Sagicor Financial Company Ltd.

Second Quarter 2023 Earnings Conference Call

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Length: 35 minutes
CORPORATE PARTICIPANTS

George Sipsis
Sagicor Financial Company Ltd. — Executive Vice President, Corporate Development & Capital Markets

Andre Mousseau
Sagicor Financial Company Ltd. — President & Chief Executive Officer

Kathy Jenkins
Sagicor Financial Company Ltd. — Chief Financial Officer

CONFERENCE CALL PARTICIPANTS

Meny Grauman
Scotiabank — Analyst

Darko Mihelic
RBC Capital Markets — Analyst
Good afternoon. My name is Jenny and I will be your conference operator today. At this time I would like to welcome everyone to Sagicor Financial Company Ltd.’s Second Quarter 2023 Earnings 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. If you would like to ask a question during this time, simply press star then the number one on your telephone keypad. If you would like to withdraw your question, please press star two. Thank you.

Mr. George Sipsis, EVP, Corporate Development and Capital Markets, you may begin your conference.

George Sipsis — Executive Vice President, Corporate Development & Capital Markets, Sagicor Financial Company Ltd.

Great. Thank you, operator, and hello, everyone, and thank you for joining us today to discuss Sagicor’s 2023 second quarter. Our Q2 results, including the financial statements and the MD&A, along with the press release and the link to our live webcast is available under the Investor Relations tab on our website at Sagicor.com. This conference call is open to the financial community, the media, and the public, with a reminder that the Q&A period is reserved for the financial research analysts.

I would like to begin by referring you to the cautionary language and disclaimers in our materials and public filings regarding the use of forward-looking statements and the use of non-IFRS financial
measures and ratios, which may be mentioned as part of our remarks today. I would like to remind the audience that actual results regarding forward-looking information could differ materially and please note that a detailed discussion of Sagicor’s risk factors is provided in our MD&A and AIF available on the SEDAR+ website along with Sagicor’s website. A discussion of the assumptions underlying our 2024 expectations is provided in our earnings release.

Comments made in reference to the pending acquisition of ivari are made based on assumptions made in respect of business strategies, including economic conditions and other factors, and actual results may differ. Sagicor is currently awaiting receipt of regulatory approvals required under the Canadian Insurance Companies Act with respect to the acquisition of ivari. All other conditions for closing, except those that are only capable of being satisfied on closing, have been satisfied. We continue to expect to receive regulatory approvals for the acquisition in Q3 2023 with closing occurring shortly thereafter.

Lastly, unless otherwise noted, all dollar amounts referenced will be in US dollars, consistent with our reporting practice.

Joining me today is our President and CEO, Andre Mousseau; our Chief Financial Officer, Kathy Jenkins; and Anthony Chandler, our Chief Controller. We’ll begin with prepared remarks by Andre and Kathy, followed by a Q&A session.

With that, I will pass the call to our President and CEO, Andre Mousseau.
Thank you, George, and good afternoon everyone. Thank you for taking the time to join us today.

First, as George said, I’ll give some brief remarks focusing on our performance for the quarter. Then I’ll hand it over to Kathy to expand on our segment performance. Then I’ll provide an update on our outlook before we open up for analyst Q&A.

Sagicor had a strong second quarter. We delivered solid core results in each of our segments. We also benefitted from refinements to the inputs to our discount rates on liabilities, which reduced the negative mark-to-market accounting volatility that we observed in the first quarter of 2023. We believe that our estimated core earnings to shareholders this quarter of $13 million is a more accurate reflection of our underlying business performance.

The strong net income for Q2 translated to substantial total comprehensive income to shareholders of $43 million, which meant that we were able to substantially grow our book value during the quarter.

We will disclose a Drivers of Earnings analysis and adopt a non-IFRS core earnings measure in future quarters to enhance investors’ understanding of our underlying financial performance and the long-term performance and valuation of our business.

