S&P Global
Market Intelligence

Aflac Incorporated NYSE:AFL

FQ4 2018 Earnings Call Transcripts

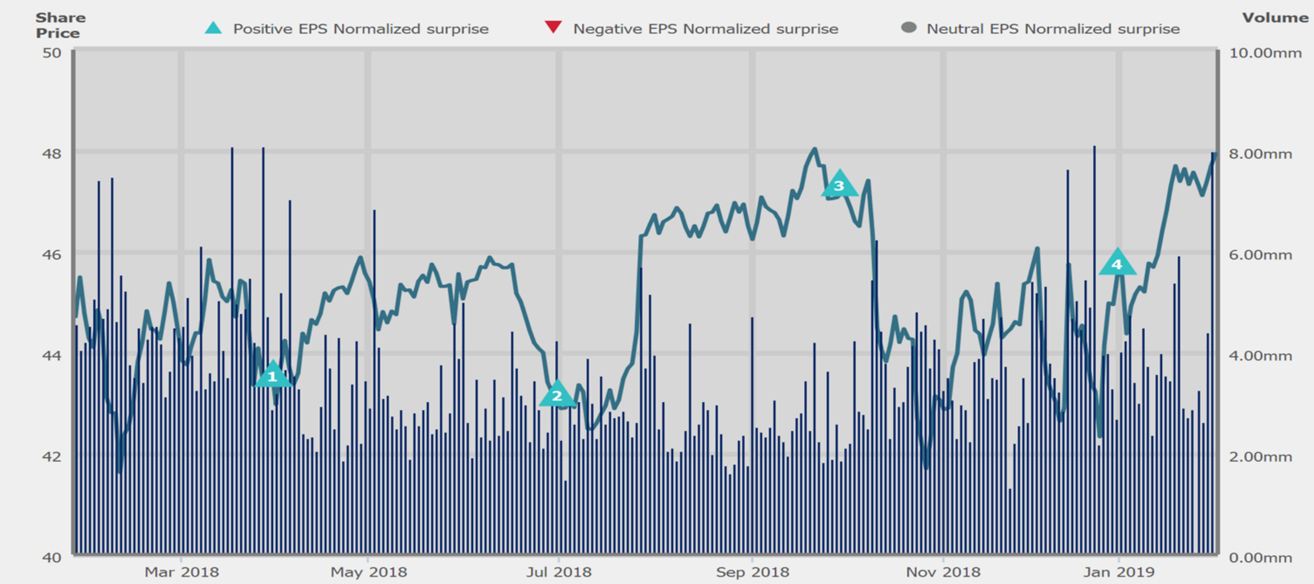
Friday, February 01, 2019 2:00 PM GMT

S&P Global Market Intelligence Estimates

	-FQ4 2018-			-FQ1 2019-	-FY 2018-	
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	ACTUAL
EPS Normalized	0.94	1.02	▲8.51	1.06	4.09	4.16
Revenue (mm)	5350.69	5126.00	▲(4.20 %)	5353.60	21773.95	21758.00

Currency: USD
Consensus as of Feb-01-2019 9:30 AM GMT

Stock Price [USD] vs. Volume [mm] with earnings surprise annotations



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ1 2018	0.97	1.05	▲1 8.25 %
FQ2 2018	0.99	1.07	▲2 8.08 %
FQ3 2018	0.99	1.03	▲3 4.04 %
FQ4 2018	0.94	1.02	▲4 8.51 %

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Chairman & CEO

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

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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
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Senior VP, Treasurer & Head of Corporate Development

Richard L. Williams
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Crédit Suisse AG, Research Division

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Autonomous Research LLP

Humphrey Lee
Dowling & Partners Securities, LLC

Jamminder Singh Bhullar
JP Morgan Chase & Co, Research Division

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

Suneet Laxman L. Kamath
Citigroup Inc, Research Division

Taylor Alexander Scott
Goldman Sachs Group Inc., Research Division

Thomas George Gallagher
Evercore ISI Institutional Equities, Research Division

Presentation

Operator

Welcome to the Aflac's Fourth Quarter 2018 Earnings Conference Call. [Operator Instructions] Please be advised that this 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. You may begin.

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

Thank you. Good morning, and welcome to our fourth 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. Eric Kirsch, Global Chief Investment Officer, will also provide some updates related to investments before we open our call to questions.

In addition, joining us this morning during the Q&A portion are members of our executive management team in the United States, Teresa White, President of Aflac U.S.; Rich Williams, Chief Distribution Officer; Albert 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 federal securities laws. Although we believe these statements are reasonable, we can give no ensuring 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 Aflac's website at investors.aflac.com and includes reconciliations of certain non-GAAP measures.

I'll now hand the call over to Dan.

Daniel Paul Amos
Chairman & CEO

Good morning, and thank you for joining us. Let me kick off the morning by saying that 2018 was another great year for Aflac as we continue to focus on supplemental insurance in the United States and in Japan. That focus sets us apart from every other competitor and has been a major contributor to our success. Through Aflac Incorporated subsidiaries in Japan and the United States, we have the privilege of helping provide protection to more than 50 million people. In both countries, we've earned our position as the leading supplemental insurer by paying cash fast and when the policyholders get sick or injured.

I'm especially pleased with the company's overall performance in 2018. Total pre-tax adjusted earnings increased 6.6%, which exceeded our expectations. This increase was driven by increased pretax profit margins, especially in Japan. These results are even more meaningful when you consider that we have increased our investment in our core technology platforms and growth initiatives with the goal of driving future growth and operating effectiveness. Investing in growth and innovation will continue to be a critical strategic focus in 2019.

