

Principal Financial Group®

4Q 2021 Earnings Call Transcript

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Call participants

Executives

Dan Houston: Chairman, President & CEO

Deanna Strable: Executive VP & CFO

Amy Friedrich: President - U.S. Insurance Solutions

Renee Schaaf: President - Retirement & Income Solutions

Pat Halter: President - Global Asset Management

John Egan: VP - Investor Relations

Analysts

Ryan Krueger: KBW

John Barnidge: Piper Sandler

Alex Scott: Goldman Sachs

Tracy Benguigui: Barclays

Tom Gallagher: Evercore ISI

Jimmy Bhullar: J.P. Morgan

Erik Bass: Autonomous Research

Josh Shanker: Bank of America

Andrew Kligerman: Credit Suisse

Presentation

Operator: Good morning and welcome to the Principal Financial Group Fourth Quarter and Full Year 2021 Financial Results Conference Call. There will be a question-and-answer period after the speakers have completed their prepared remarks. If you would like to ask a question at that time, simply press star and the number one on your telephone keypad. We would ask that you be respectful of others and limit your questions to one and a follow up, so that we can get to everyone in the queue.

I would now like to turn the conference over to John Egan, Vice President of Investor Relations.

John Egan: Thank you and good morning. Welcome to Principal Financial Group's fourth quarter and full year 2021 conference call. As always, materials related to today's call are available on our website at principal.com/investor.

There's been a key change to our Financial Supplement in the fourth quarter that I want to mention. We changed our definition of AUM to exclude assets managed by third parties on our Retirement platforms. This had an impact on our reported total company AUM and net cash flow from how we reported previously. Additionally, we broadened our definition of assets under administration to include AUM and other assets, for which we earn a fee for providing administrative services. A detailed definition for both AUM and AUA is included in our Financial Supplement. We restated historical time periods in the fourth quarter supplement to reflect the new definitions.

Following a reading of the Safe Harbor provision, CEO, Dan Houston; and CFO, Deanna Strable, will deliver some prepared remarks. Then we will open up the call for questions. Others available for the Q&A session include Renee Schaaf, Retirement and Income Solutions; Pat Halter, Global Asset Management; and Amy Friedrich, US Insurance Solutions.

Some of the comments made during this conference call may contain forward-looking statements within the meaning of the Private Securities

Litigation Reform Act. The company does not revise or update them to reflect new information, subsequent events or changes in the strategy. Risks and uncertainties that could cause actual results to differ materially from those expressed or implied are discussed in the company's most recent Annual Report on Form 10-K filed by the company with the US Securities and Exchange Commission.

Additionally, some of the comments made during this conference call may refer to non-GAAP financial measures. Reconciliations of the non-GAAP financial measures to the most directly comparable US GAAP financial measures may be found in our earnings release, financial supplement and slide presentation.

We'll provide 2022 guidance on our upcoming outlook call scheduled for Wednesday, March 2nd. Dan?

Dan Houston:

Thanks, John and welcome to everyone on the call. This morning I'll review the successful milestones we achieved in 2021, share key performance highlights for the fourth quarter and full year 2021 and discuss our go-forward strategy highlighting the growth drivers of our business. Deanna will follow with additional details on our fourth quarter and full year 2021 financial performance as well as an update on our current financial and capital position.

Reflecting on the year 2021 was truly transformational for Principal, filled with many milestone achievements. First in June, we successfully completed the integration of the IRT Retirement business, one of the largest acquisitions in our history. The remaining integration will be completed later this month when we migrate the trust and custody business to our platform. This acquisition solidified Principal as a top three retirement provider in the US with a balanced footprint across small, medium and large-sized plants and expanded platform capabilities to better serve our customers.

In October, we celebrated our 20th anniversary as a public company, a turning point that launched two decades of exponential customer and AUM growth. As we look out over the next 20 years, I have no doubt that

Principal is well positioned to lead and continue meeting and anticipating the needs of our 51 million customers.

And perhaps our most significant milestone, we completed an intense strategic review of our business mix and capital management approach. We aligned on a clear go-forward strategy focused on our growth drivers of Retirement in the US and Emerging Markets, Global Asset Management, and US Benefits and Protection. These are higher growth markets, where we have established leadership positions and differentiated solutions to compete and win. We committed to a strengthened capital management approach, improving capital efficiency, and returning excess capital to shareholders. With this focus, we announced we would exit the US retail fixed annuity and retail individual life markets, pursuing strategic alternatives for our retail fixed annuity and ULSG blocks.

Over the last seven months, we did this and more. We ceased sales of retail fixed annuities and focused our Individual Life insurance segment on serving the business market in the third quarter of 2021. We entered into an agreement to reinsure our retail fixed annuity and ULSG blocks last week, we increased our return of capital to shareholders, and we met or exceeded all of our financial targets from 2021 outlook for the enterprise and for each of our businesses.

Turning to our financial highlights on Slide 4 and 5. In the fourth quarter, we delivered strong results, including non-GAAP earnings of \$498 million or \$1.85 per diluted share, a 25% increase over the fourth quarter of 2020. Reported full year non-GAAP operating earnings were over \$1.8 billion or \$6.77 per diluted share. Full year 2021 earnings per share increased 37%, significantly higher than our 18% to 20% guided range. Overall, our strong operating performance allowed us to return approximately \$1.6 billion to shareholders in 2021. And more than \$520 million in the fourth quarter alone, capping a robust year of capital deployment. Now turning to our growth drivers and our go-forward strategy.

