S&P Capital IQ

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Aflac Incorporated NYSE:AFL

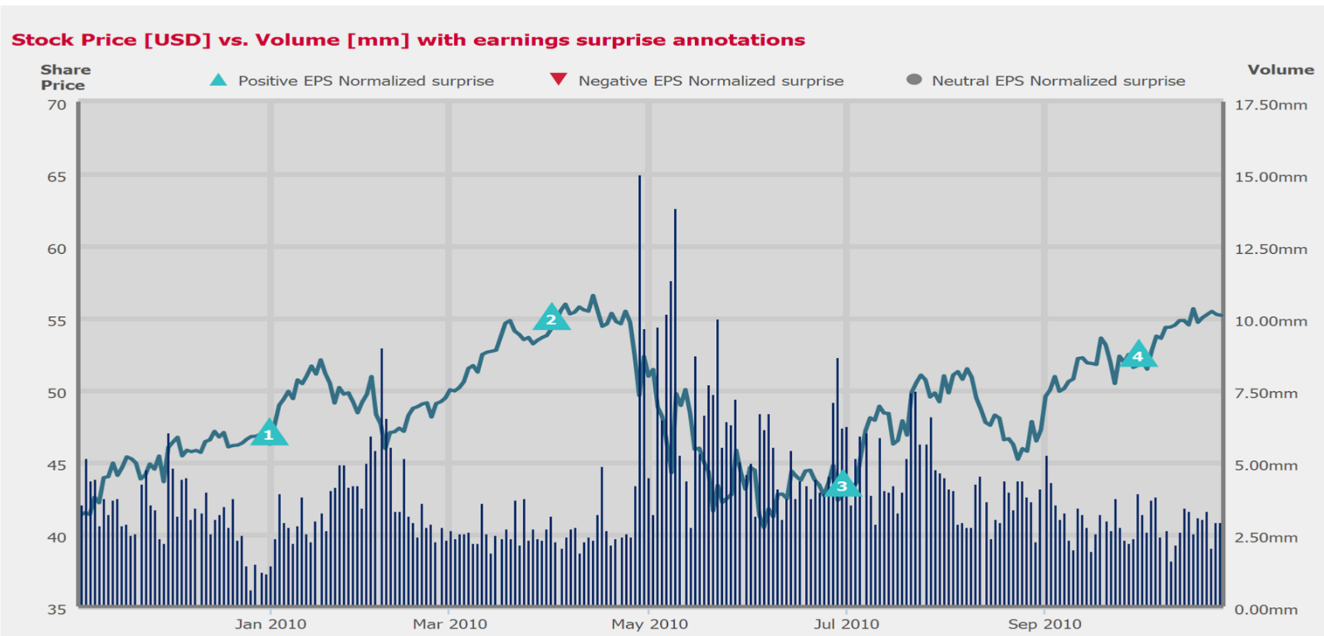
FQ4 2010 Earnings Call Transcripts

Wednesday, February 02, 2011 2:00 PM GMT

S&P Capital IQ Estimates

	-FQ4 2010-			-FQ1 2011-	-FY 2010-	
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	ACTUAL
EPS Normalized	1.35	1.33	(1.48 %)	1.51	5.55	5.53
Revenue (mm)	5594.54	5294.00	(5.37 %)	5562.72	21102.88	20732.00

Currency: USD
Consensus as of Feb-02-2011 1:40 PM GMT



- EPS NORMALIZED -	CONSENSUS	ACTUAL	SURPRISE
FQ4 2009	1.15	1.18	1 2.61 %
FQ1 2010	1.32	1.41	2 6.82 %
FQ2 2010	1.33	1.35	3 1.50 %
FQ3 2010	1.39	1.45	4 4.32 %

Call Participants

EXECUTIVES

Daniel P. Amos
Chairman & CEO

Kriss Cloninger
President & Director

Robin Y. Wilkey
Former Senior Vice President of Investor & Rating Agency Relations

Tohru Tonoike
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Presentation

Operator

Thank you for standing by, and welcome to Aflac's Fourth Quarter Earnings Conference Call. [Operator Instructions] I would like to turn the call over to Ms. Robin Wilkey, Senior Vice President of Aflac Investor Relations. Ma'am, you may begin.

Robin Y. Wilkey
Former Senior Vice President of Investor & Rating Agency Relations

Thank you, Catherine. And good morning, and welcome to our fourth quarter conference call. Joining me this morning is Dan Amos, Chairman and CEO; Kriss Cloninger, President and CFO; Paul Amos, President of Aflac and COO of U.S. Operations; Ken Janke, Executive Vice President and Deputy CFO; Jerry Jeffery, Senior Vice President and Chief Investment Officer; and Toru Tonoike, President and Chief Operating Officer of Aflac Japan, is joining us from Tokyo.

Before we start, I'd like to mention the Safe Harbor language to you. Let me point out that some statements in this teleconference are forward looking within the meaning of the federal securities laws. Although we believe these statements are reasonable, we can give no assurance that they will prove to be accurate because they are prospective in nature. Actual results could differ materially from those we discussed today. We encourage you to look at our quarterly report for some of the various risk factors that could materially impact our results. Now, I'll turn the program over to Dan who will begin this morning with some comments about the quarter and our operations in Japan and the United States. I'll follow up with a few financial highlights for the fourth quarter and the year, and then we'll take your questions. Dan?

Daniel P. Amos
Chairman & CEO

Thank you, Robin, and good morning. Thank you for joining us. Let me begin a review of 2010 with Aflac Japan. Aflac Japan generated strong results throughout 2010. We were again pleased with the financial performance of our largest earnings contributor. Sales results were especially impressive considering the tough comparisons, particularly in the fourth quarter.