In 2018, Aflac Japan, our largest earnings contributor, converted from a branch to a subsidiary at the beginning of April and generated strong financial results. Aflac Japan's 2018 third sector sales resulted in a 1.6% increase, which was consistent with our expectations of a low single-digit third sector sales growth for the year.

2018 also marked Aflac Japan's largest combined sales of third and first sector protection products in more than a decade, with JPY 93.9 billion in sales. As medical sales came off a strong 2017, bolstered by a refreshed core product, our distribution turned its focus in 2018 to launch of a Cancer DAYS 1 and Cancer DAYS 1 Plus and was tremendously successful. This laid the foundation and the groundwork for a great year for Aflac Japan's third sector sales, which came in at JPY 88.8 billion.

As we progress into 2019, we expect to see a slight decline in Aflac Japan's total earned premium in 2019, mainly due to the limited paid policies reaching paid-up status. We expect net earned premium of third sector and first sector protection products combined to grow at the 1% to 2% range.

Our focus remains on maintaining our leadership position in the sale of third sector products. In addition, while we don't lead that the first sector sales products, they complement our third sector line of products very well and have similar profitability.

From a profitability perspective, we tend to be agnostic when it comes to selling cancer, medical or first sector protection insurance. To that end, we will continue to refine our existing product portfolio to introduce innovative new products that our policyholders want and need and where they will want to purchase them.

And I think that the December announcement of the enhanced strategic alliance with Japan Post Holdings is an indicator that we're doing just that. Japan Post announcement's plan to purchase approximately 7% of Aflac Incorporated's common shares speaks volume about the overall strength and reputation of the Aflac brand and our products. We look forward to working with Japan Post to explore areas to grow our respective franchises in 2019.

Turning to Aflac U.S. We are pleased with our strong financial performance. 2018 was another year in which Aflac U.S. produced record new annualized premium sales and, more importantly, produced record pretax adjusted earnings. The pretax profit margin exceeded our expectations both in the quarter and the year. And as I mentioned, this result indicates increased expenses as a result of accelerated investments in our platform, following U.S. tax reform.

Aflac U.S.' sales for the year rose 3.2%, while our net earned premium increased 2.6%, both of which were in line with our expectations. As we indicated on our most recent out call -- outlook call, we expect Aflac U.S. to deliver continued solid growth in 2019, with earned premium growth in the 2% to 3% range and stable sales growth.

As you consider our U.S. sales, keep in mind that Aflac is unique with respect to our peers, and the majority of our sales come from independent sales managers and associates. We are fortunate to have such a strong independent field force, which is truly distinctive within our industry. These career sales agents are best positioned within the industry to [accept] and therefore, succeed with smaller employers and groups with fewer than 100 employees. Aflac's independent career agents have been the powerhouse behind Aflac's ability to dominate the smaller-case market. And I continue to believe this market is ours to grow.

Aflac's agents have also partnered with local and regional brokers as we continue to grow broker sales and while our team of broker sales professionals have made great enhancements, bolstering Aflac's relationships within the large broker community. While broker business is a smaller percentage of our overall business, it is representing a larger portion of sales in the market as well as at Aflac. It is very encouraging that as the brokers look for solutions for their clients, they have found that Aflac's product portfolio provides solutions that help fill those needs. Brokers are looking to connect with a strong brand like Aflac and leverage our outstanding track record of experience and extensive fulfillment capabilities. Aflac's expert agents and our independent field have demonstrated their ability to accelerate growth by working with brokers and broker sales professionals.

Across the company, we continue to invest in digital initiatives designed to address pain points in the development, sale, administration and customer experience related to our products. I am very pleased with our progress both in Japan and in the United States and our ability to continue these investments without losing focus on driving strong profits.

Our investment support, our distribution strategy, which is focused on being where the customer wants us to purchase protection.

Turning to capital deployment. We remain committed to maintaining strong capital ratios on behalf of the bondholders, the shareholders and the policyholders. At the same time, we're balancing our financial strength with increasing the dividend, repurchasing shares and reinvesting in our business. We continue to anticipate that we will repurchase in the range of $1.3 billion to $1.7 billion of our shares in 2019, within the range allowing us to be more tactical in our deployment strategy.

Of course, it goes without saying that we treasure our record of dividend growth. And I am pleased with the board's recent decision to increase the dividend coming off 2018, which was the 36th consecutive year of dividend increases. Our dividend track record is a nice reminder of the relative stability of our business model and earnings.

Looking ahead, we believe that our strong earnings growth will continue to reflect underlying earnings power of our business in Japan and in the United States as well as our disciplined approach to deploying excess capital in a way that balances the interest of the stakeholders. At the same time, it reinforces our dedication to delivering on a promise we made to our policyholders.

I'll conclude by reiterating how proud I am of our management team, our employees and our sales organization in Japan and the United States as they have worked incredibly hard to generate strong results that we have shared.

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

Frederick John Crawford
Executive VP & CFO

Thank you, Dan. As Dan noted in his opening remarks, we're very pleased with our overall financial performance in 2018.

Earnings results for both the quarter and the full year exceeded our expectations. For the quarter, adjusted earnings per share of $1.02 primarily benefited from stronger-than-expected pretax margins in Japan. For the full year, adjusted earnings per share on a currency-neutral basis came in at the $4.13 per share, above our guidance range of $3.19 to $4.06 a share. Setting aside the impact of tax reform on our effective tax rate and currency impact, pretax earnings for the year were up 5.7%. Coupled with $1.3 billion of share repurchases, we generated strong core EPS growth and impressive shareholder returns in a year of increased market volatility.

