today's meeting. Based on my understanding of how insurance works and having been in this business for 30 years, it's not possible to take -- to cut expense, grow sales, have a net investment income headwind and still drive earnings. You can't do all 4 of those things. There's a certain amount of sequencing that just has to happen, particularly when you're facing net investment headwinds like we've been facing. And so I think that the sequencing was the right way for us to do this.

And so now we turn to 2020. We've been pretty clear about some of the expense efforts. We signaled those. We announced them in late '19 and early 2020. We're now executing against them. We've been pretty clear about our capital and how we view the less risky nature of the company. And Paul, I still disagree with you. I think the amount of guidance we're providing is a ton. At least a ton more than I'd like to. But that's a different discussion. I think we've had a demonstrated ability and willingness to be thoughtful about how we deploy that capital. And I think we've done that in a shareholder-friendly way. And so now we look at 2020, we've got a number of different opportunities. You heard from the businesses in terms of how we're bringing some of these assets together and what that represents. So that's all fine and good, but what does it mean? You all have a lot of things you can decide to invest to -- in. And some of those choices may be within the insurance sector, some maybe outside the insurance sector. But at least, as you think about your options to invest in the insurance sector, I'd ask you to think about a couple of things when you're looking at us against other enterprises. First, about 90% of our earnings come from controlled distribution. Any company will tell you that the more business and more earnings you get from that controlled relationship, the stickier they are going to be. There's no surprise there. You don't have the same pressure to churn. That agent is tied to that one manufacturer. And 90% of our earnings come that way. I think the other thing that we've talked a little bit about, but I want to be really explicit on, when we think about that notion of controlling the client relationship, remember that when you sell an insurance product, whether it's auto or homeowners or Life or LTC or whatever it is, for every consumer, that insurance product is typically an expense. And what do we want to do in life with expenses? We want to minimize them. When you create a relationship with a consumer where you are getting assets from them, whether it's in the form of an annuity or they're investing -- the parking assets at your broker-dealer. When you have assets, the relationship fundamentally changes. You are no longer an expense to be minimized, you are an asset to be grown. And I always come back to this point. There's a fundamental change that happens because even if that consumer decides they're going to move away from you, if you've got one of their annuities or they've got money in a mutual fund with your broker-dealer, at the very least, you're going to get a chance to get that last phone call to try and hold that relationship. You don't always get that when you're in insurance sales. 2/3 of my career has been spent as an agent, and I know this the hard way. Sometimes clients just move. But if you have something that's an asset, the nature of the relationship changes. So I really want to emphasize this point, 90% of our earnings come from controlled distribution, and even within that controlled distribution, because the product mix is changing, and we're doing more things like annuities and broker-dealer, even within that, we're making the relationship that much more likely to be sticky or persistent. 65% of our business is coming from life and health protection products. Now in the last several months, part of the reason we've made this change with the reporting, it became evident to Paul and me that through these discussions, there really wasn't a lot of clarity on where our margin was coming from or an understanding of our product margin. I think there's a much more robust mix here than maybe is appreciated it first. So that's part of the reason we adopted that change in reporting. And

I think when you look at how much of it, 2/3 coming from life and health, there's a lot of volatility that's frankly isolated by virtue of this mix. This is a good thing. 99% free cash flow conversion in 2019. We continue to have an ability to generate strong cash flow, and we'll continue to be disciplined and opportunistic in how we deploy that.

As important as the agent relationships are, and as much emphasis as we place on that, we're also mindful of the fact that consumer behaviors are changing, that they expect to have research or purchase or other decisions made online or on the phone and so on. And we're adapting to that. We've got a heck of a machine at Colonial Penn in terms of using analytics, in terms of understanding how to interface with the consumer on a direct-to-consumer basis. And with our transformation to that Consumer Division, we have an opportunity to leverage that expertise throughout the organization and really share leads and drive things between all the different customer touch points.

And then finally, our Worksite business. Mike talked about the individual assets that we have there and the opportunities that we have there. Worksite is one of the fastest-growing distribution models within the insurance space. And you can see that in the way certain companies are valued in terms of the multiple they attract and so on. We ourselves have had 6 consecutive quarters of double-digit growth. Now granted, it's been a relatively small base, but we're ramping that up, and we're extremely excited because with the addition of the technology platform and the former Web Benefits Design, we really feel like we've positioned ourselves to be one of the few players in this space that, like our Consumer business, we're focusing on a smaller client, middle market consumer. And in this space, we have the manufacturing, we have the distribution and now we have the technology. I think we're extremely uniquely positioned.

