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Sun Life Financial, Inc. (SLF)

Q1 2017 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good afternoon and welcome to the Sun Life First Quarter 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. Instructions will be given at that time. [Operator Instructions]

I would now like to turn the call over to Greg Dilworth, Vice President of Investor Relations. Please go ahead.

Gregory A. Dilworth

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

Thank you, Dan, and good afternoon, everyone. Welcome to Sun Life Financial's earnings conference call for the first 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 first quarter by Dean Connor, President and Chief Executive Officer of Sun Life Financial.

Following Dean's remarks, Colm Freyne, Executive Vice President and Chief Financial Officer, will present the first 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 on today's call.

Turning to slide two, 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 afternoon'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 Dean.

Dean A. Connor

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

Thanks, Greg and good afternoon everyone. Turning to slide 4. The company reported underlying net income of CAD 573 million or CAD 0.93 a share down 2% from the same period last year and an underlying return on equity of 11.5%. Our Canadian, Asia and Asset Management pillars, each delivered earnings growth not withstanding continued net outflows at MFS.

In our U.S. business we saw lower results, due in part to higher mortality. The integration of our U.S. employee benefits acquisition progressed well in the quarter. You'll see that we announced CAD 1.50 increase in our common share dividend to bring our quarterly dividend to CAD 0.435 per share. This represents an increase of 4% and reflects our strong capital position, as well as forward momentum in our businesses.

We delivered strong sales growth in the quarter with insurance and wealth sales up by 58% and 13% respectively over the prior year. Assets under management ended the quarter at CAD 927 billion, up 8% from a year ago. In Canada, individual insurance had a strong start to the year with first quarter sales that were double the prior year from tax legislation changes and the successful transition to a new product suite.

Our individual wealth business also had a strong quarter with sales up 16% across fixed products, mutual funds, and segregated funds. Group Benefits and Group Retirement Services achieved strong year-over-year sales growth, primarily due to several large-case sales installed in the quarter. Client retention remained very strong, further contributing growth in business in force and assets under administration.

We made good progress on making it easier for clients to do business with us. For example, our top rated mobile app in Canada was updated at the end of April, and our clients are loving the convenience and functionality. Client mobile sessions are running at a remarkable 8 million per year, which means they're doing a lot they need within the app, such as submitting claims, checking coverage, finding, and rating a healthcare provider, checking on their investment accounts, and making contributions to their savings or retirement plans, all on the go.

In Sun Life Asset Management, we ended the quarter with CAD 643 billion in assets under management. At MFS, the pre-tax operating margin increased to 36% and assets under management increased to 4% from the prior quarter to $441 billon. Gross sales increased 6% to $21 billion in the first quarter and in U.S. retail we had the highest sales on record. Net outflows for the quarter were $11 billion with the majority of the net outflows coming from institutional separate accounts, as clients rebalanced their portfolios.

The fundamentals of MFS' business remain strong as the firm continues to deliver consistent long-term results that help clients meet their investment objectives. 80%, 79% and 96% of MFS U.S. retail mutual fund assets ranked in the top half of their Lipper categories based on 3-year, 5-year and 10-year performance, respectively.

In this year's Barron's ranking of U.S. mutual fund families, MFS earned the number two spot for 10-year performance by focusing on asset preservation and growth over longer horizons. And remarkably, MFS is ranked in Barron's top 10 fund families in eight of the last nine years for 5-year and 10-year returns. MFS AUM ended April 30 at $449 billion up from $441 billion at March 31, due to strong investment performance.

And while it's early in the quarter, net outflows have been running at a lower level. MFS will continue to carefully manage discretionary expenses to reflect the current environment. At Sun Life Investment Management, we generated positive net inflows of CAD 2.2 billion and ended the quarter at CAD 56 billion in assets under management.

Sun Life Investment Management continues to see strong demand for its real estate, specialty fixed income and liability driven investment solutions, and investment performance has been strong across all the businesses.

Turning next to the U.S. Sales in Group Benefits were higher from a full quarter of production from our U.S. employee benefits acquisition, higher group life and disability sales were offset by lower sales in stop loss, reflecting pricing actions in that business.

Our dental and vision businesses performed well, and subsequent to the quarter, we announced the acquisition of the Premier Dental Group. The acquisition helps expand our proprietary dental network and brings us a top dental preferred provider organization in the Midwest.

In our International life business, we saw strong sales growth over the prior year. Moving to Asia, sales of individual insurance products in Asia were up 31% driven by growth in most markets and increased ownership levels in the region.

Wealth sales increased by 84% to CAD 2.9 billion driven by strong mutual fund sales in India and pension sales in Hong Kong. Our Indian joint venture mutual fund company Birla Sun Life Asset Management now manages over CAD 40 billion in AUM and is the fourth largest mutual fund company in the country. Birla Sun Life has delivered strong investment performance and strong sales in a country where the mutual fund market is growing rapidly.

In the Philippines we maintained our number one position in the life insurance market for the sixth consecutive year based on new business premiums. Complementing our success in the Philippines, we've also seen our market share increase in other markets such as Hong Kong where we ranked second for MPF net flows in 2016.

So, to conclude, there is positive momentum in our business in the early stages of 2017. We're seeing strong top line growth, good growth in underlying earnings in Canada, Asset Management in Asia. And in the U.S. we're taking the right actions to drive profitable growth.

We're pleased with how the employee benefits acquisition is moving ahead, and in Asset Management, we're generating strong investment performance for clients and seeing increased levels of gross sales in a period of heightened industry redemptions.

I'll now turn the call over to Colm Freyne who'll take us through the financials.

Colm J. Freyne

Chief Financial Officer & Executive Vice President, Sun Life Financial, Inc.

Thank you, Dean, and good afternoon, everyone. Turning to slide 6, we take a look at some of the financial results from the first quarter of 2017. Our reported net income for the quarter was CAD 551 million, up from CAD 540 million in the first quarter last year. Underlying net income, which excludes the net impact of market factors and assumption changes, amounted to CAD 573 million. Our underlying return on equity was 11.5% for the quarter. Underlying results reflected net favorable mortality experience and gains from investing activities on insurance contract liabilities that were partially offset by lapse and other policyholder behavior experience and the impact of currency translation in our foreign operations.

First quarter adjusted premiums and deposits were CAD 44.4 billion, up 15% from the first quarter of 2016, and assets under management at the end of the quarter amounted to CAD 927 billion. We maintained a strong capital position ending the quarter with a minimum continuing capital and surplus requirements ratio for Sun Life Assurance Company of Canada of 229%.

The MCCSR ratio for Sun Life Financial Inc. was also strong at 249%. The higher ratio at the SLF level largely reflects the excess cash of CAD 1.1 billion held by SLF Inc. And our leverage ratio of 22.6% decreased from 25.2% in the prior quarter driven primarily by the redemption of CAD 800 million of subordinated debt during the quarter. We continue to progress on the transition to the new LICAT capital regime that will be effective in 2018. We filed our first test run with OSFI in January based on 2015 data. And we remind you that our current risk profile and strong capital position will assist us as we implement the new regime.

Turning to slide 7, we provide details of underlying earnings by business group for the quarter. In SLF Canada, underlying earnings reflect favorable investing activity and mortality experience in Individual Wealth and Group Retirement Services. This was partially offset by continued investments in growing our business. In SLF U.S., underlying earnings were down from the first quarter of 2016. We made good progress this quarter in our Group Disability business. However, we had higher levels of adverse mortality in In-force Management and Group Life.