In terms of segment results for the quarter, and beginning with Japan, our benefit ratio, expense ratio and investment income came in favorable to our expectations. The lower benefit ratio reflects continued favorable claims trends and associated reserve adjustments. In addition, our new cancer insurance product has driven elevated lapse and reissue activity. We believe this is a result of an improved value proposition as the product now includes a new premium waiver feature. Depending on the mix of policies being replaced, elevated lapse and reissue activity has the effect of lowering our benefit ratio, increasing our expense ratio and, on balance, contributing only marginally to profitability.

Investment income in the quarter was driven by efforts early in the year to increase our allocation to floating rate loans, which benefited from both higher spreads and higher LIBOR rates. In addition, we experienced approximately JPY 2 billion in the variable income, which includes alternative investment returns and JPY 1 billion of onetime call premium and consent fee income. Variable and onetime sources of investment income are not embedded in our run rate expectations.

Finally, while our expense ratio came in higher as compared to last year's quarter, overall expenses came in below our fourth quarter forecast and the result of lower sales promotion and systems development spend. Overall, we posted a 21.4% pretax margin in Japan among the highest quarterly performance is in recent history and a very strong 21.1% for 2018.

Turning to our U.S. results. Our total benefit ratio for the quarter was in line with guidance. Along with favorable claims trends, we are seeing the effects of business mix with a gradual shift towards product lines, with a naturally lower benefit ratio and higher expense ratio. Our expense ratio in the U.S. for the quarter came in as previously guided at 38%. Accelerated spend related to post-tax reform investments and timing related to advertising spend drove expenses higher. Our U.S. pretax profit margin for the quarter was 17%; and for the year, it was 19.9%. As Dan noted, 2018 represents a record level of U.S. segment pretax earnings.

For both Japan and the U.S., our fourth quarter performance does not change our 2019 guidance ranges for benefit ratios, expense ratios and pretax profit margins.

I'd now like to ask Eric Kirsch, our Chief Investment Officer, to discuss the positioning of our investment portfolio in view of credit markets in 2019. Eric?

Eric Mark Kirsch
Executive VP & Global Chief Investment Officer

Thank you, Fred, and good morning, everyone. While we don't try to predict the exact market moves or starting and ending dates of economic and credit cycles, we do analyze market themes.

As investors, we want to position our portfolios with a long-term investment strategy in mind. To the last year or so, we had been of the opinion that the credit cycle was in its late innings, and we could see a turn soon. With this in mind, we have managed our credit portfolio with a bias for higher quality, supported by a disciplined underwriting process for new investments and an eye towards improving our credit profile to mitigate potential impairments and losses, positioning us well for future changes in the credit cycle.

Let me review highlights of the actions we have taken this past year, perspective insights as well as reviewing key portfolio characteristics. Over the past 12 months, I would highlight the following investment activity: From a relative value point of view, we have been underway with our investment-grade corporate bond purchases, given how tight spreads had become. The recent spread widening validated our concerns of not getting paid for the credit risk. We focused a large amount of our new money investments in private markets such as middle-market loans and transitional real estate. I want to stress that we have high underwriting standards and diversification goals. Our discipline has kept our exposure to some of the private market issues you read about, such as excess of leverage, lack of confidence and aggressive underwriting to the bare minimum. While we have seen spreads compress in these markets in the latter part of 2018, the majority of our purchases were made in the first year -- first half of the year at higher spreads. We have cut back our deployment goals in 2019, while maintaining our high underwriting standards.

We implemented a number of derisking strategies, designed to eliminate or reduce credit positions that we felt could underperform in a shifting credit cycle. Highlights include: In 2018, we disposed of over JPY 34 billion of our more illiquid legacy private placements, all below investment-grade. Some names we reduced that I would mention include exposure to the governments of South Africa, Tunisia, Trinidad and Tobago and Catalonia. We also reduced exposure to Navient Corporation.

In December, we initiated a $550 million relative value derisking trade, of which $500 million was to reduce exposure to energy names, including approximately $150 million to CCC-rated issuers. The proceeds will be reinvested across a diversified pool of investment-grade credits.

In fact, throughout 2018, including the $550 million trade initiated in December, we traded over $3.4 billion of public bonds to improve the health of our credit portfolio. This includes selling $1.2 billion of investment-grade bonds held by Aflac Japan, including reducing energy by $243 million and swapping $340 million of BBB assets into higher-rated transitional real estate, while improving our maturity profile and income.

Selling $500 million of BBB-rated investment-grade names in Aflac U.S. and reinvesting in AA-rated tax advantage municipal bonds, improving quality and increasing after-tax income, selling $600 million of BBB rated bonds in the Aflac U.S. portfolio to fund corporate capital activity.

Most recently, as you know, PG&E has been in the news and this week filed for bankruptcy. We hold about $147 million and conservatively decided to take a $21 million impairment as of December 31. This story will take time to sort out. We currently believe holding our position through the bankruptcy process will provide the best economic outcome. Let me also mention that these activities supporting our high-quality bias comes at a cost to net investment income. With new investment opportunities, such as private credit, we have been able to offset some of these headwinds.

Our main objective is always to ensure the safety and quality of our portfolio to minimize potential losses, while balancing our objective of delivering appropriate risk-adjusted net investment income. At the end of the year, we had managed to improve the credit quality of the overall portfolio by having 4.6% in below investment-grade credit, of which 2.2% are fallen angels, and the remainder are high-yield bonds and loans that we purchased within our credit standards. We also maintain that we believe to be a lower consolidated exposure to BBB names than our peers. BBBs makeup approximately 23% of the portfolio and have an average position size of slightly over $50 million.

