S&P Global
Market Intelligence

Aflac Incorporated NYSE:AFL

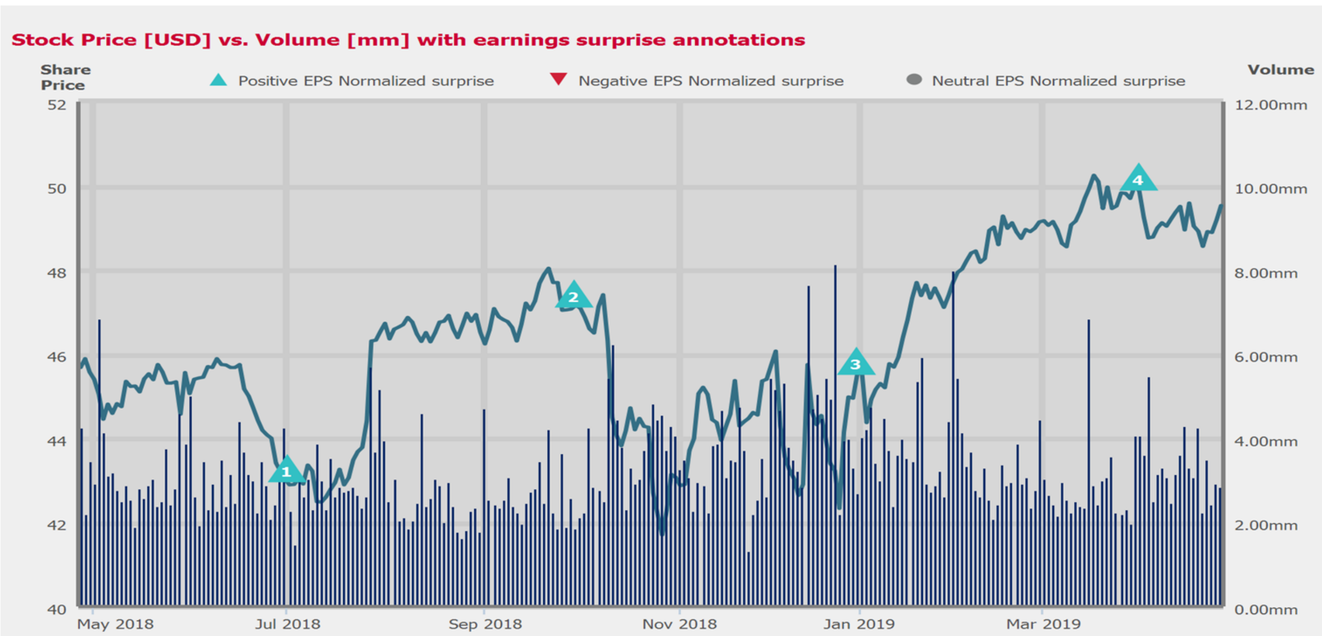
FQ1 2019 Earnings Call Transcripts

Friday, April 26, 2019 1:00 PM GMT

S&P Global Market Intelligence Estimates

	-FQ1 2019-			-FQ2 2019-	-FY 2019-	-FY 2020-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	1.06	1.12	▲5.66	1.07	4.27	4.43
Revenue (mm)	5458.38	5657.00	▲3.64	5380.16	21577.33	21808.73

Currency: USD
Consensus as of Apr-26-2019 12:35 PM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ2 2018	0.99	1.07	▲1 8.08 %
FQ3 2018	0.99	1.03	▲2 4.04 %
FQ4 2018	0.94	1.02	▲3 8.51 %
FQ1 2019	1.06	1.12	▲4 5.66 %

Table of Contents

Call Participants	....	3
Presentation	....	4
Question and Answer	....	8

Call Participants

EXECUTIVES

Daniel Paul Amos
Chairman, President & CEO

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

Frederick John Crawford
Executive VP & CFO

James Todd Daniels
Executive VP, Principal Financial Officer & Director of Aflac Japan

Koji Ariyoshi
Executive VP, Senior Managing Executive Officer, Director of Sales & Marketing and Director

Masatoshi Koide
President, Representative Director & COO of Aflac Japan

Richard L. Williams
Executive VP & Chief Distribution Officer

Teresa Lynne White
President of Aflac US

ANALYSTS

Charles Gregory Peters
Raymond James & Associates, Inc., Research Division

Jamminder Singh Bhullar
JP Morgan Chase & Co, Research Division

John Bakewell Barnidge
Sandler O'Neill + Partners, L.P., Research Division

John Matthew Nadel
UBS Investment Bank, Research Division

Nigel Phillip Dally
Morgan Stanley, Research Division

Suneet Laxman L. Kamath
Citigroup Inc, Research Division

Thomas George Gallagher
Evercore ISI Institutional Equities, Research Division

Presentation

Operator

Welcome to the Aflac's First Quarter 2019 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.

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

Thank you, and good morning, and welcome to our first quarter call. This morning, we will be hearing remarks from Dan Amos, Chairman and CEO of Aflac Incorporated, about the quarter as well as our operations in Japan and the United States. Then Fred Crawford, Executive Vice President and CFO of Aflac Incorporated, will follow with more details about our financial results.

In addition, joining us this morning during the Q&A portion are members of our management team in the United States, Teresa White, President of Aflac U.S.; Eric Kirsch, Global Chief Investment Officer; Rich Williams, Chief Distribution Officer; Al Riggieri, Global Chief Risk Officer and Chief Actuary; and Max Broden, Treasurer and Head of Corporate Development. 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 Principal Financial Officer; Koji Ariyoshi, Director and Head of Sales and Marketing.

