S&P Capital IQ

CONTENTS

Aflac Incorporated NYSE:AFL

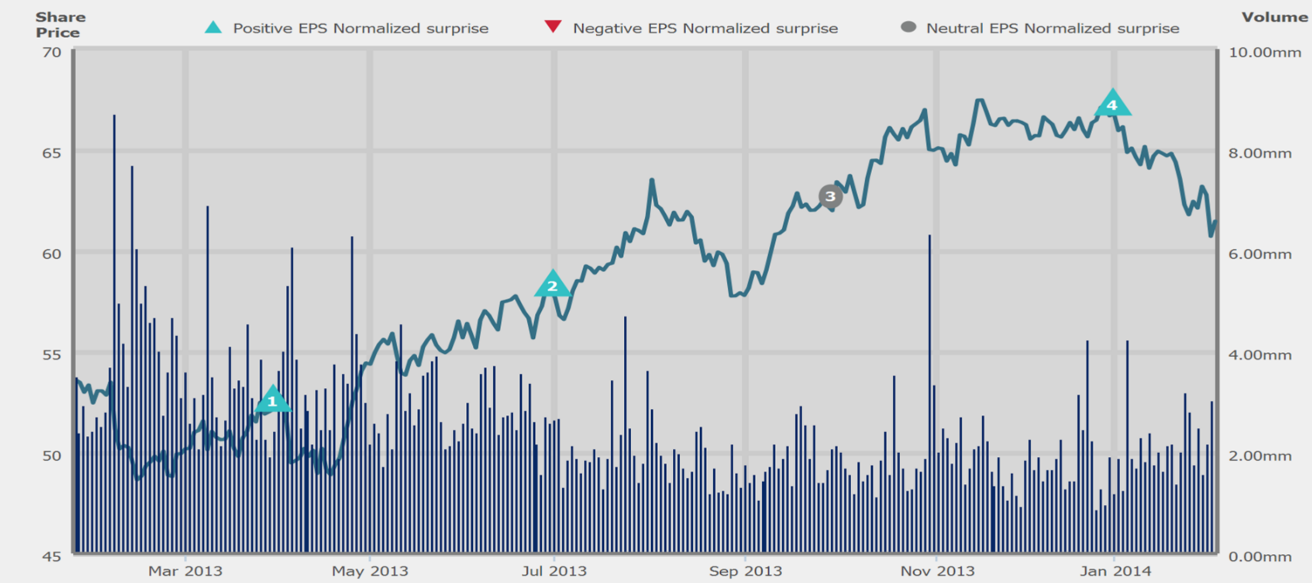
FQ1 2014 Earnings Call Transcripts

Wednesday, April 30, 2014 1:00 PM GMT

S&P Capital IQ Estimates

	-FQ1 2014-			-FQ2 2014-	-FY 2014-	-FY 2015-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	1.59	1.69	6.29	1.58	6.20	6.53
Revenue (mm)	5843.22	5640.00	(3.48 %)	5868.58	23244.28	23513.94

Currency: USD
Consensus as of Apr-30-2014 1:04 PM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ1 2013	1.62	1.69	1 4.32 %
FQ2 2013	1.51	1.62	2 7.28 %
FQ3 2013	1.47	1.47	3 0.00 %
FQ4 2013	1.39	1.40	4 0.72 %

Call Participants

EXECUTIVES

Daniel P. Amos
Chairman & CEO

Eric M. Kirsch
Global Chief Investment Officer and Executive VP

Kenneth S. Janke
Former Executive Vice President and Head of Corporate Finance & Development

Kriss Cloninger
President & Director

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

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Presentation

Operator

Welcome to the Aflac's First Quarter Earnings Conference Call. [Operator Instructions] Please be advised, today's conference is being recorded. I would now like to turn the call over to Ms. Robin Wilkey, Senior Vice President of Aflac Investor and Rating Agency Relations. You may begin.