Overall, we continually look to maintain a very diversified portfolio and shape it with an eye towards safety through the cycle.

As we look forward, despite a strong equity recovery in January, credit spreads remain elevated, and we believe it is signaling that credit investors are concerned that this may be the initial innings of a turn in the credit cycle. Regardless, our view will continue to be a bias towards maintaining a relatively higher-quality overall portfolio and proactively managing exposure to credits, whose performance may be challenged under a slower-growth backdrop.

Finally, I should highlight that this type of market environment also presents opportunities, especially when dislocations occur. Our strong current portfolio, combined with a healthy capital position, will allow my team to put new money to work and capture those opportunities that become apparent, which will improve future performance.

Now back to Fred.

Frederick John Crawford
Executive VP & CFO

Thanks, Eric. Picking up where I left off, let me comment briefly on our corporate segment. We continue to make progress on managing our economic exposure to the yen, while lowering enterprise-wide hedge costs associated with Japan's U.S. dollar portfolio. We accomplished this by entering into an offsetting hedge position at the holding company, which ended the quarter at a notional amount of approximately $2.5 billion and contributed $18 million on a pretax basis to the quarter's earnings.

In terms of capital, we ended the year in a strong position. As of year-end, our Japan's solvency margin ratio is estimated at approximately 970%, and our U.S. risk-based capital ratio is estimated in the mid-600% range.

2019 will continue the excess capital drawdown process in the U.S. as we target 500% by year-end. Over time, we believe we can run our U.S. RBC down towards 400%, given the risk profile of our U.S. business.

We ended the quarter with approximately $2.8 billion of capital and liquidity at the holding company, recognizing this balance naturally fluctuates. We have set aside $1 billion as a capital buffer and an additional $1 billion of contingent liquidity. Our liquidity position is in support of holding company derivative positions that serve to lower enterprise exposure to currency movement.

Including dividends and share repurchase, we returned $574 million to our shareholders in the quarter and $2.1 billion for 2018. As Dan highlighted in his comments, the Aflac board approved an increase in our quarterly common stock dividend by 3.8%, after back-to-back increases raised dividends 19.5% in 2018. The board continues to take a balanced approach with a desire to sustain our long-term track record of increases. While we ended 2018 strong, we need to manage through natural headwinds in 2019.

Net investment income is expected to modestly decline as compared to 2018, due in part to the derisking activity Eric noted in his -- and rolling U.S. dollar hedge positions into higher-cost contracts. While reacting somewhat to market developments, our forecast remains essentially unchanged from the outlook call, but we ended 2018 stronger than expected.

We anticipate lapse and reissue activity in Japan will slow in the second half of 2019. We are enhancing our medical product through offering writers that address a range of coverage needs and are available to existing policyholders. This strategy preserves and builds upon the favorable economics of our in-force policies but naturally pressures sales as defined by incremental annual writer premium versus a lapsed and reissued full policy.

Finally, with long-term topline growth as a primary objective, we continue our investment in product development, digital consumer-driven distribution and overall venture and incubation efforts to create future market opportunities.

We have affirmed our currency-neutral EPS guidance of $4.10 to $4.30 per share. And as Dan noted, we are maintaining our range for share repurchase at $1.3 billion to $1.7 billion. We remain tactical within the range guided by relative returns and other options for our use of excess capital.

I'll now hand the call back to David to begin Q&A session. David?

Daniel Paul Amos
Chairman & CEO
Thank you, Fred. [Operator Instructions] And we will now take that first question.

Question and Answer

Operator

[Operator Instructions] Our first question comes from the line of Andrew Kligerman from Crédit Suisse.

Andrew Scott Kligerman
Crédit Suisse AG, Research Division

Question on Japan's sales guidance of low to mid-single-digit decrease. Does that contemplate the possibility that you might sell an additional product through Japan Post?

Daniel Paul Amos
Chairman & CEO

I'm going to let our Japanese operation answer that. So Koide or whoever -- Koji. But I will say that, no, that does not contemplate Japan Post. 2018 was being able to work out the deal. 2019 is the planning process of coming up with something that we think might benefit their customers; and then 2020 I think would be more in the execution line. So I'll still let Koji and them talk.

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

[Foreign Language] Well, in terms of JP, things have not changed since our outlook call last time. In terms of target, it will be aligned with the customers' needs and we'll be setting the target accordingly. [Foreign Language] In January, we have launched a protection-type first sector product in medical -- sorry, medical product. [Foreign Language] And this medical product has a concept to be able to have the customers review their medical or the insurance product depending on their life stage. [Foreign Language] And we -- this enables customers to add a lump-sum type of coverage, especially for the young customers that we do have income support type of rider. And then for elderly customers, we are -- we make available our nursing care type of rider. Foreign Language] And for the existing policyholders, we have introduced midterm rider addition, a type of mechanism which allow our customers to be able to add to their existing base policy. [Foreign Language] And so this will be a shift from just focusing on the new -- rather than just focusing on the new business, we will now allow our existing customers to be able to expand their coverage and update their coverage based on the policies they have. [Foreign Language] And because this is a midterm rider addition, there will be less new AP, and AP policy for the additional part will be smaller. [Foreign Language] However, we will be able to maintain our existing policyholders' policies, which means that this will contribute positively to our earned premiums. [Foreign Language] And so this is our strategy to be able to really maintain the base policies of the existing customers without having them to purchase a total new policy.

