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BHF.OQ - Q4 2021 Brighthouse Financial Inc Earnings Call

EVENT DATE/TIME: FEBRUARY 11, 2022 / 1:00PM GMT

OVERVIEW:

Co. reported 4Q21 adjusted earnings excluding impact from notable items of $416m.

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PRESENTATION

Operator

Good morning, ladies and gentlemen, and welcome to Brighthouse Financial's Fourth Quarter and Full Year 2021 Earnings Conference Call. My name is Shannon, and I will be your coordinator today. (Operator Instructions) As a reminder, the conference is being recorded for replay purposes. Also, we ask that you refrain from using cellphones, speakerphones or headsets during the question-and-answer portion of today's call.

I would now like to turn the presentation over to Dana Amante, Head of Investor Relations. Ms. Amante, you may proceed.

Dana Amante - *Brighthouse Financial, Inc. - Head of IR*

Thank you. Good morning. Thank you for joining Brighthouse Financial's Fourth Quarter and Full Year 2021 Earnings Call. Our earnings release, slide presentation and financial supplement were released last night and can be accessed on the Investor Relations section of our website. We encourage you to review all of these materials.

Today, you will hear from Eric Steigerwalt, our President and Chief Executive Officer; and Ed Spehar, our Chief Financial Officer. Following our prepared remarks, we will open the call up for a question-and-answer period. Also here with us today to participate in the discussions are other members of senior management.

Our discussion during this call may include forward-looking statements within the meaning of the federal securities laws. Brighthouse Financial's actual results may differ materially from the results anticipated in the forward-looking statements as a result of risks and uncertainties described from time to time in Brighthouse Financial's filings with the U.S. Securities and Exchange Commission. Information discussed on today's call speaks only as of today, February 11, 2022. The company undertakes no obligation to update any information discussed on today's call.

During this call, we will be discussing certain financial measures used by management that are not based on generally accepted accounting principles, also known as non-GAAP measures. Reconciliations of these non-GAAP measures on a historical basis to the most directly comparable GAAP measures and related definitions may be found on the Investor Relations portion of our website, in our earnings release, slide presentation or financial settlement. And finally, references to statutory results, including certain statutory-based measures used by management, are preliminary due to the timing of the filing of the statutory statements.

And now I'll turn the call over to our CEO, Eric Steigerwalt.

Eric Thomas Steigerwalt - *Brighthouse Financial, Inc. - President, CEO & Director*

Thank you, Dana. Good morning, everyone, and thank you all for joining us. I am pleased to share that 2021 was another strong year for Brighthouse Financial. Despite the challenges resulting from the COVID-19 pandemic, we remained steadfastly focused on our mission and strategy and on delivering for our customers, partners and shareholders. Thanks to the tremendous dedication of our employees, we accomplished many important strategic milestones in 2021, including, we achieved our target of returning $1.5 billion to our shareholders by the end of 2021. As a result, we have reduced the number of shares outstanding relative to when we became an independent public company in 2017 by 35%. That includes $499 million of our common stock that we repurchased in 2021, representing a reduction of 12% of shares outstanding relative to year-end 2020.

We continued to optimize statutory capital to further strengthen the balance sheet and paid subsidiary ordinary dividends totaling $594 million to the holding company, primarily consisting of $550 million from Brighthouse Life Insurance Company, or BLIC.

Sales of both annuities and life insurance were very strong throughout the year. In each of the first 3 quarters of 2021, we delivered record sales for both our flagship Shield Level annuities and our variable annuities with FlexChoice Access. The strong sales continued in the fourth quarter, resulting in a record year of total annuity sales in 2021. Life insurance sales grew steadily throughout the year and were ahead of our expectations.

We continued to expand our distribution footprint and enhance the way we support financial professionals and the clients they serve. During the year, we added new distribution relationships, including the addition of our annuities to the SIMON Marketplace. We also added more life insurance wholesalers, rolled out SmartCare to more firms, selectively expanded into the brokerage general agency, or BGA, distribution channel and rolled out enhancements to our Shield Level annuities and SmartCare.

We launched our institutional spread margin business, which we expect will enhance and diversify our earnings profile over time. We achieved almost 90% of our run rate expense reduction relative to the first year post separation while simultaneously making strategic investments in 2021 to start up the institutional spread margin business and fund future growth. Some of these investments allowed us to provide better support to our distributors and their financial professionals as well as our policyholders and contract holders.

And finally, we completed a major platform conversion as we continue our efforts to implement our future state operations and technology platform.

