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SLF.TO - Q2 2024 Sun Life Financial Inc Earnings Call

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## PRESENTATION

**Operator**

Good morning, and welcome to the Sun Life Financial Q2 2024 conference call. My name is Gaylene, and I will be your conference operator today. (Operator Instructions) And the conference is being recorded. (Operator Instructions) The host of the call is David Garg, Senior Vice President, Capital Management and Investor Relations. Please go ahead, Mr. Garg.

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**David Garg** - *Sun Life Financial Inc - Senior Vice President, Capital Management and Investor Relations*

Thank you and good morning, everyone. Welcome to Sun Life's earnings call for the second quarter of 2024. Our earnings release and the slides for today's call are available on the Investor Relations section of our website at sunlife.com. We will begin today's call with opening remarks from Kevin Strain, President and Chief Executive Officer. Following Kevin, Tim Deacon, Executive Vice President and Chief Financial Officer, will present the financial results for the quarter.

After the prepared remarks, we will move to the question-and-answer portion of the call. Other members of management are also available to answer your questions this morning. Turning to slide 2, I draw your attention to the cautionary language regarding the use of forward-looking statements and non-IFRS financial measures, which form part of today's remarks. As noted in the slides, forward-looking statements may be rendered inaccurate by subsequent events. And with that, I'll now turn things over to Kevin.



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**Kevin Strain** - *Sun Life Financial Inc - President, Chief Executive Officer, Director*

Thanks, David, and good morning to everyone on the call. I hope you're all having a great summer. Turning to slide 4, we delivered strong second quarter results with a record $1 billion in underlying net income, representing 9% growth over the prior year, underscoring the strength of our diversified business strategy and our commitment to drive growth and deliver long-term value for our clients and our shareholders. Our results this quarter were driven by strong individual protection sales in Canada and Asia, while US Group Benefits continues to perform well.

Our wealth and asset management businesses saw good earnings momentum on increased assets under management. Strong individual protection sales for the quarter were driven by stronger sales from both SLFD and our third-party channel in Canada, strong momentum from our bancassurance partnership in Hong Kong and our joint venture sales in India. Strong individual and group protection sales drove our new business CSM growth, which was up 62% year-over-year.

Wealth and Asset Management results were lifted by higher fee income from MFS. We are also pleased to have executed the largest transaction in the Canadian pension risk transfer market by a single insurer, representing a $1.2 billion institutional sale in our defined benefit solution business. Our underlying earnings were partially offset by continued headwinds in our US dental business.

Most of the Medicaid dental business is being repriced during 2024. And as we reprice, we are seeing increased premium rates more consistent with our expectations. As a result, we continue to expect underlying earnings levels from dental to be approximately USD 100 million for 2025. MFS continues to experience net outflows this quarter at USD 14.8 billion. This was driven by secular shifts from active to passive, public to privates and alternatives, as well as cyclical impacts of investors remaining on the sideline given the high interest rates. We are confident in the actions that MFS is taking to address these challenges, including building out their retail capabilities, focus on meeting their Clients' needs and a diverse range of investment products, including active ETFs and separately managed accounts.

Our asset management and wealth pillars continue to have strong fundamentals with total SLF assets under management now $1.47 trillion, up 7% over last year. Reported earnings were lower than underlying earnings, primarily due to market-related impacts driven by the restructuring charge and real estate. Real estate continued to experience headwinds consistent with the overall industry environment.

In the quarter, we took a restructuring charge related to expense reductions, and we expect over $200 million of pretax savings to be delivered by 2026. Expense initiatives ensure that we stay efficient and competitive, helping us deliver on our purpose by aligning resources. Finally, we continue to maintain a strong capital position, reflecting our disciplined financial management and emphasis on capital-light businesses. Underlying ROE for the quarter of 18.1% is in line with our medium-term financial objective, while our LICAT ratio at SLF remained strong at 150%.

Turning to slide 5. This quarter, we delivered on several key business initiatives that helped drive our Client Impact Strategy forward. We continue to progress on our digital and innovation capabilities to support Client health and financial security. We are scaling Generative AI across Sun Life with thousands of Sun Lifers involved in more than 20 experiments to optimize, automate and transform Client experiences.

In the US, the dental team is using Generative AI to help Sun Life improve accuracy and make quicker recommendations. We also expanded our partnership with Goodpath in the US, offering disability members virtual care to help them better look after their physical and mental health. In Vietnam, a new point of sale platform allows agents to provide a digitally enhanced Client onboarding experience. This platform enables enhanced needs analysis in addition to a faster paperless application with 98% of applicants enrolled within one business day.

In Canada, we introduced Sun Life Term Insurance for Diabetes, a first-of-its-kind insurance solution designed to empower Canadians living with diabetes to make health and financial decisions on their terms. Recognizing the unique challenges of this condition, this product offers a higher chance of approval compared to conventional life insurance, more affordable premiums, and access to a customized care plan.

These capabilities and offerings reinforce our commitment to finding new and innovative ways to deliver on our Purpose. Turning to asset management, we continue to strengthen our position as a market leader. This quarter, SLC Management unveiled SLC Global Insurance Group, a dedicated team focused on serving the complex needs of the world's leading insurance companies with bespoke solutions.





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Our deep insurance heritage, combined with our diverse suite of investment capabilities, has allowed us to create a differentiated and tailored experience for Clients. SLC also launched the Scotia Private Real Estate Fund, distributed through Scotiabank. Powered by BGO's deep real estate investment capabilities, this new product will give investors an opportunity to diversify their private real estate assets that offer attractive income-focused returns, while hedging against inflation.

