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PRESENTATION

Operator

Good morning, everyone. My name is Latif, and I will be your conference operator today. At this time, I would like to welcome everyone to the Sun Life Financial Q1 2022 Financial Results Conference Call. (Operator Instructions). The host of this call is Yaniv Bitton, Vice President, Head of Investor Relations and Capital Markets. Please go ahead, Mr. Bitton.

Yaniv Bitton - *Sun Life Financial Inc. - VP, Head of IR & Capital Markets*

Thank you, and good morning, everyone. Welcome to Sun Life's Earnings Call for the first quarter of 2022. Our earnings release and the slides for today's call are available on the Investor Relations section of our website at sunlife.com. We will begin today's call with an overview of our first quarter strategic highlights from Kevin Strain, President and Chief Executive Officer. Following Kevin's remarks, Manjit Singh, Executive Vice President and Chief Financial Officer, will present the financial results for the quarter. After the prepared remarks we'll move to the question and answer portion of the call. Other members of management will also be available to answer your questions this morning. Turning to Slide 2. I draw your attention to the cautionary language regarding the use of forward-looking statements and non-IFRS financial measures, which form part of today's remarks. As noted in the slides, forward-looking statements may be rendered inaccurate by subsequent events. And with that, I'll now turn things over to Kevin.

Kevin David Strain - *Sun Life Financial Inc. - President, CEO & Director*

Thanks, Yaniv, and good morning to everybody on the call today. Turning to Slide 4. Sun Life delivered a solid start to 2022, driven by our diversified business model, prudent risk management practices and strong capital position. Reported net income of $858 million was down 8% from prior year, and underlying net income of $843 million was broadly in line with last year. COVID-19 continued to impact our businesses. And while headwinds from COVID remain, as of March, we started to see an improvement in U.S. COVID-related death, which should drive more favorable mortality experience in the second quarter.

We continue to watch the trends closely. And in most of our markets, we are seeing a transition as COVID becomes less of an impact and populations have increased immunity. This doesn't mean COVID is over, but it does suggest smaller impacts in terms of claims and business interruption going forward. We are also pleased that in most of our markets, our offices are now open, and we have people working flexibly both in the office and virtually as their day allows. With the war in Ukraine impacting economic conditions, supply chains and energy costs, the world is now facing new challenges with heightened geopolitical pressures and central banks raising rates to curb higher-than-expected inflation.

These challenges create uncertainty, but our diversified business mix and strong risk management will enable us to manage through these headwinds. We are expecting pressure on equity markets, credit and expenses due to inflation but higher interest rates, particularly at the long end of the curve, should help drive profitability. And the ongoing growth in our businesses also supports our medium-term objectives. Our capital position remains strong with a LICAT ratio of 143% at SLF. We are also pleased to announce a 4.5% increase to our common share dividend, demonstrating our commitment to deliver value for our shareholders.

Turning to Slide 5. We continue to deliver on our purpose and our ambition in the quarter as we saw continued progress in delivering on our client impact strategy. Sustainability is a key component of our strategy. And in March, we released our annual sustainability report, which outlines the areas where Sun Life can have the greatest impact, including increasing financial security, fostering healthier lives and advancing sustainable investing. The report outlines how being sustainability-driven is core to Sun Life strategy and how we're making an impact on sustainability for our clients, our employees and advisers our communities and future generations.

In Hong Kong, we announced Stellar, the first ESG savings plan in the market that actively integrates ESG concepts into its investment strategies. This enables clients to build their wealth in a way that has a positive impact while also ensuring a legacy for future generations. Stellar allocates funds to sustainable investments, such as renewable energy, sustainable buildings, energy transition and water and waste management with a particular focus on assets with relatively low carbon intensity. This is a great example of bringing a sustainable solution to market by leveraging the strength of SLC Management and our affiliate companies, InfraRed Capital Partners and BentallGreenOak as well as our local investments team in Hong Kong.

Moving to distribution excellence. Last month, we announced the expansion of our partnership with CIMB Niaga in Indonesia. CIMB is an important regional partner for us in Asia. In fact, CIMB Niaga was one of our first ever bancassurance partners. Under the new agreement, Sun Life will be the provider of insurance solutions to CIMB Niaga customers through all channels starting in 2025. We're excited about expanding our relationship with CIMB Indonesia. Indonesia is the largest economy in Southeast Asia with a young emerging middle class, one of the world's largest working age populations and low insurance penetration.

Turning to Asset Management. We continue to see strong momentum at SLC Management, where in the first quarter we raised $5.7 billion of capital, reflecting the strength and diversification of our alternative investment capabilities. Sun Life also recognized for -- Sun Life was also recognized for its inclusive culture last month when it was named one of the 2022 Best Workplaces in Canada by Great Places to Work. I'm proud of this achievement, and I want to thank our employees for making this possible. We're also excited that starting next season, Sun Life will be the official health and wellness partner of the Toronto Raptors basketball team.

