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Sun Life Financial, Inc. (SLF)

Q2 2017 Earnings Call

CORPORATE PARTICIPANTS

Gregory A. Dilworth
Vice President-Investor Relations, Sun Life Financial, Inc.

Dean A. Connor
President, CEO & Non-Independent Director, Sun Life Financial, Inc.

Kevin D. Strain
Executive Vice President and Chief Financial Officer, Sun Life Financial, Inc.

Daniel Richard Fishbein
President-US Business, Sun Life Financial, Inc.

Michael William Roberge
CEO, President and Chief Investment Officer, MFS Investment Management

Claude A. Accum
President, Sun Life Financial Asia

Kevin P. Dougherty
President-Sun Life Financial Canada, Sun Life Financial, Inc.

OTHER PARTICIPANTS

Gabriel Dechaine
Analyst, National Bank Financial, Inc.

Meny Grauman
Analyst, Cormark Securities, Inc.

Steve Theriault
Analyst, Eight Capital

Humphrey Hung Fai Lee
Analyst, Dowling & Partners Securities LLC

Sumit Malhotra
Analyst, Scotia Capital, Inc.

Doug Young
Analyst, Desjardins Securities, Inc.

Nick Stogdill
Analyst, Credit Suisse Securities (Canada), Inc

Tom MacKinnon
Analyst, BMO Capital Markets (Canada)

Paul Holden
Analyst, CIBC World Markets, Inc.

MANAGEMENT DISCUSSION SECTION

Operator: Good morning. My name is Christa and I'll be your conference operator today. At this time I'd like welcome everyone to the Sun Life Financial Q2 2017 Financial Results Conference Call. All lines have been placed on mute to prevent any background noise. After the speakers' remarks, there will be a question-and-answer session. [Operator Instructions]

Thank you. Mr. Greg Dilworth, Vice President of Investor Relations. You may begin your conference sir.

Gregory A. Dilworth
Vice President-Investor Relations, Sun Life Financial, Inc.

Thank you, Christa, and good morning, everyone. Welcome to Sun Life Financials' earnings conference call for the second quarter of 2017. 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 presentation with an overview of our second quarter results by Dean Connor, President and Chief Executive Officer of Sun Life Financial. Following Dean's remarks, Kevin Strain, Executive Vice President and Chief Financial Officer will present the second quarter financial results. After the prepared remarks, we will move to the question-and-answer portion of the call. Other members of management will also be available to answer your questions today.

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 this morning's remarks. As noted in the slide, forward-looking statements may be rendered inaccurate by subsequent events.

And with that, I'll now turn things over to Dean.

Dean A. Connor
President, CEO & Non-Independent Director, Sun Life Financial, Inc.

Thanks, Greg and good morning everyone. Turning to Slide 4, the company reported underlying net income of $689 million or $1.12 a share, up 24% from the same period last year, with an underlying return on equity of 13.7%. For the first six months of 2017, underlying earnings are up 11% to $1.3 billion and we generated an underlying ROE of 12.6% within our target range of 12% to 14%. These results reflect strong underlying business growth and continued execution across our four pillars.

Today we announced a share repurchase program of up to 11.5 million of our common shares. This program is indicative of the strength of our capital position and supports our focus on ROE improvement while retaining flexibility for future growth opportunities. We continue to grow at a good clip with Insurance and Wealth Sales up by 5% and 12% respectively over the second quarter of last year. Over the first six months Insurance sales grew by 30% and Wealth Sales were up 13%. Assets under management ended the quarter at $944 billion, up 9% from a year ago.

Sun Life Canada had a very strong quarter with underlying earnings up 33% over the prior year from good Group Benefits claims experience improving margins in GRS for management actions, strong defined benefit solutions sales and pricing gains, and growth and expected profit emerging from strong sales growth over the past number of years.

For the eighth year in a row our Group Benefits business ranked number one in premium revenue in the Fraser Group Universe Report. One reason we're number one, is our technology advantage. For example, last fall we added a provider search capability to our mobile app so that Sun Life members can search for physiotherapists and other health professionals near them, they can see ratings provided by other Sun Life members, they can book an appointment and so on. During the second quarter, we reached 1 million ratings, which is quite remarkable given that we just launched it last fall.

In group retirement services, sales increased by more than 50% partly due to the strength of Defined Benefit Solutions sales. DBS had a big quarter that included the largest ever single-day annuity purchase in the Canadian market at CAD 495 million. Assets under management and administration at GRS are now over CAD 93 billion.

In individual insurance, sales of our updated product suite were CAD 100 million for the quarter, flat to prior year following a very strong Q1 sales result due in part to the recent tax changes for life insurance products. Individual wealth had a strong quarter with sales up 17% across fixed products, mutual funds and segregated funds.

In Sun Life asset management, we ended the quarter with CAD 655 billion in assets under management. MFS had a good quarter with net income up 26% over prior year, assets under management up 9% year-over-year to U.S. $462 billion and pre-tax operating margin at 36%. Year-to-date, MFS net income is up 19% over prior year on market growth at consistency strong margin.

Gross sales were U.S. $20 billion and net outflows of U.S. $4 billion improved significantly from the prior two quarters as retail flow moved back to positive on lower redemption rates and we saw lower levels of institutional rebalancing. MFS continues to generate strong investment returns for clients with 82%, 84% and 92% of MFS U.S. retail mutual fund asset ranked the top half of the Lipper categories based on 3-year, 5-year and 10-year performance, respectively.