Total new annualized premium sales in yen exceeded our expectations, and we're up a solid 6.5% for the fourth quarter. For the full year, sales rose 11%, for the second consecutive year, we exceeded our annual sales goal of a zero to 5% increase. Additionally, the persistency improved for our large block of in-force business in Japan, rising from 94.0% to 94.2%. An improvement in Aflac Japan's persistency rate contributes to the continued growth in premium income. Although Aflac Japan's benefit ratio rose in the fourth quarter, it improved for the full year. The fourth quarter benefit ratio reflects reserve adjustments made to a closed block of Dementia Care business that we stopped selling almost 20 years ago. As we look to 2011, we expect further improvement in the benefit ratio resulting in the continued expansion of the profit margin.

In the first quarter of 2010, Japan's premium income grew 3.3% and improved to 4.4% for the fourth quarter, which contributed to a 3.8% increase for the full year. As expected, our premium pretax profits continued to expand, resulting in strong earnings growth for the year. The bank channel had a great year in 2010. Our innovative products aligned well with the product needs of the banks. Bank sales in the fourth quarter posted another record with sales of JPY 7 billion, which represents an increase of 140.4% over the fourth quarter of 2009. Last quarter I mentioned how we believe more banks and mega banks in particular would step up their efforts in selling Aflac's products, and that's exactly what happened. At the end of December, Aflac Japan was represented by 364 banks, or more than 90% of the total number of banks in Japan. Of all the banks, we now have enrolling our products, there's still many branches in their system that are not actively selling yet, which means there's still enormous sales potential.

In addition to having a great year from a distribution standpoint, we saw success on the product side of our business. Aflac Japan has honed its ability to customize our product portfolio to appeal to new market segments by enhancing the benefits of our existing product line. A good example is our expanding suite of medical products that we've successfully created over the last decade. In fact, the medical product category was the number one contributor to total sales for both the fourth quarter and full year. You'll recall that in August of 2009, we launched new EVER, an updated version of our popular medical product. Promotion for the new EVER featured the Maneki Neko or cat duck advertising campaign that literally became an overnight sensation in Japan, and prompted an incredible surge in the fourth quarter of 2009 medical sales. Although we saw a slight decline in medical sales compared to last year, this category generated a significant amount of new annualized premium.

Importantly, we maintained our position as the number one seller of medical products in Japan, which confirms the continued popularity and demand for our innovative policies. Not only was 2010 a year in which we maintained our number one position in medical sales, it also was another year where our cancer products dominated the market. Cancer insurance sales made a solid contribution to total the sales, accounting for 22% of the total sales for the year. We're introducing a new cancer policy called DAYS that replaces the base policy, Cancer Forte. This enhancement of one of our pillar products speaks to the changing landscape in cancer treatment, as well as our commitment to being the number one provider of cancer insurance in Japan. It's important to remember that the foundation of our product portfolio has been, and continues to be, cancer and medical products. This solid platform allows us to leverage our competitive advantages such as branding, administrative efficiencies and to grow our product offering and meet the evolving needs of consumers.

As the bank channel has become a larger contributor to sales, Aflac Japan has also been enhancing its product portfolio to better meet the needs of banks including WAYS and child endowment products, which were key drivers to growth for the fourth quarter and the year. WAYS is a unique hybrid whole life product that can be converted to a fixed annuity, a medical coverage or nursing care benefit when the policyholder reaches a predetermined age. WAYS was first introduced in 2006, and was revised to the bank channel in 2009. Sales of WAYS really took off in the fourth quarter, accounting for 13.6% of the total production. But the real story can be seen in the phenomenal growth rate, which was 149.9% compared to the fourth quarter of 2009.

Consumers find this product attractive because the first options offer future flexibility. Banks like to sell this product because it has high premiums. And Aflac's product margin is significantly enhanced when policyholders elect to pay premiums upfront using what we referred to as the discounted advanced premium. Importantly, 90% of the customers at the banks choose this payment option.

As our banking channel becomes a greater contributor to our top line growth, we expect sales of this innovative and flexible product to grow significantly in 2011. The other strong driver of sales growth was the child endowment product, which was up 67.4% for the quarter and 132% for the year. This product, which was redesigned in 2009, is primarily used to help fund the higher cost associated with a child entering high school and college in Japan. Child endowment policies have been very popular in Japan for many years.

Aflac's strong brand, this product's unmatched returns, our expanding presence in banks and the government's child subsidiary payments that started in June have helped make our endowment policy the product of choice. It's important to note that the average annual premium of the child endowment policy is about 3x the size of the health policy, meaning that the premium is very solid contributor to the top line growth. Child endowment also offers a discounted advanced premium, and this product's profit margin more than doubles when the policy holders elect to pay the premiums upfront using the discounted advanced premiums. About half of the consumers who purchased our child endowment policies through banks elect this discounted advanced premium method of payment. From top to bottom, Aflac Japan performed extremely well in 2010 despite tough sales comparisons. But before the fourth quarter even began, my mind had already shifted to 2011, and the challenge we would face following two years of strong sales results. Although I believe our sales momentum will continue into the first quarter of 2011, the comparisons get tougher as the year goes on, especially in the fourth quarter.

Taking all of this into account, as we noted in last night's press release, we expect sales to be in the range of down 2% to up 3%, although I thought in November that sales increase for 2011 would be closer to flat to up 5%. However, after a stronger-than-expected fourth quarter, 2010 sales ended up 11% versus our projection in November which was up 9%. With such exceptional performance, I did not want to penalize Aflac Japan sales department for pushing so hard at the end of 2010. So that's how we came up with the sales expectations for Aflac Japan.