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

Good morning, and welcome to our first quarter call. Joining me this morning is Dan Amos, Chairman and CEO; Kriss Cloninger, President and CFO; Ken Janke, Executive Vice President and Deputy CFO, Aflac Incorporated, and President of Aflac U.S.; Eric Kirsch, Executive Vice President and Global Chief Investment Officer. Also joining us from Tokyo are Paul Amos, President of Aflac; and Toru Tonoike, President and COO of Aflac Japan.

Before we start this morning, let me remind you that some of the statements in this teleconference are forward looking within the meaning of federal securities law. Although we believe these statements are reasonable, we can give no assurance that they will prove to be accurate because they're prospective in nature. Actual results could differ materially from those we discuss today. We encourage you to look at our quarterly release for some of the various risk factors that can materially impact our results.

Now I'll turn the program over to Dan who will begin this morning with some comments about the quarter as well as our operations in both the U.S. and Japan. And then I'll follow up with a few financial highlights for the quarter, and then we'll take your questions. Dan?

Daniel P. Amos
Chairman & CEO

Yes, thank you, Robin. Good morning, and thank you for joining us. I'm pleased that we met and, in many cases, exceeded our financial targets for the first quarter.

Let me begin today with an update on Aflac Japan, our largest earnings contributor. Pretax earnings in yen were up 4.6% on a reported basis and 1.5% on a currency-neutral basis. Sales of the third sector products in the first quarter were up 1.8%. This result is just slightly below our annual sales target and somewhat disappointing. Our focus this year remains on growing the sales of the third sector products.

Last quarter, we communicated our expectation that sales of first sector products would be down significantly, 60% in fact, in the first quarter of 2014. This was based on difficult comparisons to prior year for sector sales, which climbed considerably ahead of the premium rate increase in April of 2013.

This quarter, Aflac Japan's first quarter product sales of first sector products were down 67.6%, which significantly contributed to our overall new annualized premium sales decline of 48.7%. However, we continue to expect that for the second through the fourth quarters of this year, the sales of the first sector products will be down slightly compared to last year, and we still believe that will be the case.

Looking at the long-term sales growth opportunities, we remain encouraged as we continue to expand and develop distribution channels. This includes an agreement between Aflac Japan and Japan Post Holding, which I believe will gradually but steadily benefit our cancer insurance sales in the coming years. As we ramp up the sales representatives at the 3,000 Post offices that sell our products, I believe our 2014 expectations for Aflac Japan third sector sales to increase in the range of 2% to 7% is still reasonable.

Now let me turn to the U.S. operations. In the first quarter, Aflac U.S. pretax profit margin was 20.8%, and pretax operating earnings were up 7.9% for the quarter. Aflac U.S. sales declined 4.4%, which was discouraging considering our results last year. Uncertainty around health care reform implementation has prompted many business and consumers to postpone the decision related to health care coverage, especially with the groups 50 or less. However, amid this doubt and uncertainty, we believe the need for our products is just as compelling, if not more than ever before. That's the message we will continue to convey to businesses and to their employees. Additionally, I believe we've also executed -- we've not executed as well as we should have. This year, we're taking several steps we think will help sales over time. This includes a focus on recruiting and training, in addition to performance management and improvement of our sales coordinators. At the end of March, we completed the initial test work of Aflac's exchange called EVERWELL. We are analyzing the first phase of the pilot program and are making adjustments to the platform based on those insights and field sales input. Taking into account the strategic initiatives, along with the challenging economic environment, I continue to believe that Aflac U.S. sales will increase in the range of flat to up 5% for the full year for 2014.

Turning to investments. I'm pleased with the progress in the multiyear strategy to build out our investment division. Additionally, we're on track to complete this build-out by the end of this year as we continue to make strides with the infrastructure, the people, the processes and the technology we're putting into place.