At Sun Life Investment Management, investment performance continued to be strong across all the businesses. Net sales in the quarter were CAD 872 million and net sales of CAD 3 billion in the first six months of 2017 have more than tripled over the prior year. Assets under management of CAD 56 billion are up 16% over the same period last year.

Turning next to the U.S., underlying net income was up 25% over prior year, in part reflecting improved stop-loss claims experience, and the results of our pricing increases coming through in life and disability. We achieved a significant milestone in the integration of last year's U.S. group business acquisition, rolling out a combined portfolio of employee benefit products and services that represents the best offerings from both companies under the Sun Life brand.

We're tracking well on all the integration metrics disclosed at the time we announced the acquisition. Group sales were up 2% from the second quarter of last year, while sales in our international business were largely consistent with the prior year. Moving to Asia, sales of individual insurance products were up 2% driven by growth in India and Indonesia, that was partially offset by lower sales in the Philippines and Hong Kong.

In Malaysia, we announced the telco insurance partnership with U Mobile, one of the country's fastest growing telecom companies with our 5 million customers. This will be first time that Malaysians will be offered insurance via a telco service, allowing them to apply and manage their life insurance coverage entirely on their mobile devices. This is just one of many examples across Asia and the company where we're innovating and using digital capability to do more for clients.

Second quarter Wealth Sales in Asia increased by over 65% over the prior year to CAD 2.9 billion driven by strong mutual fund sales in India and growth in pension sales in Hong Kong. Year-to-date, Asia wealth sales have grown 74% to $5.9 billion and this is an important driver of our Asian growth.

So to wrap up, we delivered a strong quarter and taking stock after six months, we're having a good year. Underlying earnings are up 11% to $1.3 billion, Insurance and Wealth Sales are up 30% and 13% over the prior year respectively and underlying ROE is up to 12.6% with a very strong balance sheet and excess capital. I'm happy to see all four pillars contributing to these results, while investing and innovating for the future.

Our businesses are pulling together to achieve our ambition of being one of the best insurance and asset management companies globally by doing an amazing job for our clients. We're making measurable progress on being easier to do business with, on being more proactive and personal and by solving client problems faster. We've just combined our Toronto operations together at our new One York location in a collaborative and energetic space, strengthening our commitment to delivering on our purpose, which is helping our clients achieve lifetime financial security and live healthier lives.

So I'll now turn the call over to Kevin Strain, who will take us through the financials.

Kevin D. Strain
Executive Vice President and Chief Financial Officer, Sun Life Financial, Inc.

Thank you, Dean, and good morning, everyone. Turning to Slide 6, we take a look at some of the financial results from the second quarter of 2017. Our reported net income for the quarter was $574 million, up from $480 million in the second quarter of last year. Underlying net income which excludes the net impact of market factors and assumption changes was $689 million. Our underlying return on equity was 13.7% for the quarter. Underlying results reflects strong business growth, gains from investing activities on insurance contract liabilities and favorable credit and morbidity experience. Second quarter adjusted premiums and deposits were CAD 41 billion, up 5% from the second quarter of 2016, and assets under management at the end of the quarter were CAD 944 billion.

We ended the quarter with a minimum continuing capital and surplus requirement ratio for Sun Life Assurance Company of Canada up 229%. The MCCSR ratio for Sun Life Financial Inc was also strong at 248%. The higher ratio at the SLF level largely reflects the excess cash of CAD 1.4 billion held by SLF, Inc. And our leverage ratio of 22.5% remains below our long-term target, and as Dean noted earlier, we announced a share of repurchase program of up to 11.5 million shares, which is reflective of our strong capital and cash position. And we continue to have cash and capital available to support our growth strategies.

We're continuing to progress towards the implementation of the new Life Insurance Capital Adequacy Testing, LICAT capital regime, that will be effective on January 1, 2018. Sun Life has been actively involved with OSFI and the industry in discussing and helping to shape the recent changes in the LICAT guideline and we are well prepared to implement LICAT.

Turning to Slide 7, we provide details of the underlying earnings by a business group for the quarter. In SLF Canada underlying earnings were up CAD 266 million reflects strong new business gains, business growth and margin expansion in GRS and favorable morbidity experience in group benefits, driven by better LTD incidence rates.

At the same time we continue to make significant investments in Canada, including investments in digital and data analytics to support our client focus strategy and investments in our individual wealth business.

In SLF U.S. underlying earnings were up 25% from the second quarter of 2016 on strong gains from investing activity and favorable credit and mortality experience in in-force management and in international. Morbidity experience in group benefits improved from the prior year, although it still was below our expectations we are working through – our way through the stop-loss claims related to the 2016 benefit year.

In SLF Asset Management, MFS had strong underlying earnings growth over the second quarter of 2016, driven by higher average net assets. The pre-tax operating profit margin was 36% and net outflows were U.S. CAD 4 billion for the quarter. At Sun Life Investment Management we had net inflows of CAD 0.9 billion and generated net income of CAD 6 million.

In Asia, underlying earnings were lower by CAD 4 million over a very strong Q2 2016 as business growth and gains realized on the sale of AFS assets were offset by higher new business strain.

Turning to Slide 8, we provide details on our sources of earnings presentation. Expected profit of CAD 718 million increased by CAD 74 million from the same period last year, with increases across all four pillars. Excluding the impact of currency and the result of SLF Asset Management expected profit was up 8%, reflecting strong business growth in Canada, the U.S. and in Asia. New business strain was CAD 7 million for the quarter.

Lower levels of new business strain were driven primarily by pricing gains in SLF Canada from higher sales, including strong defined benefits solution sales in the quarter. This was partially offset by a lower pricing gains in international life in these SLF U.S. and lower sales in Hong Kong.

