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Market Intelligence

Aflac Incorporated NYSE:AFL

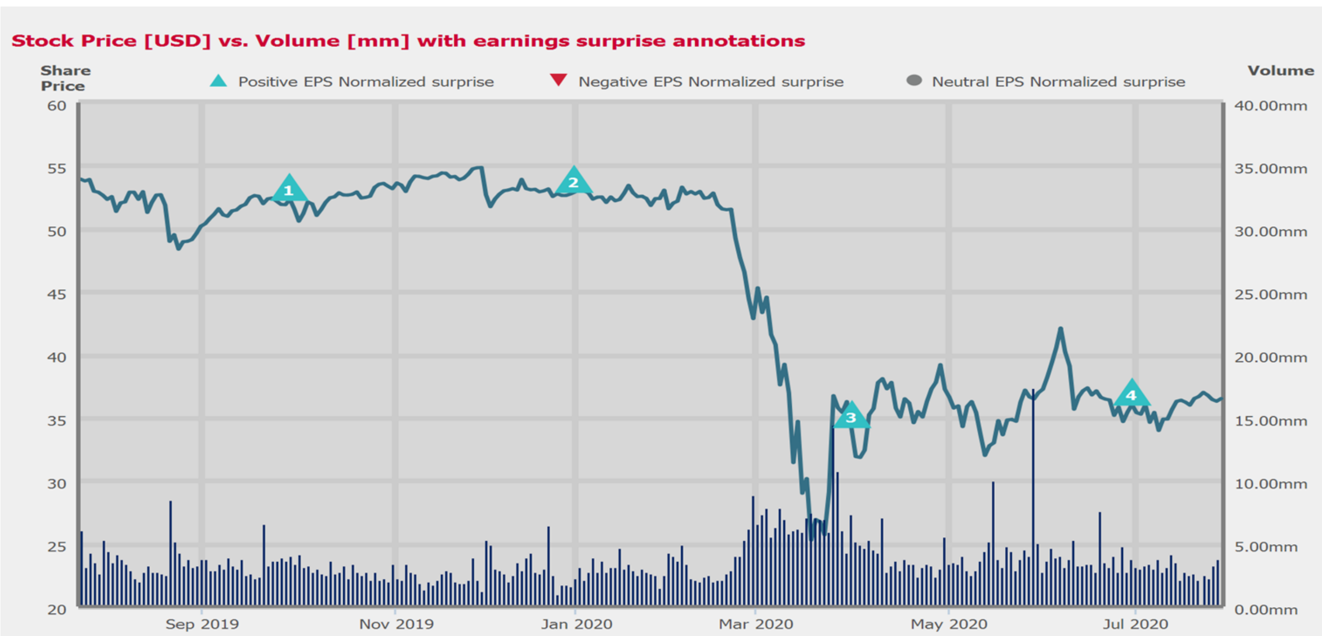
FQ2 2020 Earnings Call Transcripts

Wednesday, July 29, 2020 1:00 PM GMT

S&P Global Market Intelligence Estimates

	-FQ2 2020-			-FQ3 2020-	-FY 2020-	-FY 2021-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	1.05	1.28	▲21.90	1.09	4.60	4.44
Revenue (mm)	5487.26	5407.00	▼(1.46 %)	5460.86	21918.40	21481.82

Currency: USD
Consensus as of Jul-29-2020 11:48 AM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ3 2019	1.07	1.16	▲1 8.41 %
FQ4 2019	1.02	1.03	▲2 0.98 %
FQ1 2020	1.10	1.21	▲3 10.00 %
FQ2 2020	1.05	1.28	▲4 21.90 %

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Call Participants

EXECUTIVES

Daniel Paul Amos
Chairman & CEO

David A. Young
Vice President of Investor & Rating Agency Relations

Frederick John Crawford
President & COO

Koji Ariyoshi
Executive VP, Director and Director of Sales & Marketing of Aflac Life Insurance Japan

Max Kristian Brodén
Executive VP & CFO

Richard L. Williams
Executive VP & Chief Distribution Officer

Teresa Lynne White
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ANALYSTS

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Crédit Suisse AG, Research Division

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Dowling & Partners Securities, LLC

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JPMorgan Chase & Co, Research Division

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Piper Sandler & Co., Research Division

Presentation

Operator

Welcome to the Aflac Second Quarter 2020 Earnings Conference Call. [Operator Instructions] Please be advised, today's conference is being recorded.

I would now like to turn the call over to Mr. David Young, Vice President of Aflac Investor and Rating Agency Relations. Thank you, sir. You may begin.

Sir, could you check your mute button, please?

David A. Young
Vice President of Investor & Rating Agency Relations

Thank you, Fran. Good morning, and welcome to Aflac Incorporated Second Quarter Call. As always, we have posted our earnings release and financial supplement to investors.aflac.com.

This morning, we will be hearing remarks about the quarter as well as our operations in Japan and the United States amid the COVID-19 pandemic. Dan Amos, Chairman and CEO of Aflac Incorporated, will begin by discussing the impact of the pandemic and our ongoing response.

Fred Crawford, President and COO of Aflac Incorporated, will then touch briefly on conditions in the second quarter before providing perspective on claims exposure to COVID-19. Max Brodén, Executive Vice President and CFO of Aflac Incorporated, will conclude our prepared remarks with a summary of second quarter financial results and current capital and liquidity.