So as I wrap us up, maybe just one quick thought that's not on the slide, just to kind of summarize. If you're trying to decide whether or not to invest in this company and be a part of the story, I'd ask you to think about just a couple of really simple things. I've talked about the positioning and the key takeaways and the cash flow and all that other stuff. But let's make it even simpler. This is a company that's operating in a space where there's a tremendous secular tailwind. Meaning, you've all seen the stats, 10,000 people retiring every day, the whole baby boomer demographic, all this sort of stuff, right, we're serving a market that will continue to grow for some period of time. And within this growing market, we've got a niche called the middle market. Everybody talks about serving the middle market, but no one is focused the way we are. And it's hard to focus on this because even if you've got the cost structure to do it, the reality is, if you've got salespeople out there that like calling on $2 million clients, they don't want to go focus on the $100,000 client. And that's just simple human nature. So we've got this secular tailwind. We've got a really unique focus that nobody else is really getting after the way we are in terms of just being focused on that middle market, and we're using that focus or we're getting into those relationships, and we're staying in through a unique combination of being able to do it face-to-face or direct-to-consumer online. While we're doing that, we're throwing off a lot of cash. And the beauty of that cash is even when we enter economic times where our net investment income is challenged, and therefore, the ability to generate higher absolute earnings dollars is challenged, we can still drive EPS because of the amount of cash we're throwing off. And so as you think about some of the things we've talked about that are unique to us, and if you really boil it down that simple and think about the secular tailwind we have, think about the niche market focus, think about our ability to get in and stay in, think about our ability for the cash and then how we deploy that cash. I don't think you're going to find a lot of folks that are going to tick all those same boxes and have all those same assets.

I want to thank you again for your support and interest in CNO. I think we're going to move to a Q&A time.

So with that, I'll invite my 3 colleagues back up, and we'll go from there. Thank you.

QUESTIONS AND ANSWERS

Humphrey Lee - *Dowling & Partners Securities, LLC - Research Analyst*

Humphrey Lee from Dowling and Partners. Gary, I appreciate your comment about the -- how you anchor your customer relationship with the benefit of annuities and mutual funds. Can you maybe kind of give us some color in terms of how much of your existing customer base is also owning a -- whether it's a fixed annuities or mutual funds products through your broker and dealer network?

Gary Chandru Bhojwani - *CNO Financial Group, Inc. - CEO & Director*

We've had our annuity balances go to $9 billion right now. And our -- the assets at our broker-dealer is $1.5 billion. So as a measure of total assets, that gives you a picture. In terms of how many of the households that we serve, I don't know if we've got that data handy, I would guess it's, I don't know, less than 20% for sure in terms of have -- using our broker-dealer. Okay, single-digit percentages on the broker-dealer? And of the households we serve, what would we guess is the penetration in terms of how many of the households we serve have annuities with us right now? Single-digit percentages. So call both of those sub-5% in terms of what the current penetration is. Now the way I look at that, and I tend to look at the glass half full. I think that represents the magnitude of the opportunity we have, that the vast majority of households where we have a relationship where they trust us, we haven't yet penetrated with our broker-dealer and/or annuity offerings.

Humphrey Lee - *Dowling & Partners Securities, LLC - Research Analyst*

So I guess, my follow-up question is, what action plans do you have in order to capture more of the penetration? For like -- is it simply by having more agents that is licensed to sell securities? Or is there something else that you need to do in order to get that penetration?

Gary Chandru Bhojwani - *CNO Financial Group, Inc. - CEO & Director*

Yes. There's a couple of things I want to mention about that. So first of all, as we've demonstrated, I think, through multiple quarters, if you think about our actions at Colonial Penn, if you think about our annuity sales results last quarter and so on, we are perfectly fine taking our foot off the gas pedal on a given product set or a given customer set, if it doesn't make economic sense to us. Now in the case of annuities, I tend to think we'll do okay this year. I don't think the growth will be nearly what you saw last year. That's in part due to the fact that we're coming off of such a strong base from last year and in part because of market conditions. But what we're going to do with annuities, we continue to remain committed to the product. We think it's good. We think our customers need it. But I think right now, as an industry, fixed indexed annuities are going to show modest to slightly negative growth. And I'm perfectly fine with that. So we continue to encourage it, but we're not going to go out and go crazy with it because I think market conditions are just really tough right now. When you've got the 10-year running at 1.30%, I think it was when I last looked, I think that makes it tough. But we'll continue to encourage it because I think that trend will change.