As part of this expanded partnership, our goal together is to find new opportunities to help Canadians live healthier lives. Slide 5 and 6 also provide updates on how we continue to drive digital leadership across the organization. In Canada, we launched Prosper by Sun Life, delivering a simple and intuitive client experience. Prosper by Sun Life is a first-of-its-kind hybrid device solution that provides all Canadians a digital tool to identify, track and reach their protection, wealth and health goals all in one place. Prosper is linked to a team of salary advisers who can provide recommendations and product solutions to our clients at moments that matter.

In the U.S., we introduced Benefits Explorer. We know benefit selection can be stressful and confusing for some members. So this tool helps educate and prepare employees for benefits enrollment. The tool provides access to live benefits counselors and direct links to their employers' online enrollment and offers employees a guided path to learn about their benefits through the year so they can choose the right benefits package for their needs. And in Asia, our predictive modeling tool, Next Best Offer, helps our advisers recommend the right products at the right moment to our clients.

We've seen terrific results with over 70% product take-up from the clients we were able to engage with through this tool. These are just a few examples of how Sun Life's digital leadership is delivered on our client impact strategy while also generating business growth. I also want to provide a quick update on our agreement to acquire DentaQuest. We've made good progress obtaining necessary approvals and remain on track for a close in the first half of the year. We're looking forward to DentaQuest becoming part of the Sun Life family and welcoming their employees and 33 million members to Sun Life.

Before I hand the call over to Manjit, I want to say our hearts and thoughts remain with the people of Ukraine and everyone affected by this senseless invasion and war. Together with the global community, we're concerned about the ongoing humanitarian crisis in the country and surrounding regions and the threats to global peace and security. Sun Life, its companies and affiliates, including BentallGreenOak and InfraRed Partners, along with our employees have donated more than $1.1 million to various charities that are providing direct humanitarian support in Ukraine.

We also know that people are struggling with mental health concerns, which have been exasperated by both the ongoing pandemic as well as concerns related to world security and peace. As a result, in partnership with Dialogue, we are currently providing free access to self-guided online therapy to anyone in Canada struggling with mental health issues. All of this continues to drive home how important our purpose is, and I can't remember a time when helping people achieved lifetime financial security and live healthier lives has been more important. And our mix of asset management and insurance businesses are well positioned to deliver on this purpose, but also to manage through these economic headwinds. With that, Manjit will now take us through the financial results for the first quarter.

Manjit Singh - *Sun Life Financial Inc. - Executive VP & CFO*

Thank you, Kevin, and good morning, everyone. Slide 8 provides an overview of our first quarter results. Sun Life delivered solid results amidst a challenging operating environment with good momentum across all of our business groups. Reported net income in the quarter was $858 million, down 8%, reflecting less favorable market-related impacts. Underlying net income of $843 million and underlying earnings per share of $1.44 were down modestly from the prior year. Earnings for the quarter were supported by strong fundamental business activity partially offset by corporate-related impacts in the U.S. and Asia.

Earnings on surplus of $65 million was lower this quarter, primarily driven by higher external debt costs and lower AFS gains. With rising rates and wider spreads, contribution from AFS gains are expected to moderate. At the same time, these factors can also provide trading opportunities, which can generate investment-related gains. Underlying return on equity was 14% in the quarter. Assets under management were $1.35 trillion at the end of Q1. This was down from the end of last quarter, reflecting declines in equity markets and rising interest rates. Book value per share was up 7% over the prior year. Excluding impacts and other comprehensive income, which includes foreign currency translation and changes in available for sale, book value per share was up 11%.

Our capital position remains strong with LICAT ratios of 143% at SLF and 123% at SLA and a financial leverage ratio of 25.9%. Let's turn to our business group performance starting on Slide 10 with MFS. MFS reported net income of USD 228 million, which was up 23% from the prior year, reflecting lower fair value changes on share-based payment awards. Underlying net income was up 4%, driven by higher average net assets. And MFS generated a solid pretax net operating margin of 39%. Compared to the fourth quarter of 2021, the operating margin declined by 4 percentage points due to lower average net assets and seasonally higher compensation expense.

AUM declined 8% during the quarter to USD 637 billion, largely reflecting the decline in equity markets and USD 5.4 billion of fund outflows. MFS continues to deliver strong long-term fund performance for our clients. In the annual Barron's Rankings released in February, MFS ranked in the top 10 for the 5- and 10-year periods across its U.S. funds lineup. Turning to Slide 11. SLC Management delivered another strong quarter with a reported net income of $19 million and underlying net income of $34 million. We have provided some additional financial metrics for SLC Management that align with alternative Asset Management peers.

One of the key metrics is fee-related earnings, which represents a profitability from managing the assets before items such as realized performance fees. Fee-related earnings were up 38% year-over-year, reflecting strong capital raising activity and deployment into fee-earning AUM over the past 12 months. The fee-related earnings margin of 23% was down modestly due to higher marketing costs for capital raising activities. Operating margin of 24% was up slightly and is on track to meet our target of 30% to 35% by 2025.