SLC has grown tremendously since its inception over a decade ago. To support our plan for SLC's continued growth, I'm pleased to announce that Steve Peacher, President SLC, has been appointed to Executive Chair, SLC Management. Sonny Kalsi, Co-CEO, BGO, has been appointed to President and CEO, SLC.

Sonny will continue to spend the substantial majority of his time as co-CEO of BGO in partnership with John Carrafiell. Steve will partner with Sonny and the leaders across the SLC group of companies to help set the future strategic direction of the firm with a focus on combining the strength of its global platform to benefit new and existing Clients.

Additionally, Steve will continue to have oversight of the firm's businesses with a particular focus on leading the growth of SLC Fixed Income and driving the firm's high net worth strategy. This announcement, along with Jack Paris' appointment as Chief Executive Officer of InfraRed last July, and Chris Wright's appointment as President of Crescent Capital Group this year, lays the foundation for SLC's leadership for many years into the future.

We also completed our third sustainability bond offering, issuing $750 million. In line with our sustainability bond framework, the proceeds from this bond offering will help fund green and social projects that support the health of communities such as investments in hospitals, long-term care and emergency shelters.

Finally, we continue to be recognized for our commitment to drive meaningful, positive impacts for our Clients, society and the environment. Sun Life was selected by Corporate Knights as being one of the 50 Best Corporate Citizens in Canada for the 19th time.

In closing, we had a strong quarter against our medium-term objectives with underlying EPS growth of 10% and an ROE of 18.1%. We also ended the quarter in a strong capital position with a LICAT ratio of 150% and have announced our intention to renew our normal course issuer bid to purchase up to 15 million common shares, subject to regulatory approval. We are confident in the resilience of our strategy, our focus on execution and our sustained commitment to deliver on our Purpose.

With that, I will turn the call over to Tim, who will walk us through the second quarter financial results.

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**Tim Deacon** - *Sun Life Financial Inc - Chief Financial Officer, Executive Vice President*

Thank you, Kevin. Good morning, everyone. We're now on slide 7. We are pleased with our strong results this quarter. Underlying net income of $1 billion is up 9% and underlying earnings per share of $1.72 is up 10% year-over-year, achieving the higher end of our medium-term growth objective. Underlying return on equity of 18.1% also achieved medium-term objectives, supported by strength across our diversified businesses.

Wealth and asset management comprised 41% of Q2 underlying earnings and was up 9% over the prior year on higher fee income, largely due to higher asset levels driven by equity market appreciation. This was partially offset by higher expenses.

Group health and protection businesses comprise 28% of underlying earnings and were down 15% year-over-year. Results reflected strong business growth in the US Group Benefits and Canada, that were more than offset by unfavourable morbidity experience and lower US dental results. Individual Protection comprised 31% of underlying earnings and was up 31% from last year, driven by business growth in Asia and Canada and favourable mortality experience across our businesses.

Reported net income for the quarter was $646 million. The difference between underlying and reported net income was driven by unfavourable market-related impacts, a restructuring charge of $108 million post-tax or $0.18 per share, acquisition related items and the amortization of





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intangible assets. The restructuring charge reflects actions taken to improve productivity and help continue to deliver earnings growth at the higher end of medium-term objectives.

Actions under the program included accelerated digitization of our business, addressing duplicative and redundant capabilities and optimizing our external spend. We expect these actions to be implemented over the next 18 months and deliver over $200 million pre-tax in cost efficiencies by 2026. Market-related impacts were primarily driven by unfavourable real estate experience. This reflects modestly negative total returns in the quarter compared to our long-term expectations of approximately 2% per quarter, primarily from market-driven cap related increases.

We will continue to be cautious on real estate returns in the near term. We are long-term investors in real estate and on a 10-year basis, our actual returns are performing in line with our long-term assumptions. Our balance sheet and capital position remains strong with an SLF LICAT ratio of 150%, up 2 percentage points from the prior quarter due to strong organic capital generation, a new disclosure for us, of $588 million in Q2 and a debt issuance this quarter to pre-fund an expected third quarter redemption.

Holdco cash remained strong at $2 billion and we remain active on our share buyback program, repurchasing 4.1 million shares this quarter. We announced our intention to renew our program later this month, pending regulatory approval. Our leverage ratio remains low at 22.6%. Also of note, we had record new business CSM of $437 million, which was up 62% over the prior year, reflecting strong sales in Hong Kong and Canada.

Total CSM is now at $12.5 billion, up 11% year-over-year, representing a growing source of future profits. And finally, book value per share increased by 8% over the prior year, demonstrating our ability to generate growth while returning value to our shareholders.

Now let's turn to our business group performance, starting on slide 9 with MFS. MFS underlying net income of USD 194 million was up 4% year-over-year, as higher fee income from average net asset growth more than offset higher expenses. Reported net income of USD 194 million was up 4% year-over-year. Pre-tax net operating margin of 36.5% was in line with prior year. And AUM of $618 billion was up 5% over the prior year given higher markets, but down 2% from the prior quarter driven by net outflows.

Outflows in the quarter included two large institutional mandate redemptions and retail net outflows. Retail outflows reflected the continued preference in the current environment for shorter-term interest-bearing products. Long-term investment performance for MFS remained good, with 97% of fund assets ranked in the top half of their respective Morningstar categories for 10-year performance.

Turning to slide 10, SLC Management generated underlying net income of $42 million, down 5% year-over-year as fee-related earnings growth was offset by higher compensation and seed financing costs. Fee related earnings of $65 million was up 5% year-over-year on continued growth in fee earning AUM. Reported net income of $9 million increased $12 million, as the prior year included mark-to-market losses on a real estate investment which didn't recur.