Before we start, let me remind you 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 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. The earnings release is available on the Investors page of Aflac's website at investors.aflac.com and includes reconciliations of certain non-GAAP measures.

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

Daniel Paul Amos
Chairman, President & CEO

Thank you, David, and good morning, and thank you for joining us. The first quarter of 2019 established the solid foundation as we set out to achieve our annual objectives.

Let me give you more detail. Beginning with Japanese operations, Aflac Japan, our largest earnings contributor, generated strong financial results that are in line with our expectations for the quarter.

For 2019, we continue to expect a slight decline in Aflac Japan's total earned premium primarily due to the limited paid policies reaching paid-up status. As you saw in the release, third sector combined with first sector protection sales were down low-single digit in the first quarter, but generally in line with our expectations for the quarter. Our traditional agencies have been and remain vital to our success, as do our alliance partners.

While cancer insurance sales were up in the quarter, which strengthened our associates channel, results were weaker at Japan Post as they achieved their 2018 fiscal year targets early. Both Daido and Dai-ichi increased cancer sales in the final quarter of the Japanese fiscal year.

As per medical sales, we focused on riders in the medical area to retain and attract new customers with mid-term riders. Policy holders can update their existing medical coverage by adding a rider to their existing policy. They also have the option to purchase a new policy with an income support rider targeting young and middle-aged segment or nursing rider designed for the middle- to older-aged groups. While this strategy is effective in driving better overall economics and earned premium, it's less beneficial to the sales versus replacement of the whole policy.

As you know, we take a longer-term perspective. Looking forward to the remainder of the year, let me just say that we anticipate making our annual sales objective. Last year, beginning in the second quarter, we had a very successful launch of our new cancer insurance product, which drove a 16% increase in third sector sales for the second quarter of 2018. This makes a very difficult comparison. We want to make sure you understand that we expect third sector and first sector protection combined sales to be down in the high-teens in the second quarter of '19. This means that we expect those sales in the first half to be down in the high-single digits. Having said that, though, we anticipate a strong second half and, more importantly, we expect to achieve our annual sales objective of a mid- to single-digit decline in the third sector and first sector protection sales for the year.

Ultimately, our focus remains on maintaining our leadership in the third sector products while complementing this core business with similarly profitable first sector protection products. To that end, we will continue to refine our existing product portfolio and introduce innovative new products that our policyholders want and need and where they will want to purchase them.

Finally, with respect to Japan Post in our alliance, you may recall that at the end of February, we announced in the filing that Japan Post Holdings formed a trust that permits the trustees to purchase Aflac Incorporated shares. We continue to anticipate the completion of the regulatory approvals in the second half of 2019.

As we have mentioned previously, we view 2019 as more of a year of planning around opportunities for Aflac and Japan Post Holdings companies to collaborate.

When I was in Tokyo last month, I met with the CEO of Japan Post Holdings, along with the senior executives of both companies. We had very productive meetings to work toward areas that are mutually beneficial to both parties. As we told you, 2019 is a year of planning and 2020 will be more of an execution on our plans.

Turning to Aflac U.S. Our revenues increased 2.2%. At the same time, pretax earnings continued to reflect ongoing investments in our platform, distribution and customer experience. U.S. sales were up 1.5%, which was in line with our expectation for the quarter. Aflac is unique with respect to our peers and that the majority of our sales comes from independent sales agents. We are fortunate to be represented by such a strong field force, which is truly distinctive within our industry. These independent carrier sales agents are best positioned within the industry to assess and, therefore, succeed with smaller employers and groups with fewer than 100 employees.

Aflac's agents have always enhanced their collaboration with local and regional brokers as we continue to grow broker sales, while our team of broker sales professionals have taken and made great strides in enhancing our relationship with the large broker community.

Brokers have recognized more and more that their clients need the types of products Aflac offers. This has increased the appeal and, therefore, the interest in doing business with Aflac. With the continued growth of our broker business, our sales have been increasingly skewed toward fourth quarter with the continued growth of the broker business, and we expect 2019 to be no different.

We were also pleased with the continued improvement in productivity in the quarter. At the same time, net earned premium rose 2.4%, and we continue to expect Aflac U.S. to deliver solid results in 2019 with earned premium growth in the 2% to 3% range. Ultimately, we believe the investments we've made in our distribution and customer experience will promote increased productivity, stable persistency and improved long-term economics.

While Fred will address capital deployment in more details, we remain committed to maintaining strong capital ratios on behalf of our bondholders, shareholders and policyholders. At the same time, we're balancing our financial strength with reinvesting in our business, increasing the dividend and repurchasing our shares.

Through Aflac Incorporated subsidiaries in Japan and the United States, we have the privilege of helping provide financial protection to more than 50 million people. In both countries, we've earned our position as the leading supplemental insurer by paying cash fast when our policyholders get sick or injured.

Looking ahead, we believe that our strong earnings growth will reflect the underlying earnings power of our insurance operations in Japan and the United States. It will also reflect our prudent approach to deploying excess capital in a way that balances the interest of all stakeholders. At the same time, it will reflect our dedication to delivering on the promises that we've made to our policyholders.

Now I'll turn the program over to Fred to cover the financial results. Fred?