Strong capital raising of $5.7 billion in the quarter reflects the strength and diversification of our investments platform. And we are currently holding $18 billion of AUM not yet earning fees. Once invested, these assets can generate annualized fee revenue of more than $150 million. On Slide 12, Canada's reported net income of $263 million was down 35% year-over-year, mainly due to market-related impacts. Underlying net income of $298 million was up 5% from the prior year underpinned by broad-based business growth and higher investment gains.

Momentum in the Canadian business is strong. Expected profit growth was 7%, total wealth sales were solid, reflecting higher defined contribution sales and insurance sales were strong driven by new group benefits mandates and higher non-par life sales. We are also continuing to invest in capabilities and make it easier for clients to do business with us.

One example is our investment in predictive analytics in our underwriting process. This has allowed us to process over 60% of life policies without lab testing, further improving our overall client experience. Turning to Slide 13. U.S. reported net income of USD 133 million was down 20% from the prior year, reflecting a decline in the underlying net income. Underlying net income for the first quarter of USD 93 million includes $30 million of COVID-related impacts, mostly driven by elevated group mortality. Compared to the prior quarter, earnings were up $37 million, driven by favorable stock loss mobility and a 17% decline in working age population deaths, partially offset by higher long-term disability claims.

Looking forward, we expect pandemic-related mortality headwinds to moderate as U.S. deaths have continued to decline since early March. Similarly, we expect there will be some normalization of favorable stop-loss morbidity experience as health care utilization starts to increase. More importantly, the core fundamentals of our U.S. business remains strong, as we continue to generate high persistency, good premium growth and achieve solid pricing margins, all while making investments in our product and digital capabilities.

Slide 14 outlines Asia's results for the quarter. Reported net income was $161 million, down 16% from the prior year in constant currency, reflecting market-related impacts. Underlying net income of $152 million was down 1% on a constant currency basis. The first quarter results included lower sales in Hong Kong, driven by heightened COVID-related lockdown measures. Mortality experience was elevated in international, driven by a small number of larger claims. These factors were partially offset by higher investment activity gains and disciplined expense management. Excluding Hong Kong, insuring sales were relatively consistent with prior year, which highlights the benefits of our diversified markets and products across Asia.

Wealth net flows of nearly $300 million reflect the strength in the Hong Kong MPF market, where we continue to rank second overall for net flows. Looking forward, as COVID restrictions are slowly lifted in our Asian markets, we are optimistic that sales activity will pick up. Altogether, our business has delivered solid financial results against a challenging macroeconomic backdrop. Although we expect headwinds to continue over the near term, we believe our diversified business model, along with our strong capital position, provide a resilient foundation to manage through the current environment.

We will also maintain our focus on executing on key strategic priorities, and we will continue to invest in our businesses for future growth. Before I close off, I want to remind everyone about our IFRS 17 education session on May 31. Overall, Sun Life is well prepared for the transition to IFRS 17, and we look forward to sharing more information with you at the end of the month. With that, I'll turn the call back to Yaniv for Q&A.

QUESTIONS AND ANSWERS

Yaniv Bitton - *Sun Life Financial Inc. - VP, Head of IR & Capital Markets*

Thank you, Manjit. (Operator Instructions). I will now ask our operator to pull the participants.

Operator

(Operator Instructions). Our first question comes from Meny Grauman of Scotiabank.

Meny Grauman - *Scotiabank Global Banking and Markets, Research Division - MD of Financial Services Equity Research & Analyst*

Dan, just wanted a little bit more detail on your outlook for mortality in the U.S. It was noted that it's improving -- when do you expect it to actually normalize? And if we look at the stop loss business as well, when do you expect COVID-related impacts to fully normalize there as well?

Daniel Richard Fishbein - *Sun Life Financial Inc. - President of Sun Life U.S.*

Meny, It's Dan Fishbein. Thanks for the questions. In terms of mortality, we're certainly seeing significant improvement. As you saw in the first quarter was better sequentially than the fourth quarter. Most of that improvement occurred in the month of March. So if you look -- break it down by the months, we're starting to see steady improvement month-over-month. I can share that April improved from there. And so far in May, we see further improvement. If you look at external estimates, there were about 160,000 total deaths in the U.S. in the first quarter, and the external estimates are predicting an average of about 30,000 total population deaths in the second quarter.

So that's a reduction of about 80%. So you should expect to see significant improvement in our mortality, certainly reflecting that. As for your question as to when will it completely return to normal, unfortunately, we don't think that COVID is going away completely. And we do think there will be elevated mortality for a significant period of time. So, we are building that into our pricing, as we've mentioned before. It does take a full 3 years to cycle through the entire book of business. We started increasing our pricing at the end of last year. But certainly, we have a ways to go until that pricing catches up.

But that's probably about a mid-single-digit impact. Our hope, of course, is that, that will remain at the current relatively low level, but we're likely to see some peaks and valleys in that going forward. We are at 325 deaths a day at the moment on a 7-day average in the U.S. and that compares with numbers in the first quarter that reached as high as 2,700 a day. So clearly, mortality is at a lower level now. On stop-loss, as you noted, we had quite favorable experience in the first quarter. About half of that was due to tailwinds related to COVID delays in care. But about half of that was related to underlying favorable underwriting results. We do think over the next few quarters, utilization in hospitals will return close to normal levels, but that will take a few quarters. Our own underlying good results, though should persist.