Now I’m going to hand the call over to Kathy to discuss the segment results in detail. Then I’ll return to discuss our outlook. Kathy?
Thank you, Andre, and hello, everyone.

Turning to our results. Revenues for the quarter came in at $313 million with year-over-year insurance revenue growth across all our segments. Net income to shareholders was $49 million. New business production was robust in Sagicor Jamaica and Sagicor Life and these segments posted net income to shareholders of $10.8 million and $8.7 million, respectively. Sagicor Life USA posted excellent sales during the quarter in a favourable competitive and investment environment and reported net income to shareholders of $54.6 million.

Last quarter we noted the volatility in our results due to the delinking of discount rates between the actuarial liabilities and supporting assets and that we would continue to review and refine the actuarial liability discount rate. As a result of the review of the inputs used to derive the liability discount rate at Sagicor Life USA, refinements were made that increased the rate, thereby decreasing the actuarial liability. This resulted in a $51.3 million after-tax increase in income at Sagicor Life USA. I would note that this income is excluded from the estimated core earnings of $13 million that Andre noted earlier.

Now on to each of our segments. At Sagicor Life, our operating segment in the Southern Caribbean, revenues were $108 million, a 19% increase year over year. The segment experienced double-digit new business insurance sales, which resulted in new business CSM of $14 million, a 23% increase year over year. These drove a 2% increase in total net CSM to $246 million. Net income to shareholders of $9 million was impacted by negative market experience. During Q2, management made...
certain reorganizational changes that resulted in the Sagicor General Insurance subsidiary now being reported within the Sagicor Life segment rather than Head Office and Other. Prior period amounts were restated to conform to current period presentation.

Sagicor’s share of Sagicor Jamaica’s net income to shareholders was $11 million, driven by strong individual life production and improving results in its short-term insurance businesses. Commercial banking saw revenue growth due to greater card payment activity and increased net interest margins. The current capital markets environment in Jamaica continues to negatively impact the investment banking division, leading to lower than targeted net income. Total net CSM remained relatively stable quarter over quarter as new business CSM of $8 million was mostly offset by amortization of CSM into profit.

Moving on to Sagicor Life USA. As mentioned during our Q1 call, we timed our production later in that quarter to take advantage of a more favourable competitive and investment environment, which moved settlement of some Q1 business into Q2. The USA segment generated $439 million in annuity sales in Q2, leading to robust growth in new business CSM compared to the previous quarter. Total net CSM was $208 million, an increase of 1% quarter over quarter, as strong new business CSM of $26 million from excellent production was partly offset by amortization of CSM into profit and some additional surrenders of pre-2017 fixed income annuities. These surrenders have released statutory capital in the US to be deployed into more profitable new business in 2023. Management actively monitors this product, adjusting pricing on business that is profitable to retain and redeploying capital in other business. Net income of $55 million for the US included the impact of the change in discount rate I
mentioned earlier of $51.3 million after tax. This income was offset by an unrealized loss this quarter on Playa shares of $12.3 million.

Now I’ll provide further detail on our estimated core earnings measure. We estimate core earnings to shareholders under the currently proposed definition for Q2 2023 as $13 million, which excludes $36 million of adjustments from net income to shareholders. The adjustments in the second quarter consist of $53 million of market experience gains, half a million in losses from changes in actuarial methods and assumptions, $4 million in one-time costs from IFRS 17 implementation and the ivari acquisition, $3 million in other items such as amortization of intangibles, and $10 million consisting of the tax effects of the aforementioned. The market experience gain in Sagicor Life USA was partially offset by market experience losses in Sagicor Life and Sagicor Jamaica. Later in the year we will publish a supplemental information package, including full drivers of earnings by segment, which will provide greater visibility into our financial performance each quarter.