Experienced losses of $80 million for the quarter, primarily reflect the net unfavorable market impacts from changes in interest rates and the shape of the yield curve. Lapse, policyholder behavior and expenses also had an unfavorable impact. We had favorable investing activity during the quarter and strong credit, mortality and morbidity experience.

Assumption changes and management actions reduced pre-tax reported income by CAD 114 million in the quarter and were largely reflected in our in-force management and international businesses in SLF U.S. The net impacts were primarily related to certain reinsurance treaties and expected pricing gain on recapture of these treaties and the impact on actuarial liabilities from the resolution of tax matters in one of our U.S. subsidiaries. On an after-tax basis, assumption changes and management actions overall increased reported net income by CAD 11 million.

Looking ahead, we will complete our annual review of actuarial methods and assumption changes in the second half of 2017, with the majority of the changes being reflected in the third quarter. We note that our review requires that we assess assumptions across a large number of products, businesses and geographies and it's not possible to determine the overall impact of these reviews on a net income at this time. We can't tell you that the Actuarial Standards Board has provided an update on the promulgated Ultimate Reinvestment Rate, the URR, indicating an expected decrease of 10 basis points. And as previously discussed, this is expected to have a negative CAD 75 million impact on our earnings through ACMA in Q3.

Other, which amounted to CAD 83 million in our source of earnings disclosure includes pre-tax acquisitions, integration restructuring cost, the impact of hedges in SLF Canada that do not qualify for hedge accounting and fair value adjustments on MFS share-based awards. Earnings on surplus of CAD 134 million were CAD 16 million higher than the second quarter last year, reflecting higher levels on investment income and mark-to-market gains on real estate on recent appraisals. Our effective tax rate on reported net income basis was negative 3.7%, the unusually low rate this quarter primarily reflects assumption changes in management actions, which we saw favorable impacts in low tax jurisdictions and losses in higher tax jurisdictions. On an underlying basis, which adjusts for these impacts, our effective tax rate was 18.9%, which is in line with our stated range of 18% to 22%.

Slide 9 shows sales results from our Insurance and Wealth businesses. Total insurance sales were up 5%. On a constant-currency basis, sales were up 3% reflecting strong sales growth primarily in our Group benefit division in Canada. Total wealth sales of CAD 37 billion were up 12% over the prior year, on a constant-currency basis, wealth sales were higher by 8%. Wealth sales showed growth across a number of business primarily led by higher sales in SLF Canada, Sun Life Investment Management, rapid growth in our India Asset Management business and a growth in our Hong Kong pensions business.

So to conclude, we had a strong quarter and are seeing a good momentum in our business. Our earnings for the six months of 2017 reflects strong execution on our medium-term financial objectives. Our capital position remains a key area of strength as we head towards the implementation of LICAT as evidenced by our strong solvency ratios, excess cash position and the announcement of our share repurchase program today.

With that, I'll turn the call over to Greg to begin the Q&A portion of the call.

Gregory A. Dilworth

Vice President-Investor Relations, Sun Life Financial, Inc.

Thank you, Kevin. To ensure that all of our participants have an opportunity to ask questions on today's call, I would ask each of you to please limit yourselves to one or two questions and then to re-queue with any additional questions.

With that, I'll now ask Christa to please poll the participants for questions.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Your first question comes from the line of Gabriel Dechaine with National Bank Financial. Your line is now open.

Gabriel Dechaine
Analyst, National Bank Financial, Inc.

Q

Good morning. My first question is on the NCIB, Dean in the past when you talked about your capital management priorities, I believe it's something along the lines of funding organic growth and M&A and the dividend and then buybacks all the way at the bottom, so to me it seemed like you downplayed it in the past, I'm just wondering is there an increased appetite for following through on the buyback program at this time?

Dean A. Connor
President, CEO & Non-Independent Director, Sun Life Financial, Inc.

A

Thanks, Gabriel and your recollection is correct and we have said before that buybacks continued to be a part of our thinking around capital management. I think what you take from the announcement of the NCIB is that we are confident in our capital position both under MCCSR and under LICAT, as we continue to do work on LICAT we maintain that confidence in our capital position.

We got a business model that supports both the strong dividend payout ratio as you know 40% to 50% of earnings and generation of excess capital and so we're always trying to strike the right balance between putting capital to work behind organic growth that is job one as you're said leaving us the capacity for acquisitions that meet our hurdle rates and strategic fit requirements and as you know we deployed $2.5 billion in acquisitions over the past four years and continue to be in the flow for new opportunities and returning capital to shareholders.

So you should think of this NCIB as, we've done it before, we've said that it's part of our toolkit and you see us acting on that at this time.

Gabriel Dechaine
Analyst, National Bank Financial, Inc.

Q

All right. And my next question is about Group Insurance business in the U.S., and it looks like while we finally had a quarter where I guess you're lapping some of the tougher periods from a morbidities standpoint in last year and – past few quarters anyway, and the claims experience is improving from the sounds of it. Can you give me a quantification of what the negative experience has been in that business line in Q1, Q2 or let's say over the past few quarters? And how you see that progressing over the next few, is this going to be a material driver of growth in that business as your repricing takes hold?

Daniel Richard Fishbein
President-US Business, Sun Life Financial, Inc.

A

Yeah. Good morning. This is Dan, excuse me – qualitatively, we're definitely seeing improvement. During this particular quarter we saw improvement especially in our group disability and life businesses, which was certainly gratifying to see. We continue to have negative experience in the stop-loss business, but we would expect to see that beginning to improve in the second half of the year. The rate increases that we put through over the past 12 months would start to emerge in that period.

