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BHF.OQ - Q2 2020 Brighthouse Financial Inc Earnings Call

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OVERVIEW:

Co. reported 2Q20 adjusted earnings, excluding impact from notable items, of $39m.

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PRESENTATION

Operator

Good morning, ladies and gentlemen, and welcome to Brighthouse Financial's Second Quarter 2020 Earnings Conference Call. My name is Liz, and I will be your coordinator today. (Operator Instructions) As a reminder, the conference is being recorded for replay purposes. (Operator Instructions) I would now like to turn the presentation over to David Rosenbaum, Head of Investor Relations. Mr. Rosenbaum, you may proceed.

David Rosenbaum - *Brighthouse Financial, Inc. - Head of IR*

Good morning, and thank you for joining Brighthouse Financial's Second Quarter 2020 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 at brighthousefinancial.com. We encourage you to review all of these materials, and we will refer to the slide presentation in our prepared remarks.

Today, you will hear from Eric Steigerwalt, our President and Chief Executive Officer; and Ed Spehar, our Chief Financial Officer. Following our prepared comments, we will open the call up for a question-and-answer period. Also, here with us today to participate in the discussions are Myles Lambert, Chief Distribution and Marketing Officer; Conor Murphy, Chief Operating Officer; and John Rosenthal, Chief Investment Officer.

Our discussion during this call will 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, August 7, 2020. 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 and our earnings release, slide presentation or financial supplement. 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, David, and good morning, everyone.

I want to cover a few topics today. First, I will provide some perspectives on the current environment. Next, I will give an update on our share repurchase program. And finally, I will discuss Brighthouse Financial's results in the second quarter.

So let's start with the current environment. I hope that you and your loved ones are well and staying safe as the COVID-19 pandemic continues to unfold and impact our communities in the global economy. Brighthouse Financial's top priority remains the well-being and safety of our employees and their families, our partners and our customers.

As I have said, it is in uncertain times like these when our mission to help people achieve financial security becomes even more important. Despite the challenges created by the pandemic, we remain steadfastly focused on our mission and strategy, and on delivering for our partners, customers and our shareholders. Importantly, we entered the current climate from a position of strength and remain confident in our focused strategy. Our balance sheet and liquidity remains strong, our investment portfolio is high quality and well diversified, and we continue to believe that we are well positioned to weather the current downturn.

The second topic I would like to cover is share repurchases. Since the announcement of our first stock repurchase authorization in August of 2018, we have repurchased a total of approximately $870 million of our common stock, a reduction of more than 22% of shares outstanding from the time we became an independent public company and well ahead of our initial expectations. As previously disclosed, we temporarily suspended repurchases of our common stock on May 11, and that suspension remains in effect at this time. We continually assess market conditions as well as other factors, and we will continue to be prudent while retaining flexibility should circumstances warrant resuming share repurchases this year. Importantly, our target of returning $1.5 billion of capital to our shareholders by year-end 2021 remains in place.

Now let me turn to second quarter results. Our key highlights for the quarter are summarized on Slide 5 of our earnings presentation. First, we continue to prudently manage our statutory capitalization. Our hedging program performed as expected in the second quarter of 2020. Importantly, we estimate that our combined risk-based capital or RBC ratio remained in the range of 515% to 535%, consistent with the range disclosed for the first quarter of this year. The RBC ratio in the second quarter includes the impact of a $500 million subsidiary ordinary dividend paid to the holding company in the quarter. Ed will provide more details on statutory results shortly.

Second, we had a strong sales quarter despite the challenging environment. Annuity sales were approximately $1.8 billion, down 3% compared with the second quarter of 2019. However, I am extremely pleased that we grew our annuity sales 6% in the first 6 months of 2020 compared with the same period in 2019. Our annuity sales results through the second quarter of this year demonstrate the strength and complementary nature of our annuity product portfolio as we weather the current environment. Additionally, we generated approximately $12 million of life insurance sales in the second quarter of 2020. I am very pleased with the progress we have made as we continue to execute on our life insurance strategy.