As respect to broker-dealer, the primary way for us to continue to drive that relationship is to encourage our insurance agents to get licensed. And so that remains a press for us. I think we've previously announced guidance that we want to do 1 in 5, we envision, of our agents. So the agent force continues to grow. We believe that, over time, roughly 1 in 5 should get a securities license. And today, we're at 1 in 7, give or take. So that's what we see as the opportunity, and that's how we're going about driving it.

Humphrey Lee - *Dowling & Partners Securities, LLC - Research Analyst*

That's helpful. A question for Paul. So you talked about the expenses, how 2019 saw some mandatory expenses that drove some of the increase, and you kind of alluded to, for 2020, you should see expenses to come down. Should we expect that in terms of the mandatory expenses to be largely flat year-over-year? And so by 2021, we could see even a further reduction on overall expenses in addition to your kind of planned expense saves?

Paul Harrington McDonough - *CNO Financial Group, Inc. - CFO & Executive VP*

Yes. So our expectation and built into our plan is that expenses will actually go down in 2020 versus 2019. I don't really want to go further than that in terms of guidance. I don't want to get into a reconciliation each quarter of specific dollars versus expectations. But you should expect broadly that expenses, particularly that primary bucket that's allocated to products but not individual product lines, will go down.

Ryan Joel Krueger - *Keefe, Bruyette, & Woods, Inc., Research Division - MD of Equity Research*

Ryan Krueger, KBW. On fee income, can you just give us any perspective on how you're thinking about the potential growth rate there going forward? You obviously had significant growth in the last year. But can you help us think about 2020?

Paul Harrington McDonough - *CNO Financial Group, Inc. - CFO & Executive VP*

Sure. So Ryan, again, I don't want to give specific guidance on that sort of component of earnings as well. I think sort of trending '19 into '20 would be appropriate adjusting for the change in assumptions that had the $6.5 million benefit in Q4 would be the best way to try to model it.

Ryan Joel Krueger - *Keefe, Bruyette, & Woods, Inc., Research Division - MD of Equity Research*

And then for Eric, the last couple of quarters, you've had the book yield go down about 5, 6 basis points. You gave us a 3- to 4 basis point example. I guess, is 3 to 4 basis points more your expectation going forward? Or is that just illustrative?

Eric Ronald Johnson - *CNO Financial Group, Inc. - CIO*

I think the 3 to 4 wasn't illustrative. But I wouldn't frame it, put it in the context of guidance or anything like that. But I think it's a model framework that you can use to develop your own view as to what to expect. I think I've pretty consistently over the last number of quarters, said given the puts and takes of the noise that flows through and all the adjustments that flow through the portfolio in a given quarter, anything from, I think I've said 3 to 8 kind of fits, is a model fit. And so all those the numbers we've just discussed would be within the realm, would square with my expectations. There are many, many other puts and takes than the ones we described here today.

Erik James Bass - *Autonomous Research LLP - Partner of US Life Insurance*

Erik Bass with Autonomous. I wanted to follow-up on Humphrey's question on expenses. I think your guidance is to get to the $22 million of run rate savings by the end of this year. I guess, how quickly does that come in? And thinking about it, if you're getting to that run rate by the end of the year, it would imply kind of a lower level of expense in '21. And also, are there other expense savings that you kind of alluded to, but there may be other buckets in addition to kind of what you've outlined at this point that we should think about?

Paul Harrington McDonough - *CNO Financial Group, Inc. - CFO & Executive VP*

Sure. So Erik, I want -- I would encourage you to be careful about focusing too much on the examples that we've given. Because if you think about our direct expenses that are over $600 million, that $22 million is small. We focus on it because it's something specific that we've done that we can identify as an example of the kinds of things that we're doing to reduce expenses broadly. As I mentioned in my answer to Humphrey, I want to be very careful not to get into a scenario where we're reconciling to numbers every quarter. What I do want to leave you with is that we are being aggressive and thoughtful about how we manage expenses. Our intention and our expectation and it's built into our plan is that we reduce expenses. And that will support broadly earnings that are flat to slightly up in absolute dollars. And then through the benefit of share repurchase, achieve the 9% to 11% in our guidance.