Strength in our capital position persists with total capital of $2.1 billion, including total net CSM of $697 million being categorized as a component of capital. Our MCCSR ratio for our insurance businesses is 286% and our debt to capital ratio improved quarter over quarter to 30.4% due to an increase in total net CSM from strong new business and increased total equity driven by excellent total comprehensive income of $48 million during Q2. As mentioned in Q1, we intend to produce LICAT by year end 2023. Subsequent to quarter end we also strengthened our liquidity position with the addition of a $125 million revolving credit facility with a syndicate of Canadian banks. The facility is for general working capital purposes and is currently undrawn.
I’ll now pass it back to Andre.

Andre Mousseau — President & Chief Executive Officer, Sagicor Financial Company Ltd.

Thank you, Kathy.

Cutting through the noise of the accounting volatility, we are pleased with the $50 million of net income to shareholders delivered year to date in the first six months of the year and see it pretty reflective of our underlying business performance once you consider that it includes approximately $18 million of unrealized gains on the Playa shares year to date.

We remain very positive on the prospects for our business. The economic outlook for the Caribbean continues to be robust after a disproportionately difficult two years for our core Caribbean markets. The higher interest rate environment in the United States is making our unit economics of new policies more profitable and we’re seeing this with the spreads we’re achieving through the new annuity business that we write. In this environment, we were able to flex our production up in Q2 and further grow that business.

And we remain very excited about onboarding ivari. This acquisition will give us a new market for growth, increase the proportion of investment-grade assets on our balance sheet, and be significantly accretive to our book value and earnings per share. As George mentioned at the top of the call, we believe we are progressing well through the regulatory approval process and anticipate we will receive regulatory approvals for the acquisition in Q3 2023, with closing occurring shortly after receiving approval.
We are reiterating unchanged our guidance with respect to our financials pro forma that acquisition. We anticipate having shareholders’ equity of approximately $650 million to $725 million and CSM to shareholders of approximately $1.1 billion to $1.3 billion post close of the transaction. This means total shareholders’ equity and CSM combined to shareholders of approximately $1.8 billion to $2 billion. In 2024, the first full year post the combination, we reiterate our expectation of a return on shareholders’ equity of approximately 14% to 16%, high single-digit CSM to shareholders growth thereafter, and double-digit net income to shareholders growth post the acquisition. So, that math points you to net income guidance of $91 million to $116 million in 2024, which would be EPS of US$0.64 to US$0.81, or about C$0.86 to C$1.09. We expect to refine this guidance later in the year and believe we will have a very compelling case to equity investors once we have this transaction completed and under our belt.

With that, we’re ready to start the Q&A period please.

Q & A

Operator

Thank you. Ladies and gentlemen, we will now begin the question-and-answer session. If you have a question, please press the star followed by the one on your touchtone phone. You will hear a three-tone prompt acknowledging your request. Questions will be taken in the order received. Should you wish to cancel your request, please press the star followed by the two.

Your first question comes from Meny Grauman from Scotiabank. Please ask your question.
Meny Grauman — Analyst, Scotiabank

Hi. Good afternoon. First question, on the market experience line that you’re adjusting for, to get to the $13 million, trying to understand the main components of that. I think in your prepared comments it seems to me that a big chunk of that $51 million is related to that discount rate change that you were talking about, but I just wanted to make sure that I’m understanding that properly.

Kathy Jenkins — Chief Financial Officer, Sagicor Financial Company Ltd.

Yes. The market experience gains and losses is really the difference between the actual and expected market movements, impacting the insurance liabilities and the assets backing those liabilities, so within that is the $51.3 million that we saw as a result of the change in the discount rates.

Meny Grauman — Analyst, Scotiabank

And so the remaining portion would be something relatively small or are there other bigger numbers that are netting out? Are there other important components to that $52.7 million that we should be aware of?

Kathy Jenkins — Chief Financial Officer, Sagicor Financial Company Ltd.

There are other smaller pieces offset in the other segments, but nothing large like that.
Meny Grauman — Analyst, Scotiabank

Okay. Thanks for that. And then I just wanted to understand the outlook for the US. You highlighted a favourable competitive and investment environment that benefitted the business in Q2. We’re in Q3, so relatively early days, but just wondering how you see that competitive and investment environment. Is that changing? What’s the outlook for Q3 overall for the US?