In Global Asset Management, we continue to achieve excellent performance across our breadth of in-demand strategies. At the end of 2021, 63% of Principal mutual funds, ETFs, separate accounts and collective investment trusts were above median for the one-year time period. Performance across our strategies improved significantly compared to the third quarter. Importantly, our long-term performance for the 3, 5, and 10-year periods are all above 80%, and 79% of fund level AUM is rated 4 or 5 stars from Morningstar. This strong performance positions us well to attract and retain assets going forward.

For the full year, strong performance in differentiated solutions drove positive sourced PGI net cash flow of \$2.9 billion. Positive institutional flows were partially offset by retail outflows. Investors continue to look to us for differentiated solutions within real estate, high yield, private assets, and emerging markets.

PGI managed net cash flow was a negative \$500 million for the full year as we had outflows from our PGI managed retirement assets. Despite this, strong investment performance drove record PGI managed AUM of \$547 billion and PGI sourced AUM of \$276 billion. We continue to add new capabilities to provide forward-thinking solutions to our customers. As an example, Principal alternative credit closed 2021 with a more than eight-fold increase in committed capital, advancing on plans to expand our private debt capabilities.

As John noted on the start of the call, we changed our AUM definition in the fourth quarter, and reported \$714 billion of AUM managed by Principal, a 7% increase from 2020. Under our prior definition, fourth quarter AUM would have been over \$1 trillion compared to \$981 billion at the end of the third quarter.

Outside the US, momentum continues across our Asset Management and Retirement businesses. With record full year pre-tax operating earnings in Asia, as well as strong growth in retail equity net cash flow in China and Southeast Asia, our equity AUM in China nearly doubled in 2021 and our digital AUM grew more than 200% over year end 2020.

In Chile, we produced strong net cash flow for a second consecutive year, including positive net cash flow in Cuprum and record net cash flow in our mutual fund business. We recognized the recent election of President Elect, Boric brings a level of uncertainty for the future of Chile's longstanding pension system. We're actively engaged with the new government regarding any potential legislation to reform the pension system. And we will leverage our Retirement expertise to advocate for pension sustainability and policies that strengthen financial security for our customers.

Turning to US Retirement, despite higher dollars of withdrawal in the fourth quarter, primarily due to favorable equity market performance and seasonally higher contract withdrawals, full year net cash flow was positive for RIS-Fee. On an account value basis, net cash flow benefited from strong transfer deposits and the best contract retention rate in over a decade. Recurring deposits increased nearly 40% compared to 2020, including a 15% increase on our legacy block in addition to deposits from the IRT retirement participants. The number of participants making deferrals increased approximately 60% compared to a year ago, including a 10% increase on our legacy block.

With the integration of the IRT Retirement business now complete, we have turned our full attention to capitalizing on synergistic opportunities, both on the expense and revenue side, which are emerging in tangible ways. The transaction was done to grow scale and maximize the value of these assets, and we have clear signs this is happening.

Net expense synergies through the end of 2021 benefited earnings by \$25 million. On a run rate basis, we've realized about \$50 million, more than half of our \$90 million target. These savings will increase after The trust and custody business migrates to our platform later this month. We're also realizing increasing revenues from automatic IRAs, IRA rollovers, and expanding relationships with existing customers across the enterprise.

In US Benefits and Protection, we delivered tremendous growth aided by increased demand for benefits, robust hiring, and favorable wage trends in our target market. Notably, group benefits full year in-group growth was a record 4% for the total block and over 5% in business with under 200 employees.

Full year sales for Specialty Benefits were up 10%, and premium and fee growth was over 7%. In group benefits, we are seeing increases in the number of products per customer, both for new and existing customers. Higher sales and excellent customer retention coupled with a strong macro environment and competitive labor market give us a great deal of confidence in 2022 for continued market-leading growth rates.

Overall, Principal enters 2022 with significant momentum. The execution of our strategic review has made us a better company, prepared to compete and win in an evolving market. Our transformed portfolio was already driving terrific results, both financially and for our customers. As we look ahead, we will continue focusing on the right markets and the right customers, leveraging our competitive advantages. Executing on this strategy, we have great line of sight and confidence in achieving our long-term financial targets.

Before I turn it over to Deanna, I want to thank our employees without whom we would not have had such an exceptional year. Their dedication to Principal and their commitment to our mission is at the core of our success. We will continue to invest in our people and ensure that we are prepared as our industry evolves.

I'd be remiss if I didn't also take a moment to recognize Renee Schaaf, our President of Retirement and Income Solutions, who announced her retirement last week after 42 years with Principal. Renee has held several leadership positions across the company with global and domestic responsibilities, and most recently, led the Retirement business through a period of significant growth and transformation with the acquisition and integration of the IRT business. Thank you, Renee, for your leadership, your passion and your commitment to Principal.

We also announced Chris Littlefield, our current General Counsel, will assume leadership for our US Retirement and Income Solutions business. Chris has been with Principal since 2020 and joined us with significant C-suite operational and leadership experience having served as CEO and President at Aviva USA and Fidelity and Guaranty Life Insurance Holding. I have all the confidence in Chris's ability to grow the business, create value across our lines of business and champion digital transformation.

Mark Lagomarcino, who previously served as Senior Vice President and Deputy General Counsel, will step into the General Counsel role as Chris moves into his new role. He will also serve as Corporate Secretary to the Board. Deanna?

Deanna Strable: Thanks, Dan. Good morning to everyone on the call. This morning, I'll share the highlights of our financial performance for the quarter and full year, as well as an update on our current financial and capital position.