Now let me turn to the U.S. operations. From a financial perspective, Aflac U.S. continued to perform at expectations. However, ongoing low confidence level from consumers and small businesses coupled with fewer employees at the work site continued to pose challenges for our U.S. sales growth. As such, we were not surprised that these factors reflected in the sales decline of 2.3% for the fourth quarter and 4.9% for the year. You may recall that we acquired CAIC, now rebranded as Aflac Group, in October of 2009. New annualized premium sales for Aflac U.S. included sales from Aflac Group of $42 million in the fourth quarter. This result represented a 58.7% increase for the quarter and represented half of Aflac Group Insurance production for the year. I was very excited to see that our traditional sales force rallied to sell group products to our account in addition to individual policies that they already sold.

While I would say our decision to acquire CAIC was a huge success, let me put it in perspective. An $83 million sales contribution from the Aflac Group represents only 6% of the total U.S. production in 2010. About 90% of our businesses continues to revolve around small business owners and accounts with fewer than 100 employees. These accounts don't usually have group insurance, and our traditional individual agents continue to be the driving force behind our relationships with them. Our field force continues to be the key to our success, and no one else has been able to establish this kind of field force network that we have at Aflac. Unfortunately, both the smaller accounts and our sales agents that sell to them are the slice of America that has been hit the hardest by the economic turmoil over the last two years. As you know, consumer confidence and small business segment continues to hover at low levels. We've also been facing recruiting conditions that have not yet returned to business as usual. Although recruitment of sales associates in the fourth quarter was down 8.5%, it showed significant improvement over the 25.4% decline in recruiting for the first nine months of the year. That means we've averaged 5,500 new recruits per quarter, which is still a lot of people, but we can do better.

Despite a significantly more positive outlook on the job market, some lingering uncertainty still makes it tough to find people with salary jobs or extended unemployment benefits who are unwilling to take their chances in commission sales. We have adopted a more people-centric recruiting criteria and are continuing national recruiting contest and programs to expand our sales force, and we anticipate this will expand the number of new recruits. Beyond expanding the size and capabilities of our traditional sales force, we remain excited about developing relationships with insurance brokers. Our broker distribution initiative is still in its early stage, but our efforts are translating into sales.

The group product platform, which is preferred by brokers is an important part of our efforts to broaden our product portfolio. As I mentioned, we saw a cross-over for Aflac career agents embraced our new group products, and frankly, we also saw brokers selling individual policies. I tell our entire U.S. distribution system that I don't care whether they sell group or individual products, but I do want them to let the existing accounts with more than 100 employees know that Aflac now offers group products in addition to individual policies. That's because if we don't at least let these accounts know that we offer group option, you can bet that someone else will. If the accounts want group products, and they know that Aflac offers them, I believe they'll choose Aflac over the competition.

Although weaker sales have slowed the top line growth somewhat over the last few years, we saw a steady improvement in persistency in 2010 compared to 2009. I believe we've also done a very good job in managing our U.S. operations, including budget and people resource. Managing financial components within our control has improved our 2010 expense ratio from 33.7% to 32.5%. We're taking measures to better reach potential customers with some innovative product benefits and solutions. We also continue to believe that the U.S. provides a vast and accessible market for our products, and we are building our business with that potential in mind.

For 2011, we expect Aflac U.S. sales to be flat to up 5%. Some of you may feel that our 2011 sales expectations is too ambitious considering the environment. To that, I would say that I will remain cautious until we see some stability in the economy. But we've been adjusting our business to this environment, and we still believe strongly in the products that we sell.

Now let me update you on Aflac Incorporated results. Excluding the benefit from the stronger yen, operating earnings per diluted share rose 10.1% for the full year, meaning we achieved our goal of a 9% to 12% increase for 2010. Our balance sheet and capital position remain strong, and we believe that our investment approach of effectively matching assets to policy liabilities is the most prudent approach to our policyholders and shareholders. Clearly, a lot of attention has shifted recently to the impact of lower interest rates on earnings. As you've heard me say repeatedly since the early 90s, our greatest challenge is investing huge cash flows in Japan's low interest rate environment. To address this, we've started increasing the amount that Aflac Japan invest in dollar-denominated securities last year. This strategy, we discussed at the Tokyo Analyst Meeting this past September, produces two benefits. First, we're funding incremental dollar purchases with the sale of Japanese government bonds. These JGBs are scheduled to mature before the end of 2011, and this strategy allows us to capture the gains for tax purposes before they mature. Second, we're able to invest the proceeds in higher-yielding dollar-denominated corporate bond at a meaningful spread. The current strength of the yen and the wider spread of the dollar bond helps mitigate the currency risk associated with this strategy. While our preference is to invest in yen-denominated securities, we believe this is a short-term strategy to help enhance our yield during the low interest rate periods.

As we communicated over the past several years, maintaining a strong, risk-based capital or RBC ratio remains a priority for us, and you'll recall that it is also a component of the management incentive plan for all Aflac officers. Our goal was to end 2010 with a higher RBC than our year-end 2009 of 479%. Although we have not yet finalized our statutory financial statements, we estimate that 2010 RBC ratio exceeded 580%. I believe our ability to maintain a strong RBC exemplifies our effective capital management strategy. Our decision as to whether to increase the dividend or repurchase our shares is a function of our capital position. As you'll recall, Aflac's Board of Directors approved the 7.1% increase in the quarterly cash dividend effective in the fourth quarter of 2010 payment. That marked the 28th consecutive year of a dividend increase. Additionally, we resumed the share repurchase program in the fourth quarter and purchased 2 million shares. We still anticipate repurchasing 6 million to 12 million shares in 2011. At the same time, I remain convinced it makes sense to maintain a healthy degree of conservatism given the economic uncertainties around the globe.

We continue to focus on maintaining strong fundamentals in our core business and building on our record of consistent earnings growth. As I commented in the third quarter release, we will likely be at the low end of the 8% to 12% range for operating earnings per share in 2011. Although low interest rates have increased somewhat in the United States recently, they have not increased as much in Japan, and the yields remain very low. If we assume 8% earnings per share growth, we would earn $5.97 per diluted share, excluding the impact of the yen. If the yen averages 80 to 85 to the dollar for the full year, we would expect reported earnings to be in the range of $6.09 to $6.34 per diluted share.