Turning to our fourth quarter results. Our balance sheet and liquidity position remained robust in the fourth quarter, and we estimate our combined risk-based capital, or RBC, ratio was approximately 500%. Additionally, we ended the year with holding company liquid assets of $1.6 billion. Brighthouse delivered strong sales results in the fourth quarter. Annuity sales were $2.4 billion, driven by variable annuity and Shield product sales of $2 billion combined. Total VA and Shield sales were up 14% compared with the fourth quarter of 2020. Fixed rate annuity sales were lower quarter-over-quarter as expected.

As I have mentioned previously, we took repricing actions in the second half of 2020, given the low interest rate environment. Additionally, we generated approximately $35 million of life insurance sales in the fourth quarter of 2021, an increase of 133% compared with the fourth quarter of 2020 and an increase of 30% compared with the third quarter of 2021.

As I said, we delivered steady growth in life insurance sales in 2021, which is a result of the focus and execution on our life insurance strategy, including the addition of new distribution partners and bringing on additional wholesalers.

We couldn't be more pleased with our sales results last year. Before moving to expenses, I would like to thank our distribution partners for all they do on behalf of their clients and our customers every day.

Now turning to expenses. Corporate expenses, which do not include establishment costs, were $247 million before tax in the fourth quarter. Establishment costs were approximately $27 million before tax. I am pleased with the results for both the full year and fourth quarter of 2021. We have made significant progress in 2021, and we believe we remain well positioned to continue to execute on our focused strategy in 2022. We continue to prudently manage statutory capital and target a combined RBC ratio of between 400% and 450% in normal markets.

In addition, our business mix will continue to evolve by adding more high-quality new business. We expect to see a continued shift in our business mix profile over time as we add more higher cash flow generating and less capital-intensive business, coupled with the runoff of older, less profitable business.

As we enhance our existing products, develop new ones and expand our distribution reach, we expect to see continued sales growth across annuities and life insurance. And we remain very excited about being 1 of 2 annuity providers selected to help deliver BlackRock's LifePath Paycheck, an investment solution that is designed to provide millions of American workers with simplified access to lifetime income throughout their retirement.

We have significantly reduced corporate expenses, and we plan to continue to manage expenses effectively to drive our statutory expense ratio down over time. Additionally, we will continue to prudently manage the exit of the remaining transition services agreements as we implement our future state operations and technology platform. We expect the remaining establishment costs to occur in 2022.

Lastly, we intend to continue to deliver on our ongoing commitment to return capital to our shareholders. Year-to-date through February 8 of this year, we have repurchased $57 million of our common stock.

To wrap up, Brighthouse Financial made significant progress in 2021. We continue to believe that we have the right strategy in place, and we remain focused and well positioned to continue the execution of our strategy. As the Brighthouse Financial franchise grows and evolves to include a more diversified business mix, we are committed to consistently driving shareholder value.

With that, I will turn the call over to Ed to discuss financial results. Ed?

Edward Allen Spehar - *Brighthouse Financial, Inc. - Executive VP & CFO*

Thank you, Eric. Good morning, everyone. Brighthouse Financial reported strong results for the fourth quarter and full year of 2021. Favorable equity market performance and higher interest rates provided a positive backdrop for the year. We further strengthened the balance sheet and ended the year with an estimated combined risk-based capital or RBC ratio of approximately 500%, well above our target range of 400% to 450% in normal markets and up from our year-end 2020 combined RBC ratio of 487%.

Statutory combined total adjusted capital, or TAC, was approximately $9.5 billion at December 31 compared with $9.8 billion at September 30. The decrease is explained by $344 million of subsidiary ordinary dividends paid to the holding company in the quarter.

Looking at year-over-year, favorable equity markets and rising interest rates helped drive a $900 million increase in TAC from year-end 2020. Additionally, in 2021, the operating companies paid total ordinary dividends of $594 million to the holding company. The total Brighthouse Life Insurance Company, or BLIC, ordinary dividend paid in 2021 was more than double our initial plan for last year.

Turning to normalized statutory earnings. This metric was close to breakeven in the fourth quarter. For the full year, the normalized statutory loss was approximately $300 million. Strong core variable annuity or VA results were more than offset by a $200 million to $250 million negative impact from a decline in the statutory mean reversion point for interest rates and a loss in non-VA.

As I discussed on the last earnings call, normalized statutory earnings is meant to give an indication of excess capital generation in normal to good markets and to measure our performance managing risk in bad markets. Importantly, this measure in its current form was introduced prior to the adoption of VA reform. Starting this year, we are redefining normalized statutory earnings to better align with VA reform, and therefore, movement in the RBC ratio. At an operating company level, we believe that the RBC ratio is the best indicator of excess capital generation over time.