Full year net income attributable to Principal of \$1.7 billion included a \$137 million of net realized capital losses was lower than expected credit losses of \$31 million, \$20 million of which were in the fourth quarter. Excluding significant variances, full year non-GAAP operating earnings of \$1.8 billion or \$6.64 per diluted share increased 15% and 17% respectively, compared to 2020, above our 8% to 10% guided range for EPS growth. This included \$470 million in the fourth quarter or \$1.75 per diluted share.

The non-GAAP operating earnings effective tax rate was approximately 21% for the fourth quarter, and 18% for the full year. The quarter was above our 16% to 19% guided range primarily due to state and GILTI taxes. Since the end of 2020, we've increased ROE 340 basis points to 14.3% primarily through growth in earnings.

As shown on Slide 17, we had several significant variances that impacted non-GAAP operating earnings during the fourth quarter. Benefits from favorable variable investment income, inflation in Brazil, higher-than-expected Encaje performance and lower DAC amortization in RIS-Fee

were partially offset by COVID-related claims and IRT integration costs. These had a net positive impact to reported non-GAAP operating earnings of \$41 million pre-tax, \$29 million after-tax and \$0.10 per diluted share.

Variable investment income was \$68 million pre-tax higher than expected in the quarter, primarily driven by alternative investment returns and prepayment fees. For the full year, variable investment income was \$234 million higher than expected.

COVID continues to impact results in RIS-Spread in US Insurance Solutions. With approximately 125,000 US COVID-related deaths in the quarter, the net \$32 million after-tax impact was higher than our rule of thumb. Group Life and Individual Life COVID claims continue to be elevated as the Delta and Omicron variants have had a greater impact on the working age population. We'll provide an update on our expected COVID impacts for 2022 on our March 2nd Outlook call.

While we adjust earnings for the net positive significant variances we experienced throughout the year, our free capital flow benefited from these net positive impacts and contributed to the higher capital return in 2021, as well as our planned capital return in 2022.

Looking at macroeconomic factors in the fourth quarter, the S&P 500 index was up a 11% and the daily average increased 4% compared to the third quarter. The daily average increased 29% from the year ago quarter, benefiting revenue, AUM and account values in RIS-Fee and PGI.

Foreign exchange rates were a headwind compared to the third quarter, but a tailwind on a trailing 12-month basis. Impacts to reported pre-tax operating earnings included a negative \$4 million compared to third quarter 2021, a negative \$3 million compared to fourth quarter 2020 and a positive \$11 million on a trailing 12-month basis.

Overall, 2021 was a strong year, fueled by a favorable macro environment and growth in the businesses. PGI delivered record full year pre-tax operating earnings as revenue and margin benefited from strong

management fees, performance fees and disciplined expense management. Pre-tax operating earnings and margin benefited by \$28 million from net performance fees in the fourth quarter and \$58 million for the full year, exceeding our expectations by approximately \$35 million to \$40 million for the full year. Excluding the higher-than-expected net performance fees, PGI's margin was 42% for the full year.

Turning to capital and liquidity, we are in a strong financial position and are focused on returning excess capital to shareholders. At year end, we had \$2.6 billion of excess in available capital, including \$2 billion with the holding company, higher than our \$800 million to cover 12 months of obligations. \$80 million in excess of our targeted 400% risk-based capital ratio, which ended the year at 405% and approximately \$500 million in our subsidiaries. We will continue to maintain a 20% to 25% leverage ratio and expect to pay down \$300 million of long-term debt that is set to mature later this year.

As shown on Slide 6, we deployed approximately \$1.6 billion of capital in 2021, including more than \$650 million of common stock dividends, and approximately \$920 million through share repurchases. This includes approximately \$350 million of repurchases in the fourth quarter, and in total is higher than the \$600 million to \$800 million guided range for repurchases in 2021.

Last night, we announced the \$0.64 common stock dividend payable in the first quarter, a 14% increase from the dividend paid in the first quarter of 2021. This is in line with our targeted 40% dividend payout ratio and is reflective of our strong business performance.

As announced last week, we now plan to return up to \$4.6 billion to shareholders between 2021 and 2022 through share repurchases and common stock dividends. This includes \$2.5 billion to \$3 billion of capital to shareholders in 2022, reflecting our targeted 40% dividend payout ratio, and to \$2 billion to \$2.3 billion of share repurchases.

Before turning to Q&A, I wanted to address a question that came up on our Transaction Call last week, where we announced the re-insurance of our entire US retail fixed annuity and ULSG blocks.

At Investor Day, we provided GAAP reserves for US Retail Fixed Annuities of \$18 billion and ULSG of \$7 billion for a total of \$25 billion as of March 31st of 2021. On our call last week, we referenced statutory reserves as of the end of the year for US retail fixed annuities of \$16 billion, and ULSG of \$9 billion for a total of \$25 billion. For retail fixed annuities, GAAP reserves are relatively the same as statutory, but we had some expected runoff in the block which reduced the reserves. For ULSG, there is approximately a \$2 billion difference between GAAP and statutory reserves. Due to the specifics of the transaction, statutory reserves, this is a more relevant metric.

As we move forward with a refined focus and strengthened capital deployment strategy, we will continue to invest in our growth drivers of Retirement in the US and select Emerging Markets, Global Asset Management, and US Benefits and Protection, all with an aim to drive long-term shareholder value.

This concludes our prepared remarks. Operator, please open the call for questions.