Now we'll provide you an update on the consolidated financial performance, which was strong for the quarter. Excluding the impact of foreign currency, operating earnings per diluted share rose 5.9% for the quarter. This result puts us slightly ahead of our annual target of 2% to 5% increase in operating earnings per diluted share before the impact of foreign currency. However, as the year progresses, we expect to see increased spending and higher benefit ratios than we experienced in the first quarter. As a result, we continue to believe we'll generate operating earnings per diluted share in the range of 2% to 5% on a constant currency-neutral basis.

On an operating basis, our first quarter annualized ROE was 22.7%. Keep in mind Aflac's ROE is sensitive to currency fluctuations because we largely hedged our equity into dollars but not all of our earnings. That means when the yen weakens, our ROE declines. Had the yen remained unchanged since the end of December, operating ROE would have been 26% in the first quarter. Based on our year-to-date returns, we expect to meet our ROE target range of 20% to 25%, excluding the impact of foreign currency for the full year.

We remain committed to generating strong capital ratios, both RBC and SMR, on behalf of our policyholders and our bondholders. Although we have not yet finalized our statutory financial statements, we estimate that first quarter 2014 RBC ratio will exceed 775%. Additionally, we expect that Aflac Japan's estimated first quarter SMR will be above 750%. You'll recall we anticipated repatriating approximately JPY 100 billion in 2014. Given our strong capital ratios and risk mitigation strategies, we now anticipate repatriating JPY 127 billion this year. This increase in repatriation bolsters our liquidity and flexibility and gives us the utmost confidence in this year's plan to repurchase $800 million to $1 billion for our common stock. It also allows us to focus more on positioning the SMR repatriation and repurchase for 2015.

For nearly 6 decades, Aflac has been delivering on a promise we made to be there for our policyholders when they need us most by paying clients fairly and promptly. We continue to believe we're well positioned in the 2 best insurance markets in the world. Our success in these markets has presented us with the privilege and the responsibility, providing financial protection to more than 50 million people who count on us to be there when they need us most, and we have delivered on that promise.

Now I'll turn the program back over to Robin. Robin?

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

Thank you, Dan. I'd like to go over some first quarter numbers this morning, especially those related to the yen impact, which was notable. I'll start first with Aflac Japan, beginning with the currency impact for the quarter.

During the quarter, the yen weakened against the dollar 9.8%. And referenced to the top line in yen terms, revenues, as reported, were up 2.2%; while excluding the impact of currency, revenues were up 1.5% for the quarter.

Investment income, as reported, increased 9.4%. Excluding the weaker yen in the quarter on Aflac Japan's dollar-denominated investment income, net income rose 4.5%.

In terms of quarterly operating ratios, the benefit ratio-to-total revenues declined over last year, going from 61.4% to 59.9% in the first quarter.

Reinsurance impacted the benefit ratio by a negative 0.5 in the quarter. The improvement in the benefit ratio reflects typical seasonality as it usually increases as the year progresses. Excluding the impact of the weaker yen, the benefit ratio for the quarter would have been 60.3%.

The expense ratio increased in the quarter to 18.1%, up from 17.1% in the first quarter of 2013.

Reflecting the improvement in the benefit ratio, the pretax margin increased, going from 21.5% to 22.0%. Excluding the impact of currency, the pretax profit margin for the quarter would have been 21.5%.

With expansion of the margin, pretax earnings increased 4.6% in yen terms. Excluding the impact of the yen, pretax earnings in the quarter increased 1.5%.

Now let me turn to some numbers for Aflac U.S. Total revenues rose 1.2% for the quarter, and persistency was 73.8% compared to 74.7% a year ago. And looking at operating -- other operating ratios, the benefit ratio for the quarter was 47.1% compared to 48.0% last year. The operating expense ratio improved slightly, going from 32.5% to 32.1%. The profit margin was 20.8% compared to 19.5% a year ago. Primarily reflecting the improvement in the benefit and expense ratios, pretax operating earnings increased from 3.6% last year to 7.9% this year in the quarter.