Masatoshi Koide
President, Representative Director & COO of Aflac Japan

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[Foreign Language] This is Koide from Aflac Japan. [Foreign Language] And I just want to make sure that the new medical product that Koji has just explained about the product that we've launched in January, this is a product that is offered through channels except for the Japan Post. All the other channels apart of Japan Post offers this new product.

Daniel Paul Amos
Chairman & CEO

I want to just make sure all of you on the line pick this up because this is a little bit of a change. And it's very similar to the way we used to do business in the United States was, we would convert a policy. In essence, what you're talking about here is there won't be a new policy written in one lapse. We'll keep the existing policy in force, which will be a medical product, and we will add a rider on top of it. And therefore, the premium of that rider will be a smaller amount than a normal policy. However, they won't be lapsing the old policy. So the earned premium will ultimately be growing. But you will see a lower sales number because of that impact. So I just want to make sure everyone got that.

Andrew Scott Kligerman
Crédit Suisse AG, Research Division

Yes, that makes a lot of sense. And just a quick follow-up on corporate and other, where investment income went to $38 million versus $11 million last year, and that was the drawdown of excess capital. And then Fred mentioned that you might go from a mid-600s RBC to 500%, again, drawing down more capital. So the question is, can we expect this elevated investment income in corporate and other to kind of keep ticking up? Or is it possible you might even be able to exceed your $1.3 billion to $1.7 billion guidance on buybacks?

Frederick John Crawford
Executive VP & CFO

At this point in time, I wouldn't change our guidance on the range of buyback. That range in buyback takes into account moving additional excess capital of approximately $500 million up to the holding company. What I would say though is that from an investment income line item perspective in corporate and other, you will see that most likely increase but not necessarily because of the volume, if you will, of assets at the holding company and associated investment income, it's more driven because that's the line item where we house the benefits of our enterprise hedging program, offsetting the hedge costs and hedging dynamics in Japan. And as you may recall from the outlook call, we guided to pretax approximately $60 million to $80 million worth of amortized offset, if you will, to the hedge costs in Japan that will run through that line. To give you a comparison, that was approximately $36 million or $37 million -- $36 million in 2018. So you will see, as you look at corporate and other, essentially, the last page of our FAB supplement, most of those line items will remain relatively consistent in terms of revenue lines and expense lines. The one line that stands out is, you will see movement in investment income, not so much because of the excess capital at the holding company, more so moving because of our enterprise hedging program.

Operator

The next question comes from the line of Jimmy Bhullar from JP Morgan.

Jamminder Singh Bhullar
JP Morgan Chase & Co, Research Division

So I just had a question on the portfolio. And Eric, you mentioned sort of positioning it conservatively, given the environment. But you had fairly high investment losses in 4Q. So maybe if you could talk about to what extent do you think this is representative of what you'd expect if the environment remains challenging? Or was this more of an aberration, given how much the market moved in 4Q?

Eric Mark Kirsch
Executive VP & Global Chief Investment Officer

Sure. You really need to look and attribute all the gain and loss numbers. But if I think about impairments and loan losses, they were about $61 million for the quarter. For us, that probably was a bit elevated versus where we've been running. But recollect, over the last 2 to 3 years, our loan losses and impairments have just been very minimal. And also part of the $61 million was the PG&E situation, which is $21 million of it. So if I take the PG&E situation out, the $40-or-so million is really kind of expected, with large loan portfolio, now, other assets, nothing really too surprising in there. I certainly know going forward that the credit cycle is beginning to change. With a large portfolio like ours and other insurers, we're going to expect certain industries may have some challenges, and we'll be tracking that closely. And as I said, our job is to continue to shape the portfolio to avoid those credits that, in a tougher cycle, may have trouble. And we've been proactive, as I've said in my speech, doing that. So no doubt, if the credit cycle changes, we'll have probably larger impairments than we've had over the last 3 years. But I believe they'll be very manageable and minimal relative to the industry.

Daniel Paul Amos
Chairman & CEO

And we made the decision after the financial crisis that we were going to be all -- would have all types of assets to where we were never in a position like happened before. And therefore, when you're everywhere as you well know, the likelihood of having hits are much -- or will be escalated a lot. But they'll be small hits, and that's what's important.

Eric Mark Kirsch
Executive VP & Global Chief Investment Officer

Exactly. Just to build on that, which we've all known, we've tracked over history, we're diversified by different asset classes, by different strategies, and importantly, from a risk perspective, we're diversified by position size. We no longer hold these oversized concentrated positions. So when something should occur, it'll be in a much smaller size versus where we were historically.

Jamminder Singh Bhullar
JP Morgan Chase & Co, Research Division

Okay. And then maybe if I could ask one more, Fred, just on the timing of buybacks. I think the Japan Post can begin buying either late February, early March when your structure is completed. Would you consider front-ending buybacks to not be active at the same time as the Post is buying shares? Or do you believe it'll be more evenly spread through the year?

Frederick John Crawford
Executive VP & CFO

Yes. I -- we are not tactically changing our approach to buyback based on the Japan Post agreement. What we are doing is what we always do and that is we'll be tactical at times. For example, we accelerated a bit of our buyback right here just at year-end to take advantage of what we thought were compelling economics. And so we'll be tactical within the range, that will always continue, but we're not designing or being tactical with our repurchase surrounding the Japan Post agreement and they're building of our share count. So you should expect generally spread over the year, in other words.

Operator

The next question comes from the line of Suneet Kamath from Citi.

Suneet Laxman L. Kamath
Citigroup Inc, Research Division

Just on the first sector protection products in Japan. My sense is the market's pretty saturated with first sector products, which may be one reason why a lot of the domestics are moving into the third sector in the first place. So could you give us a sense of what is it about your first sector protection product that stands out versus the group? And are you essentially selling to the same customers that you already have? Or is it allowing you to reach a new group of customers?