Meny Grauman - *Scotiabank Global Banking and Markets, Research Division - MD of Financial Services Equity Research & Analyst*

And then just maybe just a follow-up on the pricing. I know we talked about it last quarter, but just from a competitive point of view, what are you seeing out there in the market is -- are most of your competitors viewing it the same way as you in terms of the necessity to raise pricing, COVID is not going away? Or is there -- basically, what's going on in the market now relative to the pricing that you're pushing through?

Daniel Richard Fishbein - *Sun Life Financial Inc. - President of Sun Life U.S.*

Generally, our sense is that, that mid-single digit range is what the industry is doing. There's always exceptions. It remains a highly competitive market. And so on a case-by-case basis, we still see pretty intense competition. but we believe that our level of increase is consistent with the market.

Operator

Our next question comes from David Motemaden of Evercore ISI.

David Kenneth Motemaden - *Evercore ISI Institutional Equities, Research Division - MD & Fundamental Research Analyst*

Just had a question for MFS. So could -- Kevin, could you just talk about the margin outlook there? And how do you think you can manage through the market volatility given some of the inflationary comments you made in your prepared remarks that may make it more difficult to manage the expense base than in the past?

Kevin David Strain - *Sun Life Financial Inc. - President, CEO & Director*

Thanks, David. I'm going to let Mike answer the question on that.

Michael William Roberge - *Sun Life Financial Inc. - Chairman of MFS Mclean Budden Limited & Co-CEO of MFS Investment Management*

David, I mean clearly, the -- as we made our way through Q1 year-over-year results were up -- pretax was up over last year, but as ANA has continued to come down. In the second quarter relative to last year, that's going to obviously have an impact on the profitability and the margin. The guidance we provide over time is in a normal environment, we think a net margin in the 35% to 40% range. We were at the higher end of that and well over that at late last year, given the market at all-time highs. And so what you'll see in the expense side what naturally comes down as those variable -- those things that are tied to profitability like compensation, asset-based fees that we pay distributors. And so we're still comfortable with that range, but you should expect that if the market stays where it is for the year, obviously, the margin is going to be pressured relative to last year.

David Kenneth Motemaden - *Evercore ISI Institutional Equities, Research Division - MD & Fundamental Research Analyst*

Yes. Got it. That makes sense. And then maybe just another question just for Dan. Just in terms of the non-COVID long-term disability experience, could you just talk about what you're seeing what you saw in the quarter, your expectations and if you're repricing the business? Or how you're repricing the business in response to that?

Daniel Richard Fishbein - *Sun Life Financial Inc. - President of Sun Life U.S.*

Yes. We definitely are seeing some elevated morbidity in long-term disability. Now a significant amount of that is COVID related. There is some -- we do have some long COVID cases. The good news is, although this is a little more anecdotal, we are seeing recoveries in long COVID. So those disability don't seem to be long-term persistent. But there is some overall elevation in LTD experience that's non-COVID related as well. It's modest, but it's real. We think that's related to some of the second order effects of the pandemic, including the recent moves by some employers to require employees to return to the office.

We think some of that will persist, but maybe not long term, that may be a few quarters kind of impact as the labor market and employers find their equilibrium of how they want to work in the future. However, like in our group life business, we are raising prices in our disability business as well to reflect these impacts. Coincidentally, it's the same mid-single digits kind of range. And we're generally seeing that in the marketplace as well. Same effect though, you see case-by-case intense competition, but we do believe competitors are raising rates by a similar amount.

Operator

Our next question comes from Gabriel Dechaine of National Bank.

Gabriel Dechaine - *National Bank Financial, Inc., Research Division - Analyst*

Just yield enhancement gains, big uptick this quarter from what we've seen in the prior few quarters, over $100 million. Can you tell me what that number would look like under IFRS 17?

Manjit Singh - *Sun Life Financial Inc. - Executive VP & CFO*

Gabriel, it's Manjit. As you know, the overall investment activity gains are largely driven by a couple of things, the overall market conditions and our available funds that we have to put into the market to invest. And obviously, we had some pretty good conditions in the quarter, and our investment teams took advantage of that to invest in good quality, higher-yielding assets, and that's what drove the gain in the quarter. On the IFRS 17 question, we'll handle that in our May 31 session that we have upcoming. So we'll give you more detail then.

Gabriel Dechaine - *National Bank Financial, Inc., Research Division - Analyst*

Would it be materially lower?

Manjit Singh - *Sun Life Financial Inc. - Executive VP & CFO*

Yes. I gave -- but we'll give you more details on May 31.

Gabriel Dechaine - *National Bank Financial, Inc., Research Division - Analyst*

And I guess this quarter -- I mean, in the current accounting, this quarter, you're probably seeing similar spread pickup opportunities, right?