As I reflect on all that we've accomplished since reestablishing a competitive presence in the life insurance business last year, I want to give special thanks to our life insurance team and our life insurance distribution partners.

While the current market environment remains a headwind to near-term sales of annuity and life insurance products for Brighthouse and for the industry, we remain focused on broadening our product offerings and expanding our distribution footprint. We are very excited about expanding our relationship with BlackRock as we join the effort to 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.

With respect to life insurance, we remain focused on growing our business and expanding our digital footprint. So that end, in June, we announced the launch of Brighthouse SimplySelect, a new term life insurance product available online through the PolicyGenius. Brighthouse SimplySelect features a fast and simple purchase process that doesn't require invasive testing, allowing an underwriting decision within 24 hours for most applicants.

As I have said before, rising health care costs, unforeseen health care needs and insufficient income in retirement are pervasive retirement concerns for Americans and we believe Brighthouse Financial is well positioned to help people achieve financial security and help address retirement concerns over the long term.

Third, let me turn to total annuity net outflows, which were approximately $250 million in the quarter, down from both the second quarter of 2019 and sequentially, driven by continued strong sales as well as the market environment as fewer contract holders are surrendering policies. As we've said previously, we expect to see a continued shift in our business mix profile over time as we add more cash flow-generating and less capital-intensive new business, coupled with the runoff of less profitable business.

Fourth, corporate expenses, which do not include establishment costs were $210 million in the second quarter, lower than our expectations. We remain committed to reducing corporate expenses by $150 million on a run rate basis by the end of this year and by an additional $25 million in 2021.

Finally, we continue to make necessary investments in our technology infrastructure and in our business. We have referred to these investments as establishment costs. In the second quarter, establishment costs were approximately $35 million before tax. As I have said before, we are being prudent in how we are managing our way through our expected final couple of years of TSA exits. We now believe establishment costs will be approximately $125 million to $135 million in 2020, and $55 million to $65 million in 2021, both on a pretax basis. These TSA exits and associated systems transitions put us one step closer to our future state operating platform.

Before wrapping up, I want to take a moment to once again thank our employees for their tireless work and the resiliency they have demonstrated over the past several months. Since March, our employees have remained in work-from-home environment as we've prioritized their health and safety, while continuing to monitor the COVID-19 pandemic. Despite the challenges that can come with working remotely, our employees have risen to the occasion, they're simplifying our core values of being collaborative, adaptable and passionate. I am extremely proud of their focus and commitment, which have enabled us to continue to support our customers, partners and communities during these very difficult times.

To wrap up, we believe our balance sheet and liquidity positions are strong. We continue to believe we have the right strategy in place to deliver long-term shareholder value, and we believe that we are well positioned to continue the execution of our strategy.

With that, I'll turn the call over to Ed to discuss our financial results. Ed?

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

Thank you, Eric, and good morning, everyone. I hope you're staying safe and healthy and enjoying your summer as best you can.

With our focus on prudence and flexibility, we entered this challenging environment with a strong statutory balance sheet and a material reduction in our equity market risk profile. Last night, we reported second quarter earnings along with our preliminary statutory results. And as our results illustrate, we have continued to maintain a strong capital and liquidity position during this unprecedented time.

With the recovery in capital markets during the second quarter, our combined statutory total adjusted capital or TAC increased to $7.7 billion at June 30 from $7.2 billion at March 31. TAC increased despite a $500 million ordinary dividend paid to the holding company from Brighthouse Life Insurance Company or BLIC during the second quarter. The $500 million dividend from BLIC brings the year-to-date total to $800 million. Given our strong capital position, we intend to take the remaining $450 million of our planned $1.25 billion ordinary dividend from BLIC in the second half of this year. As a reminder, the $1.25 billion is consistent with the plan that we communicated on our business update call in early March.

I am also pleased to share that our estimated combined RBC ratio remained between 515% and 535% at June 30, consistent with our estimated RBC ratio at the end of the first quarter.