Cash at the holding company is the other important indicator of excess capital. Holding company liquid assets were $1.6 billion at December 31, up from $1.5 billion at September 30. Also, in the fourth quarter, we took advantage of historically low holding company funding costs by extending debt maturities and adding more fixed-for-life preferred equity capital. We issued $400 million of 30-year senior notes and $350 million of preferred stock. The net proceeds were used to repurchase approximately $680 million of senior notes with a weighted average maturity of approximately 10 years.

As we look to 2022, balance sheet strength remains a top priority, and we continue to manage the company using a multiyear multi-scenario framework to evaluate capital, liquidity and subsidiary dividend plans to the holding company. In 2022, total subsidiary ordinary dividend capacity is approximately $1.3 billion. And we currently expect to pay ordinary dividends to the holding company of approximately $300 million.

Shifting to adjusted earnings. Fourth quarter adjusted earnings, excluding the impact from notable items, were $416 million, which compares with adjusted earnings on the same basis of $514 million in the third quarter of 2021 and $272 million in the fourth quarter of 2020. The notable items on an after-tax basis were: a $59 million debt repayment expense in corporate and other associated with the repurchase of the company's senior notes; establishment costs of $21 million, included in Corporate & Other; and $13 million net unfavorable actuarial items, including reinsurance recaptures in the Run-off segment, refinements to certain actuarial assumptions and valuation systems conversions associated with our transition to the future state platform.

There are 2 key themes when we think about the fourth quarter adjusted earnings results compared with the quarterly adjusted earnings expectation. First, while net investment income was lower sequentially, it was still very strong in the fourth quarter, primarily due to a 7.5% alternative investment return. Net investment income was approximately $165 million above a quarterly run rate expectation on an after-tax basis. For the full year, the alternative investment return was 42.6%, which greatly exceeded the 9% to 11% annual return we anticipate for this asset class.

Second, the fourth quarter underwriting margin, which included $34 million of pretax net claims related to COVID-19, was lower sequentially. There is variability in the underwriting margin throughout the year, driven by fluctuations in a number of factors, including frequency of claims, severity of claims and the offset from reinsurance. As we have previously communicated, we expect direct claims on a quarterly basis to average between $400 million and $500 million. In the fourth quarter, we were at the higher end of that range as we experienced a higher volume of direct claims.

Moving to adjusted earnings at the segment level. Annuity adjusted earnings, excluding notable items, were $361 million in the quarter. Sequentially, annuity results were driven by lower amortization of deferred acquisition costs, or DAC, and a smaller increase in reserves, both as a result of the favorable market performance in the quarter. This was partially offset by lower fees and higher expenses.

The Life segment reported adjusted earnings, excluding notable items, of $58 million in the quarter. On a sequential basis, results reflect lower net investment income, a lower underwriting margin and higher expenses.

Adjusted earnings in the Run-off segment, excluding notable items, were $6 million in the quarter. Sequentially, results were driven by lower net investment income, a lower underwriting margin and a tax true-up that was offset in the Corporate & Other segment. Corporate & Other had an adjusted loss, excluding notable items of $9 million. Sequentially, results reflect a higher tax benefit and the previously mentioned tax true-up.

Before I conclude, I would like to mention that we plan to provide an update in March on distributable earnings as we have done in prior years. Overall, I'm very pleased with the fourth quarter and full year 2021 results. We continued to optimize statutory capital, strengthen the balance sheet and return a substantial amount of capital to shareholders.

With that, we would like to turn the call over to the operator for your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from Tom Gallagher with Evercore.

Thomas George Gallagher - *Evercore ISI Institutional Equities, Research Division - Senior MD*

First, just a question on capital generation in the quarter. Ed, I think I heard you mention $200 million to $250 million negative mean reversion interest rate adjustment. Was that done this quarter? Was that like a true-up done this quarter?

Edward Allen Spehar - *Brighthouse Financial, Inc. - Executive VP & CFO*

Tom, no. That was the impact we had in the first quarter of last year. So what you're talking about in the fourth quarter, I think, is norm adjustments on a statutory basis. So the actuarial items and other insurance adjustments line when we talk about the norm stat earnings disclosure in the supplement. And let me give you a little color on it. I think it's important to understand the movement in the RBC ratio.

In the fourth quarter, we made substantial progress on transitioning to our future state platform in actuarial. And as a reminder, this is movement away from multiple valuation systems and customized models to one valuation platform and more standardized models. And so this is created and will continue to create more time for value-added analysis, more flexibility and also a better control environment. The fourth quarter was a busy quarter for this, and we had 3 models that were fully put into production and for 3 product lines. The total statutory reserves we're talking about is around $33 billion.