Now turning to some investment activity for the quarter. Let me first start with Aflac Japan. Approximately 74% of the new cash flow was invested in JGBs for a weighted average yield of 1.51%. During the quarter, 26%, or $1.1 billion, of new cash flow was invested in U.S. securities for a weighted average yield of 3.37%. As a result, the total new money yield in Japan for the quarter was 1.99%, up 47 bps from December 31 and down 104 bps from a year ago. The portfolio of yield was 2.86% at the end of March, up 6 basis points from the end of December and 15 bps lower than a year ago. In terms of U.S. investments, the new money yield for the quarter was 4.33%, up 1 basis point from December 31.

Turning to a few other items in the quarter. Noninsurance interest expense was $50 million compared to $48 million a year ago. Parent company and other expenses were $16 million compared to $17 million in the first quarter of last year.

On an operating basis, the tax rate was 33.8% compared with 34.4% a year ago. As reported, operating earnings per diluted share were $1.69, in line with the year ago.

The significantly weaker yen decreased our operating earnings per diluted share by $0.10 in the quarter. Excluding the yen impact, operating earnings per diluted share would have increased 5.9%.

Lastly, let me remind you what Dan said. We're reaffirming our objective for 2014 of a 2% to 5% increase in operating earnings per diluted share, excluding the impact of the yen. And this year, we estimate that a JPY 1 move on the average annual exchange rate will equal approximately $0.031 to $0.037 per diluted share. So if the yen averages 100 to 105 for the full year, we would expect operating EPS of $6.06 to $6.40 per diluted share this year.

For the second quarter, using the same currency assumptions, we would expect operating earnings to be somewhere in the range of $1.54 to $1.68 per share.

I'd also like to take this opportunity to remind everyone that our annual Financial Analysts Briefing meeting will be held in New York on May 22, and we hope to see you all there.
Now we're ready to take your questions. [Operator Instructions] Now we're ready to take your questions.

Question and Answer

Operator

[Operator Instructions] JPMorgan Chase.

Jamminder Singh Bhullar
JP Morgan Chase & Co, Research Division

I had a question on Japan third sector sales. Obviously, this slowed a lot from the roughly 16% growth you had in the fourth quarter, and a big part of that is the slowdown in the medical products. So maybe if you can discuss what's going on there. And then related to that, how do you feel about the Post relationship and how that's taken off, and just what your expectations for -- are for how fast you can ramp up cancer sales via the Post?

Daniel P. Amos
Chairman & CEO

Toru?

Tohru Tonoike
Vice Chairman of Aflac Japan

Yes. Yes, let me begin with the dollar sales of the medical products. We started that -- we offered the new medical product in that -- over last year and have been selling pretty well for basically the full year. And this continues to sell well even in the early part of this year. It is true that it does not sell as much as it used to be, but it's just still maintaining the momentum. And the first quarter is always a little bit slow quarter because every year that -- our agents tend to slow down a little bit after a busy fourth quarter end. So -- but we are feeling pretty confident with that expectation of our medical sales going forward. And also, that you asked about our expectation about the JP -- Japan Post cancer product buildup. And I can tell you that since October last year when we expanded our cooperation with Japan Post, Japan Post and Aflac have been trying to build up that -- the new level of the cancer business. And we did it together and we have talked to each other and made an agreement how to do it, and both Japan Post and Aflac are doing exactly what we have agreed. So -- but the basis is building up as they had planned. But because of the magnitude of the organization of the Japan Post, the low road [ph] has been slower than we had expected, but we are working on that. And now that April is the first month of their financial year, so they have been -- started a new stage in which the new things are started. For example, the sale of the cancer product -- Aflac cancer products is now clearly defined as an important part of the Japan Post and the business plan so that they have more clear vision of the importance of the cancer products among the Japan Post. So -- and also, we expect that in addition to the Japan Post, and -- the Compo, the insurance company, will be -- will start working for us when -- as soon as their application for the new arrangement with Aflac is approved. So we are -- many good things -- we are expecting many good things in the near future. But I can't tell you how soon we can do it, but we are feeling pretty confident about the way it's going.