Looking ahead to 2011 and beyond. We continue to believe that Japan and the United States each have characteristics to make them ideally suited for the insurance products we offer. And no other company is more focused on supplemental insurance products that respond to that need than Aflac. We are focused on providing value to the shareholders, and we're fortunate that in the process of doing so, we have the privilege of providing financial protection to more than 50 million people worldwide. Now I'll turn the program back over to Robin. Robin?

Robin Y. Wilkey
Former Senior Vice President of Investor & Rating Agency Relations

Thanks, Dan. Let me go through some numbers for the fourth quarter and year end, starting with Aflac Japan. Beginning with the top line in yen terms, revenues were up 3.5% for the quarter. Investment income was flat, and excluding the effect of the stronger yen on Aflac Japan's dollar-denominated investment income, net investment income rose 2.8% in the quarter. The annualized persistency rate, excluding annuities, was 94.2%, up from the nine months, and up from 94.0% in 2009. In terms of quarterly operating ratios, the benefit ratio rose in the fourth quarter to 61.0, due to reserve adjustments made to a closed block of Dementia business. Excluding the impact of the stronger yen, the benefit ratio improved for the year by 90 basis points. The expense ratio for the quarter was 20.4%, down from 21.6% a year ago. The decrease reflected tight general expense controls and lower advertising expense in the quarter. The pretax margin decreased slightly from 18.7% to 18.6% in the quarter. With the retraction of the margin, pretax earnings increased 2.9% for the quarter in yen terms. Excluding the impact of a stronger yen on Aflac Japan's dollar-denominated investment income, pretax earnings were up 5.4% in the quarter.

For the quarter, we invested our cash flow in yen securities at 2.36%, and including the dollars, the blended rate was 2.61%. As part of our strategy that Dan talked about to address the low interest rate environment in Japan, we made dollar-denominated purchases totaling $703 million through the end of 2010. And we'll continue these purchases into 2011 until we reach $1 billion. The yield on these securities was 4.19%.

The portfolio yield was 3.56% at the end of December, down eight basis points from the end of September, and 21 basis points lower than a year ago.

Now let me turn to Aflac U.S. Total revenues rose 2.5% in the fourth quarter and continued to benefit from the addition of Aflac Group sales. The annualized persistency rate for the year was 73.6% compared with 72.2% a year ago. Persistency showed steady improvement throughout 2010. The benefit ratio for the quarter was 50.1% compared with 53.8% a year ago. The decrease in the benefit ratio was due to adjustments made in 2009 that were not repeated in 2010. The operating expense ratio was 32.5% compared with 33.7% in the fourth quarter of 2009, reflecting improvement in the benefit and expense ratios, the profit margin for the quarter was 17.4% compared with 12.5% a year ago. And pretax operating earnings were up 42.3% for the quarter.

In terms of U.S. investments, the new money yield for the quarter was 5.45% versus 6.25% a year ago. The yield on the portfolio at the end of December was 6.92%, down four basis points from the third quarter and 25 basis points from a year ago.

Turning to some other items in the quarter. Excluding FAS 115, the ratio of debt to total capital was 21.7% at the end of the year compared with 22.3% a year ago. Noninsurance interest expense in the fourth quarter was $41 million compared with $25 million a year ago. The higher interest expense reflected debt issuance earlier in the year and the impact of a stronger yen on our yen-denominated debt.

Parent company and other expenses were $20 million in the fourth quarter compared with $32 million a year ago. The lower parent company expenses in the quarter primarily were the result of -- in 2009 we did not convert yen repatriation due to pending repayment of debt. In addition we had higher legal and consulting fees in 2009. The operating margins improved for the quarter. Pretax margin rose from 16.1% to 17.2%. The after-tax margin increased slightly from 11.0% to 11.2%. On an operating basis, the tax rate increased from 31.5% to 34.7% in the fourth quarter of 2010.

Net earnings per diluted share for the quarter were $0.92 compared to $0.53 in 2009. The primary difference between net and operating EPS was, again, realized investment losses, which were $0.41 per share in the fourth quarter of 2010 compared to $0.65 per share in 2009. As reported, operating earnings per diluted share for the quarter rose 12.7% to $1.33. The stronger yen increased operating earnings by $0.06 per diluted share for the quarter and $0.19 for the year. Excluding the yen's impact, operating earnings per diluted share increased 7.6% for the quarter and 10.1% for the year. Lastly, let me comment on the outlook for operating earnings per share for 2011.

As you've heard Dan say, we affirmed our objective for 2011 of an 8% to 12% increase in operating earnings per diluted share, excluding the impact of the yen. With yen yields remaining very low, we're assuming an 8% increase in operating earnings per share growth, we would expect to earn $5.97 on a constant currency basis. This year, we estimate that a one yen change on the average exchange rate for the year would equal approximately $0.045 per diluted share. If we achieve our objective of 8% growth, and the yen averages 80 to 85 for the full year, we would expect operating earnings per share to be in the area of $6.09 to $6.34 per diluted share.

Now we will start taking people's questions. We want to make sure that everybody has an opportunity to ask a question. So I'd like to ask you to limit your questions to just one to be fair to everyone else. Now we'll be glad to start taking questions.

Question and Answer

Operator

[Operator Instructions] The first question is coming from Jimmy Bhullar, JPMorgan.

Jamminder Singh Bhullar
JP Morgan Chase & Co, Research Division

I had a question on your Japan sales and then a clarification on this year earnings. I think the Dementia charge, the reserve increase and the DAC amount was $0.15, correct? On EPS?

Robin Y. Wilkey
Former Senior Vice President of Investor & Rating Agency Relations

That's correct.