Frederick John Crawford
Executive VP & CFO

Thank you, Dan. We're off to a strong start to the year on the earnings front as results for the quarter exceeded our expectations.

Adjusted earnings of $1.12 per share benefited from strong margins both in Japan and the U.S. Our reported results were modestly impacted by weakening of the yen as compared to the 2018 period, reducing our earnings by approximately $0.01 per share in the quarter.

The quarter's adjusted effective tax rate of 25.5% includes the tax treatment of equity compensation under GAAP that contributed roughly $0.01 to our adjusted earnings per share. When normalized, our effective tax rate of 26.3% came in as expected and represents a blended rate based on our current mix of Japan earnings taxed at 28% and U.S. earnings taxed at 21%.

Turning to our Japan segment results, earned premium for the third -- for our third sector products increased 1.8% and in line with our expectations. With continued headwinds from paid-up first sector products, overall earned premium growth was down nearly 1% in the quarter.

And as we move through the year, the earned premium impact from paid-up policies will remain stable. The first sector [ways] paid-up impact will gradually reduce throughout 2019. However, a portion of our medical sales in 2017 was a newly introduced [2-pay] product, which was popular in the bank channel and will have a slight impact to third sector earned premium growth for the remainder of 2019. Overall, it's important to note that this strain to the top line does not impact profitability.

Our total benefit ratio came in at 69.1% and at the lower end of our annual guidance range, driven by a favorable third sector benefit ratio and the continued shift in business mix from first sector towards third sector, which carries a lower benefit ratio.

Our expense ratio in Japan was 20.2%, consistent with our projected range. While year-over-year our expense ratio increased, expenses came in below our forecast due to timing of sales promotions and lower DAC expense as lapse experience was better than expected.

Our expense ratio outlook for the year remains in the range of 19.5% to 21.5%. Net investment income in our Japan segment contributed to our strong results. While no one area drove the outperformance, continued favorable returns in our floating rate loan portfolio, modestly lower hedge costs and variable income from our building alternative investment portfolio contributed to results.

Overall, in Japan, we've recorded a very strong pretax profit margin of 21.9%, with all key earnings drivers coming in better than our forecast.

Turning to the U.S. results. Earned premium was up a steady 2.4%. Our total benefit ratio came in at 49.3% at the lower end of our annual guidance range and generally consistent with recent claims trends and our mix of business.

Our expense ratio in the U.S. was 36.3%. Breaking down the expense ratio further, DAC amortization was elevated in the quarter, reflecting natural growth, mix of business and adjustments related to lapse experience and truing up previous estimates. In terms of general operating expenses, this quarter benefited from timing of spend, which we expect to build throughout the year. Our expense ratio outlook for the year remains in the range of 35% to 37%.

Net investment income performance was in line with expectations and reflects our continued movement of excess capital out of the U.S. to the holding company.

In our corporate segment, the main driver of improved earnings year-over-year is net investment income and amortized hedge income. Investment income benefited from the movement of capital and increased liquidity at the holding company. Our corporate hedging program reduces our economic exposure to the yen while lowering enterprise-wide hedge costs. Amortized hedge income contributed $20 million on a pretax basis to the quarter's earnings with a notional position of just over $2.5 billion.

As you may have noticed, we have added disclosures in our financial supplement with additional detail on our corporate hedging program and associated amortized hedge income.

Capital remains strong. Japan's solvency margin ratio is estimated in the 950% range. In April, we issued JPY 30 billion of hybrid debt out of our Japan subsidiary, which receives regulatory capital treatment at a very low cost to capital. We estimate that this will contribute approximately 20 points to SMR and is another example of financial flexibility stemming from the conversion of our Aflac Japan from a branch to a subsidiary.

Our estimated U.S.-only risk-based capital ratio at quarter end is now in the 700% range. RBC is a bit elevated as we have planned increases in operating dividends and the drawdown of $500 million of excess capital scheduled for later this year as we target 500%.

We ended the quarter with nearly $2.5 billion of capital and liquidity at the holding company. Asset quality remains strong with very little in the way of impairments in the quarter.

Following a solid recovery in pricing, we elected to sell our entire $146 million position in PG&E, realizing a small gain in the quarter. We had previously impaired our position in the fourth quarter by $21 million.

In the quarter, we repurchased 10.2 million shares for approximately $490 million. This amount was elevated as we tactically accelerated repurchase early in the quarter. We are maintaining our current range for repurchase of $1.3 billion to $1.7 billion in 2019.

In closing, we're off to a solid start, both in Japan and in the U.S. And I'll now hand the call over to David to begin Q&A session. David?

David A. Young
Vice President of Investor & Rating Agency Relations
Thank you, Fred. [Operator Instructions] And we'll now take the first question.

Question and Answer

Operator

First question is from the line of John Barnidge with Sandler O'Neill.

John Bakewell Barnidge
Sandler O'Neill + Partners, L.P., Research Division

Yes. So productivity in the U.S. was rather strong for 1Q. What do you see as a driver for this? And are these digital investments that you're making already yielding? And if that's what the driver of productivity is, can you maybe talk about some examples?

Teresa Lynne White
President of Aflac US

Well, I'll start off. This is Teresa. What we're seeing is, yes, so the digital investments are a business with -- especially on the broker side of the business with enrollment tools that allow us to be more productive on that side of the business. We're also seeing additional productivity based on product offerings -- portfolio offerings that we have. If you recall, we introduced some life products, and we expanded our portfolio with life and disability to help us to improve some of the -- be able to see more people and also to be able to respond to more RFPs. And so we are seeing a number of the investments that we've done not just in digital investments, but also investments in product to help us to be more productive in the market. I'll let Rich talk -- if you have anything else, Rich.