In the second quarter, we had normalized statutory earnings of approximately $600 million, bringing year-to-date results to a normalized statutory loss of approximately $200 million. Roughly 2/3 of normalized statutory earnings in the second quarter was attributable to the recovery in capital markets. The balance was driven by a rebound in nonvariable annuity results, including favorable mortality despite the impact from COVID-19 clients.

Moving to the holding company. We ended the second quarter with cash of approximately $1.3 billion, which is consistent with the estimate we provided on the first quarter call and roughly 5x annual fixed charges. We believe it is appropriate to have a conservative position at the holding company in the current environment. So in addition to maintaining a substantial cash balance, we also took the opportunity in the second quarter to extend our debt maturities. We issued senior debt and preferred stock and used the proceeds to prepay a $1 billion term loan that would have begun to amortize next year and was scheduled to mature in 2024. As a result of these actions, our next outstanding debt maturity is 2027.

Finally, even with the additional costs associated with extending our debt maturities, the combination of approximately $200 million of annual nondividend inflows to the holding company and the planned ordinary dividend from New England Life Insurance Company or NELICO covers our holding company fixed charges and other outflows.

Moving to adjusted earnings. Last night, we reported second quarter adjusted earnings, excluding the impact from notable items of $39 million, which compares with adjusted earnings on the same basis of $273 million in the first quarter of 2020 and $296 million in the second quarter of 2019. One notable item in the quarter was establishment costs of $28 million after-tax included in Corporate & Other.

When we look at second quarter adjusted earnings, there are 3 underlying themes. First, alternative investments generated a loss. Our alternative investment yield was negative 9.7% in the second quarter, which was driven by the unfavorable market performance in the first quarter. As a reminder, alternative investment income is generally reported on a one-quarter lag. As we think about alternative investment returns in the third quarter, we expect the bounce back, but probably not a full recapture of the second quarter decline, given that economic fundamentals remain strained.

Second, our underwriting margin was better than expected. Net claims on a pretax basis for the second quarter were $235 million, which is approximately $20 million below what we would consider a normal level. Results were favorable despite the negative impact from COVID-19. Net claims from the pandemic were approximately $25 million pretax with approximately $120,000 U.S. debts at the end of the second quarter. This is much better than the guidance we provided on our first quarter call.

Third, expenses were lower than expected. Corporate expenses were $210 million, which was below both the first quarter and a normal level. As Eric mentioned, we remain committed to reducing corporate expenses by $150 million on a run rate basis by year-end 2020 and by an additional $25 million in 2021.

I would now like to talk about the impact of market performance on our adjusted earnings. With separate account returns of 14%, we saw a reversal of the first quarter impact from market performance. Separate account return performance drove a decrease in deferred acquisition cost or DAC amortization for variable annuities and life insurance along with a decrease in variable annuity reserves. However, as we saw in the first quarter, the change in variable annuity DAC amortization was offset by a change in Shield DAC amortization.

Turning to adjusted earnings at the segment level. Annuities adjusted earnings, excluding notable items were $171 million in the quarter. Sequentially, DAC amortization was higher along with lower alternative investment income.

Life adjusted earnings, excluding notable items were $48 million in the quarter. Sequentially, results were impacted by lower DAC amortization and a higher underwriting margin, partially offset by lower alternative investment income.

The Run-off segment reported an adjusted loss, excluding notable items of $115 million in the quarter. Sequentially, results were driven by lower alternative investment income, partially offset by a higher underwriting margin.

Corporate & Other had an adjusted loss, excluding notable items of $65 million. Sequentially, results were driven by higher expenses and higher taxes.

Overall, I am pleased with our results this quarter. We continue to emphasize prudence and flexibility as evidenced by our strong capital and liquidity position. In these uncertain times, balance sheet strength remains paramount to protect our distribution franchise and to validate that we have a full cycle business model.