Capital raising of $3 billion, remained resilient with solid fundraising in BGO's Asia Value Fund and US Diversified Equity Fund. Deployments of $6 billion were up $1.3 billion over the prior year, primarily from strong opportunities in fixed income and private credit in the quarter. Total AUM of $227 billion was up $9 billion from the prior year.

Turning to slide 11. Canada delivered record results with underlying net income of $402 million, up 8% year-on-year on strong insurance business growth and higher net investment results. Reported net income of $292 million included unfavourable market-related impacts. Wealth and asset management earnings were up 18% year-over-year on higher fee-related earnings and lower expenses. Results included a $1.2 billion transaction in Defined Benefit Solutions, the largest sale in the Canadian pension risk transfer market by a single insurer.

Group health and protection, underlying earnings were down 5% year-over-year as business growth and higher investment contributions were more than offset by less favourable, though still positive, morbidity experience. Group health and protection sales were down 7% year-over-year due to lower large case sales. Individual protection earnings were up 18% year-over-year, driven by favourable mortality experience and higher investment contribution. Individual Protection sales were up 8% due to higher Par Life sales.



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Turning to slide 12. US underlying net income of USD 149 million was down 7% from the prior year, driven by unfavourable morbidity experience and dental results. Reported net income of USD 91 million includes market related impacts, acquisition related expenses and the amortization of intangibles. In Group health and protection, our Group Benefits benefited from strong revenue growth and favourable experience in Employee Benefits. This was more than offset by lower dental results, which I will cover in more detail on the next slide.

US Group sales of USD 243 million were down 24% year-over-year, driven by four large case government dental sales in the prior year, which occur periodically. Individual protection underlying earnings were up significantly over the prior year from favourable mortality experience.

Turning to slide 13, we provide additional details on our US dental performance. As we've mentioned in prior quarters, the headwinds experienced in our US dental business are largely driven by the impact of the Medicaid redetermination process following the end of the public health emergency. Over the past 12 months, state governments have disenrolled approximately 19% of our Medicaid membership base, which has impacted premiums. Disenrollments are now substantially complete as of the end of July.

Further, we have experienced higher utilization from the Medicaid members staying in plan compared to those who were disenrolled, resulting in higher-than-expected loss and expense ratios. Despite these current headwinds, we maintain a favourable outlook for our dental business and expect to deliver underlying earnings of approximately USD 100 million by 2025.

We will achieve this level of profitability through key actions already underway, including ongoing cost and expense management initiatives, repricing efforts on our existing block of Medicaid business and from new contract sales across Medicaid, Medicare Advantage and commercial business lines.

Slide 14 outlines Asia's results for the quarter. Underlying net income of $179 million was up 19% year-on-year on a constant currency basis, driven by strong business growth in Hong Kong, our joint ventures and high net worth. Reported net income of $151 million includes market related impacts. We continued to see strong sales momentum in individual protection, particularly in Hong Kong and India, reflecting our expanded distribution capabilities.

The strong sales also drove new business CSM of $220 million in Asia, up 82% from the prior year. Total Asia CSM increased 17% year-on-year. Overall, we're pleased with our strong Q2 results. We're entering the second half of the year with positive business momentum, having achieved all of our medium-term objectives. Our diversified and attractive portfolio of businesses, our strong LICAT ratio of 150% and our differentiated, Purpose-driven culture give us confidence to continue to deliver on our Client Impact Strategy and financial objectives.

With that, I will turn the call over to David for the Q&A portion of the call.

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## QUESTIONS AND ANSWERS

**David Garg** - *Sun Life Financial Inc - Senior Vice President, Capital Management and Investor Relations*

(Event Instructions) I will now ask the operator to poll the participants.

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**Operator**

(Operator Instructions)

Our first question is from Meny Grauman, Scotiabank.

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**Meny Grauman** - *Scotiabank Global Banking and Markets - Analyst*

Hi. Good morning. Wanted to ask about the restructuring charge and just get a better understanding of what cuts you're making and where, from a segment point of view as well. Thanks.

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**Tim Deacon** - *Sun Life Financial Inc - Chief Financial Officer, Executive Vice President*

Hi. Good morning, Meny. It's Tim. Thanks for the question. First, I would say that financial discipline is a key part of our Client Impact Strategy and is a priority for us. So I would characterize this as a modest enterprise-wide program that we expect to execute over the next 18 months. And it's really across all of our business groups and corporate functions. And the types of areas that we're focused on are opportunities to accelerate the digitization of our business, eliminating duplicative or redundant capabilities and optimizing our external spend.

I would say we've run similar programs from time to time. So this is not new for Sun Life, but it's been some time since we've executed on a focused program like this. And as we've indicated in our disclosures, we expect these actions to deliver over $200 million pre-tax of efficiencies by 2026 and this is really to help moderate expenses and support the earnings growth at the top end of our MTOs.

So you'd expect the majority of this would flow through earnings over time, starting in the second half of this year through 2026 with the small portion being strategically reinvested to help accelerate our digital transformation and areas of investment in AI. So it will really show up in a variety of line items, including other expenses, other fee income, which is net of expenses, our corporate segment results and to some extent, in CSM.

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**Meny Grauman** - *Scotiabank Global Banking and Markets - Analyst*

So just to clarify, so pretty broad-based across segments like we shouldn't expect one segment to show more of the benefit of that $200 million that you're indicating versus another?

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**Tim Deacon** - *Sun Life Financial Inc - Chief Financial Officer, Executive Vice President*

No, that's right. It's quite broad-based across all of our business groups.

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**Meny Grauman** - *Scotiabank Global Banking and Markets - Analyst*

And then just as a follow up. So you took the restructuring charge, non-core through corporate. Are there any benefits coming through this quarter already in any of the segments on an adjusted basis?