Richard L. Williams
Executive VP & Chief Distribution Officer

No, Teresa, I think you said that well. The only thing I would add to it is the engagement of our veteran associates has been very positive for us. They've adopted the training and our technology solutions with Everwell. And so I think part of the productivity is driven by our veteran associates.

Teresa Lynne White
President of Aflac US

Absolutely.

John Bakewell Barnidge
Sandler O'Neill + Partners, L.P., Research Division

And then my follow-up question, sticking with U.S. We've just completed the first tax filing season post reform. Can you talk about any behavioral changes either on individuals or business owners that stand out for distribution?

Teresa Lynne White
President of Aflac US

Do you want to take that, Rich?

Richard L. Williams
Executive VP & Chief Distribution Officer

I think the short answer is we have not seen any meaningful changes, and it's continued to be business as usual.

Operator

Next question is from the line of Nigel Dally of Morgan Stanley.

Nigel Phillip Dally
Morgan Stanley, Research Division

I had a question on Japan sales. I appreciate the color on Japan Post being down, as they've previously hit their budget. My question is whether this decline was anticipated when you set your sales growth guidance, whether the results this quarter make any full year sales growth guidance perhaps a little more challenging. Also, you seem bullish on the prospects of the second half. Has anything changed there to drive that optimism? Or was that always your expectation?

Daniel Paul Amos
Chairman, President & CEO

Koide, who wants to answer that?

Koji Ariyoshi
Executive VP, Senior Managing Executive Officer, Director of Sales & Marketing and Director

[Interpreted] This is Koji. I will answer your question. As Dan mentioned in his speech because Japan Post, or JP -- as January to March was their last -- very last quarter of the fiscal year, they focused on the sales of the proprietary product sales. And from April this year, this is the start of the new fiscal year for JP. So now they are starting to sell more cancer insurance product. However, what is different from last year is that even though their quarter is the fiscal year's starting, they will be selling their cancer insurance more in an equalized manner than compared to last year. I would say it was really focusing on just a particular quarter. So as a result, we are expecting that JP will still be in negative at the end of the second quarter. However, since last year, JP has been working on improving their productivity such as to really strengthen their sales skills. And they have also been accumulating very efficient motivation increasing efforts. And we do believe that their sales and performance will increase in the second half by leveraging all of these efforts that they have been working on. Now going onto the associates channel. The second quarter of last year was when we had a very large increase in the third sector sales because of the new cancer product launch last year. And we are expecting that the second quarter this year will be negative because of the reason that I have mentioned as well as the long consecutive holidays for our Emperor's accession to the throne later this year. However, at the end of the second quarter, there will be further revision of medical insurance, although we are not able to disclose the details at this point. However, we are expecting that we will have increase in the third quarter because we will be launching a very effective commercial together with associated direct mails, and starting with that, our activities are -- sales activities will increase. As a result, we will have a good third quarter is our expectation. So as a result, associated with the guidelines that we have -- guidance that we have indicated at the beginning of the year, we will end in a single mid-range -- negative single mid-range negative figure. That is a combined number of associates and JP channel. That's it from me.

Daniel Paul Amos
Chairman, President & CEO

Nigel, the one thing that you asked, the question was I want to be clear is that nothing's changed. We expected this. So it's just -- as we were preparing for the first quarter release, we realized we needed to make sure everyone else understood that. But when I saw the 16% coming in last year, I knew in 2019 it's going to be a big hurdle and how we're going to offset it, and the answer was even going back to the second quarter of last year, we're going to have a great second half of 2019 and so we're on plan to do that.

Nigel Phillip Dally
Morgan Stanley, Research Division

Okay. That's very helpful. Second question, I guess, on investments incorporating floating rate securities. It's been an important part of the change in the portfolio mix. Now future rate increase is looking less likely. Any implications of that expected as both positives and negatives? But I hope you can flesh that out.

Daniel Paul Amos
Chairman, President & CEO

Sure. Thanks, Nigel. And as a reminder, relative to Fed rate changes, it really impacts not only the floating rate assets, but the hedging strategy as well because they're correlated with LIBOR, which obviously is heavy influenced by Fed action. But to be specific to your question, I'll break it into 2 buckets. For 2019, we expect very little impact to our forecasted income from Fed actions. And that's for 2 reasons. One, you'll recollect that in our outlook column, we talked about hedge costs. We locked in about 85% of our 2019 hedge costs by terming them out. So in essence,, regardless of what happens to hedge costs, most of our hedge costs will be locked in if the Fed should lower rates, for instance. Secondly, on the floating rate assets, just from a mechanical standpoint, if the Fed is lowering rates and LIBOR is going down, that would certainly impact our coupons when they reset. However, in late December, we had put on an income hedged, in essence a fixed-for-floating rate swap because we had -- saw the change in the Fed view going from hawkish to dovish. So about 75% of our floating rate income is locked in as well because we did the hedge. So that's why -- that's my first part of the statement. Regardless of what the Fed does this year, our income actually from the floating rate portfolio, including the hedge costs, will be relatively stable and within a tight range. The second bucket, though, is when you look out to 2020. Obviously, when we redo our budgets at the end of this year to reflect 2020 as LIBOR continues to go down and the Fed should be cutting rates, that would get reflected in the floating rate income, but also get reflected in the marking to market of the hedge costs. And if you recollect the whole concept of the floating strategy is, you should always think of those 2 buckets together, the floating rate securities, what the hedge is, and in essence, we're earning a nice net spread. So there'd be some impact in 2020 if the Fed were to continue to lower rates and if LIBOR goes down, assuming no other factors change. And of course, the opposite is true. We don't know exactly what will happen. We just saw a good print for GDP this morning. So if rates should be rising, we should -- we'd get the opposite impact, which certainly we saw in 2018 in our results.