Joining us this morning during the Q&A portion are members of our executive management team in the U.S., Teresa White, President of Aflac U.S.; Eric Kirsch, Global Chief Investment Officer and President of Aflac Global Investments; Rich Williams, Chief Distribution Officer; Al Riggieri, Global Chief Risk Officer and Chief Actuary; and Steve Beaver, CFO of Aflac U.S. We are also joined by members of our executive management team in Tokyo at Aflac Life Insurance Japan; Charles Lake, Chairman and Representative Director, President of Aflac International; Masatoshi Koide, President and Representative Director; Todd Daniels, Director and CFO; and Koji Ariyoshi, Director and Head of Sales and Marketing.

Before we begin, some statements in this teleconference are forward-looking within the meaning of 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 discuss today. We encourage you to look at our annual report on Form 10-K for some of the various risk factors that could materially impact our results.

As I mentioned earlier, the earnings release is available on the company's investor site, investors.aflac.com, and includes reconciliations of certain non-U.S. GAAP measures.

I'll now hand the call over to Dan. Dan?

Daniel Paul Amos
Chairman & CEO

Thank you, David, and good morning. Shortly, I will provide an overview of the quarter and how we performed.

[Audio Gap]

is in their families, the people who are on the front lines fighting the spread of COVID-19 and those who are providing essential services, including our own employees.

As I shared with you last quarter, the guiding focus of our actions has centered on the healthy and safety of our employees, distribution partners and policyholders we serve. You'll recall last quarter that we ramped up our work-at-home staffing models in both Japan and the United States. We saw a little in the way of disruption in the operations and our employees adapted well. Since our last earnings call, the government of Japan has lifted state of emergency on May 25, and the country has seen new cases rise since mid-June but on a lesser scale, relative to the United States.

Recently, Japan reported a little over 900 cases in a day. With risk of infection remaining, the national and local governments are monitoring the spread very closely as the country gradually opens taking action when necessary. Aflac Japan has also taken steps with approximately 50% of the workforce returning to work on site.

Our actions are taken into consultation with leading medical experts in Japan, including Professor and Dr. Koji Wada. And following health and safety protocols for the industry developed by the Japanese Business Federation and Life insurance Association of Japan. Aflac Japan continues to monitor the situation and encourage remote work to the greatest extent possible.

At the same time, the United States has seen daily new cases and hospitalizations significantly on the rise since mid-June. Recently, new cases exceeded 75,000 in 1 day in the United States. Increasingly public health experts are advocating for the need to observe prudent protective measures through the fall and early winter.

As a result, Aflac U.S. plans on beginning a regional stage gating approach for returning to on-site work in 2021. We feel that this is the best approach for our employees as well as the health of our communities. Our employees in both countries have shown incredible determination and professionalism over the course of this year. For example, even amid the global pandemics, ever-changing working locations and conditions, our employees in Japan and the United States have demonstrated a determination to now more than ever, put policyholders first.

In fact, 2 weeks ago, Aflac Japan received the honor of being the #1 company in customer loyalty among the 13 life insurance companies in the NTT Com Online benchmark survey. This survey was conducted in May, right in the middle of the COVID pandemic, which shows our ability to adapt. Our factors customers ranked were Aflac #1 included our customer service and listing approach, our corporate and brand image, and our friendly policyholder website.

Receiving recognition such as this from the very people we support is the highest honor, especially considered in the current environment. It also reflects our collective hard work and dedication to be there for the policyholders when they need us most. Another way we have supported our policyholders through this difficult time is extending the grace periods for premium payments in both Japan and the United States. Initially, Aflac Japan followed the FSA guidance and extended the grace period on premium payments to September 30, 2020. In June, Aflac Japan like its industry peers, extended the premium grace period until April 30, 2021. Policyholders are required to file for relief through this extension.

Aflac U.S. has also implemented premium grace periods. And those periods remain in effect in 23 states as of July 20, 2020. The environment created by COVID-19, which has included sheltering in place and social distancing, continues to impact our sales results, both in the United States and in Japan.

We are carefully monitoring our core products and actual to expected non-COVID claims. We are proactively reaching out to employers and policyholders to assist in understanding our product benefits and to ease the filing of qualified claims. We are also communicating on the value of the wellness benefits attached to our products for reimbursement of routine doctor, dentist and hospital visits as shelter-at-home orders subside and normal activities recover.

We have done this in the past. And while current conditions are unique, our experience is that this will drive utilization, benefit ratios and improved persistency.

Turning to sales. Aflac U.S. total sales were down 56% in the quarter. Aflac Japan sales were down 60% in the quarter, which also reflects last year's strong second quarter sales by Japan Post. While the technology for virtual sales existed prior to the pandemic, market practice and preference favored face-to-face presentations.

In both countries, we're having to pivot to a more virtual sales execution. Within the current environment, virtual takes on greater importance, especially in those areas that are slower to open up. For Aflac Japan, this will mean additional digital transformation initiatives, utilizing artificial intelligence to better identify customers' needs and consult with customers through the web.

On July 3 at the Strategic Alliance Executive Meeting, Japan Post Holdings CEO, Masuda-san, and I agreed to a joint promotion of such digital transformation initiatives. I was glad that we were able to have our virtual meeting that evening, and I hope that we can visit very soon in person.