Daniel Paul Amos
Chairman & CEO

Koji?

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

[Foreign Language] In many cases, we are selling our first sector protection-type to our existing policyholders because they already have their policy -- our policy, we are selling on top of the existing policies. [Foreign Language] Because especially this time, we have achieved a premium rate that is very attractive to non-smokers. [Foreign Language] And the coverage, which is a smaller amount, is also made available. [Foreign Language] And because we were able to set our premiums relatively low, many customers liked the product. [Foreign Language] And it is now, it takes about 5% of the protection-type sales.

Suneet Laxman L. Kamath
Citigroup Inc, Research Division

Okay. And then on the medical rider, I think you guys went through this years and years ago with the rider max where it sort of was a source of sales for a number of years. So how long do you think you'll have this ability to sell this medical rider? Like, how many -- how long will it take you to kind of work through your existing customer base in terms of folks that might be interested in adding the rider?

Eric Mark Kirsch
Executive VP & Global Chief Investment Officer

Koji would take that.

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

[Foreign Language] And in terms of the product this time, is this -- of course, this is for our existing policyholders, and we have different products for different age group of customers. For example, young customers have certain rider that we can attach -- have them attached and older customers, we have rider that cater for their needs. [Foreign Language] And particularly, the in-force number of medical policies we have is #1 in the industry. [Foreign Language] It does make us possible to take in or retain our customers for a long time, using our customer base. [Foreign Language] And this is a differentiator against our competitors, and this will also contribute to the increase in our earned premium.

Operator

The next question comes from the line of Humphrey Lee from Dowling & Partners.

Humphrey Lee
Dowling & Partners Securities, LLC

In Fred's prepared remarks, you talked about there are some redundant reserve releases because of the lapse and reissue activities that happened in the quarter. I was just wondering, can you size the benefit of those redundant reserve releases in the quarter. And maybe how we should think about that kind of throughout 2019?

Frederick John Crawford
Executive VP & CFO

Yes, let me step back and give you some attribution, and then answer beyond that in terms of what went on with the reserves in the quarter in Japan. I don't know that I would use the term redundant reserves. They're rather just released when the policy has lapsed. But let me explain. So the lapse and reissue activity, we would estimate, impacts -- when measured against premium, okay, will serve to reduce your benefit ratio, we estimate about 30 to 50 basis points, 2018 versus 2017. It's important to note that lapse and reissue activity takes place naturally in every year. It's just this year, and to some degree last year, was a bit more elevated due to a new medical product but more particularly this year, with the new cancer product. Importantly though, while the benefit ratio measured against premium goes down 30 to 50 basis points, you have a somewhat equal impact to the expense ratio because you are now essentially amortizing the DAC more quickly or writing down the DAC upon the lapsed policy. And that has the effect of increasing your expense ratio measured against premium, again, 30 to 50 basis points. And so you end up with a somewhat negligible impact to your bottom line. Now within those ranges, you could have more of one and less of the other, and so it can either impact positively or negatively your earnings. And that depends a lot on the age of the actual policies that are being lapsed and replaced. In the fourth quarter, it was a bit more pronounced. Those metrics were more like 70 to 80 basis points in the fourth quarter improvement to the benefit ratio and then similarly, increase in the expense ratio. And you can see that in our actual numbers, of course, in the quarter. So that would be the attribution. So set aside lapse and reissue in terms of pretax profit margins because it's fairly insignificant. In terms of the quarter and the strong pretax profit margins, it was largely just the positive trends in claims. And as a result of those positive trends, particularly, in our cancer block of business, the associated release of IBNR. And we released about JPY 3 billion of IBNR, predominantly related to the cancer book of business. But I would note that this is not entirely unusual in the sense that we've been doing these types of releases now for a few years, if not multiple years, and primarily because of the continued trends in the cancer book. There's no guarantee that, that will continue. And every year represents a variable, but there's been a pattern of this because the trends have been quite consistent.

Humphrey Lee
Dowling & Partners Securities, LLC

I understand that the improvement in benefit ratio is offset by the expense ratio. And then also. I guess, in part of your early remarks, you talked about longer term, you think you could kind of draw RBC down to kind of 400% over time. Do you have any stance in terms of timing how -- like how long would you start contemplating to move down from 500% target to a 400% target?

Frederick John Crawford
Executive VP & CFO

Yes, I think, right now, the idea would be, let's get -- let's settle down into the 500% target. This -- as I've mentioned before, this will represent the first year we've printed a U.S.-only blue book in a long, long time. Let us make sure we can digest the statutory moving parts. We had very strong statutory income for 2018, up around $830 million, helped somewhat by tax reform, but that was a very strong stat earnings year. And that's what we would expect, came in right about where we predicted because it's a very stable business. And so my view is with the stability of our business, the low asset leverage in our U.S. business, we can comfortably move it down to 400%. What I would plan to do is take this blue book, take our final year-end results, start working with the rating agencies, and my guess is that in 2020, we'll start to work that ratio down.

Operator

The next question comes from the line of Tom Gallagher from Evercore.

Thomas George Gallagher
Evercore ISI Institutional Equities, Research Division

Eric, when I hear you've shifted out of public corporate bond purchases and emphasized middle-market loans and transitional real estate, I guess, from a category standpoint, it's not clear that's a risk upgrade. Can you give some examples or statistics about how that risk is better or lower?