Operator

Next question is from the line of John Nadel of UBS.

John Matthew Nadel
UBS Investment Bank, Research Division

I have a couple of quick ones. First, it sounded in your opening remarks, Dan, like Japan Post actually doesn't yet have everything in place to begin purchasing Aflac shares. Did I hear that right? And if I did, when do you expect that they'll actually get the approvals needed to get that process started?

Daniel Paul Amos
Chairman, President & CEO

I'll let Fred take that because he's been working with them.

Frederick John Crawford
Executive VP & CFO

Yes, the way we interpret Dan's comments are as follows. One is, as we may have mentioned, I think, or made public a few months ago, Japan Post has established the trust, which now allows them to move forward on the purchasing of stock when they're prepared to do so. Dan's comment was related to ongoing regulatory approvals that are required particularly in the U.S. that will go on through into -- deeper into the year. This is essentially the Form A process in various states that they need to go through. That, however, doesn't prohibit their ability to start the process of building shares. They simply needed to get the trust in place and then, of course, it's entirely up to them and their tactics as to how and when they begin purchasing, and we're sort of leaving that up to them, of course. So that's the way to interpret it, John.

John Matthew Nadel
UBS Investment Bank, Research Division

Okay. So can you actually tell us whether maybe you know, maybe you don't know whether they've actually started [indiscernible] or no?

Frederick John Crawford

Executive VP & CFO

Yes. The answer is, no, I can't tell you, and, no, I don't know. And that is somewhat by design in the sense that we -- other than the provisions of the alliance, for example, the 1-year provision that starts from the beginning of them purchasing shares and building to the 7% ownership level, we're treating them as any other institutional investor, which means we're not in a position to either know and/or report out on what they're doing relative to building the position. What I would say is this, though, it's an obvious question that we would receive, and we know that. And so what we would do is refer you to any disclosures that Japan Post makes as part of their registered environment with the Tokyo Stock Exchange or any other disclosures they choose to make. And so we'll be paying attention to that. But otherwise, we are treating them as any other institutional investor in that regard.

John Matthew Nadel
UBS Investment Bank, Research Division

Got you. And then my second question is just around expenses. It sounded also from your prepared remarks, like, you're expecting that the pace of spending, I think, both in Japan, but in particular in the U.S. will pick up as we move through the year. So I just wanted to confirm whether that's what you're actually foreshadowing. And then also specific to the U.S., you talked about DAC amortization being a bit higher. Is that a level that we should expect now on a go-forward basis? Or was there some reason why that's unusual in 1Q?

Frederick John Crawford
Executive VP & CFO

Yes. Let me answer both and give you more perspective, you and everybody else on the call, and that is, so from the standpoint of expenses, it is a timing-related area and the quarter did in fact benefit from the timing of expenses, which by default means that these expenses will start the process of building and running through in the latter part of the year. To be more specific, in the U.S., our estimates are that expenses ran approximately $20 million better than we had anticipated and, therefore, we would expect a build of that or shift of that expense into future periods. There is nothing necessarily unusual about this. It's what I would call the normal timing related to the picking up of various initiatives and spend related to that. Staying on the U.S. and answering your DAC question, we did see elevated DAC expense in the quarter. It's not unusual for DAC expense to be elevated in the first quarter. You'll see that in some of our supplemental information, and that's because you have a natural level of higher lapsation in the first quarter due to annual enrollment dynamics. And so each year, you'll notice that our benefit ratio tends to be a bit lower in the first quarter and our DAC amortization higher. And that's the result of increased lapsation, particularly as we start to change the mix of business towards a group and larger groups. You'll see that perhaps a little bit more pronounced. And so that's what's driving DAC expense up. We also had a little bit of what I would call cleanup, if you will, related to estimates we made around DAC amortization on certain groups that we anticipated lapsing or that had lapsed late in the year in December, and we had to true-up those estimates. That probably kicked up our DAC expense in the U.S. by about $5 million. So back on the delayed expense issue to Japan, Japan also had that dynamic. It was largely revolving around promotional spend, and we estimate that about JPY 1.6 billion, okay, of delay, if you will. In other words, we had anticipated JPY 1.6 billion more of expense related to promotion. That will shift into the later quarters. And then finally, on corporate. Corporate expenses were also a bit below our estimate, and that actually has more to do with the pace of spend on the new accounting adoption. As many companies are doing in our industry, we're having to adopt the new accounting, and we're starting into the more significant project spend related to that. In fact, we anticipate that spend being pretax around $20 million to $25 million in 2019, and that will start to pick up as we go through the year. So if you want me to wrap it all in a bow for you, we would estimate that the quarter benefited by approximately $0.04 a share related to these expense timing issues.