Some of this is normal volatility. However, we also intend to put through further rate increases in Group Life. Results this quarter were also impacted by adverse policyholder experience in International and In-force Management. In SLF Asset Management, MFS had underlying earnings growth over the first quarter of 2016 driven by higher average net assets and a lower tax rate.

The pre-tax operating profit margin was 36% and net outflows were $11.1 billion for the quarter. MFS saw outflows in both retail and institutional, with the majority of the outflows coming from institutional accounts driven by client portfolio rebalancing. At Sun Life Investment Management, we had net inflows of CAD 2.2 billion and generated net income of CAD 7 million. In Asia, underlying earnings grew 16% over last year, reflecting business growth across the region, and favorable net gains realized on the sale of AFS assets.

Turning next to slide 8, we provide details on our sources of earnings presentation. In the first quarter we discontinued the use of operating net income in order to streamline our disclosure by reducing the number of net income measures we provide. There is no change to reported or underlying net income. Our sources of earnings disclosure had previously been presented on an operating net income basis, and going forward, we will use reported net income as the starting point for sources of earnings disclosure.

Expected profit of CAD 666 million increased by CAD 15 million from the same period a year ago. Excluding the impact of currency and the results of SLF Asset Management, expected profit was up 9%. Year-over-year increase reflects strong business growth in Canada and Asia as well as the employee benefits acquisition in the U.S. and increased ownership levels in a number of our Asian businesses.

New business strain was CAD 33 million for the quarter. Lower levels of new business strain were driven primarily by pricing gains in SLF Canada from higher sales in individual insurance and wealth, partially offset by a higher share of strain from increased ownership levels and products mix in Asia.

At our recent Investor Day, we announced an expected range for our new business strain of CAD 10 million to CAD 20 million per quarter. This level of new business strain is based on our annual expectations for this line item. And new business strain tends to reflect higher levels of seasonality during the first quarter. We continue to believe that CAD 10 million to CAD 20 million per quarter is an appropriate estimate over the course of an annual cycle.

Experience losses of CAD 16 million for the quarter primarily reflect unfavorable policyholder behavior in the U.S. and Canada and various other experience items. These were partially offset by favorable mortality and investing activity in Canada and net gains from market impacts. Assumption changes and management actions contributed CAD 2 million pre-tax to net income in the quarter.

Other is a new category used to capture the operating net income adjustments previously excluded from our sources of earnings presentation. These items include the pre-tax impact of hedges in Canada that do not qualify for hedge accounting, fair value adjustments on MFS share-based payment awards and acquisition, integration and restructuring costs.

Earnings on surplus of CAD 132 million were CAD 9 million higher than the first quarter a year ago, reflecting higher mark-to-market gains on real estate on recent appraisals. On underlying net income attributable to common shareholders, the tax rate for the quarter was 17.5% which is in line with the low end of our stated range of 18% to 22%. Our income tax expense on a reported basis, which includes power business, was 19.6%.

Slide 9 shows sales results across our insurance and wealth businesses. Total insurance sales were up 58% with sales growth across Canada, Asia and the U.S. And in our wealth businesses, sales of CAD 37.6 billion were up 13% over the prior year.

So, to conclude, we had strong top line growth across the organization. Earnings were up across most of our businesses, and we continue to focus on areas of the business where we see opportunities for growth including expansion of margins in our U.S. business. Our capital position is one of strength and flexibility that gives us confidence as we execute on our business plans in 2017 and beyond.

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

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

Thank you, Colm. To help 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 Dan to please poll the participants for questions.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Your first question comes from the line of Seth Weiss with Bank of America Merrill Lynch. Please go ahead.

Seth M. Weiss
Analyst, Bank of America Merrill Lynch
Q

Hi, good afternoon. Thanks for taking the question. I wanted to dive in a little bit further on MFS, and on the outflows. Second consecutive quarter here of record net outflows, and similar to last quarter, you highlighted institutional client portfolio rebalancing as one of the drivers. Can we just get into a little bit more depth of what that means? And for two quarters in a row is this the start of something maybe more trendable or is this something that you could point to that's a bit more volatile and lumpy quarter-by-quarter?

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

Good afternoon, Seth. This is Mike Roberge. If you look at it by channel in the first quarter, it really continue to look very similar to the prior quarter and that we actually had a record growth sales quarter as 2016 was. What we continue to see in the industry is very high redemption rates. We're estimating, it's hard to get hard data on this, near-term that redemption rates are currently running about 33% for the industry. We're running inside of that, but clearly with record sales and slightly net outflows that had an impact on that business.

We think that, as I said at the Investor Day, we think some of that will normalize. That same thing continues to be true in the non-U.S. business, which looks similar to Q4. And then as you mentioned, in the institutional business, again a number of rebalancing is away. They're not performance related. The vast minority of when we go out to clients and poll them on reason for performance, for redemption it's not performance related. We're obviously hopeful that that's relatively lumpy. As Dean mentioned, Q2 activity appears better than that currently. And so we believe that the retail business will normalize, some of the redemption rate will come down. And we believe that we will be able to stabilize the institutional business. And over the next couple of years, we're going to continue with the strategy of diversifying in the blended and diversifying the fixed income offering.

Seth M. Weiss
Analyst, Bank of America Merrill Lynch
Q

Okay, great. And then both the fourth quarter and first quarter in terms of capital market conditions were fair to say non-normal coming off of the U.S. election. Is there an element of profit taking there on the institutional side, when you talk about rebalancing or if you look at prior patterns of redemptions? Do you tend to see it spike when you have these big jumps up or down in markets like we saw in both the fourth quarter and the early part of the first quarter?

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

You will kind of seen in periods where you do have a big spike in equities. You get de-risking within the DB world and so, clients will take advantage of the increase in equity values. If they can do that in a higher rate regime they will do that as well. So, it does tend to accelerate some of that.

And our guess is, is when clients say they've rebalanced, we think some of that is in the de-risking category.

Seth M. Weiss
Analyst, Bank of America Merrill Lynch
Q

Okay. And then just one very quick one related. You give the 3-year, 5-year, and 10-year fund performance levels. If we look at a one-year performance basis, just curious what that looks like over the trailing 12 months in terms of the percentage of funds beating Lipper averages?

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

Yeah, you've got it in the deck or maybe, you don't have it. On a one year basis, as of the quarter, it was 44%. One of the things that we – surprisingly if you go back a year ago we were coming up to the Brexit vote. We had that. It went the wrong way. I think, people were certainly concerned about Trump here in the U.S. that went the wrong way for a lot of people in terms of their thoughts and what it meant for the market.

Even with that as a backdrop, volatility has stayed low. We saw a massive increase in the market, a rotation into lower quality high beta stocks. That had a impact on one-year performance. What I would say is year-to-date is we've seen a rotation. Even though the market's up, we've seen a rotation out of that reflation trade back into higher quality parts of the market, which is our investment style. So year-to-date performance is significantly better than the one year number and we will need to roll through a couple of quarters to improve the one year, but what we focus on is 3-year, 5-year, and 10-year performance here. That's how we incent and compensate the team and we continue to generate strong performance across the platform for clients.

Seth M. Weiss
Analyst, Bank of America Merrill Lynch
Q

Great. Thanks so much.

Operator: Your next question comes from the line of Gabriel Dechaine with National Bank Financial. Please go ahead.