Jamminder Singh Bhullar
JP Morgan Chase & Co, Research Division

And as we think about run rate earnings, we shouldn't be assuming that we shouldn't be adding that entire amount back because I think you actually spent -- it seems like you spent a little bit less in advertising than you would have otherwise. So the 133 seemed close to a real run rate as opposed to a significantly higher number even with the charge?

Kriss Cloninger
President & Director

Jimmy, Kriss Cloninger. Let me just comment on that. The $0.15 is correct for dementia by itself. Dementia reserve strengthening we had and the divert costs we wrote off. But what you have to consider is we normally have a couple of different types of adjustments in either third quarter or fourth quarter or any quarter for that matter. And in the fourth quarter this year, we had some claim reserves released because we trued up some of the runoff factors and the experience analysis too, and we had some JPY 5.2 billion of claim reserves released compared to what we had posted at the end of the third quarter that offset some of that Dementia increase. Let me just make a couple more comments on that. That's not an unusual thing for us. As a matter of fact, in accordance with our SACS requirements on internal standards for financial controls, we actually have it recorded that we'll do a review of the adequacy of Dementia reserves with respect to interest rates during the fourth quarter. And we'll do certain other updates on claim runoff factors for claim reserves and the like during either the third or the fourth quarter. And we have all that coordinated with the audit work that goes on. This quarter, we did strengthen the dementia reserves, and let me just tell you why. Last year, we also strengthened dementia reserves in the fourth quarter but because they pretty much netted against other adjustments, we made the claim reserves and the like. We didn't discuss it because it didn't create any significant difference in the benefit ratio. So last year, we strengthened interest rates underlying the reserving of the closed block of dementia down to a 2.7% ultimate new money interest rate. We actually used 2.5%, upgraded it up to 2.7% because we thought interest rates were very low and likely to increase. This year we decided to eliminate the assumed increase in interest rates, so we just kept the new money rate used to reserve that block at a flat 2.5%. And that's the only thing that caused the increase in the reserve on that block of business.

Jamminder Singh Bhullar
JP Morgan Chase & Co, Research Division

Yes, and I just wanted to make sure that you weren't implying that, other than that earnings would have been higher. That's the reason I asked that.

Kriss Cloninger
President & Director

Other than that, earnings would have been higher but by not much. We take a look at the range of possibilities for reserving conclusions, and my operative philosophy, and I think I probably said it to the investment community before is always to make sure that the numbers keep moving in the right direction. I want to make sure there are numbers moving in accordance with the underlying fundamental trends of the business. And that's why we made this adjustment.

Jamminder Singh Bhullar
JP Morgan Chase & Co, Research Division

And then I had a question on Japan sales. I understand the reason for your guidance but wanted to see -- obviously, comps are tougher. Other than that, is there something else that makes you cautious that might actually result in you hitting the low end of your range versus maybe the middle of it or the higher end? And not sure if you can comment on January, or how the trends have been so far this year?

Daniel P. Amos
Chairman & CEO

We can't mention January but Toru, would you like to make a comment?

Tohru Tonoike
Vice Chairman of Aflac Japan

Yes, Dan. We have some negative factors about our expectation of the 2011 sales. For example, sales of the Dai-ichi Life was lower than the last year in 2010, but we expect that to continue to be lower in this year. And also we had a big decline in the sales by one of our big telemarketing agents. And again, we expect that sales, that part of the sales to continue to go down this year. So we have a couple of negative factors.

Daniel P. Amos
Chairman & CEO

I think though, all in all, as we review 2011, most of our channels, we expect to be up except for those two that are down. And the two that are down, we thought that there be more sizable increase in the bank channel, not to the level we saw in 2010. But it should have an increase, and that's how we ended up balancing it out and coming in with that number.

Operator

The next question is coming from John Nadel of Sterne Agee.

John Matthew Nadel
Sterne Agee & Leach Inc., Research Division

If we could talk for a second about the earnings guidance for a moment. You've obviously told us to focus on the lower end of the 8% to 12% growth, there's nothing new there. But your Japan sales in the fourth quarter were ahead of your expectations by a pretty fair amount. You had a pretty significant one-time reserve item in the fourth quarter notwithstanding -- and I understand Kriss what you just sort of talked about with maybe the offset from some claims reserves. And you've got this program where you're investing some Japanese cash flows into dollar-denominated securities that's layering in at least a little bit of additional yield. So I guess what I'm getting at is your focus on the lower end of the growth range feels more conservative now than maybe it did in the past few quarters. Is there something I'm missing that would be an offset to those positive items at the margin?

Kriss Cloninger
President & Director

Let me start with a comment there, John. One of the things that's creating us being bias toward the low end of the range is that in 2010, we had an extraordinary benefit to earnings of our U.S. operation caused by the termination of a large case, and that created a net impact to profitability of roughly $40 million that we've got to find some way to cover in next year's earning comparisons. So that $40 million is a pretty good amount. Other than that, we're concerned about layering in of more low interest rates while we've moderated sales expectations in Japan due to modest or difficult comparisons. Japan sales and Japan profitability, probably will be in line in terms of growth with 2010. We still need U.S. sales and U.S. revenue growth to recover to give us growth over and above covering this extraordinary benefit we got in 2010. So offsetting that is our ability to resume the share repurchase program, and having achieved good capital adequacy positions during 2010 will allow us to deploy some of that accumulated capital during 2011.

John Matthew Nadel
Sterne Agee & Leach Inc., Research Division

That sort of segues me to my second question for you guys, and that's really more around the capital, the investment portfolio exposures, and maybe I'll put it this way. From where you stand right now looking out at your portfolio, looking out at the risks, what would it take -- is today's environment the kind of environment that would lead you to be thinking more about the upper end of your buybacks, or do we need to see a continued improvement from here?