John Matthew Nadel
UBS Investment Bank, Research Division

That's all extremely helpful and, I guess, full employment DAC per accounts [indiscernible].

Operator

Next question is from the line of Suneet Kamath of Citi.

Suneet Laxman L. Kamath
Citigroup Inc, Research Division

I wanted to go back to Japan sales, particularly the cancer product. I get the drop-off from Japan Post, but I had thought that the second quarter '18 launch was sort of characterized as a new product, and it sounds like your second half '19 recovery is also tied to a medical product. So my question is, is the sales cycle for a new product really is that short that you get most of the sales associated with the new product in the first couple of quarters sort of requiring you guys to refresh on that kind of annual basis?

Daniel Paul Amos
Chairman, President & CEO

I'm going to let Koji talk, but I want to remind you that part of the reason that it's changed somewhat is due to this new rider concept. We were -- we would write a new policy, and they would then lapse their old one. And now what is more efficient and better for the company and for the policyholders is to add riders. So Koji, why don't you discuss that for a moment, and then I'll -- if there's anything else, I'll be glad to answer, too.

Koji Ariyoshi
Executive VP, Senior Managing Executive Officer, Director of Sales & Marketing and Director

[Interpreted] Well, first of all, in the second quarter, we once again revised medical insurance, which we also had in the first quarter. But as you know, compared with any other companies, Aflac has the largest number of medical policies. And so although the competition is very tough, it's important that we increase the number of new businesses, but then it is also important for us to protect our current existing policy especially because most of the policies are whole-life policies, and what that means is that depending on customer's life stage, the needs change and the customer's status of health also change. So what we are doing now is considering all these factors, we are developing these riders that the customer really wants to buy depending on their life stage, for example, thinking of the health state of particular age customers. And this rider strategy is a positive thing for customers, and this also aligns with our core value of Aflac. When a new -- when the existing policy is lapsed and a new policy is purchased, the premium normally goes up. And with this new rider strategy, what we are able to do for customers is that the customers will be able to maintain their policies and also just add whatever the coverage is needed with lower premium. So in the long term, what we are thinking is that we are actually responding to what the customers are wanting. And because of the fierce competition, it does cost a lot of money to change product. And I would like Todd to really follow up on the economics of what we are doing. Todd?

James Todd Daniels
Executive VP, Principal Financial Officer & Director of Aflac Japan

Thank you, Koji. Yes, as Koji mentioned, we're doing this for benefiting not just the customer, but it benefits our economics. We developed these riders that with the mid-term rider addition, they're able to add these riders to existing policies that have been issued many years ago. And so with that, we don't have to incur another acquisition expense if we were to issue another base policy. I know you mentioned earlier asking about product life cycle. We have seen shorter product life cycles on the medical particularly because there's lots of competition. But we maintained this past round with issuing the riders that the customers want withholding the base policy premiums consistent with what we had with the prior version of the product. For years, we have been repricing product as interest rates change and competitors come in the market to keep up with different benefits and features that customers need. But this time, we decided to keep those premiums consistent with the prior version. So policyholders would not want to lapse the base policy and buy a newer one, which would have a higher premium. So they're able to enjoy better economics, at the same time, we're able to enjoy better economics by having riders that are cheaper per unit to develop.

Frederick John Crawford

Executive VP & CFO

One thing I do want to step in and make a comment about -- this is Fred. That entire discussion was surrounding the very important strategy related to our medical product. But when you first asked your question, you were somewhat pointing to cancer product and be very careful about looking at the pattern of sales in cancer over the last several quarters and think of it in terms of the life cycle of the product. Last year, in the second quarter, that was the first time that we refreshed the cancer product, of course, in 4 years, which means there's substantial advancements in the quality of the product and coverage because of advancements in cancer treatment. It also included a very attractive premium labor feature, which was particularly attractive in the Japan Post channel. And importantly, it was the first time that we meaningfully revised the cancer product in the Japan Post channel. And so you saw a big spike in sales in the second quarter and then continued strength throughout 2018. You can't look at the first quarter results in cancer sales in JP, in particular, and their fourth quarter and think of that as the end of the product cycle. That has more to do with them having reached all of their goals and so they naturally pivoted towards their proprietary product. They're going to pivot back to this very attractive cancer product as we go throughout the year, and that's what's going to give the recovery. So just be careful about looking at those patterns and assume there's some sort of shortened cancer product cycle.

Suneet Laxman L. Kamath
Citigroup Inc, Research Division

Got it. And then just my follow-up, and that was all very helpful, is you have data that you can share with us in terms of what percentage of your sales are to existing policyholders in Japan versus new policyholders?

Daniel Paul Amos
Chairman, President & CEO

Koide?

Masatoshi Koide
President, Representative Director & COO of Aflac Japan

Yes, Koide speaking. Roughly speaking, 50% and 50%. The proportion will depend on the timing of launch of new products, of course, but generally, 50% and 50%.

James Todd Daniels
Executive VP, Principal Financial Officer & Director of Aflac Japan

I'll just add one thing real quick too on the cancer block. You'll recall that we're developing new cancer policies to keep up with treatments for cancer, and it's in our best interest to offer this to existing policyholders. So part of our marketing campaigns over time have been through direct mails and follow-up by our agents to offer them the latest cancer coverage, which we think is the best interest of the policyholder.

Operator

Next question is from the line of Tom Gallagher of Evercore.