Recognizing that face-to-face sales will be challenging, Aflac Japan continues to pursue new business through direct mail and calling campaigns to existing and prospective customers. We're also preparing to introduce a new system that enables online consultation by allowing the customer and our agency to see the same screen through the digital device.

Additionally, we will enhance this system to enable smartphone-based insurance application ahead of all other companies in Japan. Likewise, our production model in the United States relies heavily on face-to-face interaction at the work site and is small business oriented. As such, we were hit hard by temporary closures of business and lack of access at the work site, especially in the second quarter.

Keep in mind, the fourth quarter is typically the quarter in which we see strong results in the broker-driven group market, which has generally been more resilient to conditions. This makes us cautiously optimistic as we see potential for modest sales improvements for Aflac U.S. in the second half of the year, also contingent upon the pace of the economic recovery.

We continue to progress toward closing our definitive agreement to acquire Zurich Group Benefits business, which allows us to extend our distribution reach and extend our appeal to brokers and larger employers.

When stepping back from the quarter and reflecting on the events impacted the economy and our business model, I remain confident in how we are positioned despite our shared concerns over conditions in the United States, we're able to move forward with key growth and efficiency initiatives that require near-term investments in order to be positioned for future growth and opportunity.

We are learning more about how the pandemic is impacting our business and are quickly pivoting to better balance to face-to-face and virtual sales practices. We have thus far depended our strong margins in Japan and the United States, and asset quality remains strong.

Additionally, our overall capital and liquidity positions allow us to continue uninterrupted the balance of the investments in the business, opportunistic investments and returning capital to the shareholders. Let me conclude with the topic of social justice, which has been thrusted into the spotlight in the United States since the last earnings release.

Aflac is and has always been for fairness and justice. Diversity and inclusion are not new concepts for Aflac. We have consistently received recognition in various publications, including being named to Black Enterprise list of the 50 best companies for diversity, 13 times and LATINA Style list of the 50 best companies for Latinos to work for the United States 20 times. A key tenet of the Aflac way is treating people with respect and care. This is critical when considering that 46% of our U.S. employees are ethnic minorities and 66% are women.

We continue to partner with organizations like the Congressional Black Caucus Institute's, 21st Century Council and the Business Roundtable to raise issues that can lead to meaningful change in public policy. As an inherent part of the culture, we oppose any form of bigotry, intolerance and disrespect in our society. We are committed to fight for racial justice and equality for all. At Aflac, we have always believed that fostering a diverse workforce isn't just the right thing to do. It makes good business sense.

When our people reflect the diversity of our communities in which we operate, we strengthen our opportunities in connections with customers and policyholders.

Now I'll hand the program off to Fred and Max. Fred?

Frederick John Crawford
President & COO

Thanks, Dan. I'm going to touch briefly on conditions in the second quarter, how we're tracking to COVID-19 stress testing assumptions and an update on key initiatives in Japan and in the U.S.

In Japan, we track data coming from the Ministry of Health, Labor and Welfare as well as the COVID-19 subcommittee of the Cabinet Advisory Council for infectious disease. As of July 27, there were approximately 30,500 cases and 1,000 deaths in all of Japan. Our stress test assumed a midpoint estimate of 1.2 million confirmed cases and a 100% hospitalization rate consistent with Japan's infectious disease guidelines. When applied to our book of medical policies and assuming an average of 20 days in hospitalization, the result was a potential impact to our third sector benefit ratio of 50 to 100 basis points in 2020.

However, through the second quarter, Aflac Japan's COVID-19 impact totaled only 626 claimants, with claim payments totaling JPY 138 million. For COVID, hospitalization claims, thus far, the average stay in a hospital is approximately 20 days, with 2/3 of claims in hospital and 1/3 at home or hotel-based hospitalization. In short, we are tracking well below any risk of stress conditions with no measurable COVID-19 impact to core ratios from paid claims. The impact is somewhat isolated to sales and a related uptick in persistency, which Max will comment on later.

Turning to the U.S., the story, of course, is very different. We continue to track the rate of reported cases, hospitalization and deaths from sources such as the CDC and Johns Hopkins.

As a country, COVID-19 case levels in the U.S. now exceed 4.3 million, with deaths nearing 150,000. In addition, hospitalization rates in certain CDC red zones have been on the rise. Our U.S. stress test assumed 6.4 million confirmed cases in the U.S., 1.5 million hospitalizations and 150,000 deaths. In short, we are unfortunately tracking to our U.S. macro stress test assumptions. It is, however, important to understand the critical statistics that impact our business model that surround hospitalization and disability. Our stress test applied age-based hospitalization rates, with 40% of those hospitalized spending time in the ICU. We further assumed 75% of confirmed cases filed for short-term disability. The resulting stress test impacted our U.S. benefit ratio in the range of 300 to 500 basis points for 2020.

Through the end of the second quarter, U.S. -- actual U.S. COVID-19 claims now total 5,000 claimants, incurred claims in the quarter totaled $31 million with 70% representing COVID-specific increase in IBNR.

The majority were filed under our short-term disability policies representing 80% of claimants, and we have yet to see any expected increase in overall hospitalization and wellness claims.

To give you perspective, COVID-19 incurred claims, excluding wellness benefits, are coming in at 40% of our modeling assumptions. While still early, given a natural lag in filing claims, we suspect our favorable experience relative to stress test assumptions is partially attributed to the work site and a younger population of policyholders with a lower level of co-morbidity or preexisting conditions.