So one thing to think about when you look at these conversions, it's sort of like an actuarial assumption review for the associated product line. So while we had gone through our review in the third quarter, every time you do this model conversion, you're looking very closely at the one model versus the other model and the differences. And so as a result of this, in the fourth quarter, there was a negative impact on TAC and the RBC from the transition to the future state. And this really explains the sequential change in the RBC ratio that you see on top of the impact you calculated from the dividends we paid up to the holding company. So that's really the driver of this incremental change in RBC in the fourth quarter.

The final thing I'd say is it's important to note that if you look at these actuarial adjustments on a full year basis for statutory, it was a positive impact on our RBC ratio.

Thomas George Gallagher - *Evercore ISI Institutional Equities, Research Division - Senior MD*

Got you. So if I -- tell me if these numbers sound directionally correct. If I solve for a 30-point RBC drop, that equates to $500 million to $600 million of TAC, keeping the denominator constant. So the dividend clearly accounted for the majority of your drop in RBC or say, actually, a little less than half of the drop in the RBC. And so this systems conversion then would have been several hundred million dollars, it sounds like.

I mean I was calculating upwards of $0.5 billion negative impact on your RBC, assuming you would have had a normal level of stack capital generation in the quarter. Is it kind of that order of magnitude in the RBC adjustment or any help there would be appreciated?

Edward Allen Spehar - *Brighthouse Financial, Inc. - Executive VP & CFO*

Yes. That's high. It's not a $0.5 billion impact. Because just -- I would say this. Remember, I said the total impact for the year of actuarial adjustments was positive, right, on a stat basis. And I think on the third quarter call, I discussed that the statutory impact from our actuarial assumption review was positive by something around 20 RBC points. I think it was 21 RBC points. So I think you could use that as an anchor to think about like how much of a negative impact must there have been in the fourth quarter, if I could -- if we can still say it's positive for the full year.

Thomas George Gallagher - *Evercore ISI Institutional Equities, Research Division - Senior MD*

Got you. Okay. And then just a follow-up to this. Any -- I totally get it, but are there any further large systems conversions left where there could be adjustments here? How many of these are left when you think about the next couple of years?

Edward Allen Spehar - *Brighthouse Financial, Inc. - Executive VP & CFO*

Yes. So we have the VA transformation, which is going to occur this year. So that's it for actuarial.

Thomas George Gallagher - *Evercore ISI Institutional Equities, Research Division - Senior MD*

Okay. So -- and how -- is that a really big one? Or I assume it is when I hear VA, but how -- maybe dimension that a little bit.

Edward Allen Spehar - *Brighthouse Financial, Inc. - Executive VP & CFO*

Yes. I don't know how to -- I would say using an actuarially approved term, it's a big one. I think that, that is probably fair to say. But we've learned an awful lot along the way here with the model conversions that we've completed already. So I think we're very well positioned here, and we'll have to see what happens. But I don't -- I think we're very well positioned, obviously, from a capital standpoint and the movements we're talking about here, like I said, have not been that significant. In total, again, positive for full year 2021, when we had an awful lot of activity on the actuarial transformation front.

Operator

Our next question comes from Tracy Benguigui with Barclays.

Tracy Dolin-Benguigui - *Barclays Bank PLC, Research Division - Director & Senior Equity Research Analyst*

In the past, you referenced buying back stock at an average daily trading volume of 4% to 6%. But if I look at the last 2 quarters, you're well above that, I would say, around 9% or so. But on the other hand, your stuff may not be as cheap as it once was. So are you still targeting this 4% to 6% range? Or have you changed your thinking behind that? I'm also coupling on your expanded ordinary dividend capacity, your healthy holdco liquidity and your RBC cushion.

Eric Thomas Steigerwalt - *Brighthouse Financial, Inc. - President, CEO & Director*

My mic didn't work. Tracy, it's Eric. Look, let me just start out by saying we are laser focused on the strategy that we laid out a couple of years ago, and that has not changed at all. So you're trying to get a sense of what we're going to do going forward, and Ed will jump in here on dividend capacity. We have returned a lot of capital to shareholders as you're very well aware. And we still have over $700 million of buyback authorization. I think it's fair to say either today or any time in the future, when we get buyback authorization, we intend to carry out the buyback.

Now you're mentioning 4% to 6%. In 2021, we accounted for roughly 8%, so slightly more than that. Yes, I understand the stock price is higher. We still think it's undervalued. And as a result, we are buying back stock. You see what we bought back so far in 2022. So while I'm not going to give an exact number, 4%, 6%, 8%, and it was 8% in 2021, sounds like a reasonable guide. And of course, that excludes any time that we think there's an opportunity to purchase even more.