Kriss Cloninger
President & Director

Let me start with an answer to that. 2010, as I've said, was a year of strong capital accumulation for us. Though we haven't finalized our statutory results yet, we're confident that our statutory earnings came in at somewhat over $2 billion after tax. The realized losses on a statutory basis are pretty much pretax numbers, and that's going to come in somewhere around $850 million to $900 million. So overall, net earnings on a statutory basis are going to come in and around $1.2 billion. Now, that added to our capital position during 2010. Also, what you make in terms of statutory earnings less your realized losses gives you the amount of money you can dividend out of the like company without special approval. And let's just say that's going to be $1.2 billion, it was $1.4 billion last year, we didn't take out the $1.4 billion, but we could take out -- and I'm speaking hypothetically at the moment, because we haven't finalized the numbers, but we could take out $1.2 billion to apply to capital management purposes. And that assumes that we could absorb say another $1 billion of realized losses in 2011 if we continue making statutory earnings in excess of $2 billion and replenish the capital we took out as the dividend. So that still leaves us in a very strong RBC position. So just hypothetically again, say we took out $1 billion dividend, and I'll go over all this, as I usually do at the cap meeting in terms of sources and uses of capital. But let's say we took out that $1.2 billion dividend, we have over $600 million of cash in holding company, today, let's just say we wanted to maintain $200 million or $300 million of that, that leaves us with, say, $1.5 billion we might want to deploy. I'm giving you just a lot of numbers that are in my head. I haven't prepared them with everybody that matters around here, but this is some stuff I've been playing with. Say we got $1.5 billion available, and we've got a shareholder dividend commitment of around $500 million, a little more, maybe $525 million. Say, that leaves us $1 billion to do share repurchase or other activities, well we've said 6 million to 12 million shares while obviously at the high end of the range at 12 million say buying back shares of $58, $67 a share, we'd spend somewhere between $700 million and $800 million there, and maybe that leaves us a little bit more cushion. So I think the fact that we could I think maintain RBC levels that we ended 2010 at still absorbs some significant realized losses during 2011, which we hope not to do. But I'll let Jerry address that. Still maintained strong fundamental earnings group in statutory earnings, which I expect we'll do, puts us in a very good position for deploying capital during 2011. And I think that's sort of what's on my mind. Some people have asked me in the past, you're going to be so conservative that you'll just sit there and grow RBC levels. And I replied that, no, we're not going to just sit there and create a position where we got significant sterile capital that's not being deployed, and I just want to reiterate that. That's my conclusion. My only caveat is that I do have to worry a little bit about the impact of further strengthening of the yen on the solvency margin in Japan particularly if we increased portion of our Japanese capital that we invested dollars because we lose some solvency margin benefits from doing that. But the yen is already pretty darn strong at JPY 82 to the dollar, and Japanese industry is starting to complain about their ability to maintain exports and the like. So not to say that, that's a controlling factor for currency, and we don't really predict currency, we just try to manage in whatever currency environment we're in, but that's kind of brain dump, John.

Operator

The next question is coming from Jeff Schuman, KBW.

Jeffrey R. Schuman
Keefe, Bruyette, & Woods, Inc., Research Division

I just wondering of you could circle back more on the Japanese sales. The challenges for 2011, I think you're pretty clear including obviously the difficult comps. But I guess the reason why you have difficult comps is because you've had such strong momentum recently, including with the WAYS product, which you just launched. So I guess I want to be clear, maybe one thing that will help the rest of us better understand exactly, how much upside we have left in fully penetrating the bank opportunity? I mean are we kind of -- I mean it still feels like we're pretty early in ramping into the bank opportunity, but is that too optimistic? Are we sort of second inning? Are we seventh inning or where are we in terms of realizing the bank potential?

Daniel P. Amos
Chairman & CEO

Toru, you want to take a shot at that? Then we'll follow up here.

Tohru Tonoike
Vice Chairman of Aflac Japan

Yes, regarding the penetration to the bank channel, we have gone pretty much, but I think the percentage of the bank branches that produce at least one policy per month, that is a benchmark we measure at bank penetration. And that ratio has been growing pretty nicely. At the end of the fourth quarter, that has come to about 50%, a little -- I'm sorry, 27% for all banks and 51% for the mega banks. And that's as of the end of the 2010. And if we look at the fourth quarter, the penetration is even higher, and that has come to 6% for the mega banks. But still, we think we have a lot of potential there. So the number can obviously grow even farther, and even if we reach out the number very close to 100%, that really means that one branch says only 1% for the month. And we have no reason to believe that they can sell two policies per month, or even three policies. So I don't know which inning we are in, but I'm sure that we have a plenty of potentials on that.

Daniel P. Amos
Chairman & CEO

I think the question you're looking for is, the answer is, we're calling for about a 20% increase in new sales in the bank channel in 2011.

Jeffrey R. Schuman
Keefe, Bruyette, & Woods, Inc., Research Division

What is the long-term outlook for Dai-ichi. Is it going to be in permanent decline, or is there another scenario out there?

Tohru Tonoike
Vice Chairman of Aflac Japan

Regarding the Dai-ichi Life, there have been pretty new after becoming a public ownership company. So they are still working on ways they manage the company as a public company. And they want to forecast on that, and they have less time to spend to sell our policy. So last year and probably this year too, their sale of accounts will continue to decline. But once they are comfortably managing the company as it is, there's no reason why we should expect that sales continue to go down in the future. So we hope that can come back. But we don't know yet.

Operator

The next question is coming from Thomas Gallagher, Crédit Suisse.