Gabriel Dechaine
Analyst, National Bank Financial, Inc.
Q

All right. Good afternoon. The quarter really looks like a variety of issues or the miss, I guess, this quarter is primarily attributable to what went on in the U.S., and let's focus in on the group business a bit. Can you just tell me what's going on there? Stop-loss is experiencing some problems. What led to those problems? When do we expect that to be fixed? And when you say Assurant is progressing well, I believe you. It's just hard to tell that from the numbers. Since the deal closed, growth in that segment has been negative. So I'm wondering how you can breakdown what's going on in the legacy business versus what's going on in Assurant?

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

A

Okay. Sure. Let me first answer the first part of the question. I'll break it down into three parts. Stop-loss, disability and life because there are different things going on in each component. The stop-loss business, as we shared last year, had some adverse experience that peaked in the second quarter. We've had significantly better results in the third and fourth quarter last year. And the first quarter results were in line with the fourth quarter. So that continue to be at an improved level, but still depressed from where we'd like to see it. We took significant pricing action in the stop-loss business. Most of the business renews January 1. We've now re-priced over 80% of the business and our achieved January 1 renewal rate increases were about 17%, which was in line or even a little better than what we targeted, so that accounts for medical trend and any movement that we needed in the rates there.

In the first quarter, 97% of the stop-loss claims are still from 2016. So the experience you see in the first quarter is largely indicative of what happened prior to those January 1 renewals. And the way we do our reserving, you see not just the claims emerge, but some of the associated premium emerges when those claims show up. In the second quarter, it will still be mostly 2016 claims, but in the third and fourth quarters, you'll see the 2017 claims. There is obviously a slope going in both directions for both years. So the point is that we have gotten substantial price increases and we'll see the benefits of that in future quarters, so we're pleased with how that's progressing.

The disability business, and that of course is the business that three years ago or about two-and-a-half years ago, we said we needed to take significant action on. Our morbidity, which is the disability business, has improved and in fact the first quarter performed quite well, better than our expectation. So we are seeing the improvement in performance in the disability business that we've been targeting.

The major area of variance in the first quarter was the group life business where we had adverse mortality and that was on both an incidence and a severity basis. There's obviously some element of volatility there, but we also have put price increases in on the group life business, starting during the second half of last year to make sure that we've got that heading in the right direction.

The second part of your question was the progress on Assurant. And there's a couple of aspects to that. There's the underlying performance of the business which continues to be strong. We did see some adverse mortality in the Assurant legacy business as well, but overall the different components of that business have been performing well.

And the other aspect that we're referring to when we say it's progressing well is the integration. All of the work we're doing to merge together the organization, the systems, the products and all of that is proceeding on the schedule that we set and achieving the targets that we set.

Gabriel Dechaine
Analyst, National Bank Financial, Inc.

Q

So, if you could breakdown the profit between the legacy business and Assurant, did Assurant make money presumably and the rest didn't?

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

A

It's not as simple as that because there's multiple components including on the legacy side. So the legacy side we have disability, we have life, we have stop-loss, but it is safe to say that the variance we saw in the quarter was largely on the Sun Life legacy side, as I mentioned somewhat in the stop-loss business and in on the life side. The Assurant business has performed well with the exception that we did also see some adverse mortality on the life business there.

Gabriel Dechaine
Analyst, National Bank Financial, Inc.

Q

Okay. I'm sure there's a lot of questions about this, so I'll move on to expenses and the expense overrun, the negative expense experience wasn't a bigger this quarter. It was around about CAD 7 million after tax, CAD 6 million something like that. It was a lot bigger in Q4, but we've seen expense overruns or negative expense experience every quarter I think over the past 20 in a row plus. It was easier to accept that when MFS was growing at 15% a year whatever and the businesses generally were growing faster. But as MFS [ph] is the only thing that flows (25:47) there's some softer earnings performance in the U.S., call it that and the macro is fine, it's not flawless. Are you looking at those numbers and maybe picking a sharper pencil to your expense base and maybe there's some action that needs to be taken there because it has been a very consistent trend.

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

A

Gabriel, it's Dean. I think the expenses always get a sharp look and a sharp pencil here. And if you looked at and you peel this back and we've put these numbers out there in the past. But when you adjust for volume-related expenses and those are things like higher sub-advisor fees because you've sold a lot to of GRS business or your MPF business is growing in Hong Kong and higher producer volumes when you sell a lot of – we had very strong insurance sales in the first quarter and the fourth quarter.

When you adjust for those and you adjust for currency and you adjust for acquisitions because we've done a lot, as you know on the acquisition front. Our controllable expenses grew 3% in 2015, 3% in 2016 and 4% in the first quarter of 2017. So the expense growth you see when you just look at the total expenses that we report does in fact, I'll flip it around and say, does in fact represent very strong sales growth. So we've grown our GRS business. That's driven up sub-advisor fees. We had enormous sales in the insurance business here in Canada in Q1 and Q4 for reasons we know. And that has generated additional expense around wholesaler bonuses and wholesaler compensation. And frankly, those are expenses we like. Those are expenses that are growing the business. We continue to drive The Brighter Way, which is our Lean Six Sigma productivity machine, further and further throughout the organization. It's having real impact on cutting out waste and doing the work better and cheaper and faster. And it's producing real productivity gains and we continue to invest in growth in our business.

I mean, as we've said before, the SOE lens on expenses is not a helpful lens, because it really shows you the residual expense that doesn't emerge from balance sheet liabilities that have expenses built into them. So we produce it because it's needed by the SOE lens, but in fact, the better lens, I think, is to look at controllable expense on a net basis. We think we've got – we're producing good value.

The last thing I would say is that, just to underscore, expenses are a subject of intense focus in the company, because we realize we have to invest in future growth, invest in technology and the technology lead that we have built in our businesses, particularly in Canada, is a lead that makes a real difference to selling business. It's a lead we're proud of. It makes a difference in winning in the market, it's a decision point for clients in a scenario where we will continue to invest, to preserve that lead and in fact put more daylight between us and the other guys.

Gabriel Dechaine
Analyst, National Bank Financial, Inc.

Q

And just – the word lead is an interesting one. It implies at least to my ears that you're not in real need of a catch-up expense because you're underinvested. So restructuring charges we've seen them plenty of them from the banks, started to emerge in the life insurance space. Is that something that we should contemplate or not for Sun Life?

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

A

Well. We are not planning a major project on that front. When you think about our major technology platforms, when we integrated with Clarica many years ago, we bit that bullet upfront and integrated all the back office systems and made those investments in the platform and that's helped driven to drive our total benefits offering. It's made all the mobile tools at the frontend possible, because you're hanging them off of just one backend system. So, I think where our investment is focused around technology going forward isn't so much catch-up, it's building the next-generation of tools including digital predictive models, AI driven tools that help drive business growth do better job for our clients.

Gabriel Dechaine
Analyst, National Bank Financial, Inc.

Q

Okay. Thanks Dean and thanks, Dan, earlier.

Operator: Your next question comes from the line of Meny Grauman with Cormark Securities. Please go ahead.

Meny Grauman
Analyst, Cormark Securities, Inc.

Q

Hi, good afternoon. I want to ask a question about expected profit, and we're seeing growth there decelerate for a number of quarters now. I think if I caught you, you were explaining that it's really driven by SLF Asset Management, so I just want to confirm that? And then just ask a forward-looking question in terms of when you overlay your outlook for SLF Asset Management specifically for MFS, what does that indicate about where expected profit or the rate of growth of expected profit is going to move over the next little while?