With that, we'd 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*

Eric, just a question on your comment about maintaining the $1.5 billion buyback goal through the end of 2021. My question is, if all other conditions remain, we'll call it, relatively benign versus where things are today, credit, equity markets, but interest rates remain at around 50 basis points, would you still expect to execute the $1.5 billion buyback with those types of conditions?

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

Taking your question at face value, yes, I would.

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

Got you. And then the related question would be how should we think about whether you would build meaningful capital under those same conditions, maybe that one's for Ed, in terms of the type of cash flow or RBC build you would expect to get without meaningful credit losses, fairly benign equity markets, but interest rates remaining low through the end of 2021?

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

Tom, it's Ed. So we're not going to give a forward look on normalized statutory earnings in this environment. But I guess I would say that with the 515% to 535% RBC ratio at the end of the second quarter, $1.3 billion of holding company cash and no debt maturities until 2027, we feel very good about our position during this period of uncertainty.

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, I guess, also on the capital side. I guess, Eric, in your prepared remarks, it seemed like you left the door up a little bit to return to buying back your stock maybe perhaps this year. So what are you guys paying attention to for when you might return to buybacks? And then when do you expect to get the remaining dividend from BLIC in the third or the fourth quarter? And can you let us know the unassigned funds at BLIC in the quarter as well?

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

Hi, Elyse, it's Eric. I'll start and then I think Ed will jump in.

I just -- let me highlight that, obviously, we temporarily suspended the share repurchases in early May, as you know. And that was after we had repurchased more than 12% of year-end 2019 shares outstanding at an average price that's roughly 15% below where we are now. So we feel pretty good about where we're at.

And I'll just add kind of dovetailing off of Tom's question. Look, we would like to achieve our capital return target of $1.5 billion by year-end '21. And having said that, look, we're going to evaluate market conditions and other factors. And as we think about the environment, if it's appropriate to begin repurchases, we will.

As you've heard Ed say many times, prudence and flexibility, that's what we're thinking about along with watching market conditions, et cetera.

Ed, you want to jump in?

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

Yes, Elyse. So 2 things. First, just one thing to add on to the share buyback that we have done in the year-to-date. I just want to highlight that by taking advantage of the opportunity earlier this year with our stock price down, we repurchased more shares in the first 5 months of this year than we had thought or had planned to repurchase for all of 2020. So just to underscore that we're very pleased with the capital actions we've taken year-to-date.

And then on your specific question on unassigned funds. Unassigned fund at the end of the first quarter was negative $140 million, I think. So more than $100 million negative at the end of the first quarter. It was approximately $1 billion positive at the end of the second quarter.

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

And then my second question, it seems like annuity sales have held up pretty well in the quarter. Can you just give us a sense of how sales might trend kind of given the environment that we're in right now for the balance of the year?

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

Yes. It's Myles speaking. So what I would say is, look, we're continuing to execute on our distribution strategy. We're adding wholesalers, we're expanding into new firms as well as new channels, we're introducing products that really are complementary to all different types of market conditions, and frankly, we're very pleased with our sales results. Annuity sales, quarter-over-quarter, were down slightly, but as Eric mentioned, still up 6% year-to-date. And we continue to just make fabulous progress as it relates to selling our new SmartCare product.

As it relates to kind of forecasting the rest of the year, I really believe that until we get back to more normal business conditions, COVID is still going to have an impact on sales. What exactly that impact looks like, I just can't quantify at this time.

Operator

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

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

I just want to follow-up on your capital position and your RBC level. I'm actually, I guess, I'm a little surprised to see even after dividing up the $500 million, your RBC level still kind of stayed relatively flat kind of quarter-over-quarter. Like I thought last quarter, you talked about how the moving pieces between -- under the new VA capital reform, how the TAC and the capital requirement changed through cycle so that your RBC will be relatively stable, regardless of the market situation. But then -- so like I would expect that will be the same for this quarter. So looking at where you are right now, even after dividing up the $500 million, you're still at 515% to 535%. So maybe can you elaborate a little bit in terms of the moving pieces for the change kind of between first quarter and second quarter?