Operator:

At this time, I would like to remind everyone that to ask a question you may press star and the number one on your telephone keypad now. Again, ladies and gentlemen, that is star one for any questions. We'll pause for just a moment to compile the Q&A roster.

And your first question will come from Ryan Krueger with KBW. Please go ahead.

Ryan Krueger:

Hi. Thanks, good morning. I had a question on RIS-Spread margins of 73% for the year on a normalized basis. That was above your guided range. Can you comment on if that was driven by, maybe favorable

mortality experienced during the year, or if you think it was say just better general trends in the business?

Dan Houston: Yeah. Thanks, Ryan. Really appreciate the question. And no question, Spread was strong this – this quarter and full year. Renee, do you have the specifics on that one?

Renee Schaaf: Yeah, absolutely. And Ryan, thank you for that question.

When we look at the Spread operating earnings throughout 2021, we're very pleased with the results, of course, and they were strengthened by very positive net investment income. We also saw slightly better non-COVID experience play out through the year. We will give you more guidance in terms of what to expect in 2022 in the upcoming Outlook Call.

But the one thing that I would like to remind you of is that we remain very disciplined in how we manage this block of business. We're very careful about the risks that we take on to make sure that our pricing discipline which creates the kinds of returns that we would expect long-term. So, thank you for that question.

Ryan Krueger: Thanks. And then, do you have any updated thoughts on how to think about the sensitivity of short-term rates on the IRT business going forward?

Dan Houston: Renee, please.

Renee Schaaf: Yeah. I suspect you're referring to the sweep deposits there. Is that what you're asking about?

Ryan Krueger: Yes, that's right.

Renee Schaaf: Yes, okay. Yeah, so let me explain what we've done with the sweep deposits. As you'll recall, when we announced this transaction – the acquisition of the IRT block of business, the sweep deposits were tied very closely to the IOER rate. And, of course, IOER rate quickly went to zero, which had an impact of about \$70 million to \$80 million of revenue.

In the last half of 2021, we purposefully reached out to Trust & Custody blocks of business and began to convert those deposit accounts on to a Principal deposit sweep program that essentially moved those deposits onto our balance sheet. And so now we generate revenue on those deposits through net interest margin. The impact of this on our annual run rate basis is about \$40 million in additional revenue, which helps significantly to shore up the financials for the IRT block of business. So, we will again give you guidance on this in the Outlook Call for 2022. But so far to this point, we've had about \$2 billion of sweep deposits come onto our balance sheet.

Dan Houston: Ryan, appreciate the questions. That's a good example of Renee and her team looking at some of the challenges on the IRT block and ways to leverage current capabilities of Principal, in this case, Principal Bank, to receive those deposits and add more value to shareholders. So, we really feel good about the innovation and the creativity of the team to get us to a healthier spot. Thank you.

Ryan Krueger: Thank you.

Operator: The next question is from John Barnidge with Piper Sandler. Please go ahead.

John Barnidge: Thank you very much. Alt inflows were at the highest level in really a very long time. Can you maybe talk about that opportunity to grow that? And is that going to be a bigger focus for you? Thank you.

Dan Houston: Yeah. Thanks, John and good to hear you this morning. And I'll have Pat to take that. But again, it's an asset class we're all too familiar with real estate and it is adding a lot of value at a time of very low interest rates. Pat?

Pat Halter: Yeah, thanks. Thanks for the question, John, and as Dan mentioned, real estate is a big part of that growth in the alts AUM. As you probably know, we're one of the top real estate investment managers globally in terms of the size of our real estate footprint and the size of the assets under management we have. And we've seen, like a lot of other alternative managers, really grow their real estate capabilities and their real estate presence. And we continue to see some very, very strong deposits, some very strong ability to take the dry powder of our clients' commitments and deploy that into the marketplace and continue to see some very, very strong new commitments of capital from clients that we either serve today or new clients that we're generating a new relationship with.

So, you'll probably continue to see and hear more of the growth story around real assets – private equity, real estate assets and private debt real estate assets as a part of our growth engine going forward, John.

Dan Houston: John, do you have a follow-up?

John Barnidge: Yes, please. If I could, thank you very much. Can you maybe talk about the COLI opportunity in the backdrop of wage and benefits inflation in the fight for talent? Thank you.

Dan Houston: Yeah. You know it's exciting because that certainly fits with our strategy of exiting the retail portion of life and doubling down on the business life insurance and we see that as a real growth opportunity. Amy, more details, please?

Amy Friedrich: Yeah. So thanks for the question, John. We do see COLI as a great opportunity. And as you know, we've built up a huge market-leading position in – in terms of being experts in the non-qualified marketplace.

So whether that non-qualified funding, and again, that's going to be part of our TRS suite, and it's going to help our Retirement business as well as our USIS business. And so that knowledge is built on not only knowing what COLI business or Insurance products we can put in place to help fund those plans, but also giving them alternatives for mutual funds and other pieces of business.

So, when we look at that COLI opportunity, where we've really distinguished ourselves is we are consultants in that marketplace, we tend to know that marketplace best, we tend to also know the insurance placement products the best as well in the industry. So again, with our new narrowed focus on the business market and employer opportunities for life insurance, expect to hear more from us in terms of COLI production.

Dan Houston: Thanks, John.

John Barnidge: Thank you.

Operator: The next question is from Alex Scott with Goldman Sachs. Please go ahead.

Alex Scott: Hi. First question I had is on PGI. That's a place where you know there's no doubt you're disciplined on expenses and so forth has produced very strong earnings and margins. And so, I just wanted to understand how you're thinking about the sustainability of those margins as we think through you know some of the wage inflation impacts that are out there, as well as potentially T&E maybe coming back into that business a little bit. Any color you can provide there.