Gabriel Dechaine
Analyst, National Bank Financial, Inc.

Q

So, you can quantify that? I figured what it was in Q1 and then Q2, the stop-loss has been an issue for past few quarters anyway.

Daniel Richard Fishbein
President-US Business, Sun Life Financial, Inc.

A

I think if you look overall at the morbidity experienced for the quarter, right, it was positive '18, which reflected part coming through Canada and part coming through that the U.S., which was a significant improvement over Q2 2016; which was a low point for the stop-loss business. We haven't given guidance overall on morbidity. I would say that, it does have some vagaries in terms of what the claims experiences in the quarter, but what you're seeing is re-pricing in the U.S. and management actions in both the U.S. and in Canada that are coming out in the positive, but I would put this on the stronger side of what we would normally see.

Dean A. Connor
President, CEO & Non-Independent Director, Sun Life Financial, Inc.

A

And Gabriel, it's Dean. I would also take you back to the – and Dan has talked previously about the – expected the migration of the profit ratio – profits net income as a ratio of premium and we expressed a target for that and a big part of the improvement of that is the improvement in morbidity experience as well as the realization of all the expense gains that we're realizing through the integration work we're doing.

Gabriel Dechaine
Analyst, National Bank Financial, Inc.

Q

Okay. Thanks. And I'll take a look and make my own number.

Operator: And your next question comes from the line of Meny Grauman with Cormark Securities. Your line is now open.

Meny Grauman
Analyst, Cormark Securities, Inc.

Q

Hi. Good morning. You have been very clear about the industry-wide issues being faced by MFS. I am wondering in that context, how you view the positive retail flows, how do you interpret what we saw in Q2?

Michael William Roberge
CEO, President and Chief Investment Officer, MFS Investment Management

A

Yeah. Good morning. This is Mike. Yeah, I think, we talked about in the last quarter as we saw flows that were – net flows that were relatively weak and we spoke to much of the issue being the redemption rate which we saw really spike in Q4 and Q1, both for us. Some of it being our institutional business in the closed book that we have for many of our strategies. In addition, we just saw a big spike in the redemption rate and retail.

What really help net flows in Q2 was a decline in the redemption rate. So as per expectations, we saw redemption rates come down and we continue to see more normal levels of redemption rates and that obviously will help us in our retail business.

We will continue to be somewhat challenged in our managed business, because a fair amount of the book continues to be closed and while we've seen some outflow there and the obviously question is, does that create net new capacity to go sell? Market liquidity has come down pretty dramatically. Trading volumes in the market, which means it's harder to actually sell positions into the marketplace. So, as our assets are coming down, liquidity is coming down, that doesn't create net new capacity for strategies that we've historically closed.

The most important thing that we can do is managed performance on behalf of clients. And so, by ensuring that the asset pools are appropriate, so, we can continue to trade the pools and put up good long-term performance for clients is going to maximize the long-term value of the firm and we continue to be focused on that.

Meny Grauman
Analyst, Cormark Securities, Inc.

Q

And just to follow-up on the institutional side. Is there anything notable in terms of redemptions this past quarter in terms of particularly large, single client moves or sovereign wealth fund activity?

Michael William Roberge
CEO, President and Chief Investment Officer, MFS Investment Management

A

No. I mean, if you look at it again by – as we look at reason for termination, very little of it its performance and you can see that, given the relative performance and it is client's de-risking, client's doing asset allocation changes. Changes with staff at some of the clients and pivot to new strategies within those clients. And so, its' a variety of things that are not related to MFS, but very much what's going on with the particular client.

Meny Grauman
Analyst, Cormark Securities, Inc.

Q

Thank you.

Operator: Your next question comes from the line of Steve Theriault with Eight Capital. Your line is now open.

Steve Theriault
Analyst, Eight Capital

Q

Thanks very much. Mike, while we have you – I know, you gave the long duration metrics but just quickly can you remind us or tell us what percent of AUM is above the Lipper average on a one-year basis?

Michael William Roberge
CEO, President and Chief Investment Officer, MFS Investment Management

A

Let me pull that out. On a one-year basis, I believe it's 21% on a one-year basis. And so, when you look at it, I mean, clearly, optically when you look at it, the one year sticks out from a relative performance perspective. What I would say is we don't spend a whole lot of time evaluating one year performance, because we think about – we built long-term discipline, we think about and actually we evaluate our managers and analysts over three years, five years, and 10 years.

And so, we stay very focused on that long-term performance. What I would say, in the one year number, two of our very large strategies, international value, and large cap value – U.S. large cap value represent about 35% of assets have underperformed on a one-year basis.

And given that, what has happened over the last year post Brexit, which is in the one year number, as well as the Trump rally that we saw in Q4, the S&P at the end of June is up 18%, Russell 1000 growth 20%, the EPA up

20%, a big concentration in FANG stocks, and other narrow parts of the market. So, the one year environment has been a little bit tougher.

What I would say of those two strategies, those two large strategies that I mentioned is they significantly outperform over three years, five years, and 10 years. And so, irrespective of what has been a tougher one year number, the long-term numbers continue to be strong and we are not at risk in the very near-term of rolling out of a tough three – of a strong three and five year number.

So, the focus is on long-term performance. We think it's the right thing for our clients. We believe it allows us to consistently put up long-term performance and that's how we are evaluating the mangers.

Steve Theriault
Analyst, Eight Capital

Q

Okay. Thanks for all that color. I was going to ask if you – if it was some of that was a narrow breadth, but you addressed that well. Thanks a lot.

Michael William Roberge
CEO, President and Chief Investment Officer, MFS Investment Management

A

Okay.