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**Tim Deacon** - *Sun Life Financial Inc - Chief Financial Officer, Executive Vice President*

Yeah. A small portion has come in, but I would expect that to ramp up in the second half of this year as the actions that we're taking will occur over time, but you'll start to see that coming through, as I said, through the second half of this year on rateably through to 2026.

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**Meny Grauman** - *Scotiabank Global Banking and Markets - Analyst*

Would you be able to quantify what's coming through this quarter already?

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**Tim Deacon** - *Sun Life Financial Inc - Chief Financial Officer, Executive Vice President*

It's not very material in the grand context. It would be probably more in the second half.



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**Meny Grauman** - *Scotiabank Global Banking and Markets - Analyst*

Okay. Thank you.

**Operator**

The next question is from Tom MacKinnon, BMO Capital Markets.

**Tom MacKinnon** - *BMO Capital Markets - Analyst*

Yeah. Thanks very much. Maybe a question for Kevin. I understand that the partnership with MFS has been a long term, well-entrenched partnership, but kind of consistent net outflows really make it tough to be able to grow over time, with more normal markets, in line with your medium-term objective. So you can kind of see that if outflows are kind of 2% of the AUM in markets, you can grow at an 8% -- this is like a 6% grower, not the 8% to 10% you would want.

So in your talks to the Board, how do you justify this? Is it just strictly because you like the free cash flow? And I guess as a follow-up, are -- I assume the broad-based expense cuts that you're implementing are some of those must be in MFS and how do you think that should impact margins there? Thanks.

**Kevin Strain** - *Sun Life Financial Inc - President, Chief Executive Officer, Director*

Thanks for the question, Tom. It's Kevin. So MFS is absolutely included in our medium-term objectives and as part of those numbers that we give. So when you think about our medium-term objectives, we've factored in what MFS is going to contribute to that. MFS is an important part of our asset management strategy. We're the largest asset manager in the country. We have $1.47 trillion in assets under management. And we like the fact that we go from public equities and public fixed income into the alternatives and a growing asset management business that’s sort of combined between Manjit’s leadership and Steve in Asia.

So MFS is an important part of that. For sure they are, and you heard this in my opening remarks, they are in a cycle where they've had some headwinds around passive and alternatives, that's why we built out the alternatives platform. But we do believe that they're taking all the right actions.

They're doing the right things. They have a strong team. They're Client focused. And so they're an important part of this company and they're an important part of our overall asset management strategy. And as I said, that goes all the way. We like the fact that it goes from public equities and fixed income right to alternatives.

**Tom MacKinnon** - *BMO Capital Markets - Analyst*

And the fact that it doesn't kind of -- hasn't really hit your medium-term objectives even if you look back, you know, for the last seven or eight years. What is it that -- what does it really contribute to this story then if it's not growing at the 8% to 10% that you want it to grow at?

**Kevin Strain** - *Sun Life Financial Inc - President, Chief Executive Officer, Director*

Well, as you know, MFS AUM has been growing despite the fact that they've been in net redemptions. And I think that growth has been part of the earnings story, but they've also been an important part as you noted of cash flow. And they send cash up to the Holdco, which has allowed us to do the M&A work and the capital work we've done over the past 10 years, right? So if you look at the significant deployment of capital we've done, MFS has been a good supporter of that deployment of capital.





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**Tom MacKinnon** - *BMO Capital Markets - Analyst*

Okay. Understood. Thanks.

**Operator**

The next question is from Doug Young, Desjardins.

**Doug Young** - *Desjardins Securities Inc - Analyst*

Hi. Good morning. Maybe just a kind of a big picture question for -- it's like $1.72 of underlying earnings Kevin, like is this the true earnings power of the company. Obviously, it was a lot less last quarter and it's bounced around a little bit. And can you talk a bit about when you think of that and trying to gauge whether that is the case. Like what went for you and against you this quarter when you think through that?

**Kevin Strain** - *Sun Life Financial Inc - President, Chief Executive Officer, Director*

So, Doug as we talked about -- I see last quarter as more of the anomaly and this quarter as a return to sort of what our expectations would have been. We had a number of things that went against us last quarter, and we talked about those. For sure the dental results will continue to impact us this year, but we see ourselves earning our way through that. So I see this as a return to more of what our expected levels of underlying earnings would be.

**Doug Young** - *Desjardins Securities Inc - Analyst*

Okay. And then -- Okay. I'll leave it at that. And then, Dan, on the US stop-loss side, you had negative morbidity experience yet it was attributed to just normalizing claims utilization. So does this imply that you're baking in more COVID utilization into your pricing? Or can you help me think through this and talk about pricing trends in this business and why if dental gets better, should we -- obviously, there's going to be potentially a deterioration in the stop-loss business. Why shouldn't we be kind of worried about those two opposing trends?

**Dan Fishbein** - *Sun Life Financial Inc - President - Sun Life U.S*

Sure, Doug. What we've seen this year is, as we've talked about, the normalization of utilization, especially hospital utilization and things like outpatient surgery. That normalization back to pre-COVID levels happened a little faster over the past two or three quarters than I think anybody was expecting. It had been happening gradually over time. Most likely that it is due to hospitals, big hospital systems, especially now being able to staff fully when that was a challenge for quite some time, even lagging after the worst of COVID.

So we seem to be back to normal utilization. As far as the particular sequential quarter results, we do have some seasonality in our reserving. Generally, the way the reserves emerge, we release some reserves in the first and fourth quarters and strengthen reserves in the second and third quarters. So most of the sequential difference that you saw was simply that seasonal reserving pattern. What's most important and what we look at is the year-to-date result. And right now, both our loss ratio and our margins in the stop-loss business are consistent with our pricing targets.