I know Ed wanted to say this, but I guess I'll say it. We bought back 17% of our shares in 2020 at around $26 a share. So I think all of what I just said gives you a good -- some guidance on what we intend to do going forward. Ed, I know you want to add.

Edward Allen Spehar - *Brighthouse Financial, Inc. - Executive VP & CFO*

Yes. Tracy, the only thing I would add is we don't target a percentage of average daily volume. The reason that we have quoted those statistics today and in the past is just to give you a sense of how much we're buying back and how active we are. So we bought back 12% of our shares outstanding last year. We've -- as I think Eric said, we bought back 35% -- shares outstanding have declined by 35% since we separated. Obviously, we take capital return very seriously, and we've been very active. And it's our strategy, and I don't really see our strategy changing.

Tracy Dolin-Benguigui - *Barclays Bank PLC, Research Division - Director & Senior Equity Research Analyst*

Got it. And...

Edward Allen Spehar - *Brighthouse Financial, Inc. - Executive VP & CFO*

I'm sorry. What was the -- yes, sorry, I know you had another question, just if you could repeat that.

Tracy Dolin-Benguigui - *Barclays Bank PLC, Research Division - Director & Senior Equity Research Analyst*

No. I think you answered my first question. And then I guess my second question is, you mentioned in March, you're going to provide a refresh of your distributable earnings scenarios. But should we expect it to be directionally more positive, particularly given the 10-year treasury is now sitting above 2%. I think the assumptions last year, you shared was at 0.93% as of year-end 2020? Or is it really not comparable because of what you said earlier about redefining normalized stat earnings?

Edward Allen Spehar - *Brighthouse Financial, Inc. - Executive VP & CFO*

Well, I wouldn't say that the change in the definition of norm stat earnings is really going to be a meaningful factor here. I mean we are aligning norm stat with the RBC ratio. And the RBC ratio, as I said, is the best indicator over time of excess capital generation. And so when we think about distributable earnings, we think about what can we pay up to the holding company while still maintaining a strong capital position at the operating company level.

In terms of the -- sorry, I'm not going to give a preview of what we're going to say in March. I mean clearly, we are happy that interest rates are higher than they were when we did it last time.

Tracy Dolin-Benguigui - *Barclays Bank PLC, Research Division - Director & Senior Equity Research Analyst*

Okay. I mean just considering that you early adopted the VA capital reform, so it's been a little bit while. So it's almost like same-store basis because that's how you were thinking about it last year. So it should be on the same basis, is that fair?

Edward Allen Spehar - *Brighthouse Financial, Inc. - Executive VP & CFO*

Sorry, what should be on the same basis?

Tracy Dolin-Benguigui - *Barclays Bank PLC, Research Division - Director & Senior Equity Research Analyst*

Viewing -- your view of distributable capital being some derivative of excess RBC?

Edward Allen Spehar - *Brighthouse Financial, Inc. - Executive VP & CFO*

Yes. I'm not -- I mean, I guess I'm not 100% sure what you're asking, but let me try this. When we give you distributable earnings disclosures for VA and for the company under various scenarios, we're looking at what can we pay up to the holding company and still support the appropriate level of capital at the operating company. So nothing's changed in terms of how we think about that today versus a year ago because, as you said, VA reform was in place a year ago and it's in place today.

Tracy Dolin-Benguigui - *Barclays Bank PLC, Research Division - Director & Senior Equity Research Analyst*

Yes. I guess the big difference would be under RBC, you're looking at CTE98. And I think under your definition, normalized stat earnings, you were looking at CTE95. So I just wanted to make sure that the assumptions would be similar, if I just want to make a comparison, your disclosure this in March versus we shared last year.

Edward Allen Spehar - *Brighthouse Financial, Inc. - Executive VP & CFO*

Yes. I don't think you're going to have a problem.

Operator

Our next question is from Ryan Krueger with KBW.

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

Ed, based on where rates are right now, would you expect the mean reversion rate to come down 25 basis points in the first quarter of 2022? And if so, is the impact still $200 million to $250 million?

Edward Allen Spehar - *Brighthouse Financial, Inc. - Executive VP & CFO*

Yes and yes.

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

All right. That was easy. And then I guess, secondly, just on the subsidiary dividend to the holdco, I guess is there -- your RBC is a fair amount above your target. Would you consider, at some point, starting to take additional dividends to work down closer towards your -- the high end of the 400% to 450% target? Or at this point, are you just still looking to run the stat capital within the subs with more of a cushion?