As Dan noted in his comments, the impact of COVID-19 incurred [times] in the quarter was more than offset by a temporary reduction in routine doctor and hospital visits, driving down our benefit ratios. We believe this is largely timing related and not likely to change our view of expected lifetime loss ratios. In fact, while still below pre-COVID volume, we have seen frequency of claims rise in the last few weeks of June and into July.

Recall that in the U.S., we are stressing persistency, which has historically been [indiscernible] unemployment. We have thus far seen limited impact to cash receipts and persistency and believe this is somewhat supported by the Paycheck Protection Act that is set to expire August 8.

As Dan mentioned, premium grace periods are still in place in many states, thus somewhat supporting persistency. We see the third quarter as a critical period with state regulatory orders expiring and further stimulus under consideration.

A key pressure point for our U.S. business model as we enter 2021 is earned premium. We are, therefore, focusing on retention efforts that include proactive outreach to policyholders, conversion of payroll deduction to direct bill and campaigns to work with the employers and employees on how best to leverage health and wellness benefits.

We are also naturally focused on expenses carefully regulating staffing models and giving investment priority to initiatives designed to drive a lower cost structure.

Turning to Aflac Global Investments. We remain focused on asset quality, monitoring global economic conditions and sourcing new investment opportunities in this low interest rate environment. Our firm view is that we will experience a checkmark-shaped recovery, meaning a slow road to recovery with pockets of volatility along the way. We have moved away from the notion of a V-shaped or even U-shaped recovery as the basis for tactical asset allocation, capital management and maintain cautious credit view. Therefore, our tactical approach has included further derisking activity on vulnerable exposures. While net investment income is tracking ahead of our original outlook guidance for 2020, we do see a slower build in our loan portfolios as well as lower variable net investment income from alternative investments that we originally forecasted.

While retaining more invested capital, we are also remaining more liquid, thus enjoying very little contribution to net investment income.

We continue to explore ways to optimize our approach to currency hedging, and just this week, completed locking in a portion of our hedge costs for 2021, given a low relative hedge cost environment. Finally, this is the first quarter recognizing income from our Varagon strategic investment, booking $4 million of income through our corporate segment and integrating their investment expertise into our investment strategy.

While modest, we see our tactical approach to strategic investments as a natural extension of our external manager platform and an area of growth in sourcing new investment opportunities while taking minority stakes in attractive asset management franchises.

Let me switch gears and comment briefly on key initiatives within our insurance segments. Despite an understandable focus on COVID, we continue to push forward on significant initiatives in readying our platform for future growth and efficiency.

On our first quarter call, I noted our paperless initiative in Japan, specifically in our Policyholder Services division. We have completed further analysis and now intend to expand beyond policyholder services to a broad commitment across all operations in Japan. Our decision to expand the scope is driven by economic return but also to improve business continuity and work-from-home capacity while reducing our carbon footprint, which is consistent with our commitment to ESG.

This is a 3-year and roughly JPY 10 billion investment that is front-end loaded with approximately 40% to 50% of the investment targeted for 2020. The expanded and accelerated scope is expected to reduce the production and circulation of 80 million pieces of paper per year with run rate savings in the range of JPY 3 billion annually once completed. Our product pipeline is also a key work stream in Japan, and we have altered our strategy to recognize launching new product in 2020 as suboptimal given the reduced face-to-face sales environment. This strategy also recognizes conditions at key banking, post office and other agent-driven alliance partners. While critical work will be accomplished in 2020, we plan to relaunch our enhanced cancer product early in the fourth quarter and have postponed the timing of our new medical product to early 2021.

Turning to the U.S., we accelerated certain investments-specific elements of our digital road map into 2020. These initiatives include advancing virtual tools as part of the rollout of our refreshed small business enrollment platform, allowing our agents to be more productive in a virtual-engaged model.

Group ecosystem investments to automate account onboarding and in advance of integrating our Zurich Group Benefit acquisition, advancing My Aflac digital self-service, both web and mobile for more intuitive customer experience and to reduce reliance on expensive call center support. And then finally, investment in digital claims automation, requiring an agile approach from product design to ultimate payment of claims.

These investments are multiyear and larger in scale, the total incremental or accelerated investment in 2020 is approximately $25 million. The build-out of U.S. network dental and vision remains on track. We have successfully filed our new network dental and vision products in 40 states and expect to ramp up as we move towards 2021. Very important is the introduction of this product into our new enrollment tools to drive small business opportunities, including further penetration and improved persistency.

Our consumer markets platform remains on track with product filings underway and systems work to ensure a digital end-to-end experience. We are currently offering accident, critical illness and cancer products on our platform as well as partnering on other third-party digital platforms. In terms of our March announcement on Zurich Benefits, we continue to track towards closing later in the year with good progress on the regulatory approvals and day 1 integration planning.

We're very excited about welcoming the Zurich team to Aflac and are focused on limiting any disruption as the acquired business strives to hit existing growth targets. In both Japan and the U.S., we view 2020 as a critical year of execution and readying for 2021, and hopefully, the other side of this devastating pandemic.

I'll now pass on to Max to discuss our financial performance in more detail. Max?