Colm J. Freyne
Chief Financial Officer & Executive Vice President, Sun Life Financial, Inc.

A

Hi, Meny, it's Colm here. So, yes, on the expected profit line, you'll have seen that the growth was modest on the expected profit, the total number CAD 651 million a year ago to CAD 666 million in the current quarter. However, when you adjust for Asset Management, and we'll come back to Asset Management, and you adjust for currency, you saw a much stronger growth than you've seen good growth in Canada, and that's driven from growth in our group offerings on the Group Benefits side, the Group Retirement Services, good growth in the U.S. And again, taking account of currency adjusting for that and the Assurant acquisition, good growth in Asia.

And if you think about at the Asset Management side from a modeling perspective, it's less. I mean, we fit the Asset Management into the source of earnings lens, of course, because we report on a consolidated basis. But Asset Management is really driven by the factors that we've talked about previously, which is of course, the rate of growth in the assets under management driven by both the equity market performance but also our particular performance, our outperformance, as Mike has mentioned, over long periods of time, and again, assumptions around the rate of flows, which are difficult as we've commented on to predict.

So, I think on the insurance side, you can expect to see us continue to drive growth in the expected profit there because of the activities that we've been taking and we've got good momentum. You saw that in very good sales numbers in the quarter. And we have no reason to believe that we won't maintain a good momentum on the sales side for the various reasons we've talked about.

So, that's how we would see that. We don't see particular issue with the expected profit. Clearly, where there are expense investments, and Dean mentioned some of those around technology, they do tend to pull down the expected profit because some of that investment is going to go into that expected profit line. Gabriel previously mentioned the negative expense experience in the quarter which was a relatively small number, but we do remind you that ongoing investment in new initiatives, if it's going to continue for a period of time, does emerge into the expected profit. So that's also a factor. But, no, we take all of those things into account and we have a view that we should be able to continue to drive forward on that line.

Meny Grauman
Analyst, Cormark Securities, Inc.
Q

Thanks. And if I can just ask a question on the stop-loss business, the balance between pricing and sales always a consideration. Looking at just the sales results for the stop-loss business and wondering that balance, when you look at those kind of sales numbers, is there any concern you have in terms of pricing, in terms of the plan for pricing? Is there anything in those sales numbers that gives you a little bit of concern that maybe you're going too far in terms of addressing the pricing issue?

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

Sure. We continue to have strong sales in stop-loss, although obviously they're somewhat moderated now that we've taken pricing action. The first quarter is not a significant quarter for stop-loss sales. It's a pretty small percentage of the annual total, so not a great deal could be gleaned from the first quarter results. But if we look back on a trailing 12-month basis, the business in force has continued to grow. It's up by about 4% versus the same time this year. So we think we've hit the right balance there of getting the rates we need by continuing to grow the business.

Meny Grauman
Analyst, Cormark Securities, Inc.
Q

Thank you.

Operator: Your next question comes from the line of Sumit Malhotra with Scotia Capital. Please go ahead.

Sumit Malhotra
Analyst, Scotia Capital, Inc.
Q

Thanks. Good afternoon. I want to go back to Dan, and just want to start with the Assurant business. So, it seems like in talking about the experience challenges the group business is having, you're drawing a line between SLF legacy business and the acquired franchise. Can you tell us, as you've worked through this integration over the last year plus, is there anything in respect to the Assurant – the acquired business that you've had to adjust in a significant way either from a pricing perspective or in terms of, let's call it, underwriting quality that you weren't comfortable with?

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

A

There really is not. I mean, that business came over to us in very good condition, and we've been pleased with it and its performance and especially the people that came with it, who have stayed with us and continued to manage that business. They are very different businesses, we have to recognize that, although they fit together in a complementary way. The acquired business was mostly in the small group segment, mostly employers fewer than a hundred employees. And that business has some different and unique characteristics and they had built an infrastructure designed around that which we're obviously continuing.

It also has a dental business which was not something that we had in any significant way inside the legacy Sun Life organization. By the same time, the Sun Life business is quite different in that a very significant portion of the total is stop-loss. So, it's a little hard to draw precise comparisons. But to your specific question, we've not had to make any significant changes to manage that business.

Sumit Malhotra
Analyst, Scotia Capital, Inc.

Q

Well, maybe just whatever the opposite of stars aligning is this quarter because mortality in In-force and Group, policyholder behavior in International, morbidity and stop-loss, it seems like everything from a policyholder experience perspective went against your business this quarter. So, without giving you too much of a softball here, is this bad luck that hurt the quarter or, in your view, is it going to take some time for some of these changes that you've implemented in terms of pricing to improve experience over the course of 2017?

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

A

Well, thank you for enumerating it that way. That is similar to how we're looking at this. It is a diversified portfolio of businesses and there's quite a few components in the business. And the advantage of a diversified portfolio is that, quite often, some things break your way and some things don't break your way. This does seem to be a quarter where virtually everything except maybe for one item broke in the same direction.

So we certainly would hope that wouldn't tap in too often. The probabilities of that seem low. At the same time, we wouldn't say everything is bad luck. We can't be that complacent, so obviously, we are making sure that we're taking action wherever we can.

For example, we are going to be very judicious about expenses for the rest of the year, and we're taking some actions there. Certainly, I mentioned earlier, we've made some adjustments to our life pricing as we think that's prudent at the moment. So we've selectively taken some actions, but I think your characterization is a reasonable one.

Sumit Malhotra
Analyst, Scotia Capital, Inc.

Q

And last one maybe just a little bit more numbers based, we missed you directly at the Investor Day, we obviously heard from your colleagues. The margin improvement that Sun Life has targeted for the Group business from 3.5% up to closer to 6%, in your view, what's the key variable that gets that margin moving in the right direction?

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

A

Well, it's clearly getting all three things right, pricing, claims management and expenses, and that's how we get to the right margin. In the U.S. Group Benefits business, it's intensely competitive. There are many, many players and you have to get a lot of little things right in order to get to the right margins.

So we are focused on all three of those things that we've talked a lot already today about pricing. Obviously, we're quite focused on that. We continue to leverage expenses including through the synergies that we'll get from the integration. And we also have been investing in claims management, particularly in the areas where we can have some real influence over that. For example, getting people back to work in our long-term disability business and we're making good progress there. We're pleased with the progress. But we have to fully execute on all three of those and then we'll get to that target margin.

Sumit Malhotra
Analyst, Scotia Capital, Inc.

Q

Thanks for your time.

Operator: Your next question comes from the line of Humphrey Lee with Dowling & Partners. Please, go ahead.

Humphrey Hung Fai Lee
Analyst, Dowling & Partners Securities LLC

Q

Good afternoon and thank you for taking my questions. I just want to follow-up on the MFS flows. So, in Mike's response to Seth earlier, mentioning there is a mix between de-risking and the ongoing active to passive trend for the institutional outflows. I was just wondering if you can provide a little bit color in terms of the mix between the two or at least based on your estimates?