Thomas George Gallagher
Crédit Suisse AG, Research Division

I had a few investment questions for you. Kriss, you'd referenced $1 billion of credit losses for 2011, and I know you were just talking hypothetically. But if I think about where your heads are at in terms of your portfolio, potential de-risking, I guess I'd like to hear maybe from Jerry, what you're thinking about the Greek banks' exposure that would appear to be your next big slog that you'd need to make a decision at some point or not? And then the other credit side, I'd like you to comment on would be InvestCorp, the Tunisia Exposure and Israel Electric, which I believe was downgraded in 4Q to below investment-grade by S&P, and that's nearly $1 billion position.

Kriss Cloninger
President & Director

Before he starts, I just want to reiterate you gave me the benefit of reminding him it was a hypothetical comment I made. I would just say on statutory basis it was $800 million to $900 million capital loss in 2010. And we could absorb that in 2011 without disturbing RBC. I'm not saying we're going to, I hope we don't, but I'll let Jerry take it from there.

William Jeremy Jeffery
Former Senior Vice President of Fixed Income Investments

Let me just say one thing at the outset. The number one concern that I have and have had is in terms of risks to the portfolio's concentration risks, that continues to be our highest priorities, to look for intelligent ways to reduce our concentration and diversify our risks. And so you've brought up a number of topics that kind of speak to that the first being the Greek banks. I think that obviously that's a very fluid situation. Sure there would be liability management exercises among the Greek banks in 2011 or maybe beyond that. And we'll keep an eye on that, and if it's advantageous to us we may act on it. But we're constantly evaluating that prospect. I got to turn to Israel Elec first. Israel Elec, as you know, is in effect a government agency, if you will. They're more than 99% owned by the government. I think given the structure in Israel, it is highly unlikely that they would have any other owner other than the government in the foreseeable future because of the way their rate structure operates. I think nothing has changed materially in their business model. And in fact, unlike what you've seen happen in Europe, their ability to raise capital in public markets has been unaffected this past month. They just hit the domestic debt, the largest in their history. So their liquidity remains pretty secure. But the problem there has been on what their return on capital can be, and given their capital expansion needs that is something of a sore spot for them, but their operating model hasn't changed. What has changed is that S&P took a look at what has been the status quo for years and decided to kind of fire a shot across the balance, seems to me, and downgrade them and it was a warning shot I guess to Israel they need to ensure Israel Elec can achieve greater profitability. So we'll see what goes there, but they still are monopoly there and essential service in Israel. And their profits while low are adequate. So we're not concerned about their ability to service debt. Turning to Tunisia, what we can say about there is I think it's an interesting situation because one of the key reasons that Ali left Tunisia was he was not able to demonize the opposition because it was not Muslim fundamentalist opposition. It was really much more of a secular opposition. So therefore, I think you have a well educated, very secular population, that I would say that the outcome politically is highly uncertain there. But I would also say that the market has not responded with any material devaluation of their bonds. If you look back to December valuations on Tunisian public debt, and then you look at the valuations today, many of their issues trade well above par, and none of them have been devalued by more than 5% in the marketplace. So I think globally there's not the level of concern about Tunisia that there is in Egypt, which is much more, the opposition there is probably a little more troubling. InvestCorp, I think is again, an interesting situation. I think we remain pretty comfortable with InvestCorp it is a large exposure but they have really shifted much towards a key-based business model as opposed to direct investment and hedge fund et cetera. So their profitability is much more stable. They were able to raise significant capital over the last 18 months. So I would view that as a fairly stable situation.

Thomas George Gallagher
Crédit Suisse AG, Research Division

So given what you've said about Israel Electric and Tunisia, that they're actually trading well, should we view those as opportunities to shrink the size of those positions? Because at least from what I've heard from a number of investors, they're just uncomfortable based on the share size as opposed to the credits.

William Jeremy Jeffery
Former Senior Vice President of Fixed Income Investments

Let me answer the question this way. As I said in the outset, my number one concern is concentration risk. So if there are ways to reduce concentration risks that are beneficial to us, we'll do it.

Operator

The next question is coming from Randy Binner, FBR Capital Market.

Randolph Binner
FBR Capital Markets & Co., Research Division

I think this is another question for Jerry. But I was just trying to understand what changed in your approach to the impairments this quarter, so the two Irish items and Aiful, and how that differs relative to other below investment-grade holdings you have, which kind of had similar unrealized loss positions? Just trying to understand kind of what changed for those and what triggered you to take an impairment on those, and how that differed from some of the other distressed items in the below investment-grade holdings?

William Jeremy Jeffery
Former Senior Vice President of Fixed Income Investments

Let's start with Aiful. The Aiful, as part of the Japanese consumer finance industry, as you probably know, we had an exposure to talk to Fuji and we sold our final exposure in the first quarter of 2010. Aiful was quite a different situation because -- and is quite a different situation, they have a significant amount of liquidity, and they have sources of funding that will last them for at least the next three or four years. But they are operating in an industry where the rules have changed materially in the last couple of years, and it changed negatively for them. But given the support of their banks and given their liquidity, we continue to support them. But when they came out with earnings results, and I think that they came out in October, we became somewhat uncomfortable with the disclosures we were receiving. And so that really precipitated the impairment there. We view their future is, I guess, more opaque than it had been. So that speaks to the Aiful situation. With our Allied Irish banks, really, I guess there were two things there that triggered our decision to sell, impairment sell. First is they started receiving -- and the two are related, the first is that they started receiving significant amounts of support from the Irish government, and as a result the politicians have kind of taken over rule of law when it comes to the rights of the bondholders. We did own a subordinated debt, which prior to the Irish banking crisis, had debt was considered exempt from law sharing. But in Ireland, there are no rules about subordinated debt anymore that we can take comfort in, and we were concerned that the Irish government was going to do exact serious law sharing penalties from subordinated debt holders of Allied Irish. So when Allied Irish announced a tender offer, we pursued that with them. Irish Life & Permanent kind of similar background, quite a different situation or they have not taken on any government support. And at this point it's unclear whether or not it will. But we decided to be proactive in that situation because they too are governed by Irish law that there's no clarity as to why it's going to resolve itself. Did that help?