Manjit Singh - *Sun Life Financial Inc. - Executive VP & CFO*

Yes. I guess it will depend on sort of the market availability as well as the funds that we're putting into the market. So, so far, the market is continuing to provide some opportunities.

Operator

Our next question comes from Scott Chan of Canaccord.

Scott Chan - *Canaccord Genuity Corp., Research Division - Director of Research of Financials & Financial Services Analyst*

Maybe for Manjit or Steve on SLC, I really appreciate the increasing -- the updated disclosure on that segment. So specifically on FRE versus kind of the net income target that you updated last quarter. And maybe going down to the margin, I don't think you're prepared to do an FRE target. But margins were in the low 20s for FRE. And you talked about a 30%, 35% operated target by 2025. Would it be safe to say that FRE margin would be in line with that operating target? Or would there be nuances up or down?

Stephen Clarkson Peacher - *Sun Life Financial Inc. - President of SLC Management*

Thanks, Scott. This is Steve. I can answer that. I think over time, you're going to see -- the main difference between FRE fee-related earnings and operating income is going to be that under -- between those 2, you're going to have performance fees and income from seed investments, that would be the difference between operating income and FRE margin. I think that those -- over time, you're going to see more performance fees as the business grows, I think you're going to see more seed capital investments. So you'll see more seed-related income.

I think with our margin for the quarter, we're on track, we think, for the margin parts that we set out for 2025. And some of the fluctuation you'll see in margin quarter-to-quarter or even year-over-year can relate to things like catch-up fees, which could impact the margin or marketing costs where we have a big fundraising and new expense marketing costs in the given quarter, but you haven't earned the revenue yet because that will play out over time as the money is invested. So you are going to see a bit of fluctuation in that, but we do think we're on target for our -- on track for our targets.

Scott Chan - *Canaccord Genuity Corp., Research Division - Director of Research of Financials & Financial Services Analyst*

Great. And while I have you, Steve, we're all seeing what's happening in the public markets, but the private markets or your old platform. Can you maybe describe any market headwinds that you're seeing or perhaps tailwinds in the current environment?

Stephen Clarkson Peacher - *Sun Life Financial Inc. - President of SLC Management*

I think it's a little bit too early to see what the long-term impact is on either the underlying portfolios and our different asset classes or on the fundraising. I would say the first quarter fundraising, we feel really good about. We haven't really seen examples of investors pulling back from these asset classes yet. If market volatility picks up, you could see that. We haven't seen it yet. I think the market environment actually can cut both ways. I mean, with rates going up and spreads going up, that could have an impact on asset classes like real estate, though I would say our real estate portfolios were up strongly during the first quarter.

But on the flip side, with raising with rising rates, we've actually seen money coming back into our fixed income portfolios as pension funds. This actually helps the funding ratio for pension funds. And in some cases, they're more willing to now put more money back into fixed income in higher yields. So a little too early to see what the longer-term impacts are, but I think it cuts a couple of different ways.

Operator

Our next question comes from Paul Holden of CIBC.

Paul David Holden - *CIBC Capital Markets, Research Division - Executive Director of Institutional Equity Research*

So going back to the U.S. Group and the conversation around the normalization of experience and perhaps mortality staying higher for longer. Is there anything in your mind that's changed your profit margin expectation, excluding the DentaQuest acquisition?

Daniel Richard Fishbein - *Sun Life Financial Inc. - President of Sun Life U.S.*

Paul, it's Dan Fishbein again. There really isn't. Now obviously, the fact that we may see somewhat elevated mortality, although certainly nowhere near what we've been seeing in over the past couple of years. In the short term, could affect margins. But as we reprice for that, and we should be able to reprice for that, that would put us back at the same margins. As I mentioned in the last call, overall, our Group Benefits business is in the best condition that it's ever been. Sales are strong. Persistency has improved. We're getting the pricing that we ask for, that we need.

We've had significant gains in expense efficiencies, introduced new products capabilities and digital programs into the marketplace. All of those things position us very well. And the previous margin guidance that we've given of 7% or greater is still very much our expectation absent COVID effects. But the fundamentals of the business remain strong and remain as they were.

Paul David Holden - *CIBC Capital Markets, Research Division - Executive Director of Institutional Equity Research*

Great. And then a capital allocation question for Kevin. You noted the capital strength of the business, which is obvious. We're seeing valuations drop. Is this leading to increased potential capital deployment options? And would you be willing to be opportunistic in this type of environment with capital deployment?

Kevin David Strain - *Sun Life Financial Inc. - President, CEO & Director*

Well, thanks, Paul. And as you know, and we've talked about in other quarters, our priorities for capital deployment remain largely the same, right? We're focused on supporting our organic growth. And you know our organic growth target for EPS is 8% to 10% and continue on that. We're committed to supporting our dividend and the dividend growth, and we've outlined 40% to 50% of underlying earnings, and you saw the 4.5% increase in our dividend this quarter. Of course, we've been able to deploy into M&A that improves either scale or adding new capabilities like the DentaQuest that's going to be closing soon, and that's going to use a big chunk of capital.