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

A

Humphrey, it's Mike. It's hard to drill down and get too granular there, because when we reach out to clients, they generally will put it in broader buckets. And so, we try to get them very specific and you tend to get rebalancing. So, when we look at and we got out to clients and try and allocate it across the number of dimensions, most of it falls in the reallocation category. So the vast majority of those outflows are reallocation. That can again be de-risking. It can be moved to passive, it can be – and we've seen this recently is if you perform well on a certain strategy, they're rebalancing you down to reduce their exposure to you. And so very hard to get really granular. I think most importantly what I would say is when we look at it, far less than 10% of the rationale for the redemptions is performance, that's where we'll be much more concerned around it.

Humphrey Hung Fai Lee
Analyst, Dowling & Partners Securities LLC

Q

Yeah. I guess my question is more thinking along the line that if it is for a de-risking reason, given your fixed income products or with the recently introduced fixed income products, that could be a potential area that you can use to retain some of the assets. And if it's because of active to passive [indiscernible] (42:16). So maybe help us to kind of better understand in terms of some of the discussions that you have with your clients when they indicated they would like to [indiscernible] (42:29) and what you would do in order to retain some of the assets and maybe share some of the discussions or kind of feedback that you've got?

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

Yeah, great question. So, midyear last year we created a new group. We call it the Client Solutions group reporting in to Carol Geremia who runs distribution for us. That group – their job is to get out to clients and obviously be in front of clients all the time, but where we begin to have discussion with clients where a client-facing person is talking to a client about de-risking, that group will get in front of the client to try and understand what they're doing, why they're doing it, are there ways in which as assets are going to move from MFS that we can actually position a product alongside that. So, that is an effort that very recently we put in place to go at exactly that, which is how do we understand what clients are doing from a allocation de-risking perspective, how do we then diversify the offering that we can – and the product set that we can sell into those particular clients. So that is actually an issue that we're currently working through.

Humphrey Hung Fai Lee
Analyst, Dowling & Partners Securities LLC
Q

So I guess, at the end of the day, so you're looking at kind of the quarter-to-date the outflow situation is better than the same time during the first quarter. How should we think about – I guess, where you're seeing now versus at the same time during the first quarter, how much better are we talking about?

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

Well, we're not going to give that number. That's not information we're going to make public. I think, as we think about it over a longer period of time because we're not managing this business for the second quarter. So as we think it over a longer period of time, we think that redemption rate in retail will normalize some. We think it is at a level that is far too high to make sense through this cycle. We think that will normalize. That will drive positive flows in retail. We think that a non-U.S. business has a little bit of sales issue, which we think normalizes and the redemption rate comes down which can get that back into positive flows.

We do think that you'll see stabilization in institutional business, as we broaden and diversify the offering to fixed income, we think that we can get that back into positive flows over a period of time as well. The challenge with all of that in terms of predicting quarters is, we are generating lots of sales, but we're seeing our clients do a lot of things on the redemption side. We need that to slow down. We cannot predict when that's going to happen and what clients are going to do quarter-to-quarter. So we try to get people a little bit of a little help to think about it through an entire cycle.

Humphrey Hung Fai Lee
Analyst, Dowling & Partners Securities LLC
Q

Okay. Thank you.

Operator: Your next question comes from the line of Steve Theriault with Eight Capital. Please go ahead.

Steve Theriault
Analyst, Eight Capital
Q

Thanks very much. First, I have a couple of questions on Asia, sorry, but first, just a follow-up for, Dan, if I could. And, Dan, thanks for all the color around the stop-loss. Am I right then in interpreting that as in we're going to see one more quarter likely of negative morbidity experience before 2017 starts to drive the [indiscernible] (45:28).

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

A

The second quarter would still be dominated by 2016 experience. Of course, we can't necessarily predict what that experience will be. All we can say is that quarter will be mostly reflective of 2016. And then we should see the effective 2017 both claims and the rate increases in the third and fourth quarters.

Steve Theriault
Analyst, Eight Capital

Q

Okay. Thanks for that. And then skipping to Asia for Kevin, a couple of things. First just some color on the sales. The India sales were the stand out, I think at CAD 40 million they're double or more than double what we've ever seen. So, maybe just to start a bit of color there, what's going on in that geography insurance wise.

Kevin D. Strain
President Sun Life Financial Asia, Sun Life Financial, Inc.

A

Yeah. Thanks, Steve. Well, there's two things our buy-up in India. So we went from 26% to 49%, so that comes during the quarter. But they've also been investing a lot into the agency and the quality of the agency. And we're seeing some of the – reaping some of the benefit of those investments and the agency starting to perform quite strongly there. So, we're very happy with the buy-up and how it's progressing on the life side. And I think those sales you should continue to see us build out on the agency side and we've just signed some additional bancassurance agreements including an agreement with DBS in India and also a bancassurance agreement with HDFC. We're going to become an additional provider for HDFC in India.

Steve Theriault
Analyst, Eight Capital

Q

Okay. That's great. Sorry, I thought we already had a quarter under our belts, but I guess that just closed.

And then the second question around ROE, the ROE was – it's been 7.5% in 2015, same in 2016, same this quarter. In the past we've talked about getting that ROE higher and eventually getting that I think, to double-digit levels. Maybe just if you could talk a bit around why we haven't seen more momentum in the near-term and how long until that starts to march a little bit higher.

Kevin D. Strain
President Sun Life Financial Asia, Sun Life Financial, Inc.

A

I should just point out on the earnings side, we did have a currency headwind in the quarter. It cost us about CAD 5 million on a Canadian dollar basis. So, that growth would have been substantially higher if you went on a constant currency basis. We continue to see our sales grow quite well and our VNB. And as I said in the past that, the way to grow in Asia is to continue to invest in distribution, continue to build the business, continue to sell profitable products, so get the mix right and get the VNB right, and that will start to come into income.

And you've seen that in the growth and expected profit. We had a significant growth in expected profit in the quarter. You can see that in the growth in earnings. And over time that ROE is going to continue to grow on a fairly regular basis. We are going to be also looking at sort of the capital and the capital regime.

Steve Theriault
Analyst, Eight Capital

Q

Okay. I may follow-up. Thank you.

Operator: Your next question comes from the line of Nick Stogdill with Credit Suisse. Please, go ahead.

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

Q

Hi, good afternoon. Just going back to the U.S. Is it possible to get a breakdown of the negative experience by business line in the U.S. maybe, just order of magnitude how much was in stop-loss versus Group, versus the In-force?

Kevin Morrissey
Senior Vice President & Chief Actuary, Sun Life Financial, Inc.

A

Yeah. Hi, Nick. This is Kevin Morrissey. So, when I look at the breakdown across those different contingencies, maybe I'll just start with morbidity. Most of that, I think as Dan mentioned, is in on the stop-loss side. So we actually had favorable morbidity across all the other lines within the U.S., so stop-loss is really the key there. When I look at the mortality side, when I break that down, it's more the In-force Management, where we saw some of the higher claims. And this is a normal seasonal pattern that we see in terms of mortality. In developed countries, normally, we do see higher claims in the winter months. And so where SLF does business and especially in the U.S. that would be Q1. We often see 10% to 20% higher claims and it's especially higher when we look at older ages. So that's starting in both the 60s and going up to ages 70s and 80s, it gets significantly higher.

And when we look at the In-force Management business, because – remind everybody that is a runoff block and so the average age in our block is going to start increasing. And so we did see kind of what we would expect as a normally higher mortality claims in the quarter. So that was mainly where we saw the morbidity side. Maybe lastly, I'll talk a bit about the policyholder behavior. We saw some lapse losses on the In-force Management that we've called out as well as International life. On the In-force Management side, it was lower lapses on some of the NLG business in the U.S. For the International life, it's more of the early duration lapses where we saw a bit of losses fairly marginal, but a bit of negative experience there as well.