Dan Houston: Yeah, appreciate that – that question, Alex. You know, one thing I will say about the asset management business, it's incredibly scalable, and there is higher cost of doing business, but we have a lot of capacity and a lot of ability to add assets to existing capabilities. And PGI frankly has got a

great track record as you point out of aligning their expenses with the revenues. And so, with that, Pat additional thoughts?

Pat Halter:

Yeah. So, Alex, appreciate the question. First let me start with just on the revenue side. We have, I think a broad depth of specialist investment capabilities. So I feel very good about the diversification of our revenue streams and diversification of the solutions we can offer to the clients throughout the world, whether it's retail, retirement or institutional. So, I feel good about the revenue sort of side of the equation.

Relative to the margins, as you heard in our sort of discussions, we continue to see some very strong margins north of 40%. I think you know 2022 will be a year where we're going to try to continue to maintain strong margins, we'll probably at the Outlook Call discuss margins going forward in terms of what we see. But we're going to continue to absolutely manage our business very aggressively, in terms of both generating growth, with that very depth and broad depth of specialist investment capabilities we offer to the marketplace, but also to continue to have very strong expense management discipline.

That being said, Alex, we will continue to invest for growth. We're developing a very strong alternative credit platform in terms of private credit to the marketplace. And we're very excited about that platform, what it may mean in terms of revenue growth in the future. We are investing in talent. You highlighted wage increases and we're not immune to that. But we believe we need to continue to invest and continue to nurture new talent within the organization. And that will be a very keen focus for us.

If you may recall in December, we actually were noted again for the 10th straight year as best place to work in money management. We're one of only five asset managers in the globe that have achieved that recognition for 10 straight years. So we're very proud of the fact that we can attract and retain talent. And we're going to continue to aspire for that in the future.

We'll continue to invest in new technology to make sure that our client experience continues to be very strong. So we will continue to be investing for growth and for the retention of a very important client experience going forward. So, I feel good about the year ahead. And for those reasons, Alex, hopefully has helped you in terms of our story as we think about profitability and sustainability organization.

Alex Scott:

That was very helpful. Thank you. And I had a follow-up question on international. I think Mexico has some pension reform that goes into effect at the beginning of the year that has an impact on the commission rates. And so I just wanted to see if you could help us think through like quarter-over-quarter, what that commission rate decline will do to revenue? And you know, I assume you know it may take some time to offset the expenses. And what that can mean for the bottom line for that business? And you know I think there's puts and takes, it sounds like AUM probably in terms of flows, you'll benefit over the long-term. So I appreciate you know there's two aspects of it that maybe you can comment on. But I just wanted to make sure I had my hands around you know immediate sort of decline in revenue that we should expect.

Dan Houston:

Yeah, hi Alex. Really appreciate the question. And there's been sort of two bites to the apple, if you will, in Mexico, because they had codified a new set of rules on what the fee structures could be and then what the change. Look, frankly, with a stroke of a pen, they adjusted even further downward. And so we're well under way to aligning expenses with future revenues, we had a path that was charted in terms of, as you pointed out, growing our AUMs at lower basis points. And now we're sort of back at the table again, looking at our expenses to ensure that we can align those expenses with the new projected revenues.

All of that is to say, we still believe that the Mexican Afore business is one worth investing in and continuing to be part of. Scale matters, capabilities matter, we do have a differentiated capability. And as you know, we've streamlined some of the operations down there with the divestiture of our life and annuity business that we mentioned last week on our call. And when we get to the 2022 Outlook call on March 2nd,

we'll provide you with a little bit more color on PI and some of those challenging spots. But again, we feel that it's a business that we can continue to participate in. Appreciate the question.

Alex Scott: Thanks.

Operator: The next question is from Tracy Benguigui with Barclays. Please go ahead.

Tracy Benguigui: Good morning. It was nice to see last week that you upsized your capital return target, and I'm curious when you're coming up with that, did you take into account potential implication of the S&P proposed capital model? And I guess what I'm speaking specifically about is their treatment of structured assets, especially those not rated by S&P, Moody's or Fitch, because it looks quite onerous and Principal just holds more of that asset class.

Dan Houston: Yeah, great question. That's right down the wheelhouse for Deanna.

Deanna Strable: Yeah, a couple of things that I would say there. What we came out with last week would not contemplate any impacts on that. I'd say we're still working through the model to understand changes, and it's really too early to speculate on how that would impact us. As we think about our targeted capital as you're aware, we have grounded ourselves on RBC as well as a certain amount at our Holdco. But we do look at the rating agencies and their capital formula as well. But I'd say it's still too early to speculate on how that will impact us as we go forward.

Tracy Benguigui: Okay. So maybe it will just be helpful to understand the proportion of your CMBS, RMBS assets that are not rated by those big three rating agencies instead by the likes of Kroll or Morningstar?

Deanna Strable: Yeah, Tracy, I think that's a great question, and we'll follow-up with you after the call on that.

Tracy Benguigui: Okay.

Dan Houston: Did you have a follow-up question, Tracy?

Tracy Benguigui: Yes, my follow-up question, you mentioned Chile I know we're really early. In your reform discussion, do you have any update on how AFPs could be charged if there are no longer any mandatory contributions?

Dan Houston: Yeah. You know, I think the reality is, there's been a lot of discussion around pension reform in Chile. And as you may have already also noticed, they did pass a universal guaranteed pension, which is going to really help out sort of on pillar zero, making sure that lower income Chileans have a bit of more certainty about their retirement income. There seems to be support for the AFP model.