Max Kristian Brodén
Executive VP & CFO

Thank you, Fred. Let me begin with a review of our second quarter performance and focus on how our core capital and earnings drivers have developed over the past quarter. As was the case when we announced first quarter earnings, the timing and magnitude of the COVID-19 impact on 2020 earnings continue to be uncertain. For the second quarter, adjusted earnings per share increased 13% to $1.28, driven primarily by favorable benefit ratios in the U.S.

The strengthening yen impacted earnings in the quarter by $0.01. As a result, adjusted earnings per share on a currency-neutral basis rose 12% to $1.27 per share. Adjusted book value per share, including foreign currency translation gains and losses grew 7.5%, and the adjusted ROE excluding the foreign currency impact was a strong 16.3%, a significant spread above our cost of capital.

There were no onetime items to call out for normalizing purposes in the quarter. As expected, given market conditions, our alternative investment portfolio recorded a loss in the quarter of $7 million and was approximately $20 million below our long-term return expectations for the portfolio-adjusted for the J-curve. We have a modest but building portfolio, which currently stands at $657 million.

Turning to our Japan segment. Total earned premium for the quarter declined 2.5%, reflecting first sector policies paid up impacts while earned premium for our first sector protection and third sector products was flat year-over-year.

Japan's total benefit ratio came in at 69.8% for the quarter, up 90 basis points year-over-year, and the third sector benefit ratio was 59.6%, up 110 basis points year-over-year. The main driver for the increase was lower lapses associated with policyholders updating their coverage, which tends to lead to reserve releases, boosting current quarter results by lowering the benefit ratio.

Given the current lower new business activity, this naturally pushes up our benefit ratio due to lower reserve releases, decreases DAC amortization and improves reported persistency. We did experience all of this in the second quarter, manifested by our persistency improving 70 basis points year-over-year.

Our expense ratio in Japan was 20%, down a 50 basis points year-over-year. In the current environment, we did incur lower acquisition expenses like lower promotional spend and lower surrenders brought down our DAC amortization, as previously mentioned. We view this as primarily timing related and would expect our expense ratio to increase when a new business environment normalizes.

Net investment income increased 2% in yen terms despite lower variable investment income, driven primarily by higher allocation to U.S. dollar floating rate assets early in the year. The pretax margin for Japan in the quarter was a strong 22%.

Turning to our U.S. results. Earned premium was down 0.1% due to weaker sales results and a flat persistency year-over-year. Our total benefit ratio came in at 44.3%, 590 basis points lower than Q2 2019 driven by reduced claims from accidents, less wellness visit and elective surgeries.

Our expense ratio in the U.S. was 35.3%, up 50 basis points year-over-year as the inclusion of Argus and direct-to-consumer digital investments structurally has increased the expense ratio by 140 basis points. Lower sales bonus, travel and expenses associated with claims adjudication were a meaningful offset to the Argus consolidation and lowered earned premiums. Net investment income in the U.S. was down 4.4% due to capital management actions in December 2019, leading to a reduced invested balance and 13 basis points contractions in portfolio yield year-over-year. Profitability in the U.S. segment was boosted by the previously discussed benefit ratio, leading to a pretax profit margin of 25.7% in Q2, up 510 basis points year-over-year.

As Fred noted, we are carefully monitoring persistency in the U.S. as premium grace periods expire and economic, particularly unemployment conditions develop. We expect the combination of reduced sales and persistency to weigh on revenue during the second half of 2020 and more materially as we enter 2021.

We expect the earned premium decline in the range of minus 3% to flat for the full year of 2020, and we'll update our forecast for 2021 later in the year, given the number of variables involved.

In our Corporate segment, amortized hedge income contributed $27 million on a pretax basis to the quarter's earnings. And we had an ending, notional position of approximately $5 billion. Our capital position remains strong, and we ended the quarter with an SMR of above 900% in Japan and an RBC of approximately 600% in Aflac Columbus.

Holding company liquidity stood at $4.7 billion, $2.7 billion above our minimum balance. In terms of credit conditions in our insurance general account, we took further derisking actions selling out of approximately $320 million of COVID-exposed securities, triggering a realized loss of $45 million.

While total impairments and losses may appear elevated, the $166 million net investment loss includes an increase in CECL reserves of $161 million, reflecting ratings downgrades and calibrating our third-party model inputs for COVID-driven economic conditions.

We remain cautious in regards to both the economic outlook and spread of COVID-19, leading us to retain more capital in our subsidiaries as a first line of defense in case of any sudden deterioration in capital markets or virus-related claims. At this point, we deem it more efficient to temporarily hold capital at the subsidiary level versus at the holding company.

It is the flexibility in our capital structure and capital resources that gives us this option, while continuing to deploy capital to the benefit of our shareholders through dividends and buybacks.

In the second quarter, we repurchased $188 million of our stock. Going forward, we will continue to be tactical around both our capital structure and deployment in order to drive a balanced risk-adjusted return on capital within the company.

Now let me turn it over to David to begin Q&A. David?

David A. Young
Vice President of Investor & Rating Agency Relations
Thank you, Max. Now we are ready to take your questions. [Operator Instructions]. Fran, we will now take the first question.

Question and Answer

David A. Young
Vice President of Investor & Rating Agency Relations

Fran, are we open to take questions? We're not hearing anything.

Operator

Yes, we definitely are. We had a delay there. [Operator Instructions] Our first is from Jimmy Bhullar with JPMorgan.