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

Sure, Humphrey. So the discussion we had about the interplay between capital -- required capital and reserves. So the CTE70, the CTE98 movements of convergence in bad markets and divergence in good markets. We saw that again this quarter in terms of divergence. But it's important to keep in mind that we're just talking about in the framework relative to those 2 different measures of averages of the worse scenarios. We clearly benefit from better markets and that is the source of our normalized statutory earnings over time and therefore, our distributable earnings over time. So if you look at our results this quarter, we talk about normalized statutory earnings in total of $600 million with about 2/3 of that related to VA. And if you were to look at CTE98, which is what's important for RBC, you'd see the same dynamic of adding to assets above, just like you saw with the normalized statutory earnings. So it's not surprising given the magnitude of those numbers that if we take a $500 million dividend out in the second quarter and we have roughly the same amount of norm stat earnings, that you would see no material change in the risk-based capital ratio.

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

Okay. Got it.

And then my second question is on the annuity sales. So I guess in terms of the mix for the quarter, we saw Shield coming down. Fixed annuities actually went up. I think many of your peers have talked about difficult to get return for fixed annuity products in current environment. So maybe just talk about what you saw in terms of how you find attractive return for all your fixed product? And also what you saw in terms of Shield maybe in terms of market competition?

Conor Ernan Murphy - *Brighthouse Financial, Inc. - Executive VP & COO*

This is Conor. I'll start, and I'm sure Myles will add to the distribution story.

So starting with the fixed products. So really, we -- and I'm referring to the supplement, we have both the fixed indexed annuities and the fixed deferred annuities. You'll see an increase in fixed indexed annuities because we've added a new product just -- we added it late in the first quarter. So that's leading to some of the increase there, at least sequentially. And on the fixed deferred side, so we -- well, actually, overarching from all of our pricing. We've remained very disciplined. We're very comfortable, very pleased with our returns. Specifically, with the fixed deferred, our expense basis continues to improve, which helps us. But we also have a reinsurance agreement in place on that, which also helps with our product as well. And I'm sure, as I said, Myles, we want to add in terms of the interest in that product in the current environment. But just from an overarching perspective too, Humphrey, and Eric said this in his prepared remarks, we -- when Brighthouse came into being, clearly, we had Shield as our marquee product and it still is, and it represented about half of our sales this quarter. It was probably 60% a year ago. But we've been intentional. We had a VA flex product as well, and we've been intentional about adding a pair of fixed indexed annuities and a pair of fixed of deferred annuities because as you know and as we refer to at Investor Day, we are continuing to change the mix of business from where we began to continue to dilute the more capital-intensive VA piece, getting up from roughly 1/3 of our business when we started out to 1/6 of our business by 2025.

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

Yes. And I'll jump in here as it relates to fixed sales as well. So I think Conor just kind of touched on it.

Fixed sales are absolutely part of our strategy. The products that we're offering right now do have competitive rates, but I also think this market volatility in this environment is also making an attractive solution to many clients out there. We've had a number of marketing efforts, which has been part of our strategy direct to advisers to make sure that they understand the competitive nature of the product that we have right now. And we've been really focused on the bank and wirehouse channels with the sale of our FRA product, and we're seeing great growth in those channels.

As it relates to your question pertaining to Shield, we still remain incredibly positive and we're very pleased with our Shield sales. We did over $900 million of sales for the quarter. And yes, you had mentioned some decline sequentially and quarter-over-quarter. One -- actually 2 of our major distributors, our sales are down relatively significantly, and we're attributing most of that to their pivot in adjusting, working remotely in COVID. Other than that, if we take our sales across the board with most of our other firms, are still very, very strong. So I think if you see some of the negative impact as it relates to sales with Shield, it's more derivative to a couple of our major distributors and their pivot during the pandemic.

Operator

Our next question comes from Ryan Krueger with KBW.

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

DAC amortization in annuities has bounced around a lot last couple of quarters. Can you give a sense of what you would view as the more normalized level going forward?