But we're always looking sort of forward at what the opportunities are across the 3 of those, and we always keep buybacks as an alternative, if we see that the level of capital is more than what we need, we give it back to shareholders. So at this point in time, it's a combination of economic conditions, uses we have for capital, and we continue to look at all of the uses.

Operator

Our next question comes from Doug Young of Desjardins Capital Markets.

Doug Young - *Desjardins Securities Inc., Research Division - Diversified Financials and Insurance Analyst*

I guess this question is for Jacques. I think group morbidity experience in Canada was adverse once again. And I think that's been a recurring theme for a while here. Just -- and I know that you're taking actions putting through price increases. I just wanted to get a better sense of what you're seeing on the ground. And what level of price increases are flowing through and when we might see that turn?

Jacques Goulet - *Sun Life Financial Inc. - President of Sun Life Canada*

Doug, thank you for the question. This is Jacques. You're right on the morbidity experience is unfavorable in the quarter, and it has to do with GB disability, as you say. I might just remind you that we've got 2 things we're looking at: one is the volume of cases, which we call the incidence; and then how long for the duration of cases before people get back to work. In May 2019, we decided to increase our pricing quite materially. And that was to do with the fact that when it comes to incidents, our view and our models were suggesting that the trend up was what I would call, durable trend.

And so we took action. And today, I can tell you, Doug, that the incidence is in line with our pricing and our expectations. So the issue is, indeed, as you point out, on the duration. Now unlike incidents on duration, we don't see this for now as a durable trend. It's taking -- part of this is COVID, access to care has been an issue with people getting surgeries and so on. So our view remains that this is temporary. Of course, if signals were to change and suggest that, that has a more durable pattern to it, we would take action. But at this stage, we think that's not the case.

Doug Young - *Desjardins Securities Inc., Research Division - Diversified Financials and Insurance Analyst*

Okay. And then just a question on the Asia business. There's a large India state rent insurance company in India going public and -- which is interesting and topical. I'm just curious what, if any, this has impact wise on your viewpoint in India or your India Life Insurance business?

Kevin David Strain - *Sun Life Financial Inc. - President, CEO & Director*

Yes, I can start, and then Ingrid's also -- it's Kevin. Ingrid's also on the call, so I can let her add some color. Yes, the LIC, we're well aware of is going public. The LIC is the largest provider of insurance in the country. It's an amalgamation in 1956 or 1957 of all the insurance companies. I think being a public company provides a level of discipline and transparency, which is probably long term good for the industry. We really like our partnership with the Aditya Birla Group. We have a strong position in both the insurance company and the asset management company.

I think that, that doesn't change from the LIC going public at all. They are already a big competitor. And so it's -- we're still optimistic about India, and we think there's great potential there. I don't know, if Ingrid, if you wanted to add anything?

Ingrid G. Johnson - *Sun Life Financial Inc. - President of Sun Life Asia*

No, other than you would have seen, we still had relatively strong sales in the quarter, and we're excited about the business and also the digitalization that's taking place. And we are well positioned both in Life and Asset Management.

Kevin David Strain - *Sun Life Financial Inc. - President, CEO & Director*

I would see that the valuations in India are quite high. And I would -- you would note that the PE multiples are high. And that shows you I think the long-term value creation opportunity in India.

Operator

Our next question comes from Mario Mendonca of TD Securities.

Mario Mendonca - *TD Securities Equity Research - MD & Research Analyst*

If we go back to policyholder expenses or the policyholder experience. I noticed that expense experience was positive this quarter. I kind of look back at the model to see the last time that was true. And I think I have to go back to Q3 2019. So can you talk a little bit about why it would have flipped signs this quarter? And then on a related note, the other expenses or the other experience was rather negative. I'm referring to the minus $41 million. Is that expense? I mean, should we be looking at those 2 together is what I'm getting at.

Manjit Singh - *Sun Life Financial Inc. - Executive VP & CFO*

Mario, it's Manjit. So on the first item, the sort of credit that you see in expenses this quarter is largely due to some compensation adjustments that happen as part of the year-end process. And so that's what -- there was a true-up for that. So that drove -- that was a recovery in the quarter. So that's what you saw. On the other expenses that you mentioned, we do have some investments that we make in businesses over time that are reflected in that line. And one of those investments, obviously, that's happening right now is IFRS 17 along with some smaller investments we're making in the BG Group. So that's what's in that line.

Mario Mendonca - *TD Securities Equity Research - MD & Research Analyst*

Manjit, I appreciate that you're doing your update IFRS update in -- sorry, later on this month. But given the market interest in this, is there anything you can offer in terms of what the transition could mean to the company's book value today?

Manjit Singh - *Sun Life Financial Inc. - Executive VP & CFO*

Again, I think, Mario, it's -- as you sort of say, there's a different component to that. So I don't think it would really be helpful to give you a short answer to that. I think we want to take the time to walk you through the various elements of that and how they come together on May 31.