Jamminder Singh Bhullar
JPMorgan Chase & Co, Research Division

So I had a question on your sales in the U.S. and it doesn't seem like there was much of an improvement in sales as you went through the quarter. But as businesses are opening up, are you seeing your sales recover? Or the companies are still reluctant to have agents come in and try to sell to their employees.

So just any sort of color on what's going on, obviously, in the fourth quarter, the broker sales will pick up, but any color on the agency channel. And I think last quarter, you had given some guidance on April sales, if you have anything similar to July.

Daniel Paul Amos
Chairman & CEO

Teresa, would you like to answer that?

Teresa Lynne White
President of Aflac US

Yes. I'll start, and then I'll pass it to Rich. Certainly, I think the environment is impacting the sales results. And specifically in the small case market, we see it being more pronounced. As we see states start to open back up and our sales teams starting to adjust, I think they're trying to find the right balance between safety and productivity.

And so from an Aflac perspective, what we're attempting to do is provide support, ensuring that the accounts -- that our accounts and their employees have information. So the sales teams were equipping them with information to provide to accounts. And this is really to get activity, get people back out and get people to utilizing their virtual tools. While also, we're working to preserve the distribution platform for our agents, specifically by providing loans, technology and training, preparing for a virtual sales environment. So we do realize that it's going to take time for adoption. I'll let Rich speak specifically on the quarter and go forward. Rich?

Richard L. Williams
Executive VP & Chief Distribution Officer

All right. Thank you, Teresa. So specifically to the question, in the month of July, we have definitely seen levels that are better than what we experienced in the second quarter, but clearly not at pre-pandemic levels.

As we think about the second half of the year, very consistent with guidance we've shared. We tend to see more broker sales in the second half of the year and in larger cases. And so the larger case market is more receptive to virtual enrollment. And so we do expect to see some progress there. Obviously, in smaller business market, it will just simply depend on businesses availability and adoption of virtual enrollment.

But as Teresa mentioned, the long-term play is to recover our distribution platforms for 2021 going forward to use the virtual tools that we've had for many years and really just to pivot to a new way of doing business.

Frederick John Crawford
President & COO

Jimmy, this is Fred. One other thing, and Rich can comment on this. But 1 other dynamic that we're experiencing is recruiting. Recruiting normally strengthens during weak employment periods. That's been our history through, say, normal economic cycles. And it's no different here. We can see a tick up in eligible recruits and recruiting activity during weakness in the economy. The problem is a unique one, and that is the licensing processes at the state level are often closed or slow to operate with backlog. Some of that is related to gathering people for more larger licensing processing.

And so because we recruit so many people across the country that come to us without previous insurance experience, that licensing becomes critical. It's very different if you had a model that was recruiting previously licensed agents away from other insurance carriers, et cetera. That's not our model.

So we also would like to see that open up as time goes on at the state level, and that would help with the natural volume of new sales that comes as you bring in new recruits.

Jamminder Singh Bhullar
JPMorgan Chase & Co, Research Division

Okay. And any comments on what you might have seen in Japan since the end of the quarter or as things are getting at least a little bit better than they were earlier?

Daniel Paul Amos
Chairman & CEO

All right. Japan, who would like to take that? Koji?

Koji Ariyoshi
Executive VP, Director and Director of Sales & Marketing of Aflac Life Insurance Japan

[Interpreted] So during the state of emergency declaration in May, shops were shut down, and we were not able to conduct face-to-face sales.

So we were in a very difficult position.

And we have been continuing nonface-to-face solicitation through phones and mail. And since June, after the state of emergency declaration has been lifted in Japan, we've been following the guidelines issued from the government as well as life insurance association of Japan in terms of prevention of infection, and we have gradually started our solicitation through face to face.

Our shops have resumed or reopened. Now that the shops have been reopened for a while, the number of customers and the traffic coming into shops are on the increase. In June, we had about 50% of customers compared with our normal times coming into our shops. And in July, we are back to 70%. However, we are still not at a point where we had lots of customers coming in pre-COVID-19.

And at the same time, face-to-face solicitation is also recovering as well. I mean it is very gradual that we are starting. And because face-to-face solicitation is very challenging under the current COVID-19 situation. And since it's very difficult to see customers face-to-face directly, what we are doing is developing a tool to have virtual face-to-face meeting with customers using digital tools on the web.

And we are trying to develop this tool so that the tool itself will allow the concluding of the entire process to the application for the insurance policy. And this tool and this kind of activity is -- we are taking this activity ahead of others.

So what we'd like to do is to really strengthen our response capability to customers under the new normal after the COVID or during the COVID-19 because of the current situation. So what we are planning to do is, of course, continue to use our phones and mails as we did in our previous or the current non face-to-face environment, but we would also like to be adding like a virtual face to face through the web and then perhaps have the application be submitted through this virtual web face -- non-face-to-face tool.

That's all for me.

Operator

Our next is from Humphrey Lee with Dowling Partners.

Humphrey Lee
Dowling & Partners Securities, LLC

A question related to the U.S. to benefit ratio. I think you talked about the deferral treatments have helped -- some of the -- have delayed some of the expected claim activity but you assume some normalization. I was wondering if you can elaborate a little bit more about your kind of expectations for your claims experience for the second half of the year?