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

Q

Thanks. If we just take the experience gains and assumption changes in the U.S. business though, and then try and allocate that roughly to the various lines, – how much is for stop-loss, or can you give us a sense there? I'm just trying to get a sense that if this improves next year in the back half of the year, how much might be there to fall away?

Colm J. Freyne
Chief Financial Officer & Executive Vice President, Sun Life Financial, Inc.

A

Yeah. It's Colm here, Nick. I mean I think Dan really addressed the point around stop-loss earlier in a fair bit of detail. We don't provide that level of granular P&L by each of the subsets of our business.

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

Q

Okay. Thank you. Just my next one on the investing gains, I know the expectation was for a bit more of a normal run rate compared to last year but could you just maybe give us an outlook? And then again refresh us on what's really changed relative to what we saw throughout most of 2016, where the investment gains were around CAD 50 million a quarter?

Colm J. Freyne
Chief Financial Officer & Executive Vice President, Sun Life Financial, Inc.

A

Yeah. It's Colm here again. And I think on the investment gains, we have pointed out in the past that somewhere in the CAD 10 million to CAD 20 million, we would consider to be on a net of tax basis level that we're comfortable with from a sustainability perspective. Now, clearly in 2015 and 2016 we had quarters that were significantly higher and during those quarters, we did speak to some of the drivers behind the higher amounts. And it is a bit lumpy so it can happen that there's a particular activity, ALM activity, asset liability management activity in a quarter that might drive that higher.

One way to think of it is to think of it in the context of overall investments including, for example, our credit experience. And I think you'll note that this quarter, if you look at the investment gains, it was within the range we targeted but our credit experience was certainly lower than trend. And again, we think that there were couple of items that were very specific to the quarter around credit that don't necessarily portend to give a signal as to what might happen in the next quarter.

So, I think investment gains including credit were a little bit on the low side, but within the range certainly on the invest and gains.

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

Q

Okay. thanks. The credit looks like it's a bit seasonal. The Q1 2016 and Q1 2015 were both kind of on the low side, [indiscernible] (53:10) a seasonal factor or?

Randolph Brill Brown
Chief Investment Officer, Sun Life Financial, Inc.

A

Hi. This is Randy Brown. No, it's not really seasonal. This was really two particular one-off situations. It's not really representative of the broader portfolio where in general we had a quite benign credit experience. So, as Colm said, net credit experience was still positive despite these two particulars, but I would not call it seasonal rather one-off situations.

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

Q

Thank you.

Operator: Your next question comes from the line of Doug Young with Desjardins Capital Markets. Please go ahead.

Doug Young
Analyst, Desjardins Capital Markets

Q

Hi. Good afternoon. I guess a question for Dan. If I back of the envelope into what your net margin on the Group business would have been for – after normalizing mortality, morbidity, and stop-loss and then the restructuring charge. I think, I get the 3% to 3.5%, you can correct me if I'm wrong. And obviously you've targeted 5% to 6% and I guess my question is, do you have everything in the system in terms of pricing, in terms of expense reductions to make up that gap? Or what else needs to happen to make up that gap? And is this more of a 2018-2019 target? Is that when we should expect to move in that direction, just some color would be helpful?

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

A

Sure. You're referring to some of the commentary from Investor Day, where we said our long-term target for the Group business is 5% to 6%, after tax margins, so that was not meant to be a 2017 target. Your math sounds reasonable. It's certainly close to what we would think about. So, we think, we've taken all the steps necessary, as I mentioned earlier. We've recently pulled some additional levers, but we think, we're on a path to get to that level of margin. What's necessary is it obviously will take some more time, as we go through all of these steps, the integration, the synergies, the continued impact of claims management, and our pricing actions. It will just take a little more time to get there.

We're obviously at a margin that's quite a bit higher than where we were when we started this two-and-a-half to three years ago, but we still have a ways to go.

Doug Young
Analyst, Desjardins Capital Markets

Q

And so the pricing actions you've taken, as you look out on your plan, are you pricing with the 5% to 6% margin in mind or is that – or do you have to take gentle steps with your price increases, so that you don't disrupt the In force.

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

A

So, we are pricing with that long-term margin in mind. Absolutely, we know what we're targeting in terms of margins and ROE, as well. You don't always get 100% of what you're targeting, so some times it does take more than one renewal to get to full target, but certainly our pricing is designed to achieve those margins.

Doug Young
Analyst, Desjardins Capital Markets

Q

Okay. And then, Dean, you've talked about strong capital position, you increased the dividend because of your confidence in the outlook in the business. Yet you don't have an NCIB in place. And so, in days like today when your stock gets hit, just wondering if any further thoughts to put in an NCIB in place or why not?

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

A

Doug, thanks for the question. As you know on capital, our first priority is to fund organic growth and we've certainly been doing that. And our second priority is to fund acquisitions, but acquisitions that number one fit our strategy. Number two, bring us capabilities that allow us to grow faster than we could otherwise grow on our own. And three, as well must clear our economic hurdles. So those criteria for acquisitions, which we've applied over the CAD 2.5 billion we've deployed in the last three years or so, those criteria continue to apply. And then we turn our minds to share buybacks, we, as you know, how we've done them in the past, we will likely do them in the future. I think combined with the dividend payout ratio, we've had a healthy return of capital to shareholders. As Colm noted and as I noted, we're in a very strong capital position. And so this – buybacks will continue to be part of our thinking in the future.

Doug Young
Analyst, Desjardins Capital Markets

Q

Is the – I mean, the movement in 2018 to the LICAT model, does that give you any pause to put a buyback in place or is this just internal thinking?

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

A

Our thinking around the buyback is not limited or constrained by LICAT.

Doug Young
Analyst, Desjardins Capital Markets

Q

Okay. Thank you.

Operator: And your next question comes from the line of Paul Holden with CIBC. Please go ahead.

Paul Holden
Analyst, CIBC World Markets, Inc.

Q

Thank you. Good afternoon. So, Dean, you made that first point there that your first priority is organic growth and you've invested heavily in Canada over the last few years in terms of technology capabilities. Seems to be translating into a very strong sales growth both on the Group and individual side. So wondering if you or Kevin or someone else can just talk about progress in terms of market share gains, if any, within Canada, again both on Group and individual.

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

A

Sure, Paul. It's Kevin Dougherty speaking. Yeah, if you look really across the board in Canada, we've been making progress on market share. So in the Group Benefits business, went back four or five years ago, we would have been quite – just behind Great-West, then Manulife did their acquisition. We've passed both of them and we're now somewhere around 23%. I think they would be around 21.5% in terms of overall market share.

In GRS, despite our – we've got a very, very large market share there. We've increased that from 40% to I think 41.5% market share over the last two years and have really tremendous momentum in that business.

Individual insurance, if you take a slightly longer view maybe four or five years, we've moved from 12% of new sales to now around 21% of new sales in the market and kind of reversed places with the number two player. So, good progress there.

And if you went into specific businesses like defined benefit solutions where we're somewhere around 45% to 50% market share of that business. And finally growing and picking up nice momentum in Sun Life Global Investments and so we're having significant market share over, and we're just really 12, 15 months into having five-year track records and are in the top five in that flow. So, I think we're making very good progress and all of that is related to investments in technology in some cases, in distribution in other cases and I just think the team's executing really, really well.