Andre Mousseau — President & Chief Executive Officer, Sagicor Financial Company Ltd.

I’d say the environment remains very constructive. In terms of spread, it’s well ahead of what we would have had in our modelling plans. The $440 million of production in Q2 was ahead of what our aggregate plan would be. It would be a catch up for Q1 where production was lower than our run rate target. So, at this point we would expect that production in Q3 would be as profitable as it is in Q2, but managing capital to budget, we’d expect production somewhere between where Q1 was and where Q2 is.

Meny Grauman — Analyst, Scotiabank

Understood. And then I wanted to understand a few of the dynamics impacting Sagicor Life. I think I saw in the prepared documents new products and services being launched in Q3 and Q4, so just wanted to understand what kind of launches you have ready to go, and can you highlight the financial impact of those launches? Is there anything material there that we should be aware of?
Andre Mousseau — President & Chief Executive Officer, Sagicor Financial Company Ltd.

The focus within Sagicor Life is on changing the channel for an increased emphasis on technology. We’re doing more and more with respect to direct-to-consumer through the digital channel there, and it’s early days of the digital strategy that we’re launching in conjunction with launching the digital bank, which went live earlier this year in Barbados. So, it’s not new products in terms of whole new categories beyond the ones that we’re in, it’s more around streamlining and improving the way that we access those customers. It’s our traditional core individual life products through a digital channel.

Meny Grauman — Analyst, Scotiabank

Got it. That’s it for me. Thank you.

Operator

Thank you. Your next question is from Darko Mihelic from RBC. Please ask your question.

Darko Mihelic — Analyst, RBC Capital Markets

Hi. Thank you. Good afternoon. I just have a few modelling questions, please, but before I get there, just a quick question to Kathy about the adjustment to the discount rate. Am I correct in thinking that work is now all done or is there potential for further work on the discount rate or any other aspect of IFRS 17 in the works right now?
Kathy Jenkins — Chief Financial Officer, Sagicor Financial Company Ltd.

This relates to reviews of the financial inputs, so it’s something we would look at each quarter as normal course, and then in Q3 is when we take a look at our management assumptions on the actuarial liabilities. So, we continue to look at it.

I’m not sure if there’s anything else, Andre. That’s part of normal course.

Andre Mousseau — President & Chief Executive Officer, Sagicor Financial Company Ltd.

Well, normal course in some sense but, Darko, I think the goal in setting up what we’ve put forward this quarter is a calculation that will result in less volatility around the movement of liabilities versus the assets than what we saw in the first quarter and the second quarter. When we were talking about the first quarter, we had a net income number that we suspected was low because even as our assets appreciated our liabilities appreciated more in Q1, much more than you would have expected given our ALM position, and so Kathy’s right; you look at this every quarter, and coming up in Q3 we’re going to do a comprehensive review of the entire book and valuation, but the goal of this refinement to the calculation in Q2 was to make it less volatile going forward.

Darko Mihelic — Analyst, RBC Capital Markets

Okay. But just to be crystal clear, I understand that the liability rate will go up and down, as will, obviously, the assets, and whatever drives the liability will be however you’ve set that liability discount rate. But what I’m talking about specifically is it sounds like you refined something; you actually altered a
methodology somewhere or somehow. I understand in every quarter these things will change, but what I’m interested in is the refinement that occurred; that that’s a one-time thing. Correct or no?

Andre Mousseau — President & Chief Executive Officer, Sagicor Financial Company Ltd.

You reserve the right to change it, but we would not expect to do a refinement of this magnitude every quarter.