Operator: And your next question comes from the line of Humphrey Lee with Dowling & Partners. Your line is now open.

Humphrey Hung Fai Lee
Analyst, Dowling & Partners Securities LLC

Q

Good morning. And thank you for taking my questions. Just a follow up on MFS a little further. So, the institutional flow is definitely seeing some improvement in the quarter. I was just wondering how much of that was benefit from the reopening some of the previously closed [ph] strategies (28:08) versus a slowdown in the rebalancing activities by the clients?

Michael William Roberge
CEO, President and Chief Investment Officer, MFS Investment Management

A

Yeah. We – it did help some and so depending on the strategy, there are various levels of restrictions that we will put on strategies depending on whether they're institutional or primarily retail strategies, whether they're separate accounts relative to commingled vehicles. And so, I think, what we've seen is, by loosening some of the restrictions on strategies that had some benefit to the overall net number quarter-on-quarter. But we don't believe as we look forward, it's going to have a dramatic impact on the net flows of the organization.

Humphrey Hung Fai Lee
Analyst, Dowling & Partners Securities LLC

Q

But would you say that the impact for this quarter is more because of the slowdown in rebalancing activities by your institution clients, more than that of reopening the strategy?

Michael William Roberge
CEO, President and Chief Investment Officer, MFS Investment Management

A

I mean, if you look it on – if you look at across channel, I mean, that contributed modestly. When you look at across channel what happen quarter-on-quarter as I mentioned is that redemption rate across our business came down pretty dramatically. That is not just related to restricted strategies. And so, the restricted strategies had a modest contribution relative. It really was redemption rates, which normalized for us in the industry in the second quarter.

Humphrey Hung Fai Lee
Analyst, Dowling & Partners Securities LLC

Q

Okay. Got it. And then just follow-up on the more recently launched products, those fixed income and the hybrid – the blended research products that now currently have three to five year track record. Where do those strategies rank in terms of the Lipper rating?

Michael William Roberge
CEO, President and Chief Investment Officer, MFS Investment Management

A

I don't have that. I mean fixed income products, you can see the performance of fixed income continues to be very strong with almost 90% of our 10 years or 86% of 10 years and high 70s to 80s overall period. So the relative performance in fixed income continues to be strong and our Blended Products relative to benchmark have good long-term numbers as well.

Humphrey Hung Fai Lee
Analyst, Dowling & Partners Securities LLC

Q

Okay, got it. Thank you.

Operator: Your next question comes from the line of Sumit Malhotra with Scotia Capital. Your line is now open.

Sumit Malhotra
Analyst, Scotia Capital, Inc.

Q

Thanks, good morning. My question is for Claude in the Asia business. It's been a long time since we've seen underlying earnings in this business post to decline. And a couple of metrics stand out to me, your individual insurance sales certainly seem to be decelerating after the strong growth you've had. I know the Hong Kong issues with or the issues with Mainland China are affecting a large portion of that. But I wanted to take your view on the growth outlook for individual insurance and specifically how that's leading into the expected profit line in this business?

Claude A. Accum
President, Sun Life Financial Asia

A

Thanks Sumit, Claude here. So if you look at the underlying earnings, you're right to call out that it's down from 85% a year ago down to 81%. Last year was actually the highest we had seen in quite some time. And so I looked to expected profit to try and pick out the trend. Expected profit last year was $82 million is $86 million this year, so it's up 5%.

If you break out the components of that, the business growth across the region was actually quite strong, a lot of pension growth in the Hong Kong business and so the business growth was stronger than plus 5%. And then we saw some of the expected profit was offset by higher investment expenses in the regional office as we build out our digital expenditure.

And then if we look at some of the components pieces, and some of the businesses had a particularly strong expected profit a year ago, China in short-term products, there has been some regulatory changes, and so they've rotated away from those products to other opportunities. And so some of those earnings have gone down, but we expect them to replace that.

If we look at insurance sales which you also mentioned, they are flat year-over-year, a 2% growth. If you back out currency, it's closer to flat. But the businesses are quite resilient, they're in seven countries, multiple channels, and if you look at Wealth Sales, Wealth Sales are up 66% over the years. So, you need some mechanism to blend them to try and detect or observe the growth and the best way we have to blend it, is to look at VNB. And if you look VNB growth for Asia, we see it's up 13% in Q2 this year over Q2 last year, and year-to-date is actually up 17%.

And so we're still observing some significant growth – good growth, in Asia, as centered around 15% or higher. And we are seeing some of that, when you look at the business earnings is dropping into expected profit.

Sumit Malhotra
Analyst, Scotia Capital, Inc.

Q

I hear you on the wealth trends, which you're right, continue to be very good. But to the extent this Hong Kong issue is something you're going to have to deal within the interim, is it enough going on in the rest of the insurance business in your Asia components that life insurance sales are going to be able to stay in a positive trajectory or you're in a period of consolidation here in the foreseeable future?

Claude A. Accum
President, Sun Life Financial Asia

A

I think, the Hong Kong, Mainland China Visitors business – those sales will be down. We have an opportunity to offset the – probably half of it in Hong Kong alone. They have a good opportunity to boost agency sales in Hong Kong. They have the opportunity to get stronger wealth sales, which I called out and they have the opportunity to introduce new products, high-end medical and obtain high net worth individual from other countries other than Mainland Chinese visitors.

So we think, Hong Kong will find ways to offset a good part of it. We're seeing particular strength in some of the other businesses. India is very strong on Life Sales, Indonesia showing a tremendous growth and even Vietnam is showing growth. And so, we're seeing this is an opportunity for the other countries to pick it up and see good insurance sales in Asia.