Paul Holden
Analyst, CIBC World Markets, Inc.

Q

Good. And then a big picture question probably for Dean. Your overall ROE the last two quarters has fallen below the 12% to 14% target. I realize it's not a quarterly target, but it's kind of trending below. So what do you view as the most direct or simple path to get back to that target, and don't need to know all [indiscernible] (01:01:36), but again, maybe the most direct or a simple path to getting back to target?

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

A

Well, thanks for the question, Paul. There's obviously a numerator and a denominator to that question. Blinding glimpse to the obvious. On the numerator, I think we – as we said, we continue to be committed to our medium-term goals, 8% to 10% EPS growth. And just to link that back to your prior question on Canada, you would have noted we talked about this at Investor Day that the underlying earnings in Canada have grown at 4.5% CAGR over the last three or four years. And as we look ahead, we would expect to see that number pick up to a higher number closer to 8%. And I think all of the investments that we've made in Canada, they're showing up in sales growth and starting to punch through in terms of net income will help deliver that.

So in terms of growing the numerator ROE, I think we have – we've set the table nicely. We've got lots of levers. And as we see progress in the U.S. business, U.S. repricing and other changes that Dan's making, continued growth in Asia and growth in Asset Management. We grew our earnings in Asset Management pillar again this quarter, and that should help on the numerator side.

The denominator, clearly, we have a fair bit of excess capital and that has grown over the last year, and that is one of the headwinds on ROE. And we've been there before. When we sold the VA business in the U.S., we were carrying out substantial slug of additional capital on the denominator and that had a headwind effect on the ROE. And I think we got good support from investors as we deployed that, thought about how to deploy it in a disciplined way, and I think we'll continue to do that as we think about our excess capital position today.

Paul Holden
Analyst, CIBC World Markets, Inc.

Q

Great. Thank you.

Operator: Your next question comes from the line of Mario Mendonca with TD Securities. Please go ahead.

Mario Mendonca
Analyst, TD Securities, Inc.

Q

Good afternoon. If we can go back to the In-force business in the U.S., I don't know how important the experience losses were to the quarter and I understand why you haven't disclosed that. But maybe what will be helpful is, it's a big business. The In-force business has got about CAD 4.5 billion account value and the International approaching CAD 12 billion in the U.S. So, what I'm trying to understand is, this business is – are these experience losses the sort of thing that you would adjust for or you would account for with reserve adjustments say in a Q3 or – because presumably you can't price your way out of this like you could in some of the Group Disability or stop-loss businesses. So, how do you address a period of experience losses like this? Probably for Kevin.

Kevin Morrissey
Senior Vice President & Chief Actuary, Sun Life Financial, Inc.

A

Yeah. Thanks for the question, Mario. This is Kevin Morrissey. So, just to remind everybody, as you mentioned, this is a Closed Block in the In-force Management, so it is in runoff. We continue to monitor it as well as the In-force on the International business where we're still selling. When I think about the experience this quarter, maybe I'll just break it down into a couple of the details. First on the mortality side, I did mention the seasonality of mortality and higher death claims.

And so when I look at the In-force Management where we had some loss overall and the company was positive, but the In-force Management was a loss, we've had elevated mortality losses for the last two quarters, but when I look back over the last five or six quarters, I'm not really seeing a trend there. So, at this point, that's not something that really concerns me.

When I look at on the lapse side, the loss was about I think about CAD 7 million on the In-force Management side. So, not a huge number after tax. It is still early in the year and it is certainly something that we'll continue to monitor. And it will certainly be part of our Q3 assumption and asset reviews. So, it's on the list with a number of other items. And we have to follow the data, we'll complete our full experience studies, which will be over a longer time horizon, and you'll hear more from us back in Q3 on that.

Mario Mendonca
Analyst, TD Securities, Inc.

Q

And on the International side, would the lapse experience there be similarly modest?

Kevin Morrissey
Senior Vice President & Chief Actuary, Sun Life Financial, Inc.

A

Yeah. It was even more modest, that's right.

Mario Mendonca
Analyst, TD Securities, Inc.

Q

Okay. So, ultimately, if this persists for any period of time, despite the size of the account value, we're not looking at large numbers here, if you had to adjust reserves?

Kevin Morrissey
Senior Vice President & Chief Actuary, Sun Life Financial, Inc.

A

Yeah. If we had to adjust, at this point, based on the trends we're seeing, we wouldn't be looking at something that would be that big, that's right.

Mario Mendonca
Analyst, TD Securities, Inc.

Q

That's helpful. Thank you.

Operator: Your next question comes from the line of Tom MacKinnon with BMO Capital Markets. Please go ahead.

Tom MacKinnon
Analyst, BMO Capital Markets (Canada)

Q

Thanks very much. Good afternoon. Question for Colm about the corporate segment. The expected profit in the corporate segment was a loss of CAD 39 million, and if we add that with the earnings on the surplus, we get a loss of CAD 23 million. And that CAD 23 million loss generally compares to numbers that jump around between like a positive 4% and negative 4%. So, something funny going on in the quarter. Maybe you can elaborate on that. I don't think it was expense related, because the corporate expenses are in fact down year-over-year and generally flat probably if we include the impact of currency. So, maybe you can elaborate on what's driving that in the quarter, and how we should be looking at that going forward, especially given the fact that you just redeemed some debt as well.

Colm J. Freyne
Chief Financial Officer & Executive Vice President, Sun Life Financial, Inc.

A

Yeah. So, no, I think the debt piece, I'd kind of leave that to one side. It wasn't a driver in terms of the impact in the quarter. On the expected profit, I didn't quite catch all the numbers you quoted, and on the corporate side...

Tom MacKinnon
Analyst, BMO Capital Markets (Canada)

Q

Loss of CAD 39 million expected profit.

Colm J. Freyne
Chief Financial Officer & Executive Vice President, Sun Life Financial, Inc.

A

Yeah. So that includes the UK, so in that sources of earnings view that we provide for corporate, you have to recall, that the UK is in there as well. So, the increase year-over-year in the expected profit/loss, that particular line item is CAD 22 million, so the UK would account for half of that. And the corporate expenses are higher. There's a few project costs that are going through in the first quarter, and I would remind you that with a lot of project activity underway, so for example getting ready for LICAT is an example of something that does cause us to run with a somewhat higher expense base.

We're also mindful that when we have fourth quarter, we've had some higher expenses in the past, and we've looked at our accrual rates, so we are accruing a little bit higher in respect of some items, so that would come through in the corporate segment. So, nothing unusual. We've looked at it pretty carefully. We look at the overall corporate segment excluding the UK in terms of the net loss in the quarter, and that loss, as you know, covers things like our governance costs, et cetera, we didn't really see anything in there that would cause us yet to be concerned. And just on that point around the UK, why did the UK decline by approximately CAD 10 million? Well, FX was a big factor and I think a lot of people start to forget that while the UK is not a separate pillar for us, but it does generate strong earnings. And with the decline in sterling year-over-year, that had a CAD 6 million impact for example on that line alone.

Tom MacKinnon
Analyst, BMO Capital Markets (Canada)

Q

Okay. But your corporate expenses were CAD 61 million and last year they were CAD 74 million. So this is the lowest level I see for corporate expenses in a quarter over the last nine quarters. So you talk about elevated corporate expenses, I can't see that in the disclosures that you have.