Thomas George Gallagher
Evercore ISI Institutional Equities, Research Division

Also, a few questions on Japan sales. Any product enhancements or product expansion in terms of the relationship between you and Japan Post that you're planning? Or are you just still selling the same initial cancer product that you launched there?

Daniel Paul Amos
Chairman, President & CEO

What I would do is ask Koide to talk about the 4 different groups that are formed within Japan Post. Koide, you want to talk a little bit about that?

Masatoshi Koide
President, Representative Director & COO of Aflac Japan

[Interpreted] This is Koide from Aflac Japan. As you note in the strategic alliance released in December last year, the first pillar of the 3 pillars of the strategic alliance is to work on a new collaborative work with JP. We will be working on 4 themes: leveraging digital technology, a new product in development corporation, a joint investment into third-party or domestic or internationally business expansion together, and cooperation with investments. And for all of these 4 themes, we have already launched working groups and have started to have discussions. That's all from me.

Daniel Paul Amos
Chairman, President & CEO

And so what I would say is that we're proceeding in a very methodical and cautious way to where we can have products and services that will enhance not only our business, but also enhance Japan Post business. And it never moves as fast as any other's launch, but I'm very pleased with the cooperation of both Aflac Japan's management team and also what they're doing with Japan Post. So as I said, 2019 is a year of planning, 2020 will be part of execution and moving forward. So we are working toward that end.

Thomas George Gallagher
Evercore ISI Institutional Equities, Research Division

Okay. That's helpful. And then my follow-up is just, did I hear correctly in one of the responses that you're revising the medical rider again in 2Q after revising it in 1Q? Or did I not understand that correctly? The reason I ask is, are you changing something relative to what you did initially with the launch of that product? Or is that -- can you elaborate on that?

Daniel Paul Amos
Chairman, President & CEO

Let's have -- go ahead, Koji.

Koji Ariyoshi
Executive VP, Senior Managing Executive Officer, Director of Sales & Marketing and Director

[Interpreted] Well, what we are going to do is that there are some things that we will [not] be able to incorporate some of the changes incorporated in the January change of revision. And I'm not able to elaborate on the details because it has not been announced yet. As we try to provide various products based on the needs, we would like to be providing these kind of benefits and coverage any of the status of customer's health because our policy life is very long.

Daniel Paul Amos
Chairman, President & CEO

Yes, let me just say that this is not unusual in that when we're dealing with our sales people, they come up with ideas and thoughts, and we look back to see if there's anything that we can ultimately make it more sales appealing. So I wouldn't take into this anything major. This is a minor adjustment and -- but if it will help our sales people, then we try to work toward that end.

James Todd Daniels
Executive VP, Principal Financial Officer & Director of Aflac Japan

But just to be clear, though, this has always been our plan. We're not redoing anything in June or second quarter in response to result of the first quarter. This has been our plan all along.

Operator

Next question is from the line of Jimmy Bhullar of JPMC.

Jamminder Singh Bhullar
JP Morgan Chase & Co, Research Division

First, I had a question for Eric on just the new money yield. It was up a lot, I think, 3.29% in Japan and a lot higher than the portfolio yield. So to what extent is this a better rate environment? Or what I suspect it is, is just the decision to allocate more money, I guess, to U.S. dollar investments. And would you expect the new money yield to drop as the year goes on versus the 1Q level?

Daniel Paul Amos
Chairman, President & CEO

Thanks, Jimmy. Well, it's definitely not a function of the rate environment because the rates are lower all around the globe. But it is more a reflection of asset allocation. So you're right on that part. And for Aflac Japan, approximately half -- just a little bit under half went into U.S. dollar assets, and a good portion of that went into our loan portfolio, transitional real estate and middle-market loans. And those are having average yields from 5.5%, 6% up to 7% on middle-market loans. So that's really the driver of the higher new money yield. It's really asset allocation because from a new money perspective, as you know, yields have been coming down, spreads have gotten tighter. Fortunately, for us, relative to our income objectives for the year, that's not a big driver of whether or not we would make our numbers, and the asset allocation I described is within our plan. So there's nothing that deviated. And for the loan portfolio, we start to receive prepayments on those loans and, therefore, they get reinvested back into dollars. So our asset allocation is very much in line with our strategic asset allocation and how the underlying loan portfolios are performing. For the rest of the year, I wouldn't expect big deviations necessarily subject to, of course, market yields and any tactical actions we might take if something were to present itself in the market.

Jamminder Singh Bhullar
JP Morgan Chase & Co, Research Division

And then maybe a question for Todd on the -- just the whole -- full policy versus the rider dynamic. Can you sort of give us an idea on what the premiums per policy are if you sell a rider versus selling stand-alone policy just to be able to assess how much is that weighing on your sales this year?

James Todd Daniels
Executive VP, Principal Financial Officer & Director of Aflac Japan

Yes, I'm going to hand it to Koji. They had some numbers and can refer to those.

Koji Ariyoshi
Executive VP, Senior Managing Executive Officer, Director of Sales & Marketing and Director

[Interpreted] The riders versus the base policy is 15% to 16% premium. In the case of income support riders, 15% to 16%. In the case of care riders, 15% to 20%.