Darko Mihelic — Analyst, RBC Capital Markets

Okay. And now that you’ve done that, going to your commentary, Andre, where you mentioned year to date $50 million of earnings ex unrealized gains of $32 million, is that another way of interpreting that, year to date, $32 million would more or less be core? Or I guess what I’m asking in a backhanded way is, and I’m not sure you’ve done this technically, but if the current setup for the liabilities were used in Q1, what would the core earnings have been in Q1 and Q2, and year to date what do core earnings look like. Does that make sense?

Andre Mousseau — President & Chief Executive Officer, Sagicor Financial Company Ltd.

It does make sense and that’s what we’re trying to allude to. In my comment I said we’re at $50 million in net income to shareholders. That includes $18 million of the unrealized equity gains, so let’s call that $32 million for half the year. In this quarter’s disclosure we have $13 million as an estimate of our core, so both those numbers would annualize to a number in the $50 million to $60 million ZIP code in terms of sustainable, non-noisy, annualized net income. And we will have more disclosure around the
core earnings once we think it’s fully ready to go, but directionally that’s where we would have expected the profitability of the Company to be right now on a core basis.

Darko Mihelic — Analyst, RBC Capital Markets

Okay, that’s helpful. Thank you. And then if I look at this quarter’s, and this has been something that we’ve bumped into all reporting period long with all the other lifecos, is trying to sort of nail down... Like presumably within your core earnings view, you would have a core expected investment result, right? Is it fair to say that the result this quarter, once I take out the $52 million and change of adjustments, that is a relatively good clean number? And if I take that number, would it be similar proportionate to the general account for ivari? I guess what I’m getting at is, is that a clean investment number this quarter? And proportionately, I would think ivari’s number should be lower, but I’ll leave it there for you. I’ve only got one quarter of ivari’s results and I can kind of get a sense of what you’re guiding towards, so I just want to understand if the big difference between your guide on ivari and what the first quarter result would look like is really all in the investment account. Or the investment result, sorry.

Andre Mousseau — President & Chief Executive Officer, Sagicor Financial Company Ltd.

Kathy, do you want to give a comment for ours and then I can address ivari?

Kathy Jenkins — Chief Financial Officer, Sagicor Financial Company Ltd.

I just want to make sure I’m clear. You’re trying to get a sense of is this kind of more of a run rate? Is that what you’re trying to get behind?
Darko Mihelic — Analyst, RBC Capital Markets

Yeah. So clearly, this quarter, first with respect to just Sagicor, overall, all group level, I take the investment result, I make the adjustment for the $52.8 million, is that the way I should think about your investment result sustainably as a core expected investment result?

Kathy Jenkins — Chief Financial Officer, Sagicor Financial Company Ltd.

Yeah, if you took that out, that would be more the expected investment result. And that’s what we took out to come up with that $13 million core earnings. So that’s kind of more akin to what would be expected.

Darko Mihelic — Analyst, RBC Capital Markets

Okay. That’s helpful. And then the secondary question to that is, when I look at your forward guidance, $91 million to $116 million, I can sort of pop in some idea there for ivari. It looks pretty different though from Q1. I realize it’s only Q1. So is the difference the investment result? Is that what I should be looking at or is that what you’d point me to, Andre?

Andre Mousseau — President & Chief Executive Officer, Sagicor Financial Company Ltd.

I’d rather not talk about the source of earnings for ivari until we’ve closed the transaction. I would say the guidance that we’re giving is a budgeted kind of clean core number, and there is going to be noise around that every quarter. If we were taking a different view of what that net income would
be, we would be changing our guidance right now, but I think we’re comfortable with what we’ve guided towards. That number and our own number combined for 2024 is all kind of a clean core number.

Darko Mihelic — Analyst, RBC Capital Markets

Okay. And then my last question is just, and I apologize, I may have made some modelling errors with Sagicor and ivari, and specifically I think it revolved around the negative goodwill. So, I just want to confirm a couple of accounting, and if you can imagine, in all my career I’ve never had to actually model negative goodwill, so kudos to you guys. But when you have negative goodwill, it’s my understanding that it’s run through the income statement. Is there any tax implication around that?