Eric Mark Kirsch
Executive VP & Global Chief Investment Officer

Sure, absolutely. First, I would say it's diversified. And that goes to the point of diversification pays dividends over time. But remember, in our program for middle-market loans, for example, we determine the underwriting standards. So we have first-lien secured loans, highly diversified, high degree of [confidence.] And the market has gotten frothy, and we're aware of that. But we've not lowered our underwriting standards, which is why, as I said, in 2019, our deployment goals are a bit less than they were in 2018, and we were fortunate to build a good portion of that portfolio in the first half of the year. So it comes down to underwriting. And in addition, because those companies, we're lending them money, we have first insight into whether or not they're having any difficulties with their business. Now most of them are doing quite healthy and very seldom we do have any issues. But when they do, we can walk in and make a difference. Now in the public sector, they are bigger companies, but we can't influence what company management's necessarily are going to do. So when the credit cycle changes, we've got to be more proactive in trading those assets. And then finally, I would say, when you look historically at the private markets, even through tough times, the default rates are low, and the recovery rates are fairly high because of the strong negotiating leverage that you have.

Thomas George Gallagher

Evercore ISI Institutional Equities, Research Division

And Eric, from a yield standpoint, what -- was it a yield enhancement from shifting out of the public corporates going into the transitional real estate and middle-market loans? Are you still making an excess spread?

Eric Mark Kirsch
Executive VP & Global Chief Investment Officer

Absolutely, Tom. Absolutely. So thank you for raising that. Substantial. I mean, you're getting paid for the additional risk, for sure. So in the investment-grade space currently for BBB type of names, you're in the 3.75% to 4% area for long duration. In the loan space, middle-market loans' gross yields, we're looking at 6.5% to 7%. Those are typically 3- to 7-year maturities. So the coupons are based off of LIBOR, which has been in our favor since we've started the program. So you earn a substantial yield advantage for a shorter-duration of maturity. And finally, let me add, just to put total context in it, remember, those floaters play a very important role in our dollar program and particularly with respect to the hedging program. Because of that yield advantage, I'm starting out with a 6% to 7% instrument, paying 3% or so in hedge costs, and I've got a net spread to 4%. With an investment-grade bond, I've got a duration mismatch between the asset and the hedge. And I maybe might be earning a spread of 1%. So again, it goes to diversification and looking at the entirety of the risk and the return. So thank you again for bringing up the return side of it. That's obviously an important element.

Operator

The next question comes from the line of John Barnidge from Sandler O'Neill.

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

This is a question on U.S. productivity. I know there's some seasonality that weights 4Q more heavily, but this looks to be a record this year. Do you see more -- this more coming from maybe cracking the distribution for broker nut? Or more from efficiencies that have been delivered on some of your tech and digital investments? As a reference point, I'm talking about Page 18 of the supplement.

Eric Mark Kirsch
Executive VP & Global Chief Investment Officer

Go ahead, Rich.

Richard L. Williams
Executive VP & Chief Distribution Officer

Okay. So as you noted, definitely was a record sales year and really coming off momentum of 8 consecutive quarters of growth and really was a balanced delivery. Our veteran associates provide strong contribution to our sales growth. Broker sales, as you mentioned, continued the positive momentum, and that's both with our broker sales professionals and our associates who work with brokers. And then as Teresa has continued to mention, we continue to focus on improving producer productivity and their long-term development. So I would say it's the balance of all those.

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

Okay. And then my follow-up, dovetailing on that. The recruited agent brokers definitely increased in the fourth quarter year-over-year and was twice what it was in 4Q '16. I know you talk about recruitment, and when the economy is doing really well, it's harder for the agents because of the commission structure. The brokers doesn't work that way, correct? And that is somewhat opposite of maybe how the agent recruitment flows through the economic cycle? Or could you talk about that a little bit more?

Richard L. Williams
Executive VP & Chief Distribution Officer

Sure. Obviously, recruiting overall is important to Aflac and will continue to be so. And more and more brokers are getting into supplemental insurance voluntary benefits. And so I think, as you look at the increase in broker recruiting, that's reflective of the overall market, more broadly. And as Dan eluded, brokers want to work with a company like Aflac that has a strong brand. So I think that's where you're seeing the elevation. And as we mentioned in FAB, we continue to want to increase the number of local regional brokers that work with Aflac in addition to our national broker partners.

Operator

The next question comes from the line of Alex Scott from Goldman Sachs.

Taylor Alexander Scott
Goldman Sachs Group Inc., Research Division

The first question was kind of a follow-up on the investment conversation. I guess, most of what you've talked about are U.S. dollar investments, and you gave a good amount of detail there. I guess, I'm just looking at the 10-year JGBs are back down to basically 0. And certainly, there must be limitations to how much you can kind of keep investing in the U.S. dollar portfolio. So I'm just kind of wondering like how should we think about new money rates -- new money yields rather, in Japan. And where those should trend? And at what point you sort of have to begin investing more heavily again in JGBs or yen-denominated assets, more broadly?