Frederick John Crawford
President & COO

Yes. We -- what we're seeing is, I think what you're starting to see across the industry as more companies report, and that is there's been the natural putting off, if you will, of routine doctor, dentist and more routine hospital visits due to the shelter-in-place and general concerns over COVID.

And we are, in fact, starting to see that open back up again in select areas of the country, where people are coming back in, and we're starting to see claims pick up, particularly in the last week or so of the quarter and then into July.

What I would say is that we're still traveling at levels lower year-over-year than the claims experience in those products last year this time. So they have not recovered back up to what we would call a normal level, but they are certainly more elevated than what we experienced in the early part through, say, midway into the second quarter.

What we are doing, however, is also very important, and that is we are proactively reaching out to employees and employers to remind them of the benefits that they have in our policies how to consider whether or not they're eligible or have a qualified event and can file a claim, how easy it is to file a claim, how quickly the money comes directly to them.

And in particular, we're focused on wellness claims, which are attached to many of our policies, but most notably our accident policy. And by proactively reaching out to policyholders to remind them that if they did, in fact, go to see the doctor or dentist on a routine measure or they plan to, to remember that they've got a wellness benefit, which will typically reimburse them to the tune of, say, $60 or so by visit.

Historically, we've done this on a kind of a state-by-state basis at times and usually, what we find is that there'll be a pickup in utilization, which you would expect, but we also hope to achieve better persistency by reminding people of their benefits.

The key time to do this is, in fact, typically in the third quarter, not just because of COVID dynamics, but because that's also about the time when people are reviewing with their employer, their benefits and considering whether to sign up again.

It's also particularly important for us right now because it's a way to moderate to some degree, the risk of these state orders falling off throughout the quarter as well as the possibility of stimulus falling off.

So we would expect to do some outreach in the third quarter. We would expect that to increase utilization. It's very difficult to project it and so can't really guide on what we expect. But we think those activities will recover some of the benefit ratio, second half.

Humphrey Lee
Dowling & Partners Securities, LLC

That's helpful. Shifting gears to kind of the investment portfolio, so in Max's prepared remarks, he talked about there's some CECL allowance in the quarter.

My understanding is that it's largely for the middle market loan portfolio. Can you talk about -- for the balance of your portfolio, kind of what percentage of that is on kind of potential downgrade watch right now?

Max Kristian Brodén
Executive VP & CFO

So this is as you mentioned, it's predominantly in the middle market loan portfolio that we did experience some rating migration. We're not going to speak to specifically on any breaking down the whole portfolio, what is sort of on any sort of watch list. But I would say that the 2 categories that primarily is driving the CECL reserve to increase is the middle market loan portfolio and the transitional real estate portfolio. Those are the 2 asset classes that primarily drove that. Of the $161 million of this generic increase in the CECL reserve, about half of it was driven by ratings and about half is driven by updated economic outlook input into the model.

And keep in mind that this model is a third-party model that we utilize. And there is a lag impact. So you may question, why is the increase coming now, not at the end of the first quarter? It's really because there's a moving window in terms of data that goes into the model. And obviously, we now have greater weight on 2 quarters of, let's call it, COVID-related economic input and outlook and that's really what's driving it.

Operator

Our next is from Andrew Kligerman with Crédit Suisse.

Andrew Scott Kligerman
Crédit Suisse AG, Research Division

Thinking about Japan Post, just given the tremendous disruption that they've had. How are things moving along with them on the regulatory front, customer perceptions and when might they get back on it -- assuming we could get beyond COVID-19 pressures, when might they get back on a track that was consistent with, say, 2017 or 2018 in terms of sales?

Daniel Paul Amos
Chairman & CEO

Well, I'll start and then maybe, Aflac Japan, I'll want to make some comments as well. I think our relationship with Aflac, I mean, with Japan Post and Masuda-san is good as it could possibly be. They are positive. They are very interested in the new technology and the ability to use digital to help. In my opinion, they're wrapping up all phases of past issues because you've got a new management team. I think the press has pretty much seen and heard everything. And now it's just being repetitive. So I'm hoping that by certainly, end of August, September, it will kind of finish out and then they'll move forward. Now how the impact of that will go in regard to COVID and the ability to sell is uncertain. But the willingness on their part to want to sell and move forward is very positive.

And I think they would like to see the numbers go back to where they were as well. Of course, not only for sales, but also being a large shareholder themselves. They're interested in that.

So what I would say is, is we're well positioned. We're looking forward to that movement. And I think they are as well. So let me turn the program over to Koji [Foreign Language] to see what else he might want to add in that regard.

Koji Ariyoshi
Executive VP, Director and Director of Sales & Marketing of Aflac Life Insurance Japan

[Interpreted]

This is Koji from Aflac Japan. Currently, Japan Post group is prioritizing their activities to win back the customers' trust.

So Aflac Japan, of course, is supporting their activities. And for example, helping them with conducting training to really have focus on more customer-oriented activities. Under these circumstances, today, Japan tan -- the Japan Post group companies, they are Japan Post Holdings, Japan Post company and japan Post Insurance called the press conference to announce various things.

Andrew Scott Kligerman
Crédit Suisse AG, Research Division

All right. Great. And then just shifting over to capital management. I think Max used the term tactical with regard to...

Koji Ariyoshi
Executive VP, Director and Director of Sales & Marketing of Aflac Life Insurance Japan

Excuse me, may I continue? This is Koji.