James Todd Daniels
Executive VP, Principal Financial Officer & Director of Aflac Japan

So I think it varies greatly by which rider you're looking at versus a base policy. And one thing to keep in mind is these riders are limited benefits versus buying the entire base policy. For our income support rider, yes, it's covering long term being out of work and supporting your income, where this rider that we've developed is a lump sum onetime payment. So it's limited benefits to try to make it more affordable for the customer to purchase this as a rider. Same thing with the care option. For the older-aged people, it's sold as a lump sum benefit so the premium is going to be quite a bit less than if you were to design and develop a true nursing care policy.

Jamminder Singh Bhullar
JP Morgan Chase & Co, Research Division

Okay. And just lastly for Fred. Will the Post be required to file the [DSCC] once they get to 5% stake. I'm assuming they will be. But...

Frederick John Crawford
Executive VP & CFO

Yes, yes, we would expect them to have to, obviously, follow all of the guidelines associated with reporting the NYSE.

Operator

Next question is from the line of Greg Peters of Raymond James.

Charles Gregory Peters
Raymond James & Associates, Inc., Research Division

I was wondering if we could just step back from a bit picture perspective and, I guess, I've got to say upfront, I realize your U.S. business has a different focus. But I was hoping you could comment on all the recent political rhetoric around the possibility of medical -- Medicare for All and what your perspective is on that.

Daniel Paul Amos
Chairman, President & CEO

I'll say something and then I'll see if Teresa -- our Medicare for All is nothing more, in my opinion, than some form of what we see in Japan with their national health care system. Granted they've gone from no deductibles to 10% to 20% and to 30%. But we have been selling in an environment since inception that consumers would own some type of major medical insurance, whether it be Blue Cross Blue Shield to Obamacare to anything that might be out there because there are costs associated with unexpected expenses that are not covered by any type of Medicare, Medicaid, whatever it might be. So from our standpoint, I don't think it's going to change how we address these issues. I do think it will -- we will hear a lot about it with the election in 2020, but I don't think when it all boils down that it's going to change anything in terms of the way we're selling now. So I really don't worry about that from that standpoint. I'm paid to worry so I do watch it carefully, but there is nothing on the horizon that makes me nervous about that. Teresa?

Teresa Lynne White
President of Aflac US

I think you've pretty much summed it up. At the end of the day, I think it becomes more apparent to the consumer about their risks and gaps when they have whichever coverage, whether it's Medicare for All or it's Blue Cross Blue Shield, as you mentioned. So from that perspective, I think the value of our product, the value of what Aflac offers continues to be apparent whichever major medical you have as a consumer.

Daniel Paul Amos
Chairman, President & CEO

Let me say this, as a company, we want everybody to have health insurance.

Teresa Lynne White
President of Aflac US

Absolutely.

Daniel Paul Amos
Chairman, President & CEO

We're absolutely for that. We think it's in the best interest. The costs associated with it are going to be through the roof because, as you know, in other countries, they have -- they limit medical access on different things. And we would be the first country that would go to a period of where you would have unlimited access with unlimited costs. So the cost associated with it is another issue, a political one, in my opinion. But just know, we as a company want people to have it because we think we've got the product that will help fill those gaps that are going to be created in today's society.

Charles Gregory Peters
Raymond James & Associates, Inc., Research Division

I guess, staying on the same theme of politics, there's also been rhetoric around share repurchase activity. And I'm curious, Dan, at the Board level, if you guys are starting to change your thinking around capital allocation as it relates to share repurchase versus, say, perhaps possibly a dividend or special dividend or anything like that?

Frederick John Crawford
Executive VP & CFO

This is Fred. I'll answer, and then Dan can pick up from the Board level. But I think just in terms of capital allocation, obviously, after a 36-year track record of increasing the dividend and certainly intending to continue that track record, we feel like we're in good shape on balancing the dynamics of investing in our business, buying back stock and paying out a common stock dividend. In terms of stock repurchase, it remains a very good investment of the company particularly on a risk-adjusted basis. And it also is the basis upon which we measure up other opportunities, the degree to which other nonorganic, for example, opportunities can come into play. I think from the political perspective, the only thing I would generally agree with because I think it's just good management, and that is, you don't -- as a company, you don't deserve to be significantly buying back your stock and, frankly, paying a high dividend until you, first and foremost, secure your balance sheet and secure your capital ratios in such a way that you can meet all the promises of your policyholders and, frankly, meet any obligations you have to your employees that includes pension obligations. And so there's elements of it I agree with. However, I don't see any need to regulate that type of dynamic. I think, frankly, good management and governance self-regulates those issues, in my view. So that's my opinion.

Daniel Paul Amos
Chairman, President & CEO

And I think our position all along has been a very moderate position. We haven't been at an extreme on any area, and it's the extremism that brings on the most criticism. And so I think we're very well positioned. I think we will continue at this pace. The Board will, of course, constantly review that to see if there is any area that they think we should be looking at. But I think that anything you know about our company is, we try to look ahead of what the trends are, no matter what they might be, political, consumer activism, whatever it might be, to make sure we're on top of what's taking place. So I can assure you this is a top-of-mind subject that we will continue to monitor. But we feel we're well positioned right now.

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

And that brings us to the top of the hour at 10:00 a.m. I appreciate everybody joining us this morning. If you have any other follow-up, please feel free to reach out to the Investor and Rating Agency Relations department. We'd be happy to help you out as we can. And before we end, I want to just remind you that we have our Financial Analyst Briefing in New York on September 25, and I hope you'll consider joining us then, and we look forward to speaking to you soon. Thank you very much.

Operator
Thank you. That concludes today's conference. Thank you for participating. You may now disconnect.