Eric Mark Kirsch
Executive VP & Global Chief Investment Officer

Yes, thank you. Good question. First, if you look at last year's final tally, we were about a little over 50% in yen assets and the rest in dollar assets. So it's not like it's predominantly just dollar assets because we do have risk limits and limitations to our dollar allocation. Secondly, just to frame, I know the 10-year JGB is the benchmark yield for Japan, but it's not the benchmark yield for us from an investment standpoint. We have long-term liabilities. So when we're in the yen-fixed income market, we're typically thinking about 20- to 30-year-type maturities and durations. And 20- to 30-year JGBs are anywhere from 70 to 90 basis points, depending where on the curve, but it's in that range. Thirdly, and very critically, just as a reminder from an asset liability management standpoint, all of our liabilities in Japan are in yen. And when we think about economic capital, our other solvency ratios, yen is the baseline. So when we think about the strategic asset allocation, about 70% of our book is targeted towards yen assets precisely to manage our asset liability management and obligations to our policyholders and our regulators there. So yen assets will always be part of it. Next, we're not just buying JGBs. We would acknowledge amongst our choices in yen, JGBs are the least attractive. But the choices we have include yen private placements, which over the last few years, we have improved our private placement program through higher diversification standards and finding better deals. And typically, we get paid for that risk. It just depends on the deal and the maturity but 20 to 30 basis points over a JGB yield. And then also, in the Japan market, there is a growing yen credit market and yen municipal market, and we deploy in that sector quite a lot. And we're also typically earning anywhere from 20 to 30, 40 basis points over JGB yields. So while we don't like the low yields, buying yen assets does serve our capital and serve our -- serves our asset liability management. But we're using our tools through the investment team to find non-JGB yen investments and at least earn a spread commensurate with the risk over the JGB yield.

Taylor Alexander Scott
Goldman Sachs Group Inc., Research Division

That's really helpful. Second question I had was just on the riders in Japan. I was wondering if you could give some more color on what the riders are. And what's the sort of mix expected from nursing riders versus income production riders and so forth? And I mean, with the nursing care rider specifically, I mean, could you just talk a little bit quickly about how that's different from sort of stand-alone, long-term care risk in United States? And what sort of makes you more comfortable with that rider in Japan?

Frederick John Crawford
Executive VP & CFO

Yes, I might say, and Koji, you may be good to just discuss the riders we're talking about and importantly, the notion of, as you've mentioned, carrying the policy through the lifecycle of the policyholder from income to nursing. Todd, it may be good for you to chime in on how this nursing care riders should not be confused with the types of [boosts] that one takes long-term care-type benefit. Koji?

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

[Foreign Language] Let me start from nursing care. [Foreign Language] This is the type of coverage that offers lump-sum benefit to customers. [Foreign Language] And the level of the nursing care need is determined by the [indiscernible], the certification or eligibility by the national government. [Foreign Language] And we are making this lump-sum amount payment to [reduce] the risk amount, and since this will be paid based on the eligibility determined by the national government, the amount will be limited. [Foreign Language] And for the middle to younger generation, we do offer income support rider, and this is also a lump-sum type of coverage that will be paid when the policyholder is not able to work. [Foreign Language] And we also have a standalone product, income support product. [Foreign Language] And because this standalone product's coverage is extended for a longer period of time and it requires explanation of the social worker benefit that is being offered by the government, so this standalone product is not selling as well as cancer or medical. [Foreign Language] And -- but this time, as I mentioned, the rider is a lump-sum payment type of product, and the explanation is much simpler. So if we are able to identify the needs of this kind of product, we might want to think about revising our income support standalone product. [Foreign Language] And this medical insurance that we have launched this time is not only the hospitalization benefit or the surgery benefit that we have always had. This also -- new product also allows to offer outpatient product as well. [Foreign Language] And as I mentioned earlier, we are the #1 medical policy-offering insurance company in the industry. So there is a big potential in terms of our business here.

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

I'll just add what Koji led with. You don't often get marketing leading with the risk aspects of the product. But just to emphasize on the care rider, it is a lump-sum benefit, and the definition of a claim is tied to the government definition. And those 2 things, we believe, differentiate it from a long-term care product in the U.S.

Operator

Our last question comes from the line of Eric Bass from Autonomous Research.

Erik James Bass
Autonomous Research LLP

You recently announced an investment in Singapore Life. And I was just hoping you could talk about the opportunity you see in the business and whether you expect to look at other investments in new markets with higher growth potential over time?

Frederick John Crawford
Executive VP & CFO

Yes, Max Broden led that investment for us. So I'll have Max comment on the nature of the investment and our expectations.

Max K. Broden
Senior VP, Treasurer & Head of Corporate Development

So we made a small investment of $20 million in Singapore Life. And this is a digital life insurance company in a region that we see great potential in for protection-type products. Together with that announcement, we also announced that we will collaborate on product development to develop cancer- and protection-type products together with Singapore Life. And we also will enter into a reinsurance agreement with them, but we would reinsure those products back to Aflac. So we see this as a very interesting opportunity for Aflac to use some of our skillset to deploy in this region. But we also understand that it might be tricky for us to do this by ourselves, and that's why we have aligned ourselves with a very strong partner with very strong and dedicated digital experience. And that's what we intend to lead with.

Frederick John Crawford
Executive VP & CFO

Yes, I think it steps you back to really the broader strategy, and that is, if we're going to enter or be involved in any way in a new geography, it's going to be on the back of digital; it's going to be with on-the-ground partners, so that it doesn't consume management time and attention; it's going to be with a measured amount of capital at risk; and it's going to be careful, but we would not -- we don't see the sense in what we would call kind of a traditional entry into those types of markets on the back of large-scale acquisition, large capital at risk, the building out of traditional distribution platforms of agents and so forth. That typically is a lot of money, a lot of risk, and your ability to compete with other players in the market is questionable. And so we think of this as a smart way of entertaining and exploring what might be possible, and that's our philosophy.

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

And thank you, operator. I believe that's the end of our call. We've reached and exceeded the top of the hour. If -- please feel free to contact Investor and Rating Agency Relations if there are any other questions or for more information. And we look forward to speaking with you soon. Thank you all for joining us today.

Operator
Thank you. And that concludes today's conference. Thank you all for joining. You may now disconnect.