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

Sure. Ryan. So I think on last quarter's call, I said that a more normal level of amortization for annuities was probably around $100 million a quarter. And in the first quarter, when we had a 20% decline in the stock market and the benefit of Shield offset, I think we had around $40 million of DAC amortization. So $60 million off of what I said was normal. If you look at this quarter, where we have a reversal largely of what happened in the first quarter and the DAC amortization and annuities was roughly $160 million. So I think you take an average of the first 6 months, you're right in the middle of what would be a normal quarter. So like -- your DAC amortization is going to bounce around. Obviously, we're running the company based on statutory and distributable earnings and cash and all the other things that we talk about most of the time on this call, but it's one of those things that we're not providing an updated kind of rule of thumb at this point. We're looking at it. Obviously, with the growing importance of Shield, it has changed the amortization dynamic for us. But what's most important about the growing importance of Shield is the fundamental benefit we get as a hedge to our in-force book of VA and the attractive profit characteristics of that product and the other products that we sell today, which over time, I think, is a critical driver of the valuation story for the company.

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

And then can you discuss, I guess, what the NAIC is considering in terms of lowering their interest rate assumptions for variable annuity accounting and how you think that may play out and how it could affect you?

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

Sure. I mean, I'll start off by saying that generally, as you can imagine, we are very engaged with the NAIC and regulators on all matters of importance to Brighthouse. I would say on your specific question, it is premature to discuss any change to VA reform, I think, considering the fact that many companies haven't even adopted VA reform yet, remember, we adopted early at the end of 2019. What I would say is, obviously, you hear us emphasize statutory balance sheet, holding company position, prudence, flexibility, all the words that we use frequently when we talk about this stuff. We're managing balance sheet considering current market conditions over an extended period of time. So current market conditions over an extended period of time. So if we look and think about where we were at the end of the second quarter, with the 515% to 535% RBC ratio, with $1.3 billion of cash holding company and no debt maturities until 2027, we are positioned to comfortably manage through whatever equity, interest rate or credit environment we think we'll face over the coming years.

Operator

Our next question comes from Andrew Kligerman with Crédit Suisse.

Andrew Scott Kligerman - *Crédit Suisse AG, Research Division - MD & Senior Life Insurance Analyst*

I want to come back to capital for a moment to better understand the development in total adjusted capital. So in the first quarter, Brighthouse went from $9.7 billion to $7.2 billion, including a $300 million dividend. So there was a $2.2 billion delta. In the second quarter, you went from $7.2 billion to $7.7 billion, including a $500 million dividend. So there was a $1 billion delta. So your $2.2 billion against $1 billion, if you take out the dividend impacts, and given the magnitude of the markets was similar, maybe interest rates played a role a bit last quarter, much more so than this. But why the big differential in the movements in the 2 quarters on total adjusted capital?

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

So I think if you look at the rebound in this quarter. So as you said, we took a $500 million dividend. So the actual increase in TAC of $1 billion this quarter was really driven by a rebound in the capital markets. And the equity market came back a lot in the second quarter, obviously, but was still down for the first 6 months. So you didn't recoup everything that you lost. I mean, that's the biggest answer -- that's the biggest portion of the answer. And we also had like modest non-VA losses as well. So the combination of those 2 factors really explains the dynamic you're looking at.

Andrew Scott Kligerman - *Crédit Suisse AG, Research Division - MD & Senior Life Insurance Analyst*

Okay. Also, with respect to mortality. So you have guidance around, what is it, like $70 million per 100,000 lives, and it seemed that the estimate for COVID-19 mortality this quarter was around $25 million. So far less than your sensitivity provided last quarter. So is Brighthouse in a pretty favorable position relative to the sensitivities? And would you like to change that trend going forward at this stage?

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

Andrew, you cut out a little bit at the end there, but I think I get the gist of the question.