Andre Mousseau — President & Chief Executive Officer, Sagicor Financial Company Ltd.

No, I don’t believe so.

Darko Mihelic — Analyst, RBC Capital Markets

Okay. So, if I just run that through and run it through the income statement additive to equity, I should end up in that ballpark range you guys gave. Okay. That makes a lot of sense to me. The last question then is, when you guys mentioned the accretion to 2024 with the full year of ivari, is that accretion sort of to assume that it’s as if ivari wasn’t there in 2023?

Andre Mousseau — President & Chief Executive Officer, Sagicor Financial Company Ltd.

Yes, but having the full year will also be accretive on 2023 if we have it for one quarter. Now, net income for 2023, based on our guidance, is going to be unusually high if we run that negative goodwill
through the income statement. But I guess the accretion point is just very simple earnings per share, which is going to be significantly higher with than without.

**Darko Mihelic — Analyst, RBC Capital Markets**

Yeah, absolutely. And there’s no interesting little mathematical gymnastics around cost of debt or anything like that included in your accretion. I realize you’re not giving me an actual accretion estimate, but I just want to make sure, as I sit here and think about it, there aren’t any really big moving parts apart from the ivari contribution.

**Andre Mousseau — President & Chief Executive Officer, Sagicor Financial Company Ltd.**

No. There’s no corporate finance adjustments of let’s assume you normalize the cost of capital. We’re just saying earnings per share with; earnings per share without; number is significantly higher with.

**Darko Mihelic — Analyst, RBC Capital Markets**

Okay. And maybe just roughly speaking, I’m not sure when you intend to provide the drivers of earnings and segmented core, but are you intending to also give us like a flow of the CSM per segment?

**Andre Mousseau — President & Chief Executive Officer, Sagicor Financial Company Ltd.**

Even if it wasn’t in the drivers of earnings when we put out a statistical supplement, we would show beginning CSM runoff into the income statement, any changes, and then new CSM from new business.
Darko Mihelic — Analyst, RBC Capital Markets

Okay. And when you say LICAT, you’ll get to LICAT by year end, you clearly mean just for the overall company, right? I mean presumably, when you close ivari, ivari will have its LICAT and you’ll make that available to us?

Andre Mousseau — President & Chief Executive Officer, Sagicor Financial Company Ltd.

Yeah, correct. ivari has a LICAT today. Our Jamaican subsidiary right now is moving to a Jamaican version of LICAT, which will be finalized later this year. So what we’re talking about is like what we do for the MCCSR now, just update that to say, okay, all of the lifecos combined, this is the LICAT.

Darko Mihelic — Analyst, RBC Capital Markets

Okay. Excellent. Thank you very much for your time and for answering my questions.

George Sipsis — Executive Vice President, Corporate Development & Capital Markets, Sagicor Financial Company Ltd.

Darko, it’s George here. I just wanted to confirm your question on the CSM, if your question is different than what we already disclosed in the MD&A?
**Darko Mihelic — Analyst, RBC Capital Markets**

No, I just want to make sure that the CSM is there for ivari. The reason why I ask is it just seems like, well, we can take this off line. There’s a little bit of technicality around ivari and I realize you guys don’t want to talk too much around ivari, so we could probably just take this off line.

**George Sipsis — Executive Vice President, Corporate Development & Capital Markets, Sagicor Financial Company Ltd.**

Yep. Sounds good.

**Operator**

Thank you. There are no further questions at this time. Please proceed.

**George Sipsis — Executive Vice President, Corporate Development & Capital Markets, Sagicor Financial Company Ltd.**

Great. Thank you, operator, and thank you, everyone, for joining the call today. A replay of this call will be available for one month on our website and a transcript will be posted as soon as available. If you have any additional questions, please do not hesitate to reach out to any one of us. With that, thanks again for your participation and interest today. Have a great day, everyone.

**Operator**

Thank you. The conference has now ended. Thank you all for joining. You may all disconnect.