Randolph Binner
FBR Capital Markets & Co., Research Division

It's a very kind of credit-specific decision all the time based on the variety of circumstances. So there's no kind of rule that we can apply to the other unrealized loss positions on the below-investment grade, and I'm just trying to think ahead of what might come down the pike.

William Jeremy Jeffery
Former Senior Vice President of Fixed Income Investments

You have hit the nail in the head. That's always how we approach these situations. And I'm glad you appreciate it, and we'll continue to approach it that way.

Operator

That next question is coming from Ed Spehar, Bank of America-Merrill Lynch.

Edward A. Spehar
BofA Merrill Lynch, Research Division

Kriss, I wanted to go back to clarify some of your statutory comments. I guess first on statutory operating earnings, I think your stat operating earnings to the first nine months were about $1.8 billion. So you're running about $600 million a quarter. Did something happen in the fourth quarter? Or are you just rounding down in terms of what you're saying stat operating earnings were for the full year?

Kriss Cloninger
President & Director

Maybe rounded down a bit, Ed. But we did, I'm sure, carryover the dementia reserve adjustment to the statutory and things of that nature. So like I said, I don't have the final numbers, but you can assume I've rounded some of those down. Remember, too, that the ILT impairment, we'd impaired it before using the equity impairment method because it's perpetual. It had not been impaired on sets. So when we impaired it in the fourth quarter of '10 for credit purposes, a much greater amount hit stat.

Edward A. Spehar
BofA Merrill Lynch, Research Division

Right, but that would be net. But I'm talking about operating. So that would have been through operating, correct?

Kriss Cloninger
President & Director

I'm sorry. Yes that's a net only.

Edward A. Spehar
BofA Merrill Lynch, Research Division

And Kriss, your comment about pretax and after-tax losses being the same on stat, is that what we should expect going forward? Or should we expect that you would be able to have tax offsets, if you did have some high levels of losses?

Kriss Cloninger
President & Director

Well on a stat basis, we don't get the same deferred tax treatment that we get under GAAP. We don't get the full benefit of a deferred tax offset on realized losses. On stat, it's more keyed to, tied into the cash tax return. There are some deferred tax provisions, but they're normally lower than you get on GAAP. And I'm not an expert on deferred tax statutory accounting. So I probably need to get back to you on that some. But I know we don't get the full benefit under stat that we get under GAAP.

Edward A. Spehar
BofA Merrill Lynch, Research Division

But you would assume that on a normal basis you get some offset, correct?

Kriss Cloninger
President & Director

Yes, there's some. But it's not the full tax rate, assuming that you can fully utilize realized losses in future tax returns.

Edward A. Spehar
BofA Merrill Lynch, Research Division

And the question on margins. If you look at your sales expectations in Japan for 2011, and you think about what the mix is of sales in 2011, what would be -- if we're trying to sort of think about the margin dynamics here with the mix shift, if your margin in 2010, your pretax margin on revenue was, I think it was 20.6%, if you just looked at the collection of business you're going to write, or you think you'll write in 2011, what kind of range of margin would you think if you try to put it on a comparable basis thinking about pretax margin on revenue?

Kriss Cloninger
President & Director

It depends. I know you know that production in the bank channel, particularly of the child endowment and WAYS, is going to drive the overall margin down a little bit because those two products produce more investment-spread income than they do -- let me use a property and cash context underwriting income, the difference between premiums, benefits and expenses, particularly child endowment, that's kind of as close to zero underwriting product we're putting equals benefits and expenses at the assumed pricing interest rate. And then what you do is make a spread on the reserves based on the difference between earned interest rate on investment assets and the required interest rate on reserves. And that's going to emerge more over time, Ed, on that child endowment. And also I've talked about advanced premium deposit funds of being spread-type generator, too. So those spreads don't emerge in proportion to premium. They emerge over time in proportion to invested assets and earned rates versus credited rates. And WAYS is similar though not quite as extreme as child endowment. So I'm telling you that if the margin, the underwriting margin goes down, it's going to be replaced to some extent by increased investment spreads that you won't directly see. The way we look at the numbers now, I'm promising you all, we talked about this some the many fab in September, we didn't talk about it on the program, but I talked to a number of you. I'll mention it again, I think in the third quarter report and at the fab meeting in May, I'm going to try to lay out a lot more about the impact of child endowment and WAYS on the margin computations. But I want to assure you that those products are expected to produce profits, not quite at the level of our medical products. And I've told you that, that they're going to add to the overall profitability of corporation by growing revenue faster than we otherwise would have grown it, and by producing margins, they're going to add to total profits.

Edward A. Spehar
BofA Merrill Lynch, Research Division

Anyway Kriss, if you can just tell us what you think about just on a statutory our cash basis what type of internal rate of return you think you'll get on selling those products?

Kriss Cloninger
President & Director

Yes, it's in the teens, I don't think it's in the 20s.

Edward A. Spehar
BofA Merrill Lynch, Research Division

High or low?

Kriss Cloninger
President & Director

Huh?

Edward A. Spehar
BofA Merrill Lynch, Research Division

High teens, low teens, mid-teens?

Kriss Cloninger

President & Director

I'd say mid to more like, let me just say, 15 to 17 I think is what I've been seeing out of some of our profit testing work.

Robin Y. Wilkey
Former Senior Vice President of Investor & Rating Agency Relations

Catherine, it's just past 10:00. So I think it's time for us to close the session, please.

Operator

And would you like to take one more question?

Robin Y. Wilkey
Former Senior Vice President of Investor & Rating Agency Relations

I'm sorry, we're past 10:00 already. Thank you.

Operator
Thank you for participating in today's conference. This will conclude today's session. All parties may disconnect at this time.