Going forward, we see some signs that utilization is stabilizing. You may hear that from some of the health insurers as well. And we are taking, as we always do, a conservative approach toward pricing. Over the past few years, some of our competitors were, this is what happens. They have good results. They get aggressive. We generally did not participate in that. And now in some other competitors' calls, they've talked about raising rates. So we're probably looking toward a one-one next year where the market starts to push pricing upward.



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**Doug Young** - *Desjardins Securities Inc - Analyst*

Okay. Appreciate the colour. Thank you.

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**Operator**

The next question is from Tom Gallagher, Evercore ISI.

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**Tom Gallagher** - *Evercore ISI - Analyst*

Good morning. A few questions on the US. The $100 million of dental earnings that you're guiding to for '25, is any of that driven by this $200 million of cost saves planned for '26? Or is most of it expected to come from loss ratio improvement?

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**Dan Fishbein** - *Sun Life Financial Inc - President - Sun Life U.S*

It comes really from all of that and other things as well. So we have a series of initiatives that are underway, most of which, even though they've been underway for some time, will start to show in the results in the second half of the year. So, on the expenses, that is one of the tactics we're using. The dental business is one of the larger consumers of the reserve and of those actions. So there's quite a bit of that, that will start to layer into the results in the second half of the year.

We also have a robust set of dental cost management actions, additional utilization review claims that it -- and also adjustments to network composition to make sure that we're matching the cost to the prices that we're getting. And then prices themselves are a big aspect of this as well. 13 contracts have so far been renegotiated. 12 of those 13 have been at or above the levels that we thought were needed.

There are -- that represents about half the business. Another 40% or so will reprice between now and the end of the year. So we will start to see meaningful impact from the repricing as well. So it's really on all of the above kind of strategy.

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**Tom Gallagher** - *Evercore ISI - Analyst*

Got you. Thanks. And then my -- just for a follow up on medical stop-loss. So it sounds like pricing is firming a bit based on how you described it. Would you -- even though your, I guess experience has been trending in line with pricing. Would you still expect to be able to get some rate yourself? Or would you expect to take some market share and see better growth?

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**Dan Fishbein** - *Sun Life Financial Inc - President - Sun Life U.S*

Yeah. Of course, it's been a very unusual last four to five years with COVID. There's been a historic -- a classic underwriting cycle on stop-loss, three years of improving results where pricing gets more aggressive and then three years of deteriorating results where pricing goes up. That whole cycle was delayed by three to four years by the impacts of COVID, particularly around utilization. We've seen a pretty aggressive pricing market in the last year, including currently.

We're anticipating that pricing will firm as we head towards the one-one cycle, as you're seeing other companies report loss ratios substantially higher than ours. We have been taking some share, although most recently, a lot of that has been coming from new partnerships that we've put in place. We have a really good set of partnerships, both with health plans in certain markets as well as with captive management partners. And that has contributed to our growth.

In general, in the direct market, we're a careful pricer, and this is the time where we really have to be the most careful. But we're optimistic, especially as we head into 2025 that the market will be one that's favourable to us.



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**Tom Gallagher** - *Evercore ISI - Analyst*

Okay. Thanks.

**Operator**

The next question is from Gabriel Dechaine, National Bank Financial.

**Gabriel Dechaine** - *National Bank Financial Inc - Analyst*

Good morning. Just a question on the dental business again. Similar to the last question, the $100 million target, that's an absolute target, it's not an annual run rate, exit rate kind of thing for next year? I'm assuming that's the case. And then from a glide path sort of way, is it more of a back end loaded figure? How should we be anticipating that to evolve over the next course of next year?

**Dan Fishbein** - *Sun Life Financial Inc - President - Sun Life U.S*

Yeah. So to your first question, it is a full-year target that we're talking about, they are not just getting there at the end of the year. There is some seasonality in the dental business. So we have to remember that the -- there's a big portion of our dental business, of course, that's Medicaid, and a big portion of that is kids. So we actually see some significant seasonality in the business.

For example, the summer is when a lot of kids go to the dentist, getting ready for the school year. So those kinds of things will create some natural volatility quarter to quarter. We think -- we see recovery of the business beginning in the third quarter and then a significant recovery in the fourth quarter of this year. It kind of puts us in a good position for next year.

**Gabriel Dechaine** - *National Bank Financial Inc - Analyst*

So Q3 of this year, you expect better dental despite the whole back-to-school, kids going to the dentist thing.

**Dan Fishbein** - *Sun Life Financial Inc - President - Sun Life U.S*

Yes. So I think that is a mitigating factor. So we wouldn't expect to see a dramatic increase in the third quarter, but we do expect a more significant increase to emerge in the fourth quarter.

**Gabriel Dechaine** - *National Bank Financial Inc - Analyst*

Got it. And then, your comments on stop-loss in the US again. I hear that competitors are going to be repricing because of under-pricing previously. I'm not quite sure I got what your strategy is. Can you talk about the duration of these contracts as well and how quickly repricing can actually have an effect?

And then in Canada, I guess the normalization of morbidity experience is still positive, but less positive than it was before. So that tailwind is fading, correct me if I'm wrong there. Like is this something that we should view as we're back to a new normal? Or is there a similar repricing strategy afoot for the Canadian business?





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**Dan Fishbein** - *Sun Life Financial Inc - President - Sun Life U.S*

Sure. This is Dan. I'll start with the US stop-loss question. So the -- we tend to be a conservative pricer. So when there are these cycles, we are not one of the carriers that goes out and prices aggressively for market share. You saw we had good sales results in the second quarter, but a lot of that came from some of these new partnerships versus from aggressive pricing. We do think that pricing will get more rational as we head into next year because a lot of our competitors are not having that same kind of experience.