Sumit Malhotra
Analyst, Scotia Capital, Inc.

Q

Thanks for that. I'm going to close with one from Mike. Mike, if I go back to your presentation at the Investor Day in March, one topic, I don't think we spoke too much about was the potential impact on margins of MiFID II. I know certainly on our side of the street, we've been focusing a lot more on – how that's going to potentially affect business. When it comes to margins of MFS this quarter, pretty good result, 36% and in line with where you've been. Do you feel that some of the effects of MiFID II intended or unintended are going to have a meaningfully detrimental impact to margins at MFS or are there offsets that the business has in place?

Michael William Roberge
CEO, President and Chief Investment Officer, MFS Investment Management

A

Yeah, good question. I would say as MiFID II comes into effect on January 1 and the industry is still trying to grab hold with exactly what needs to be done and how we're actually going to comply with the regulation. And frankly, given the various differences in regulations around the world trying to get some harmonization across geographies, so that we can ensure, that we are in compliance in multiple geographies.

So, a little unclear, as we sit here today. What I would say is when you say material I don't think it will be materially detrimental to the industry. But it's not clear, exactly, what – how the research costs will actually get paid. The mechanism today is that we do it through a commission sharing agreement, it's – one of the regulators in Europe are going to make us specifically set it clients, set aside money and accounts where it will be very transparent what we're paying for research.

So, I think, the challenge of the industry longer term is whether we move away from soft dollars, and the industry has to actually take these costs on their income statement over time. Again, not clear at the moment, the regulators are going to have to provide a lot of clarity. But I don't think, at the end it will be material to margins, but it will have some detrimental impact on margins.

Sumit Malhotra
Analyst, Scotia Capital, Inc.

Q

Thanks, for your time.

Operator: And your next question comes from the line of Dough Young with Desjardins & Capital Markets. Your line is now open.

Doug Young
Analyst, Desjardins Securities, Inc.

Q

Hi, good morning. I guess, the – my question is for Dan. Just going back to the U.S. Group business. And I know, that you've had some rollover of claims from 2016, as weight on the first half results. How much is left to come through from a claims perspective and this is, I guess, to be clear on the stop-loss business, how much is left to come through on that 2016 business? Or is that all done now?

Daniel Richard Fishbein
President-US Business, Sun Life Financial, Inc.

A

Good morning, Doug. In the first half of the year, as we said before, most of the claims that we see in specifically the stop-loss business, which is what you're referring to, are from the prior year, just to give you a couple of stats on that. In Q2, about 64% of the claims that we saw were still from 2016, that drops to about 40%, is our expectation in Q3, and then it drops further from there in Q4.

So starting in Q3, most of the experience that we would be seeing would come from 2017 policies and we have significantly re-priced the block over the past year, our rate increases year-to-date are averaging over 17%. So as the effect of the current year starts to phase in the third and four quarters, we should see some significant impact from that.

Doug Young
Analyst, Desjardins Securities, Inc.

Q

And how much of the block has been reprised? I think it was 80% at the end of Q1, or we closer to 100% now that has been reprised?

Daniel Richard Fishbein
President-US Business, Sun Life Financial, Inc.

A

Yeah. We began that process last September 1st. So at this point, we're virtually done with that process because the entire block of business or virtually entire block is one-year contracts.

Doug Young
Analyst, Desjardins Securities, Inc.

Q

Okay. And then I guess – and Dean's remarks mentioned that this is the first quarter where you brought together the Sun Life and the Assurant business in one common platform. And I guess, this is for Dan or for Dean, but I just noticed that the employee benefits sales did decline 2% to 3% year-over-year. Just wondering if there's anything to read into that, was there – was most of the focus as a result of merging the organizations and less on sales, how worried should I be about that?

Daniel Richard Fishbein
President-US Business, Sun Life Financial, Inc.

A

Yeah. And what we're referring to in saying we're bringing the platforms together is really forward-looking. So, that began at the end of June and was not really in place for all of Q2. But the way I would look at Q2 that's actually one of the smallest sales quarters of the year only about 15% of our sales happened in the second quarter, 75% of sales happened in the third quarter and fourth quarter. But if you looked at year-to-date, which is combined Q1 and Q2, we're actually up 12% in employee benefits year-over-year. So, I don't really get a read into that single quarter results.

I would comment, we are seeing some pressure on our dental sales specifically and that seems to be an industry wide phenomenon at this point. There was a lot of focus during the first half of the year amongst employee benefits decision makers on what might happen to their health plans with changes potentially occurring to the Affordable Care Act, and that seems to put a little pressure on just leaving dental business where it was. Although, with those efforts failing in Congress to change the Affordable Care Act, we don't expect to see that trend continue in the second half of the year.

Doug Young
Analyst, Desjardins Securities, Inc.

Q

Okay, great. Thank you very much.

Operator: Your next question comes from the line of Nick Stogdill with Credit Suisse. Your line is now open.

Nick Stogdill
Analyst, Credit Suisse Securities (Canada), Inc

Q

Hi, good morning. My question is on the new business gains in Canada. Maybe could you – I know there was two things going on in this quarter. Obviously, the big sale in GRS and then obviously some actions taken in Individual. Could you maybe try and separate how much was coming from the GRS sales versus the changes in Individual, I'm just trying to get a better sense of maybe the sustainability of the pickup in the gains this quarter?

Kevin P. Dougherty
President-Sun Life Financial Canada, Sun Life Financial, Inc.