We've been participating heavily, Roberto Walker, who leads our Latin American operations as well as located right there in Santiago, Chile. There's some you know recent statistics that we found very helpful. There were 28 million distributions that took place as part of that hardship, and that was \$50 billion that went back into the hands of Chileans, and there's been a lot of survey work that's been done about AFPs and their viability. But right now, we know that 92% of Chileans favor keeping their pension savings in an individual account. And we know that 73% of Chileans want to choose their own pension provider.

So the ongoing dialogue with the regulators and the government is around, how do we peacefully coexist and ensuring that the AFP model continues to be in the private sector supporting the needs of the people of Chile, and so again, those conversations are ongoing. It isn't without its challenges, but we feel as if there are options available to Principal, and we'll continue to refine that work. We have a lot of work going on to look at what is the most successful path forward for our customers as also recognizing the impact it has on our shareholders. Hopefully that's helpful.

Tracy Benguigui: Thank you.

Operator: The next question is from Tom Gallagher with Evercore. Please go ahead.

Tom Gallagher: Good morning. Just curious on PGI, I've always thought of that business being well positioned in a low-rate environment just because of the strength of your commercial real estate, fixed income, real estate broadly. And if I'm not mistaken, your equities business has also done well from a growth over value standpoint. I don't even know if that's entirely still true today.

But my question is, if we're in a rising rate environment and we're seeing a broad shift from growth to value on the equity side, do you view that as a headwind for flows and the business model or do you believe you're more balanced. You still look good from a flow visibility standpoint?

Dan Houston: I think, Tom it's been intentionally balanced. And I don't even think that the observation on growth versus value, I think there's been a tendency to be cognizant in the marketplace and have solutions that fill all the gaps. But I think we're a bit of an all-season manager of assets across the broad range of asset classes. And so, with interest rates rising, I don't see that necessarily as a bad thing. As a matter of fact, I think I can see where it would be quite helpful. But let me turn it to Pat where he can provide some additional thoughts on where we think we can win in the future here. Pat?

Pat Halter: Yeah, Tom. I think you know from my perspective, I'd like to broaden the discussion a little bit, because to Dan's point, we really want to make sure that we are intentionally very nimble in terms of the capabilities we can offer to the marketplace, as Dan mentioned, in all seasons.

We do have, in general, a high-quality growth bias in our equity platforms. But we do have capabilities that are diversified in terms of philosophy, diversified in terms of approach, and our original sort of intention to create a boutique model in terms of different investment

teams that operate a different and unique philosophy approach and process within the organization, I think has served us well to be quite nimble in terms of different markets.

I would also sort of suggest to you though, that there is still a very strong interest in fixing some income investment capabilities. And a suite of investment capabilities that we still offer in the marketplace are still very viable. So, for instance, in the fourth quarter, one of our largest institutional flows was in emerging market debt. One additional sort of very large flow again in the fourth quarter institutional side was high yield.

So, we continue to see some very strong interest in some of the more sort of higher returning unique investment capabilities in fixed income. And then as I mentioned earlier, there is absolute significant growth going on in the broader private markets. And we are pivoting and positioning ourselves to build upon our strong, very deep credit analytics to offer more private capabilities going forward, more solutions in that space. So, I think we're in a good place, both on the equity side, on the fixed income side, and in the alternative side, Tom.

Dan Houston: Tom, did that help?

Tom Gallagher: That does. Thanks, guys. My follow-up is, when I look at Specialty Benefits, and I strip out the COVID impact, you are kind of unique somewhat in the industry, you've had good underlying performance below – I think below your guide actually, if I look at it this quarter, that 60 to 65 benefit ratio guide. Any reason to think that this may be sustainable? And why any sort of guesses you have at this point as to why PFG is seeing favorable experience, excluding COVID, when a lot of your competitors are seeing adverse trends?

Dan Houston: As you might expect, Amy is in a really good position to respond. But I would say this, Tom, you know, there is an advantage of that SMB space, where you look at the small employers and they have to go back to work, they're taking care of customers, less flexibility and maybe the large plan

market and frankly, good underwriting, but I think all of those, sort of go into the mix and having very favorable results. Amy?

Amy Friedrich:

Yeah, thanks for the question. And I agree. When you look across the industry, Principal's block that we've built in Specialty Benefits really is a positive outlier. And what I would go back to is, you know, sometimes this isn't one factor, but a collection of factors. I think Dan's already hit on one of them which is that small market focus. What that means is, we're not always doing competing against another company for takeover. But sometimes we're establishing some of these benefits for the first time.

When you're establishing a benefit for the first time, you often are in a position you can help consult. You can actually help the broker or advisor get educated about these products, and you can help that business owner get educated. So with that education and with that consulting side of the practice on building new market, you also get a relationship established, and that relationship tends to pay off. We mentioned, existing cases in terms of how much we're penetrating in terms of number of products per case. When you look at 2020, we had in our existing cases, 2.66 average number of products. When you look at 2021, that's gone up to 2.75. That is unique in the industry as well.

And so, when you look at our ability to have multiple products that we touch, to have disciplined pricing and underwriting, strong claims management and then limited concentration risks, often because of that small to medium size focus, we have the ability to grow, but to do so in a way that has really stable results. So when I look at the industry it probably is those collection of things that make us a bit different than everybody else.

Dan Houston:

Hopefully that helped, Tom.

Tom Gallagher:

That does, thank you.