Daniel Paul Amos
Chairman & CEO

[Go on] here.

Koji Ariyoshi
Executive VP, Director and Director of Sales & Marketing of Aflac Life Insurance Japan

[Interpreted]

So let me repeat again. Today, Japan Time, the CEOs of the 3 Japan Post group companies, Japan Post Holdings, Japan Post Company and Japan Post insurance held a press conference.

And the announcement that they have made in the press conference was the disciplinary actions over sales representatives. So for the first one related to the inappropriate sales, this announcement makes clear Japan Post framework apply disciplinary action to address the market conduct issues in response to stakeholder demand.

And then given the current status and the announcement that they have made, Japan Post Holdings CEO, Mr. Masuda said, that with this clarity -- with this clarity on Japan Post framework for disciplinary action, the Japan Post Group has largely met the 5 evaluation criteria established by the Japan Post Reform Execution Committee for resuming sales activities.

And he also stated the decision to restart sales will be made by the Board of Directors of the 3 Japan Post Group companies possibly within August or September. Having said that, once the decision to resume sales is made, Japan Post will begin with customer visits to express apologies.

So against that backdrop, we expect it will take some time before sales of Aflac's Cancer insurance to begin in earnest.

And the disciplinary actions that were announced today were on the sales of Japan Post insurance products and has nothing to do with the sale of Aflac's Cancer products.

And that is the current state of Japan Post.

Daniel Paul Amos
Chairman & CEO

Thank you, Koji. Now we have the second part to that question.

Andrew Scott Kligerman
Crédit Suisse AG, Research Division

Yes. No, just kind of shifting real quickly over to Max's comment that he wanted to be tactical on capital management. You did about $188 million of buybacks in the quarter, which relative to other companies in the spectrum is quite strong. So can I take -- and that's about half the level that you've done historically, maybe a little less. So could I take tactical to mean that, that's probably the level you'll be going at over the next few quarters until you can get visibility on COVID-19? And maybe could you rapidly increase it beyond historic levels given that you have slowed it down?

Max Kristian Brodén
Executive VP & CFO

So Andrew, tactical, that word means tactical. We have, by any matter, very strong capital positions in our operating subsidiaries and very strong capital and liquidity at the holding company. But we also recognize that the economic environment continues to be very uncertain. And also the spread of the virus obviously is clearly linked to that. And I would say that until we get better clarity, we will continue to be fairly cautious in terms of how we deploy capital. But we will also look for opportunities. And when we see that we would have a good opportunity, and we think that the risk/reward given all the risks out there is appropriate or is good for us, we will deploy capital.

All this means that we may have -- if you think about the run rate we were running at the second quarter, we may decrease the buyback going forward. We may keep it at the current level, and we may even increase it. But at this point, given everything that's going on and all the uncertainty out there, we want to keep all options available to us.

Daniel Paul Amos
Chairman & CEO

We'll take 1 more question.

Operator

Our last question then is from Mr. John Barnidge with Piper Sandler.

John Bakewell Barnidge
Piper Sandler & Co., Research Division

Can you talk about how you approach the rollout of dental and vision nationally beginning in January when individuals are largely underutilizing dental benefits possibly catch up in 2021? And then how do you manage the pricing and rollout of such?

Frederick John Crawford
President & COO

Sure, John. I'll -- just a couple of quick things, and then I'll hand off to Rich, and he can spell out the rollout. But just note that we do have a dental product out there right now, which is our historical indemnity product, and that continues to sell. It represents only about 3% of our earned premium and around 4% of our sales. Where we are going with the Argus acquisition and then the rollout of dental and vision is with a true network dental and vision, which is just in the building mode. I think we have, for example, this year, we're targeting something less than $5 million in sales of that product once we get up and running.

As mentioned in my comments, we've got the product actually rolled out and approved in 40 states, which is a more significant task or undertaking than you might think on the surface, particularly in the current environment. So we're quite pleased with that. And now we'll start to be in a better position come 2021 to roll out. So with that, Rich, why don't you take it from here in terms of how we see the rollout.

Richard L. Williams
Executive VP & Chief Distribution Officer

Okay. And as everyone will recall, last year at our financial analyst briefing and our outlook, we talked about 2020 being a measured rollout of Aflac dental and vision. And we are pleased to say, consistent with Fred's comments that we have done that here in 2020, rolling out the product in 10 states in significant areas for our distribution. So 2020 really is the burn in and the implementation for our field training, our enrollment platform and making sure that we have a very favorable experience for our customers and for our agents and our brokers. So 2021 will be the actual ramp-up of the volume for Aflac dental and vision, and we are on track to have the national rollout in 2021.

Daniel Paul Amos
Chairman & CEO

Thank you, Fran. And just before we conclude our call today, I wanted to remind you that we have combined financial -- combined our financial analyst briefing as well as our 2021 outlook call or a special webcasted event on November 19 in that morning. And we will have more details on that. We hope you will join us. And please feel free to contact Investor Relations for more information with any questions that you may have before then, and we look forward to speaking with you soon. Wish you all continued good health. Thank you.

Operator

This conference has concluded. Again, thank you for your participation. Please go ahead and disconnect. Thank you very much.
[Portions of this transcript that are marked [Interpreted] were spoken by an interpreter present on the live call.]