A

Yeah. So, it's Kevin Dougherty speaking, thanks Nick. It was a very good quarter in terms of new business gains, and what you are seeing, really both of those items mainly, the DB solutions sales as well as the retail insurance sales. And as we really – we took the opportunity to re-launch the entire retail life insurance product line, with the tax changes. I think if you, I think I should come back to you with that number, I'm not sure if you have it, Kevin?

Kevin D. Strain
Executive Vice President and Chief Financial Officer, Sun Life Financial, Inc.

A

I can talk about the total company level, Nick, if you look at the total company. We're still expecting new business strains in the neighborhood of CAD 10 million to CAD 20 million. So, we were a little under that this quarter on the positive gains for DBS which was the majority of the additional piece this quarter, the mix in Individual was a little bit smaller than the DBS overall. And then we had a negative in Hong Kong of about CAD 10 million on the lower sales and a little bit of a negative in our International business, that came through as well in the quarter. But, if you think about it, on a quarterly basis on a run rate our expectation remains around the CAD 10 million to CAD 20 million, up straight.

Nick Stogdill
Analyst, Credit Suisse Securities (Canada), Inc

Q

Okay. Thank you. Right, thank you.

Kevin P. Dougherty
President-Sun Life Financial Canada, Sun Life Financial, Inc.

A

Nick and John, actually I have the number here on...

Nick Stogdill
Analyst, Credit Suisse Securities (Canada), Inc

Q

Oh, you do, okay.

Kevin P. Dougherty
President-Sun Life Financial Canada, Sun Life Financial, Inc.

A

Yeah, for the GRS the uptick was about CAD 11 million from – related to that increase in sales.

Nick Stogdill
Analyst, Credit Suisse Securities (Canada), Inc

Q

Okay. So, CAD 11 million of the CAD 25 million year-over-year was the...

Kevin P. Dougherty
President-Sun Life Financial Canada, Sun Life Financial, Inc.

A

Yes, after tax, yes.

Nick Stogdill
Analyst, Credit Suisse Securities (Canada), Inc

Q

And the rest would be sort of the Individual and maybe other things going on?

Kevin P. Dougherty
President-Sun Life Financial Canada, Sun Life Financial, Inc.

A

Exactly.

Nick Stogdill
Analyst, Credit Suisse Securities (Canada), Inc

Q

Great. And then just a second question for Mike on MFS. Just going back to the Lipper rankings. Its – on the 10 year ranking it's been fairly steady in the high 90s for the past three years or four years and it dropped to the low 90s this quarter and I'm sure it's maybe just a blip or an aberration. But at what point, should we care or at what point would you look at – take a closer look at the changes in those ratings on the 10 year performance?

Michael William Roberge
CEO, President and Chief Investment Officer, MFS Investment Management

A

Yeah. I mean, we've sustained 90-plus percent 10 year numbers for very long period of time, very hard to do. And so, I'm pleased with where it is, and if it's going to move around a couple of percentage points, it's certainly nothing we're going to worry about.

Nick Stogdill
Analyst, Credit Suisse Securities (Canada), Inc

Q

Sure. So just maybe a blip this quarter? Because I mean, it's been again high 90s for three years or four years and so maybe just nothing to call at this quarter?

Michael William Roberge
CEO, President and Chief Investment Officer, MFS Investment Management

A

Yeah. I mean, it's 4% of...

Nick Stogdill
Analyst, Credit Suisse Securities (Canada), Inc

Q

Yeah.

Michael William Roberge
CEO, President and Chief Investment Officer, MFS Investment Management

A

...4% of over $200 billion of assets, so no, it's nothing that we would be worried about.

Nick Stogdill
Analyst, Credit Suisse Securities (Canada), Inc

Q

Okay. Thank you.

Operator: Your next question comes from the line of Tom MacKinnon with BMO Capital. Your line is now open.

Tom MacKinnon
Analyst, BMO Capital Markets (Canada)

Q

Yeah. Thanks very much. Just looking here at the expected profit growth in the U.S. it was up $10 million in U.S. dollars, pre-tax year-over-year. Now, I think, you had talked about a $100 million in cost synergies from the Assurant deal, and that you got annual and that you had realized 40% of those. So that's $40 million, that would be $10 million a quarter. So, would the math then suggest that the only increase you got year-on-year in expected profit was really just due to the cost synergies from the Assurant deal?

What – how should we be looking at growth and expected profit in this business going forward as the more of these Assurant type cost saves begin to get realized, because it doesn't look like there is much organic growth in this business?

Daniel Richard Fishbein
President-US Business, Sun Life Financial, Inc.

A

Yeah. I think, when we look at expected profit, of course we're looking at that for the entire SLF U.S. business and there is a lot of different components in there. And certainly the expense synergies are one of the significant components, but there is also the volume changes in each business. We have two run-off businesses, the individual IFM Life business and International Wealth business, that has some impact, this currency change impact on a number of different things.

So I think we're looking at the product of all of those. What I would say about the synergies is we're very much on target for the $100 million to achieve as we stated originally by 2019, and we fully expect to see that impact emerge in the business. At the same time, we should see other impacts emerging into the results including the repricing of the group business, other expense efficiencies in our overall improvements in claims management. So, I think that we'll all be there overtime, but I can reiterate that we're very much on target with the expense synergies as well.

Tom MacKinnon
Analyst, BMO Capital Markets (Canada)

Q

Okay. And then a question for Mike, with respect to MFS margins at 36% this quarter. I think at the Investor Day you had said that fees were down – fee rates were down 6% over the last four years, and you could see them down another 6% in the next four years. I think MFS continues to have some investment spends as well. So, how should we be looking at margins going forward for this block, given the context of those statements?