And on your question about how often this reprice is. One of the things we love about the business, but also one of the things that makes it most challenging is almost all of it renews every year. So we're able to reprice business annually. Now that of course, means we also have a big task, we have to try and renew all the business every year. But it does enable us to react pretty quickly to these kinds of changes in the market.

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**Gabriel Dechaine** - *National Bank Financial Inc - Analyst*

Okay. And then Jacques.

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

Hello, Gabriel, this is Jacques. Good morning. So you're correct. The experience in disability is positive this quarter, but not as positive as the same quarter last year, as you pointed out. Keep in mind that the $372 million of earnings last year, that was already a record quarter for us.

In terms of your comment on sustainability, I remind you, as we've discussed before, that some of it comes from the pricing actions that we've taken. We've been quite disciplined in terms of our pricing and wanting to make sure that we deliver on our objectives. So some of it will continue. I mean at the level we're at now in terms of earnings, I would say there's probably going to be some moderation. But some of it is definitely going to continue.

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**Gabriel Dechaine** - *National Bank Financial Inc - Analyst*

Okay. Great. Enjoy the rest of your summer, everybody.

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

Thank you.

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**Operator**

The next question is from Paul Holden, CIBC.

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**Paul Holden** - *CIBC Capital Markets - Analyst*

Thank you. Good morning. Let me ask a question on the new disclosure around organic capital generation, so $588 million for the quarter. So first off, thanks for that new disclosure. I find it very helpful. But my question really is, is that a good indicative run rate of what we should expect quarterly? Was there anything that may be added to it this quarter, subtracted -- just trying to get a sense of run rate. Thank you.

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**Tim Deacon** - *Sun Life Financial Inc - Chief Financial Officer, Executive Vice President*

Hi, Paul, this is Tim. Thanks for the question. You're right. This is a new disclosure, and we really sought to help give more transparency to how we view a more normalized capital contribution in the same way we think of underlying net income, but for capital. So this would be excluding market related impacts, so taking our underlying net income and our organic CSM movement, less our shareholder dividend.

So you're right that the number that you referenced, the $588 million for this quarter was net of dividends, and we haven't set a formal target, but generally expect that organic capital generation should range between 20% to 30% of underlying net income. So for Q2, at almost $600 million, that's almost -- it's 60% of UNI. So obviously above target result and really driven by strong sales in Canada and Asia that we referenced, and that created the higher new business CSM versus our expectation. So elevated this quarter and last quarter because of the strong sales growth, but over time within that 20% to 30% range, net of dividends.

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**Paul Holden** - *CIBC Capital Markets - Analyst*

Got it. Okay. Thank you for that. I guess second question is with respect to SLC and the net income target there for 2025. So just looking for confirmation that that has not changed and wondering if the recently announced cost restructuring will have any impact on or really help your ability to achieve that $225 million target? Thank you.

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**Steve Peacher** - *Sun Life Financial Inc - President - SLC Management*

Hi, Paul. Thanks for the question. This is Steve Peacher. Yeah, I think that we're still on track for the targets that we put out there. We'll talk more about our expectation -- longer-term expectations for '25 and beyond at the Investor Day in the fall. We did for -- SLC is participating in as part of the cost reduction initiative that was discussed. But I would say, as much as anything as we -- we're also looking to keep investing in the business as we tried to get benefits out of the platform, as we approach the put calls and we invest more in distribution with resources that can sell the entire range of products we have across SLC.

So I would say we expect to get -- we expect to grow earnings by growing AUM and delivering more strategies to existing clients and to new clients over time. And while cost discipline will certainly be part of that, it's really about growing revenue and AUM and less about cost. So will we get some benefits out of cost reduction, certainly, and we're trying to be mindful of that. But I don't view that as a driver of our earnings going forward.

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**Paul Holden** - *CIBC Capital Markets - Analyst*

Okay. That's helpful. I'll leave it there. Thank you.

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**Operator**

The next question is from Mario Mendonca, TD Securities.

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**Mario Mendonca** - *TD Cowen - Analyst*

Good morning. This might be for Dan, maybe Tim. Tim in your opening comments, you referred to the higher loss ratio in Medicaid. You said it was largely related to the redetermination. And I look at that increase in the loss ratio from 86.2% to 94% in four quarters, and it just seems like such a significant increase for the 19% that have left -- that notion that the stayers have much higher utilization.

It made me -- that chart makes you think that there's more going on here than just the redetermination and then your phrase, the turn of phrase, but largely related to the redeterminations, made me think there's more going on. So maybe this is a question for Dan. What else is going on in dental beyond Medicaid redeterminations.



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**Dan Fishbein** - *Sun Life Financial Inc - President - Sun Life U.S*

Yeah. In terms of the dental, the Medicaid loss ratio, it really is the redeterminations. And let me give a little more colour on that kind of loss ratio impact. A lot of the people who had become enrolled during the public health emergency, no longer needed the coverage. There's a fair amount of churn, people coming on and off the Medicaid rolls as they get jobs, et cetera, which is -- and they get other coverage. So there were a significant number of people who -- for whom the states were paying premiums, but who were not using the benefit.

And the way they price, of course, as any actuary would price, they look at the most recent periods of experience and that got baked into their pricing. And then when you have -- and in some cases in a very short period of time, a state disenrolling a big portion of the membership, you can get a very big mix shift. So Texas, for example, disenrolled one-third of its entire Medicaid population. So it's not surprising that you get a 6% or 8% change in the loss ratio with a 19% change in membership.