Colm J. Freyne
Chief Financial Officer & Executive Vice President, Sun Life Financial, Inc.

A

Yeah. So, Tom, I may need to take this one offline with you because I'm not...

Tom MacKinnon
Analyst, BMO Capital Markets (Canada)

Q

Okay.

Colm J. Freyne
Chief Financial Officer & Executive Vice President, Sun Life Financial, Inc.
A

...I'm not quite following your point. I hear your point, but as I said, there's no particular reason, no particular concern on our end around corporate expenses in the quarter.

Tom MacKinnon
Analyst, BMO Capital Markets (Canada)
Q

Okay. And then just a quick one for Dan. I know you guys talked when you got Assurant of $100 million in terms of cost saves and that two thirds of the accretion you were going to get was going to be through cost saves and was CAD 0.17 accretion from the acquisition by 2019. Is there any way if you can update us as to how you're progressing on these targets? We're about a year through Assurant right now.

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

Sure. First of all, on the expense portion of that, we had divided that up into three years, 2016, 2017 and 2018 primarily. And in 2016, we achieved the portion of the saves that we planned to, which was significant. And then, we believe we're still on target to achieve the accretion goals that we set out.

Tom MacKinnon
Analyst, BMO Capital Markets (Canada)
Q

Okay. Thank you.

Operator: And your next question come from the line of Darko Mihelic with RBC Capital Markets. Please go ahead.

Darko Mihelic
Analyst, RBC Capital Markets
Q

Hi, thank you. A question with respect to again, MFS and outflows. And the perspective that was given to me by a couple of my clients is that, what if these outflows don't stop? What if we continue to have quarter-after-quarter very large outflows? What would your plan B be?

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

Good afternoon. Well, I would say given the investment performance, it the outflows don't stop, you've got a greater industry problem that continues to persist. And so, our strategy is built around what our clients are ultimately going to need. When we look – our expectation of global equity returns in the next 10 years is returns are going to be about 4% a year in equities, given the starting valuation levels.

When we look at global fixed income markets, we think returns are going to be 3%. You take a blended return for balanced clients returns are going to be 4%. And so, if you can add a couple of 100 basis points of outflow to a client in a 4% return environment, they're going to pay for that, they're going to need that because indexed returns aren't going to provide enough return for clients to meet their investment goal.

So I think, you're talking about the basic thesis of the business, the active business. We continue to think that the active business will continue to be demand for the active business. And our strategy is to stay focused on providing return for clients, building really strong relationships with our clients, going deeper with our clients. And we believe that active is still relevant and we believe if we continue to do that through a cycle you can generate flows in this business.

Darko Mihelic
Analyst, RBC Capital Markets

Q

So there would be nothing done on the fee side, passive side, it would be effectively just run the business as is now.

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

A

Well, there isn't anything you can do on the passive side, that business is won. So, today you've got three big players. It's really two big players and State Street today. You've got BlackRock, Vanguard, State Street [indiscernible] (01:13:01) business. No one really can get into that business. It's a scale business. Those firms have scale. They've got massive investments in that business. And frankly given the fees, you wouldn't want to even be getting to get in that business today from scratch. And so that business has been won. I do believe and you've seen it with some competitors that fees will continue to come down in the active space.

We do, particularly, institutional sub-advised clients continue to come at us pretty hard on fees. And I think you'll continue to see fees come down. If you go over the last four years, active fees have come down 6%. So, we're not seeing a collapse in pricing in the business, but you are seeing some degradation of fees. But you contrast that with what's going on in the passive space, fees have come down 25% in that particular space. So, this is a through the cycle, you get revenue growth in this business because markets go up. If you control and drive some organic growth, you can grow earnings.

It's capital light, it generates high returns and net income converts to cash. And so our focus on the business is protecting the book of business, diversifying the business and ensuring that we can continue to perform well for clients through the cycle.

Darko Mihelic
Analyst, RBC Capital Markets

Q

Okay. Thanks for taking my question.

Operator: And your final question from the line of Gabriel Dechaine with National Bank National. Please go ahead.

Gabriel Dechaine
Analyst, National Bank Financial, Inc.

Q

Hey, I just didn't – I wanted to follow up on the Group. There was one element in my question that we didn't get a change to go over, but what was the – I guess, what was the cause behind the deterioration in stop-loss margins? I assume it's – you went pretty aggressively after sales that's usually the pattern. And then if I take that to what's going in the business today, and I see Group insurance sales in Canada doubled year-on-year, there is a large-case sale in there and I know it's a different geography. But how can I be comfortable with that type of growth?

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

A

This is Dan. Let me take the stop-loss portion of the question. And we have talked about this in previous quarters as well. We really saw adverse claims experience, higher claims than were expected. Now, very likely, there is some component to that of pricing but we also have seen an increase in large and very large claims than the number of large claims as well as the size of them. Some of that is actually attributable to a change that was made in the Affordable Care Act of about six-and-a-half years ago that eliminated annual and lifetime caps on benefits in employer-based plans in the U.S.

And that helps facilitate a lot of investment in specialty drug companies and investment in new drugs, and takes a while obviously for that to work its way through the pipeline and through the system. But some of the large claims that we've been seeing indeed are from specialty drugs including multimillion dollar drug claims, which is kind of remarkable.

So, we've done two things there. One is obviously made sure we're reflecting that experience in our pricing. But also we're taking actions to better manage and influence those claims. And then overall, obviously, we've adjusted our pricing to make sure that we've got adequate pricing to cover all experience regardless of what that is. And I'll let Kevin handle the Canada question.

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

A

Sure. Gabriel, it's Kevin speaking. So, yeah, we had some good new business in the Group Benefits business in Q1. It was driven largely by – the largest account in that group was won – I know for sure we – it wasn't won on price, it was won on capabilities in partnership with a third party administrator and so we feel very good about the quality of that business.

Coming back to the growth in the GB and GRS business overall, if you really look at our story, it's not so much about sales volumes, but about customer client retention over many years. So we've got lapse rate in Group Benefits and GRS that are really the best in the industry. And it's easy to underestimate the impact of that, but we're basically 2% below, around 3.5% competitors, around 5%, 5.5% lapse rate. So CAD 10 billion block that's CAD 200 million, you can think of as another CAD 200 million of sales that they're not achieving. Over five years, that's CAD 1 billion of revenue on a CAD 10 billion business, and that's really the story in both Group Benefits and GRS. In GRS, our client retention rate is 99%. So we feel good about that growth and the reality is in this business the existing clients are well more profitable than new business. And so we feel good about how we're growing the business by really focusing on the clients that we have and building from there and bringing on new business at a good clip, but not outsized.

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

And it's Dean Connor here. Before we wrap up the call, I just wanted to acknowledge the leadership changes that we announced in the quarter and in particular to acknowledge that this is Colm Freyne's last earnings call as the Chief Financial Officer of Sun Life Financial. And I think it's been 32 quarters, eight years, started in the teeth of the financial crisis. And has done a tremendous job, I think on behalf of the company but also on behalf of investors in supporting analysts and investors in better understanding how this company works. So, Colm thank you to you. And Kevin Strain, we welcome you. Kevin will be on the call for the second quarter call. And with that...

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

Great. Thanks, Dean. I'd like to thank all the participants on the call today. If there are any additional questions we will be available after the call. And 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: Thank you to everyone for attending. This will conclude today's conference call. You may now disconnect.