Edward Allen Spehar - *Brighthouse Financial, Inc. - Executive VP & CFO*

Yes. So obviously, we have a high RBC ratio and a lot of cash to the holding company. And I guess, I would just say with $1.6 billion of cash at the holding company, most of our fixed charges covered by nondividend flows from the operating companies and with our first debt maturity in 2027, which, by the way, has been reduced by more than 40% because of the capital transactions we did late last year. So we issued $750 million of a combination of 30-year debt and fixed for life preferred and took out that shorter debt, most of it in the 2027.

So we're very happy. We locked in historically low funding cost for us. I mean as you can imagine, the yields on our debt and preferred are up a fair amount from where they were at that point in time. It also means that there's less -- even in 2027, the amount that's coming -- that's maturing is small. So we have the ability to complete the authorization without any reliance on dividends anywhere, certainly not from BLIC over time. I mean so I don't really -- that's point number one.

Point number two, we look at taking dividends based on, as you've heard me say repeatedly this, in a multiyear multi-scenario framework. And so it's great to have a lot of dividend capacity, but that's not what's going to drive us to determine what we're going to take up in any 1 year.

Operator

Our next question comes from Alex Scott with Goldman Sachs.

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

I just wanted to circle back on the comments about transforming the platform for variable annuities. Could you talk about what that entails? What are some of the changes that are made? And I guess specifically on the scenario generator, I mean, is that one of the changes that occurs with that kind of a platform switch? So just anyway you could help us demystify that?

Edward Allen Spehar - *Brighthouse Financial, Inc. - Executive VP & CFO*

Yes. There's no change in the scenario generator. I think you're referring to the discussions around the new scenario generator for statutory, which is going to be a -- I think it's going to be a long process. Obviously, we're very engaged. There's a lot of work to do. As you can imagine, it's extremely complicated. And it's going to take time. And I am optimistic that the industry and regulators will come to a good framework. And I'd just say, look, we've proven we can manage through VA reform. We've got a lot of capital. I'm not really concerned about the change in the ESG.

In terms of the VA, I would just say that we have -- there are multiple systems that are in place now, and we're going to, as I said, a single environment for all of our products. So it does provide simplification. It does provide, I think, ease of use and frees up the time for people to do more value-added analysis. So I'm really looking forward to the opportunities we're going to have as a result of completing -- fully completing this transformation and the benefits that we'll realize. But I don't know if there's anything specific I would go into on the VA system.

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

And so should I take that to mean that when we think through what you're going to bring forward in March or in cash flow scenarios and so forth, that's not really a consideration that we need to take into account?

Edward Allen Spehar - *Brighthouse Financial, Inc. - Executive VP & CFO*

That is correct. You do not need to take it into account.

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

And maybe for my follow-up, I just wanted to find out how you guys are thinking about inflation on the expenses? And just is there any impact that we should expect from that into next year and maybe if you could shed any light around how much of the institutional platform investments in 4Q was?

Edward Allen Spehar - *Brighthouse Financial, Inc. - Executive VP & CFO*

Well, I'll start on inflation. I would say if we assume that inflation translates to higher interest rates, which certainly yesterday's market action would suggest that's a reasonable linkage to think about. Inflation is an overall good guy for us. And obviously, people have to deal with wage inflation across all industries, and we'll have to do the same. But higher interest rates, higher inflation is not something that we're afraid of.

Eric Thomas Steigerwalt - *Brighthouse Financial, Inc. - President, CEO & Director*

Yes. It's Eric. I'll add to that. So I think over time here, you can count on us talking about our sort of stat expense ratio continuing to go down despite any effects that might hit us with respect to inflation. You should expect continued sales growth and margin expansion as we think about the stat expense ratio coming down. This particular year 2021, we did start up -- it's a new business for Brighthouse. Certainly for some of us, it's a business we've been in for a long time, but the institutional spread margin business. And I think you specifically asked about that.

So it was in the neighborhood of $10-ish million to get that all up and running in 2021. And of course, that affected our expenses, right? That made them $10-ish million higher. And you didn't ask this question, but I'll answer it anyway. So we had originally set out to save $150 million off our sort of starting expense base and then another $25 million in 2021. So we did not hit that for 2 reasons. One, the institutional spread margin business, which was about half of the difference. And then we did a lot of investing this year, and we'll continue to do that in distribution. You will see that in 2022 as well and probably in 2023. And along with your comments on inflation, we will still lower our stat expense ratio. So I hope that helps.

Operator

Our next question comes from Elyse Greenspan with Wells Fargo.

Elyse Beth Greenspan - *Wells Fargo Securities, LLC, Research Division - Director & Senior Analyst*

My first question goes back to capital return, I guess. I'm assuming you guys -- I'm assuming given where your stock price is, even though I think someone pointed out earlier, it's obviously more expensive than where it was, but you would still look for share repurchase for your return of capital as opposed to instituting a dividend. But I would interpret if you had any updated thoughts there.