Daniel Richard Fishbein
President-US Business, Sun Life Financial, Inc.

A

Yeah, I think I've said in this last couple of quarters, and I couched it in the industry context is given continued fee pressures that – and by the way you look at the last year fees across the industry have come down, about that 1% to 1.5%, which I think is probably reasonable estimation to use on a go forward basis, is fees will continue to come down in the industry. I think there will continue to be cost, regulatory cost and others that will force firms to have to invest in the business as well. And I think, you'll see industry margins creep down, we're not immune from that.

But what I would say is, year-on-year if you look at our results in the quarter is one of the thing that we did well was control expenses. So, those discretionary items that we have control over, we're being very careful with. We are investing in the business where we need to, but I think industry margins come down some, we're doing everything we can to control discretionary expenses here, and we're pretty pleased with how we ended up in the quarter.

Tom MacKinnon
Analyst, BMO Capital Markets (Canada)

Q

Okay. Thanks for your comments.

Operator: Your next question comes from the line of Paul Holden with CIBC. Your line is now open.

Paul Holden
Analyst, CIBC World Markets, Inc.

Q

Hey. Thank you. Good morning. So, just want to ask a question on the Canadian operations. So very good results year-to-date, underlying earnings up by 18%. Maybe you can walk us through some of those factors that you think are sustainable in terms of producing what I would say above-industry earnings growth?

Kevin P. Dougherty
President-Sun Life Financial Canada, Sun Life Financial, Inc.

A

Okay. Paul, it's Kevin Dougherty. Yeah, very strong quarter and I think if you look through to the fundamentals, there are some very good things going on inside virtually all of the businesses. I think GRS in particular made a significant contribution to the growth and expected profit you saw. I think Dean mentioned AUM or AUA has now just crossed over $93 billion. So continued growth there and expansion of margins and great momentum in the business SLGI has grown from $14 billion last year to over $18 billion at this point. So, is now breaking into profitability. So you're seeing that. On the Group benefits side, we've seen continued good experience in both disability and the healthcare book of business and it was maybe exceptional this quarter, but very strong continue to be very strong and we see that going forward.

The new – we mentioned the repricing of the Individual Life Insurance business and the pricing gains coming out of there. Actually, sales were flat year-over-year, but you'll notice from looking across the industry, most were down quite a bit year-over-year. So we've got really great momentum in that part of the business. Even during sort of this kind of this pause or slowdown. And I think, that's a reflection of really some excellent improvements in the product that are capturing the attention of advisors and new advisor and ultimately our clients. So we see good quality inside this lift and we'll keep working hard at it.

Paul Holden
Analyst, CIBC World Markets, Inc.

Q

Okay. And then, Kevin, maybe you can drill down a one of the comments you made and that relates to the Group Benefits business and their positive experience this quarter. You pointed out a little bit abnormal, but you expect positive experience generally to continue, maybe you can just explain, why that is?

Kevin P. Dougherty
President-Sun Life Financial Canada, Sun Life Financial, Inc.

A

Yeah. So we saw in Group Benefits this quarter, we saw both a slight decline in incidence rates and an improvement in recovery rates. And incidence rates do move around from quarter-to-quarter, though – over time you can't count on that every quarter. But we saw both happening in this quarter. So, I think the group business is moving to another level and you can see it in our numbers. But the uptick was a little bit outsized. So, I kind of thought off halfway maybe.

Paul Holden
Analyst, CIBC World Markets, Inc.

Q

Okay.

Kevin D. Strain
Executive Vice President and Chief Financial Officer, Sun Life Financial, Inc.

A

It's Kevin Strain. If I looked at it, I'd say, very, very strong morbidity in the credit experience. And when you look at the notable items for the total company, Canada is a big part of those and we talked about the new business gains in the quarter, which were strong on the DBS sale and some other factors. So you can – I would say, that – that while – these were driven by management actions, you may not see that level of positive every quarter. So, I think Canada was a big benefiter of those. But you will see that there was a very good growth and expected profit in Canada of CAD 19 million as well.

As Kevin said, there is a lot of things firing in the right direction for Canada. Even if a lot of the normal items that they benefited from were from management actions, but you may not see that level of notable items every quarter.

Paul Holden
Analyst, CIBC World Markets, Inc.

Q

Understood. That's helpful. Thank you. One final quick one as going back to U.S. Group. Do you have an update on the profit margin you are realizing in 2017 year-to-date versus the – I think it was a 3.5% number you provided for 2016. Mike, I guess it would be at somewhere running around – somewhere around the same level and so – what was the expected margin opportunities still ahead of you, is that accurate?

Michael William Roberge
CEO, President and Chief Investment Officer, MFS Investment Management

A

Yeah. I don't have the exact number in front of me for the whole Group Benefits business. But year to – we are making progress, let me just take a look at what we've got here. Yeah, we're running on an underlying basis, so far year-to-date between 3.5% and 4% profit margin. So, we're certainly making good progress. Obviously, what we talked about at the investor day was ultimately getting to 5% to 6% not there yet, but certainly in their – heading in that direction.

Paul Holden
Analyst, CIBC World Markets, Inc.

Q

Great. Thank you.

Operator: And there are no further questions at this time. We'll turn the call over to Greg.

Gregory A. Dilworth
Vice President-Investor Relations, Sun Life Financial, Inc.

Great. Thanks, Christa. I'd like to thank all of our participants today and if there are any additional questions we will be available after the call. If you wish to listen to the rebroadcast, it will be available on our website later this afternoon. Thanks very much, and have a great day.

Operator: This concludes today's conference call. You may now disconnect.