Operator

Our next question comes from Tom MacKinnon of BMO Capital.

Tom MacKinnon - *BMO Capital Markets Equity Research - MD & Analyst*

Just with respect to an unexpected dividend increase, it kind of just shows there's some reasonably good capital generation here. I don't think we've heard anything about kind of excess capital generation since you gave us an $800 million annual figure several years ago. So is there anything you can share with us with respect to excess capital generation at Sun Life? And then I have a follow-up.

Manjit Singh - *Sun Life Financial Inc. - Executive VP & CFO*

Tom, it's Manjit. I'll take that. So as you know, we've maintained a strong capital position for many years, and that's really underpinned by our disciplined approach to capital management. And as you say, an important component of that disciplined approach is generating strong capital from our diversified portfolio of businesses. And as Kevin outlined, we do have a very clear and consistent approach to how we manage our capital. We first invest in organic growth for our businesses and that consumes about 25% to 35% of our overall capital generated from underlying net income. Next, we focus on growing our dividend.

And as we talked about, our payout range is 40% to 50% of underlying income. And so that leaves about 25% to 35% of underlying net income for excess capital generation to deploy before the impacts of market-related items. And if you were to take a look at that for the past year, that would have been about $1 billion before those market-related items. So a bit higher than the $800 million we saw earlier.

Tom MacKinnon - *BMO Capital Markets Equity Research - MD & Analyst*

Okay. That's great. And just with respect to some of the discussions with -- on group morbidity, is the thinking that we should be looking at here more -- just confirming that it might be more short-term related, is -- and more COVID related, should the focus be more on unemployment? There is sometimes any selection in group morbidity. So as long as we stay with relatively good employment levels, would you expect to group morbidity, just a modest uptick that we saw in the quarter to come back in as a result of unemployment being fairly muted here?

Kevin David Strain - *Sun Life Financial Inc. - President, CEO & Director*

Tom, I think we can let Dan answer that first for the U.S. and Jacques answer a second for Canada.

Daniel Richard Fishbein - *Sun Life Financial Inc. - President of Sun Life U.S.*

Sure. In the U.S., as you noted, unemployment is almost at a historically low level. In fact, there's 11.5 million open jobs in the U.S. right now. So we don't think unemployment is really a factor here. We think there are other second order effects. As I mentioned, including employers, requiring people to come back into the office who might not be fully comfortable doing that. That's likely a transient effect. The marketplace will find its equilibrium as labor and employers decide how they want to work together in the future. So we don't see that as necessarily a persistent impact.

Jacques Goulet - *Sun Life Financial Inc. - President of Sun Life Canada*

And Tom, this is Jacques. Similar to Dan, I would say, we don't see employment levels as being a material issue at the moment to what we're seeing. It's really about duration, as I said earlier. I didn't mention it earlier, but mental health cases tend to be a bit longer than other cases. So we -- with the access to care, it's really an issue of how quickly we can get people back to work. And at the moment, I would say, we don't expect that to be a durable trend, but we're obviously watching it very closely, Tom, since it has obviously an impact on our results.

Tom MacKinnon - *BMO Capital Markets Equity Research - MD & Analyst*

Okay. If I could just squeeze one more as an impairment in the quarter, if there's any kind of color you can shed with respect to that? And how we should be thinking about credit going forward.

Randolph Brill Brown - *SLC Management - CIO*

Tom, this is Randy Brown. I'll take that. Yes, the impairments were under a couple of credits within our private fixed income portfolio. They were entirely idiosyncratic in nature, and so not indicative of any trends, either within PFI specifically or in the overall portfolio. I think overall, you'll see another positive credit release this quarter, albeit down from prior quarters. I'm very comfortable with the composition of the portfolio. So we have to see how markets play out as we look forward.

Operator

Our next question comes from Lemar Persaud of Cormark.

Lemar Persaud - *Cormark Securities Inc., Research Division - Research Analyst*

My question is probably more suited for Manjit. It's around the -- I guess, the outlook for earnings and surplus and that kind of rough $100 million range. I understand it's a rough target and may bounce around from quarter-to-quarter, but just looking at that target in the context of what we've seen over the past 2 quarters, some of the challenges associated with generating AFS gains and seed investment gains and what's playing out in the market and rate environment. Does it feel like that $100 million target is achievable in this market backdrop? I guess the reason I've asked you is that you have to really go back like over a decade to find a 2-quarter string of earnings on surplus this week. Any comments would be helpful.

Manjit Singh - *Sun Life Financial Inc. - Executive VP & CFO*

Sure. Lemar, it's Manjit. So as you mentioned, our earnings and surplus has kind of been in the $100 million range. And this quarter, we saw $65 million. And there were a couple of items that led to that lower result. We had lower mark-to-market seed investment losses. And that really reflects the wider credit spreads you're seeing. There were some timing items in our investment income. We also had some higher debt costs reflecting the higher float rates on floating rate debt as well as the debt that we issued to fund DentaQuest and as you mentioned, a lower AFS gains.