Edward Allen Spehar - *Brighthouse Financial, Inc. - Executive VP & CFO*

Yes. I think that's a good assumption.

Elyse Beth Greenspan - *Wells Fargo Securities, LLC, Research Division - Director & Senior Analyst*

Okay. And then my second question, you guys had a reinsurance recapture that you pulled out of earnings in the quarter. Could you just give us any additional color there?

Edward Allen Spehar - *Brighthouse Financial, Inc. - Executive VP & CFO*

Yes. Sure, Elyse. So the recapture was not a meaningful impact from a statutory basis. In the total items on a GAAP basis, which had a net unfavorable impact of $13 million, the reinsurance recaptures had a $36 million unfavorable impact included in that number. And I think, as you know, when we're presented with the rate increase, we evaluate whether it makes sense to accept that or just to recapture the business. And in this instance, we decided it made sense to do the latter.

Operator

Our next question comes from John Barnidge with Piper Sandler.

John Bakewell Barnidge - *Piper Sandler & Co., Research Division - MD & Senior Research Analyst*

Maybe if we talk about other companies have announced cost-cutting programs after close to 2 years in a heavily hybrid world, totally understand you're able to start up your company and digitize it very quickly. But with establishment cost set to end in '22, how do you approach future expense rightsizing opportunities?

Eric Thomas Steigerwalt - *Brighthouse Financial, Inc. - President, CEO & Director*

We will -- I think we -- there's still room for us to take out some expenses. You mentioned the digitization, it's taken a while, by the way. We started this a number of years ago. So it's finally coming to fruition here after a number of years. There will be still some areas where we can take some expenses out, maybe some rents over time here. But I think from a previous question, obviously, inflation will be a factor. It is not going to preclude us, as I've said twice now, from lowering our stat expense ratio. But also, we are never going to shy away from making investments in growth.

We've made investments for the BlackRock LPP product. We've made investments in new products, which we'll -- you'll see this year and next year. And we will continue our sort of digitization for the financial professionals that we work with. So there are going to be opportunities. But frankly, I'm pretty focused on growth and investing in growth as well.

John Bakewell Barnidge - *Piper Sandler & Co., Research Division - MD & Senior Research Analyst*

And maybe my follow-up. Last quarter, you added 13,000 agents to the 50,000 you had previously. Can you talk about performance of those new agents in the quarter and then success in recruitment of new agents as well?

Myles Joseph Lambert - *Brighthouse Financial, Inc. - Executive VP and Chief Distribution & Marketing Officer*

Ye. It's Myles Lambert speaking. So we did launch several new relationships, and I think you're referencing specifically for our SmartCare product in August and throughout the fall of last year. We brought on about 13 new distributors giving us access to approximately 14,000 additional advisers, and we also expanded into the BGA channel. And it happened, like I said, throughout the summer and the fall, and we're starting to slowly see some growth from that new distribution opportunity -- from those new distribution opportunities.

Operator

Our next question comes from Humphrey Lee with Dowling & Partners.

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

Just looking at the mortality claims, there's definitely ups and downs for the quarters. But if we are taking a step back and look at kind of the direct claims, maybe, say, over the past 4 to 6 quarters and compare to the reinsurance recoveries, where do you end up relative to your expectations?

Edward Allen Spehar - *Brighthouse Financial, Inc. - Executive VP & CFO*

Yes. Humphrey, it's Ed. So yes, we pointed out that underwriting was a little less favorable than what we would consider to be normal. And I think that has been the case generally in the pandemic. And we talk about, obviously, there's the COVID impact that's direct that explains part of that.

I also think, and I don't believe we can prove this, but there could be a knock-on effect here, right, where you have people that aren't as quick to go to the hospital. They're not as quick to go to the emergency room. We know the cause of death reporting is imperfect. So what we identify as COVID-related deaths are the deaths that are tagged as COVID. And we know that has to be, I would say, the minimum number of COVID deaths because there are others that are possibly not categorized correctly.

So I think it's difficult to really be that precise about what's pandemic and what's not. I would say that this is not something that is an issue for us. I talked about in the third quarter, how we generally had very little change in our mortality expectations based on our experience studies. So our heavy third quarter actuarial assumption update analysis of this issue, we continue to look at it.

Reinsurance percentage was a little lighter this quarter than what we would consider to be the average. It can bounce around a lot and the direct claims themselves. The fact that I give a range of $400 million to $500 million gives you some indication of the type of volatility you can see. So I would say there's nothing to see here, but I think there is probably somewhat of a pandemic impact that's affected the last year or 2.