Let me start off by sizing this a little bit for you overall, okay? So if we look at -- let's just put COVID claims aside for a second. Our quarterly average direct claims in life insurance are north of $400 million, okay? So quarterly average of net -- of direct claims north of $400 million. And our net claims are around $250 million a quarter. So I think in the context of the number of claims that we have on both a direct and net basis, we ought to think about the numbers we're talking about here with COVID and the difference between the sensitivity and is it going to be higher, Is it going to be lower, we don't think it's worth trying to get more specific on this. We're happy that in the first -- in the second quarter, we had better experience than what our guidance had suggested. We had talked about, as you said, $70 million, which was an after-tax number for $100,000 U.S. debts. We had $120,000 U.S. debts, and our pretax number was around $25 million. So obviously, much better, but this is still an uncertainty. We're just not going to provide any update beyond what we said so far.

Operator

Our next question comes from John Barnidge with Piper Sandler.

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

Your $150 million corporate expense reduction in 2020, an additional $25 million in 2021. Does that reflect any potential lease or real estate savings that may emerge from a changing working environment?

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

It's Eric. Not really. We've been on that journey for a while and so we don't have anything like that figured in. We don't actually have -- we have maybe a small lease coming up soon, but bigger ones are out, so no.

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

Okay. And then can you also talk about rental forbearance in your commercial real estate portfolio and the investments?

John Lloyd Rosenthal - *Brighthouse Financial, Inc. - Executive VP & CIO*

It's John. As of June 30, we had $763 million of loans, a relatively small portion of the portfolio of less than 8% with debt forbearance agreements in place. Virtually all were hotel and retail mortgage loans. And we would expect substantially all of them to repay eventually.

Operator

Our next question comes from Erik Bass with Autonomous Research.

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

I was hoping you could talk a little bit more about the new annuity product with BlackRock and the potential you see for sales over time. Is this a near term opportunity? Or is it something that's more, gives you access to kind of a new and potentially growing market?

Conor Ernan Murphy - *Brighthouse Financial, Inc. - Executive VP & COO*

Eric, it's Conor. So as you know, this was just announced in the second quarter. So it's near term, but it's going to be most of the rest of this year, I think, kind of getting organized. We don't expect it to be a source of revenue until 2021. Obviously, while we're very, very excited about it, and we think it's a great endorsement for Brighthouse, and it's a continuation of a great partnership we already have with BlackRock, it's too early to frame what the economics might look like. So we'll certainly be back to you about that. We're excited to be able to do that, but it's too early at this stage.

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

Got it. And then maybe if you could talk a bit more about your strategy for growing life sales from here and how you're adapting to the current working environment?

Conor Ernan Murphy - *Brighthouse Financial, Inc. - Executive VP & COO*

Sure. I mean, I can start a little bit on the product side, but it's -- and then I'll give it to Myles. I talked a few moments ago with Humphrey about the expansion of the annuity side. As you know, on the life side, we reentered the life space with SmartCare last year and we've been pleased with that. And then we reentered the term space just this quarter. We launched the SimplySelect term with PolicyGenius. And again, bear in mind, those are -- when we say reenter, we do still retain almost $550 billion of Life in-force before reinsurance and close to $400 million after reinsurance.

But I'm going to let Myles speak to the emerging strategy on the life side.

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

Yes. So we're really pleased with the progression we've made regarding SmartCare. We're selling the product now at over a dozen firms, and we have access to approximately 60,000 advisers. And the plan moving forward is to continue to develop and grow the wholesale in-force. We have a number of plans underway as it relates to bringing on new additional major firms starting next year. We also have a channel expansion strategy that's well underway. And we feel really good about the progress that we've made. The product is absolutely resonating in the marketplace. It's got a competitive indemnity benefit and it's the only linked benefit product in the market right now that has a cash value that potentially could grow with market conditions. So the reception from our advisers and our distributors has been really positive, and we're going to look to just continue to expand on that as well as introduce new products at some point in time in the future, as Conor just mentioned.

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

Got it. And those new products, I'm assuming are things you would hope to kind of be able to bring directly into the distribution that you're building out on SmartCare?