Now related to that. Of course, there are dentists and what are called DSOs, large groups of dental practices that primarily serve the Medicaid market. So if they lose 19% of their members and therefore 19% of their revenue and they have a certain amount of capacity, they're going to do everything they can to sell that capacity.

That meaning in some cases, that means taking people off of waiting lists and getting them in for care sooner, which is a good thing. But in some cases, it may mean providing more dental care to those people in order to fill those appointments. So that's part of the story here as well. And it's also the reason why we're putting in place significantly more robust utilization management capabilities to make sure that we're facing off appropriately against that dynamic.

**Mario Mendonca** - *TD Cowen - Analyst*

Okay. Maybe a sort of follow-up question to that and more from a positive perspective. Sun Life paid, I believe it was USD 2.5 billion for DentaQuest back in 2021. Your aspirations are for USD 100 million next year. My just looking at those two numbers makes me think that your longer-term goals must be for more than $100 million. So what do you think this business is capable of in a normal environment?

**Dan Fishbein** - *Sun Life Financial Inc - President - Sun Life U.S*

Yeah. So absolutely yes, is the answer to that question. Our longer-term aspirations and all the modelling we did is obviously much greater than that number. And generally, we -- the way we thought about this is we still think that all of that is applicable but pushed out by about a year or so by the events of the redeterminations.

One good way to think about the business is a 5% after-tax profit, that seems to be what most of the business supports in across the states and the non-government business as well. It's a little different in the different segments, but that's a reasonable rule of thumb. So we are a little shy of $3 billion in revenue today, but we see lots of growth opportunity in the business.

First of all, Medicaid continues to grow, and will now that the redeterminations are over, we continue to have a great pipeline there and to win contracts. But we also have lots of opportunity to grow in Medicare Advantage and Affordable Care Act exchanges and especially in commercial. So we see significant revenue growth in the future, and you can do your own calculations based on that 5%.

**Mario Mendonca** - *TD Cowen - Analyst*

Thank you.





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**Kevin Strain** - *Sun Life Financial Inc - President, Chief Executive Officer, Director*

Hey, Mario, it's Kevin. I would just add to it that, when we did the acquisition, it was during COVID and we actually knew that the public health emergency would end, we did modelling of that. The public health emergency went longer and was deeper than we expected, and some of the impacts were probably more than we expected in this year. But over the long term, we still expect that, as Dan has talked about that this is going to be a very good business for Sun Life, and we'll return back to the sort of pricing that we would have expected, and we're seeing that as we reprice the business.

So I think overall, our thesis for the dental business in the US hasn't changed. And I think you see our culture and our financial discipline in action by how we've disclosed this transparently to our investors and how we're taking action to deal with it.

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**Mario Mendonca** - *TD Cowen - Analyst*

Thank you.

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**Operator**

The next question is from Lemar Persaud, Cormark Securities.

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**Lemar Persaud** - *Cormark Securities Inc - Analyst*

Yeah. Thanks. My first question just going back to the restructuring is probably appropriate for Tim. Is this the first of more restructuring charges? Like is this a broader restructuring program? How big could further restructuring charges be. And then I guess you mentioned the $200 million pre-tax savings. A portion of that -- is a portion of that $200 million pre-tax going to go through the CSM or is that $200 million pre-tax all going to go through the underlying earnings? Thanks.

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**Tim Deacon** - *Sun Life Financial Inc - Chief Financial Officer, Executive Vice President*

Thanks, Lemar. So this was a program that we just initiated now. It's a one-time charge of $138 million pre-tax, $108 million post-tax that flows through reported net income. And that's a singular program that will be executed over the 18 months that I had referenced. As I also referenced, financial discipline is a core part of our Client Impact Strategy. So we're always going to be continually focused on cost discipline. But as I said, we hadn't run a program like this in a little while.

So it was time for a bit of a catch-up just as we looked at our expense growth and relative to continuing to ensure we can get to the top end of our earnings growth objectives. In terms of where this shows up, this will come off across a variety of line items. So it's not all CSM. It will come through other expenses. It will come through other fee income, which is net of expenses. So you'll see it in a bunch of places.

And as I referenced earlier, we'll likely look to maybe take a portion of that, a small portion for reinvestment, as I said, to probably accelerate our digitization efforts and look at areas like Generative AI and the progress that we've been making there as a way to accelerate that. So this is a singular program, but we'll always be focused on cost discipline going forward.

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**Lemar Persaud** - *Cormark Securities Inc - Analyst*

Okay. And what about the mix through CSM and regular earnings?

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**Tim Deacon** - *Sun Life Financial Inc - Chief Financial Officer, Executive Vice President*

Yeah. Predominantly earnings, but there is a portion through CSM. But expect most of that through earnings.

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**Lemar Persaud** - *Cormark Securities Inc - Analyst*

Okay. Perfect. Thanks. And then just moving onto a different type of question here on MFS. If we see rate cuts play out of the US, do you think that's going to be helpful to the net flows performance at MFS, just given its product's mix more towards like value-based equities. Is that kind of the right way to think about the impact of lower US rates on that bit, on the MFS business?

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**Michael Roberge** - *Sun Life Financial Inc - Chairman of MFS Investment Management*

Hey. Good morning, Lemar. It's Mike Roberge. Yeah, I mean that's how we're thinking about it. If you look at prior cycles as the Fed and central banks start to cut rates and people look at their cash yields going down, they re-engage back into the market with longer-term fixed income and equity products.