Gary Chandru Bhojwani - *CNO Financial Group, Inc. - CEO & Director*

Just one general comment to add to that. I think Paul touched on this. I just want to make sure I'm a little bit more forceful about it. We can't do anything about what's happening with interest rates and the impact on net investment income. But we also recognize that our shareholders expect us, fine, if you can't control certain things, you better go look at everything else that you can control. And that's the mind-set we're bringing. We have to do that every day, every quarter, we have to do that in this NII environment. We can't just let the NII control us. We have to do what we can do.

Taylor Alexander Scott - *Goldman Sachs Group Inc., Research Division - Equity Analyst*

It's Alex Scott from Goldman Sachs. Question I had was just on the cash flow numbers that were mentioned. Should we consider the, I guess, what you've been doing in terms of capital behind new business, it was -- I just want to clarify, it was net of that? So that was what was it, $30 million to $50 million roughly? And then I also just wanted to inquire as to how much excess capital that assumes in terms of the drawdown? And I appreciate you don't want to give more detailed guidance, but just having that composition would help us better think about just ongoing regular way ex drawdown of excess capital, cash flow?

Paul Harrington McDonough - *CNO Financial Group, Inc. - CFO & Executive VP*

Yes. So maybe, Alex, just to clarify, when we talk about gross and net, what are we talking about? So for the last year or 2, we've referenced free cash flow before the capital needed to support growth. And that's basically assuming no growth. That when we say gross, that's really what we're referencing. What I think is more meaningful is what actually comes out of the Opcos up to the Holdco. And so the net free cash flow is what I'm referencing there. So the $290 million in 2019 was actually at Holdco and available for dividends, share repurchase and other growth opportunities. Well, largely M&A opportunities. The guidance that I've provided for 2020 is that same net concept at the Holdco, is between $330 million and $380 million. And my guess is you and others are doing the math and saying, well, wait a minute, if it was $330 million gross in '19 and you freed up $125 million, the $330 million to $380 million seems light. And it is based on that math. And obviously, the reason is we're hedging a little bit and retaining more in our model in the Opco for growth, potentially redeploy some capital in the asset portfolio, as Eric said, to the extent that -- the opportunities to take risk, and we feel we're being compensated, we could deploy some capital there.

Randolph Binner - *B. Riley FBR, Inc., Research Division - Analyst*

Randy Binner, B. Riley, FBR. Just kind of a follow-up there. The sense -- is there a sensitivity in the lower RBC goal or guide to the move that we've had in interest rates? When you formulated this plan, the 10-year wasn't in the 1.30s. So is there kind of a quantum for every 25 basis points in the 10-year that we might want to not assume we get that cash out. Is there some kind of sensitivity you can provide on that?

Paul Harrington McDonough - *CNO Financial Group, Inc. - CFO & Executive VP*

Randy, thanks for the question. It's a good question. I'm just going to think out loud a little bit here. I don't -- I mean, the biggest exposure is to equities. And we actually saw that in the fourth quarter of '19. It had a big impact on our year-end -- sorry, fourth quarter of '18, had an impact on our year-end '18 RBC. Our exposure to equities is much lower today than it was back then in the wake of the up-in-quality trade that Eric talked about. So we don't have nearly the exposure there. In the fixed income portfolio, I mean, to the extent that the lower interest rates is causing stress for companies and the companies get downgraded, you could see an impact there, but I'm not sure, at least in the short term, there's a direct correlation. Eric, would you add anything?

Eric Ronald Johnson - *CNO Financial Group, Inc. - CIO*

Yes, Randy. As of today, I think we have an assumption for a certain amount of capital strain from assets that we build into the planning process every year. I don't see anything that threatens to turn that upside down at all right now. Paul mentioned, for example, that we have a substantially lower equity exposure or allocation than we did in 2018. It's about 1/10 of the size. So that's not going to do it. I think, while there have -- there's always going to be, if we have 900 CUSIPs, corporate CUSIPs, there's going to be a downgrade here or there. Some sparrows can fly into the window. I don't think any really big birds are going to fly into the window that are going to do any violence to the arithmetic Paul is talking about.

So no. I think to the extent NII corrodes by a small amount in absolute dollar amount because of the interest rate environment, then, I guess, you might have that marginally small, less amount of stat income. Again, not going to do violence to the numbers that Paul is talking about.