So altogether, that's what drove that number. And given the current environment that we're in, and as I mentioned in my prepared remarks, you'd expect the AFS gains to be more muted, which would result in a surplus number below the $100 million range that we've been seeing previously. But the other thing that I mentioned, obviously, is also there's other components that also have different impacts on those market-related items. And we talked about it earlier in this call that, that could also provide some opportunities on the investment activity gain side.

Lemar Persaud - *Cormark Securities Inc., Research Division - Research Analyst*

Okay. And then if I could squeeze another one in. Maybe just circling back to an earlier question around capital allocation for Kevin. Does management have the capacity to integrate DentaQuest while still digesting another acquisition? Or would M&A kind of be off the table for a period of time?

Kevin David Strain - *Sun Life Financial Inc. - President, CEO & Director*

It's a great question. Thanks. If we look at DentaQuest, it is the second largest acquisition we've ever made. It's -- but it's got a great management team. Dan and his team have executed on a large acquisition. And you have to remember, it's really bringing a larger dental business into a smaller dental business alongside of ours. And so we're pretty confident that, that integration is going to go well. Manjit actually mentioned we've got the debt costs running through our earnings right now, but we don't have the benefit of the earnings coming through. So that's one thing that we're looking forward to.

But from the overall capital position, it's obviously going to use a big chunk of the $4.7 billion we have at the holdco. We obviously see that we're in stressed times right now. And if you look at the economic conditions, but we are -- we do have a solid capital position, and we continue to assess what the opportunities are. So it is a use of the majority of the capital at the holdco when the deal closes, but we continue to have an eye on things that will improve the business. But we're -- that financial discipline will not change. And I think part of the financial discipline is looking at the economic conditions and what you're purchasing.

Operator

Our next question comes from Nigel D'Souza of Veritas Investment Research.

Nigel R. D'Souza - *Veritas Investment Research Corporation - Investment Analyst*

I had a follow-up for you first on SLC. I believe you mentioned the $150 million in annualized fee revenue that could be generated from AUM not yet invested. Wondering if you had a period over which you expect to realize that? And what margin do you expect to earn on that revenue?

Stephen Clarkson Peacher - *Sun Life Financial Inc. - President of SLC Management*

Nigel, thanks for the question. When we raise money across our platform, the expected investment periods can vary. But I would say we'd expect to get that money invested over 12 to 24 months generally. In some funds, the investment period can be 3 years. So that can be the case. But I would say if it goes into the third year, in a given fund, you've invested most of the assets by that time. The type of funds that lead to these non-fee earning assets are generally higher fee asset classes. So it's real estate, it's alternative credit, it's infrastructure where you raise money in a fund and then you draw it down.

And as you draw it down and invest the money, you start earning the fees. As I said, those are higher fee assets. So not sure I'm prepared to give out a specific margin on that. But I would say that across our platform, those would be the higher fee assets that we manage. And therefore, there are some additional costs to go with those assets, but those would generally be our higher-margin assets as well.

Nigel R. D'Souza - *Veritas Investment Research Corporation - Investment Analyst*

Okay. So I think it's fair to assume it's probably above 20% based on what you disclosed on your fee-related earnings margin. And then the next question that I had was on your impact on investment activity. It's favorable experience this quarter. And I was wondering if you could provide some color. Is that mainly yield enhancement? And how sustainable do you think this quarter's run rate is given the yield environment that we're seeing today?

Randolph Brill Brown - *SLC Management - CIO*

Nigel, it's Randy Brown. I'll take that. Some of what you heard in prior quarters is that we had built some dry powder coming into this period with the expectation or the observation that credit spreads were near all-time adjusted lows. Real rates were at all-time lows, equities were at all-time highs. So we took some risk off the table and built dry powder. Some of that dry powder was deployed this quarter. Some of that drive -- this past quarter. Some of that dry powder will be deployed as we see opportunities in Q2 and forward.

And we are seeing opportunities with the dislocations in the market. And so that was a nice piece. So we had another piece as mentioned, was the strong PFI originations and spreads, and we are seeing that continue in Q2. It's a matter of deployment on the balance sheet in terms of how they flow, but we are seeing strong -- achieving strong spreads there as well.

Nigel R. D'Souza - *Veritas Investment Research Corporation - Investment Analyst*

That's helpful. And the last question I have for you, and apologies if you already answered it, on the IFRS 17 update later this month, did you mention that you'd be providing an update on the expected impact to underlying earnings? Or is that still further out?

Manjit Singh - *Sun Life Financial Inc. - Executive VP & CFO*

Yes. I think we're going to cover a range of topics, including our outlook for our medium-term objectives.

Operator

Thank you. We have no further questions at this time. I will turn things over to Mr. Bitton for closing remarks.

Yaniv Bitton - *Sun Life Financial Inc. - VP, Head of IR & Capital Markets*

I would like to thank all of our participants today. Should you wish to listen to the rebroadcast, it will be available on our website later this afternoon. Thank you, and have a good day.

Operator

This concludes today's call. Thank you for your participation. You may now disconnect.