If you look at industry sales rates, you look at our sales rate pre-COVID, which is probably the last normal environment that we have, and you apply that to our asset base today that would take you back to net positive US retail flows at MFS. And so the question ultimately becomes is what does normal look like. We think that industry is going to look a lot more normal as cash rates begin to come down and people have to seek returns in other parts of their portfolio other than cash.

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**Lemar Persaud** - *Cormark Securities Inc - Analyst*

Okay. Thank you. That's it for me.

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**Operator**

The next question is from Nigel D'Souza, Veritas Investment Research.

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**Nigel D'Souza** - *Veritas Investment - Analyst*

Thank you. Good morning. I wanted to follow up again on the restructuring initiatives here. Cadence of the timing of how that flows through into earnings, is this a linear ramp up or is it more back-end loaded? And is the right way to think about this, that the $200 million will be fully flowing through underlying net income in Q1 of '26?

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**Tim Deacon** - *Sun Life Financial Inc - Chief Financial Officer, Executive Vice President*

Hi, Nigel, it's Tim. Yeah. It's referenced earlier in some of the questions. We will start to see some of that expense savings come through earnings in the second half of this year. It was mostly rateably through 2025 into 2026. So by the time we hit 2026, we'll have achieved the full $200 million pretax. In terms of how it shows up, as I said, it will come through the variety of the line items that I referenced because of the way our disclosures under IFRS 17 require us to report expenses themix of the directly attributable as well as these other expenses that don't get allocated.

So you would expect to see that occur over time. As we said, it's an 18-month program so there are some actions that we've already taken now. Dan referenced some of the dental business actions that were taken and will be -- starting to show through in the second half of this year, but it really is over time. And I guess just to reemphasize, this is really to help again hit our earnings growth targets towards the top end of our MTO. So in terms of how you think about that in terms of forward guidance.



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**Nigel D'Souza** - *Veritas Investment - Analyst*

That's helpful. And then my second one was on other fee income. There's a bump up there in the line item this quarter, I understand part of that is related to expenses. The other part is related to wealth income. Could you kind of break that out for us and kind of get a sense of what the run rate is for other fee income going forward.

**Tim Deacon** - *Sun Life Financial Inc - Chief Financial Officer, Executive Vice President*

Great. So I'll take that one and see if others want to supplement. So that quarter over quarter increase, as you noted, we're seeing a nice uptick in that, and that's really up on the strong performance of our wealth businesses, that's both in Canada as well as in Asia. So in Canada, we had strong performance in the GRS business. We had favourable markets. Our AUM was up 10% year-over-year. We had net inflows of just under $1 billion coming into that business. And then similarly, in Hong Kong, in particular, MPF business, we saw strong growth there. So that's really driving the majority of it.

On the quarter-to-quarter variance, we also had some costs because this other fee income also includes our ASO businesses. So whenever we are onboarding new clients, sometimes there's startup costs related to that and the buildup to that. So we had costs in the first quarter and now we're reporting the revenue on those businesses for us for some of our larger programs.

And so that's now improved the results because we're starting to report revenue through that. So it obviously varies based on markets and where AUM positions are, we will get variability in that line item from time to time. But on the basis, that markets continue to perform, and our AUM comes up, that's a healthy run rate for us.

**Nigel D'Souza** - *Veritas Investment - Analyst*

Okay. That's it for me. Thank you.

**Operator**

The next question is from John Aiken, Jefferies Securities.

**John Aiken** - *Jefferies LLC - Analyst*

Good morning. I apologize if you've addressed this already in the past. If that's the case, just send me back to the transcript, but wanted to drill down a little bit more in terms of the performance in Asia. Can you give us a little more detail in terms of, as you talk about the joint venture contributions that occurred in the quarter. And secondarily, talk about the sustainability of the sales levels the new business CSM was generating in the region.

**Manjit Singh** - *Sun Life Financial Inc - President - Sun Life Asia*

Good morning, John. It's Manjit. In terms of the sales performance, I'm very pleased with the year-to-date sales performance that we've seen in Asia. And looking forward, I remain confident in our ability to continue to generate good sales growth, and that's really underpinned by a number of things; we have a good presence in growing markets with good and attractive demographics. We have strong focus on making sure that we're meeting our Client needs. We've also broadened out, as we've talked about in the past, our distribution capabilities, both through new bancassurance partnerships, but also through growth, in organic growth in our agency of workforce as well.



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And that's resulted in good market share gains in several markets that we operate in. We're also investing in digital capabilities to make sure that we deliver simple, fast and easy experiences for our Clients. We've noted that we've also invested in brand and we're seeing really good uptick in our brand awareness across our markets. And of course, all of that's underpinned by our strong team that we have in Asia. So with all of that, I remain confident in our ability to grow -- continue to grow in Asia.

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**John Aiken** - *Jefferies LLC - Analyst*

And sorry, Manjit, can you address the sustainability of the new business CSM that was generated in your segment?

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**Manjit Singh** - *Sun Life Financial Inc - President - Sun Life Asia*

Yeah. I think that is partially related to the sales growth, John. So I think we continue to remain optimistic in that as well. You're going to see quarter-on-quarter volatility from a number of factors, macro factors and competitive factors. But over the medium-term, we continue to view our ability to generate CSM in the mid-teens rate that we've talked about.

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**John Aiken** - *Jefferies LLC - Analyst*

Great. Thank you.

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**Operator**

We have no further questions at this time. I'll turn things back over to Mr. Garg.

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**David Garg** - *Sun Life Financial Inc - Senior Vice President, Capital Management and Investor Relations*

Thank you, operator. This concludes today's call. A replay of the call will be available on the Investor Relations section of our website. Thank you, everyone, and have a good day.

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**Operator**

This brings to a close today's conference call. You may disconnect your lines. Thank you for participating, and have a pleasant day.

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