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

That's right. I mean, we're highly focused on major financial institutions as well as the expansion into the BGA marketplace, and we will be developing products that are very complementary to those type of advisers and financial professionals.

Conor Ernan Murphy - *Brighthouse Financial, Inc. - Executive VP & COO*

Yes. So just to elaborate a little further. So SmartCare, which is a hybrid LTC product. We developed a lot of the infrastructure for that within Brighthouse and the data-driven underwriting and so on. So we were able to leverage a lot of that when we did the SimplySelect term. And we continued to -- we expect we'll continue to develop other products that are complementary to those, both in terms of architecture and to Myles' point, our distribution capabilities. Bearing in mind that SimplySelect term through PolicyGenius is actually a different avenue for us, but you should expect that a lot of what will develop from here will be more complementary to the overarching core distribution network.

Operator

Our next question comes from Suneet Kamath with Citi.

Suneet Laxman L. Kamath - *Citigroup Inc., Research Division - MD*

I think in your prepared remarks, you talked about lapse rates in VA, and I'm assuming it's the legacy VA being lower than the usual. Is that been a one-quarter phenomenon? Or has that been going on for a while? And can you talk about what your lapse rate assumption is that's built into your statutory VA capital and reserves?

Conor Ernan Murphy - *Brighthouse Financial, Inc. - Executive VP & COO*

Well, I'll start, Suneet, thank you. It's Conor. Just from a flows perspective and what we've been seeing.

I would say at this stage, it's been a 4-month phenomenon. We did see lower outflows. I think everybody knows our outflows have been running pretty consistently about $1 billion a month, $3 billion a quarter. We had lower outflows a little bit in the first quarter because we had lower outflows in the month of March as this was already getting underway. So yes, so instead of $3 billion in outflows this quarter, it's closer to $2 billion. As everybody knows, those are really made up of 4 things. We still have almost exactly the same amount of people annuitizing and almost the same amount of people who are dying, which leaves your partial and full withdrawals, and we had a noticeable decline in partial withdrawals and a very significant decline in full withdrawals, which I think speaks to the, maybe the safety haven nature of Brighthouse in this environment. Hard to say what will happen, obviously, from here though. I'm going to let Ed speak to the overall lapse assumptions, if he wishes.

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

Yes. Suneet. Obviously, there was a lot of work done around VA reform in terms of assumptions for key policyholder behavior and obviously, we have dynamic lapse assumptions. We've always had them, but the assumptions we have are consistent with the work that was done around VA reform. So there isn't just one lapse rate to quote for you. It's a dynamic lapse formula obviously, so that depends on market conditions. But consistent with VA reform.

Suneet Laxman L. Kamath - *Citigroup Inc., Research Division - MD*

Okay. And then just as we think about the third quarter assumption review, you're not going to front-run it, but have you given any guidance in terms of the impact if you change that 3.75 long-term interest rate assumption?

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

We have not given any guidance. Sorry, I was on mute. We have not given any guidance. I will tell you that, obviously, we look at all of our assumptions in the third quarter. It is a significant undertaking. With regard to this single assumption that you're talking about, we would consider both internal and external models as well as the forward curve.

Operator

Ladies and gentlemen, I will now turn the call back over to Mr. Steigerwalt for closing remarks. .

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

Thank you, operator. Thanks for participating on today's call.

Just to recap, we entered the current climate from a position of strength and remain confident. As you heard today, our balance sheet and liquidity remains strong, and our investment portfolio is in good shape. We continue to believe that we are well positioned to weather the current downturn.

Also, I'll just add, we celebrate our third anniversary today as an independent public company. And I want to give a special thank you to all our employees for their tremendous hard work and dedication and also a shout out to our distributors, who we very much appreciate. I hope that you and your loved ones stay safe, and we look forward to speaking with you again at the next quarter.

Operator

Ladies and gentlemen, this concludes today's conference call. Thank you for participating. You may now disconnect.

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