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

Okay. My second question is related to kind of how to think about the market impact running through annuities? I think you used to provide some guidance in the past. But as the product mix continues to shift to Shield from your legacy GMIB, like can you just give us an updated rule of thumb in terms of how to think about the market impact?

Edward Allen Spehar - *Brighthouse Financial, Inc. - Executive VP & CFO*

Sure. So we're not identifying a specific market impact. I think we qualitatively said that if you look at market impact that it was an offset to, say, the slightly less favorable expenses as well as the underwriting issue that we talked about when we -- if you're thinking about run rate.

If you look at the annuities segment, the DAC this quarter, I believe, was $49 million. Now that has an impact from the systems conversions that we talked about. So there's actually a DAC benefit. So unlike statutory where there was the negative impact, there was a positive impact for GAAP because of DAC. So if you adjust for that, the run rate or the number in the quarter for DAC related to adjusted earnings in annuities was more like $80 million to $90 million.

And I have said in the past that a more normal quarter for DAC amortization is probably in the neighborhood of $100 million. I think it's fair to say that it's a higher number than that now. So that should give you some indication of how to think about the market impact.

Operator

Our next question comes from Erik Bass with Autonomous Research.

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

I wanted to follow-up on Elyse's question, not a potential common dividend. And well, certainly, it's hard to argue with the value of buying back your stock. A dividend could potentially expand your shareholder base and send a strong signal that your confidence in the sustainability of cash flow. So just interested in getting a little bit more thoughts on how you're thinking about that?

Eric Thomas Steigerwalt - *Brighthouse Financial, Inc. - President, CEO & Director*

Erik, well, I'm having problems with this microphone today. Look, it's not like we never discuss it. And certainly, this is a Board topic as well. But at this point, it still strikes us that buying back our stock is the right way to go. Does that preclude eventually a dividend? No, it does not.

And as I kind of hinted and I'll say it more formally, we will talk about this. This is a topic that we should be talking about both as a management team and as a Board. And over time, there is a -- certainly, there is a possibility that we will pay a common dividend. But for the time being, and I think the words I used were buying back stock is probably a good assumption when you think about capital return for us right now.

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

Got it. And then I know you'll provide obviously the update on VA cash flows in a month or so. I was just hoping you could remind us of kind of the relative sensitivity to interest rates versus equity markets. And if we have an environment of higher rates but modestly declining markets like we've seen year-to-date, is that still something we should think of as a net positive for you?

Edward Allen Spehar - *Brighthouse Financial, Inc. - Executive VP & CFO*

Yes. Erik, I'm not going to get into the specifics here like ahead of the DE tables. The only thing I'd point out is when we did this last year, I remember, we talked about how our DEs -- our DE tables look very similar to the prior year adjusted for the $1 billion of additional capital that we took out 2 years ago because of the derisking of the hedge strategy, right.

And the point that I was making then was, look, it's -- interest rates had come down a lot. It is down 100 basis points. But at the same time, the equity market had performed very well. So it gave you an indication that they're both important, right?

Operator

Our next question comes from Mike Zaremski with Wolfe Research.

Michael David Zaremski - *Wolfe Research, LLC - Research Analyst*

Just 1 question. When you talk about your RBC ratio target, you used the word normal markets. Maybe you can comment on what is your view of normal markets? And has it evolved over recent quarters?

Edward Allen Spehar - *Brighthouse Financial, Inc. - Executive VP & CFO*

Mike, happy Friday to you. And it probably won't be a surprise that Eric just waved the hand to me to discuss the answer to this question. We were just sort of having a few lasts about what exactly does normal markets mean, right? Because it doesn't feel like normal, maybe ever. It's a guide for us to say that 400% to 450% is -- it feels like the right number for an RBC ratio during a -- kind of on a full cycle basis.

And so when times are really good, you would expect it to be above that. And if times got tough, certainly, you'd expect it to be below that. So that's why I think you want to make sure that you are positioned -- we've had a very good run here. I mean the stock market's done very well. Interest rates, not so much. But until recently, now we're seeing rates going up, too. So I don't know that now is the time to get too aggressive in terms of how you think about your capitalization at the operating company level.

Operator

Thank you. Ladies and gentlemen, I will now turn the call over to Dana Amante for closing remarks.

Dana Amante - *Brighthouse Financial, Inc. - Head of IR*

Thank you, Shannon, and thank you all for joining us today and for your interest in Brighthouse Financial. Have a great day.

Operator

This concludes today's conference call. Thank you for participating. You may now disconnect.