Daniel Basch Bergman - *Citigroup Inc, Research Division - VP*

Dan Bergman with Citi. Any help you can give us in terms of how to think about what level of interest rates is embedded in that 9% to 11% EPS growth guidance? If rates remain at current levels, is there some risk to hitting that range? Just any thoughts around how we should think about that would be helpful.

Paul Harrington McDonough - *CNO Financial Group, Inc. - CFO & Executive VP*

Sure. So in our 2020 plan, in the 2020 outlook that we shared, we presumed a new money rate of around 4%. With the 10-year sitting at 1.30% that might be a little bit of a stretch. But given that you get some of that back with spreads, we're probably not too far off. And my guess is we don't sit here at 1.30% forever. My, just my two cents is we end up settling out maybe at 1.50%. Again, with slightly wider spreads, we're probably not too far off 4% new money rates. We're also 2 months into the year. I think our new money rate for the fourth quarter will probably be at or around 4%. To try to dimensionalize it, if instead of for the full year, if instead of a 4% new money rate, it was 3.50%. That would reduce full year earnings by $6 million, $7 million pretax.

Ryan Joel Krueger - *Keefe, Bruyette, & Woods, Inc., Research Division - MD of Equity Research*

Ryan Krueger, I just -- separate follow-up. Maybe I'll get an answer from Karen, let you talk up there. On the indexed annuities, the 3 -- you have over a 3% spread, which is generally higher than I think most peers, at least that we see. I guess, are you still achieving similar spreads on new business at this point?

Karen Jeannine DeToro - *CNO Financial Group, Inc. - Chief Actuary*

I mean, just like Gary said, we're always looking to see how we manage our spreads relative to the competitive environment. So we will get how we balance that out over the course of the year. But I would say, in general, yes, we're still looking to achieve those spreads. And I want to point out, too, that when you think about our spreads, you need to remember what I said before, which is, that's where the benefits expenses get paid out of and then that some portion of it gets dropped into our profit. But then generally, just like Gary said, we are looking to maintain our pricing discipline, even as we're tackling those interest rate headwinds.

Taylor Alexander Scott - *Goldman Sachs Group Inc., Research Division - Equity Analyst*

Alex Scott from Goldman Sachs. I had one more follow-up. Just was interested, you mentioned the work you've been doing on LDTI. So just thought I'd ask if you have any updated comments you could provide on how you think that will change the way that we need to view your reporting. And I thought it was interesting that when you showed the asset liability durations that the assets actually had a little bit more duration than the liabilities. I think that probably is not the case for a lot of peers. So just thoughts around how that could affect what we kind of conclude as we get through all of that work and you guys disclose?

Paul Harrington McDonough - *CNO Financial Group, Inc. - CFO & Executive VP*

Sure. So maybe I'll start, Karen. And so on the LDTI, as I think I mentioned in my earlier comments, or maybe it was during the break, I don't recall. But in any event, we feel like we're ahead of the curve in terms of our planning and preparation for adoption in Q1 '22. We're not far enough along to have a view that we're prepared to share as to what the impact is upon adoption, and how to think differently about our financials on a quarterly basis post adoption. So that -- I think that's really all we can say on that topic unless you want more color around what we're doing to get prepared. On the ALM...

Karen Jeannine DeToro - *CNO Financial Group, Inc. - Chief Actuary*

Yes, I think I would look to Eric to sort of talk about that, the fact that our assets are looking a little bit longer than our liabilities.

Eric Ronald Johnson - *CNO Financial Group, Inc. - CIO*

Yes. And that's worked well for us, as you can imagine, for a really long time, given the path of rates. It's also worked well for us because by the nature of having the captive distribution and the nature of the products we sell, they don't tend to be very interest-sensitive on the liability side. So the cash flows on the liability side are quite predictable. And that allows us to be thoughtful around duration matching. And we've been -- very consistently, we've applied pretty strenuous product level guidelines, where we don't allow ourselves very much tolerance at all for out -- being out of match with more interest-sensitive products in maybe some of the annuity type things, investment leverage type products. They're closely matched. You get into long-term care or a specified disease or universal life, some of the really longer tailed products. We tend to be a little more flexible. Because those cash flows happen a long time from now, and they're also, tend to be pretty consistent. So I think this is an area we thought pretty hard about. We have a very intentional process, and we're positioned very intentionally in that way.

Jennifer Childe - *CNO Financial Group, Inc. - VP of IR*

Any other questions? Okay. We'd like to thank everyone very much for your attendance, both in person and online and look forward to speaking with you again soon.