Operator: The next question is from Jimmy Bhullar with JP Morgan. Please go ahead.

Jimmy Bhullar: Hey, good morning. So first just had a question on RIS-Fee flows. And they were negative this quarter and I realized that with the market going up through withdrawals might have ticked up. But if you could just comment on what drove that, and what you're seeing in terms of deferral rates, matching contributions and stuff and what your outlook is for the business?

Dan Houston: Yeah, thanks for the question, Jimmy. You know, I'd be remiss if I just didn't call out specifically how the strong underlying fundamentals are of this business, whether (Hello?)

Jimmy Bhullar: Not my line.

Dan Houston: Jimmy. Okay, Jimmy, you can still hear me?

Jimmy Bhullar: I can hear you and that wasn't mine, unless someone's in my room that I don't know. But -

Dan Houston: Okay. It's okay. It's okay. All right. So I lost my train of thought there just for a second, okay. Underlying fundamentals of that business remain incredibly strong, whether it's reoccurring deposits, the sales number doubling from a year ago you know \$24 billion plus in total sales. And this net cash flow is worth spending a little bit of time on this morning to understand how these inflated equity markets look and have the appearance that the business fundamentals are not as good. But the reality is, they're incredibly strong. And Renee can walk us through the sort of the math of why the net cash flow looks soft in spite of the strong underlying fundamentals. Renee?

Renee Schaaf: Yeah, absolutely. Thank you, Dan. When you look at fourth quarter, fourth quarter was impacted by seasonally higher contract withdrawals. And of course, as already mentioned, strong equity markets tend to have

an adverse impact on net cash flows, because of the impacts specifically on withdrawals. When we think about net cash flow, I think it's helpful to look at a trailing 12-month basis to eliminate some of the impact of seasonality.

And so to Dan's point, when you look at transfer deposits for the trailing 12-month period, they were up 87% over 2020. So very strong result, and it reflects that our value proposition continues to resonate in the marketplace. And that goes across small, mid and large plans. So our established footprint is really paying off and it's generating those important transfer deposits.

From a recurring deposit perspective on a trailing 12-month basis, we're seeing recurring deposits up 40% year-over-year. When you isolate and you peel back the onion, you see that the legacy Principal business had an increase in recurring deposits of about 15%, and if you take that 15% and you drill down even further, there are two primary factors that are creating this very positive and strong recurring deposit result.

The first is simply the increase in the deferrals themselves. That's about a third of that 15% and the rest of it is an increase in the number of participants in our block. So then you take a look at the withdrawals, and of course, this is where strong equity markets tend to have a really negative impact on net cash flows. So, the way to look at it then to help put that into context is to take your withdrawals and express that as a percent of average account values.

When you do that for 2021, you see that withdrawals were 14% of average account values. That compares favorably to what we saw in 2020, which was a 15% withdrawal rate. And as Dan mentioned in his comments to start, we see record, the best in the past 10 years in terms of contract retention. So we're very pleased with results, we think the underlying fundamentals of this business remain very strong.

Dan Houston:

Jimmy, do you have a follow-up?

Jimmy Bhullar: Yeah. Just on the Chilean business with the Presidential election, do you have a better idea on what some of the proposals could be or what some of the changes could be? And how they would potentially impact your business?

Dan Houston: Yeah. So we're dissecting every one of those suggested proposals. And the reality is, today, there are a lot of ideas that are floated in the market, one might put more constraints, if it remains a private system, where you could have more constraints on the actual charges that you could make. There's all the way to the range of where the government would have a competing AFP system.

So there are probably a half a dozen different ideas ranging all the way from no change, the AFP stays at it is to a complete government run AFP, and as I said, choices in between. The job of the industry and the job of Principal is to work with the elected officials and the regulators to find a sensible solution.

And as I said earlier, the universal pension solution that has already been enacted, the guaranteed pension, I think it has helped where some of the concern was for lower income individuals, it does go a long way in helping provide them with a base. And now the question is, how do we modify AFP to meet the needs of everyone? Hopefully that helps, Jimmy.

Jimmy Bhullar: That does. Thank you.

Dan Houston: Thanks.

Operator: The next question is from Erik Bass with Autonomous. Please go ahead.

Erik Bass: Hi, thank you. I just had a follow-up to Ryan's question on the sweep deposits and want to make sure I was following the answer correctly. So I think you said that the change that you made is adding about \$40 million to revenue. So offsetting about half of the decline from the lower IOER rate. But I'm wondering, do you still have sensitivity to short-term

interest rates where you benefit if they go up? Or is that sort of a locked in revenue stream at this point?

Dan Houston:

Renee, please

Renee Schaaf:

Yeah. So the earnings that we will capture on these deposits are a function of the net interest margins. And so, it's going to be less sensitive to short-term interest rates overall. But more importantly, it simply gives us and restores a revenue stream that we had lost when it was attached to IOER rates.

Erik Bass:

Got it. And then that should start coming through with that higher level kind of immediately in 2022?

Renee Schaaf:

That's correct, because we have \$2 billion of those deposits, a little over \$2 billion, on our balance sheet right now. That'll increase a little bit in 2022. There's a little bit more to come over. But will provide guidance on what 2022 will look like in the upcoming Outlook Call.

Erik Bass:

Perfect. And then just to clarify, all of that's getting booked in RIS-Fee or does any of that show up as revenue in the Bank?

Renee Schaaf:

That is all being reported in RIS-Fee.

Erik Bass:

Great, thank you.

Dan Houston:

Thanks, Erik.

Operator:

The next question is from Josh Shanker with Bank of America. Please go ahead.

Josh Shanker:

Yeah. as I'm looking over the Group Benefits segment, as I compare to pre-pandemic years, our Group life and disability have sold more, the dental and vision is down relative to pre-pandemic years. Can we talk about what's been successful in selling? What the pipeline is and whether

or not you expect to grow in the various products in Group Benefits in 2022?

Dan Houston: Some of that will, of course, will get added to 2022 Outlook Call. But you want to talk about your pipeline in your current opportunities, Amy?

Amy Friedrich: Sure, happy to do that. Thanks, Josh. So, I think you know we'll get after again, as Dan said in the Outlook Call. But when I look at kind of pipeline and I look at reestablishing sort of the pre-pandemic baseline, you had characterized some things around dental, vision, and life and disability. And here's the way I would think about it.

Dental and vision and life and disability as well as our, what I would consider sort of supplemental and worksite products, all play a role in meeting our employer-customer needs. So, some of the things that we look at is, what benefit design are they trying to fill? Sometimes they're looking after dental and vision first, because they're the most utilized benefits, sometimes they're doing something different in terms of life and disability. What we've seen post-pandemic is the heightened awareness of needing life and disability coverage has kind of brought those to the forefront. So we're seeing small employers almost start the conversation there and then fill in with some of the other benefits.

The piece I would pull some attention to is we are going to continue to see build up in our portfolio of those things that are more worksite or pure voluntary-based. So accident and critical illness -- those pieces get reported through that disability line today. And we're going to continue to see them make good progress as they position in our portfolio.

So one other thing that probably doesn't get as much attention is sort of that voluntary or worksite portfolio, we've been quietly and slowly building up those capabilities. And we see those as a potential future margin expansion opportunity, as well as of high interest to our customer base.

Josh Shanker: Okay, thank you very much for a thorough answer.

Dan Houston: Thanks, Josh. You know, one thing is for sure that's happening out there right now is, with wage inflation, there's also the built-in benefit that the value of life insurance goes up, the disability goes up. And employers are trying to attract retain talent and benefits have historically and continue to be a way to differentiate out there. Next question, please.

Operator: The final question is from Andrew Kligerman with Credit Suisse. Please go ahead.

Andrew Kligerman: Thank you. A question on the transaction announced last Monday, I understand there was a closed block in their life insurance business. And as we looked it up, I think there was a reserve deficiency of \$400 million. So my question is – is the \$400 million part of that \$800 million of capital freed up? Did you free up \$400 million on the closed block? And if not, what might have been released?

Dan Houston: Deanna?

Deanna Strable: Yeah, a couple of things on there. You know, as we talked about on the call, you know we aren't going to itemize all of the things that go up to the \$800 million of proceeds. We had capital release, we had a net ceding commission that was negative, we had to kind of true up our economic reserves, we had one-time negative impacts regarding loss of covariance benefits, as well as financing break fees.

And then what you're referring to is, we did do some capital optimization on our remaining life insurance business, part of which was the closed block but not all of it. And so, you know, all those pieces came together to get to the net proceeds of \$800 million of the deployable proceeds, which was in line to slightly better than what we would have contemplated at the time of the Investor Day.

But every transaction and financing that we did was contemplated back at the time of Investor Day. So all in line with what we had anticipated.

Net proceeds were at or better and there were a lot of moving pieces that got to the \$800 million of proceeds.

Dan Houston: Andrew, do you have a follow-up?

Andrew Kligerman: Yes, please. It sounds, Dan, like you're somewhat more or maybe a little bit optimistic about Chile. And I was kind of thinking and maybe in a worst-case scenario, I just like to size it. Would I be correct in that roughly 4% of operating earnings is attributable to Chile? And then I was curious how much capital is allocated to that business?

Dan Houston: Yeah. So in Chile, it's actually, let's talk specifically around Cuprum, it's about 4% of our earnings on just Cuprum and we'll get back to on the capital allocation. But again, I think we're a long way from that because it relates to sort of a doomsday approach. We think there is a lot of road to travel.

We have, as I said earlier, Andrew, we had some very helpful dialogue with government officials and legislators. And again, with the passage of the universal guaranteed pension product, we think there is a viable path. Again, having said that, we're not pollyannish. We're looking at all possible outcomes, and we'll continue to manage that effectively, and as things change and become more clear, we'll be sure to update the investors. Appreciate the question.

Andrew Kligerman: Thank you.

Operator: We have reached the end of our Q&A session, Mr. Houston. Your closing comments, please.

Dan Houston: Yeah, thank you. And again, appreciate everyone tuning in this morning. I think what you've seen in the most recent quarter and year is strong results. And it was benefited from being in the Fee, the Spread, and the Risk businesses focused in on the business markets. Again, as I said in my earlier prepared comments, we think that the strategic review was very

helpful and focusing our attention on high growth markets and opportunities across each of those areas.

And again, we're very pleased with the capital deployment, from the dividend to the share buyback, to the acquisitions, as we, you know, see the value of IRT. So, we'll look forward to visiting with all of you on March the 2nd, when we'll have our Outlook Call, and we appreciate your input and your insights. Thank you, have a great day.

Operator:

Thank you for participating in today's conference call. This call will be available for a replay beginning at approximately 1 PM Eastern Time until end of day, February 15th, 2022. 4488026 is the access code for the replay. The number to dial for the replay is 855-859-2056 US and Canadian callers or 404-537-3406 International callers. Ladies and gentlemen, thank you for participating in today's conference call. You may all disconnect.

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