Operator

John Nadel, Sterne Agee.

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

Maybe a question for Kriss. Kriss, you've been -- if I've been following this correctly, I think you've been trying to shift our focus on repatriation from Japan from what used to be more of an earnings-driven level of repatriation to one that's more of a function of the capital ratios or SMR. So I guess the question is this. With the increase in your expected repatriation, how should we think about what you guys are targeting for an SMR ratio if you allow for some stress? And maybe more specifically, the incremental JPY 27 billion, how do we think about that in terms of the impact on the SMR in points?

Kriss Cloninger
President & Director

Okay. Well, you're correct; I'm trying to refocus the orientation of repatriation from FSA earnings toward the absolute level of the SMR, it's not to say that we ignore FSA earnings at all, John. But in making a decision to target a higher repatriation than originally projected, specifically JPY 127 billion instead of about JPY 100 billion, I was in Japan a week before last and looking at projected SMRs as of the end of the first quarter and the like and concluded that if we kept about the same SMR that we had at December 31, which was around 777% specifically, but in the 750% or 775% range, we could bring back about 25% more than we expected or the JPY 127 billion number and still achieve that level of SMR. Now you made the observation that -- what's our kind of risk-adjusted SMR target. I forget what the exact words you used were, but it's not the 775% is our target SMR. That's got a cushion in it to allow for the fact that unrealized gains are substantial at the moment. What would the impact on the SMR be if interest rates went up some? What happens if we have some currency changes? What happens if credit spreads increase? And so we can absorb a fairly significant change in those factors and still stay above what I'd call the core target, which is going to be closer to 600%. It might be even a bit below that. Now we're going to build out some of that, John, at the FAB meeting. We've got presentations Todd Daniels, our Chief Risk Officer, is going to make, and Ken and I will offer additional comments. But you're right on, we're trying to produce an appropriate level of repatriation primarily in relation to where our capital ratios are.

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

Very helpful. And then just one quick follow-up on the level of investment spending. In the quarter and for the year, I -- if memory serves, you had expected about $0.12 or $0.13 of incremental investment spending in 2014 over '13. Can you give us some sense for how much of that was in the 1Q numbers? It doesn't seem like much.

Kriss Cloninger
President & Director

Well, let me start and Eric may want to follow up. The $0.12 you mentioned was what I categorized as our headwind to increase in operating earnings per share on account of several investment-related matters. One was lower yields than we started with at the beginning of last year because at the beginning of last year, we put a lot of money into U.S. corporates in the first half of the year. So we had a very good start on yield. This year, we pulled back the second half of the year to invest more in JGBs. But we restarted the U.S. corporates in the first quarter, and I want Eric to comment on that. But a combination of lower investment yields in the first part of the calendar year 2014 compared to 2013, a somewhat lower level of new cash flow because of the decline in the first sector sales also impacted that $0.12 estimate, and very little of it related to investment operating expenses. So [indiscernible].

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

And I appreciate that. I was actually referring more to this modernization-type project you've got under way, particularly in Japan, I'm sorry.

Kriss Cloninger
President & Director

All right, the so called CVP project? Yes, I had estimated about $0.12 a share for that one also. So that's where I got confused. But...

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

Yes, sorry. And then -- and my only point is that it doesn't look like expenses really picked up very much at all in 1Q. I'm just wondering if there was any portion of that $0.12 already incurred in 1Q.

Kriss Cloninger

President & Director

Yes, there was. What we budgeted in estimating the $0.12 for CVP was, in fact, incurred in the first quarter of 2014. So our spending is in line with the budgets that underlie the financial estimates.

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

Okay. But is that more back half of the year-loaded? Like is it $0.03 a quarter. It doesn't seem like it's $0.03 a quarter.

Kriss Cloninger
President & Director

I think it ramped up some. I don't specifically remember what it was by quarter, but I believe spending was scheduled to ramp up some throughout the year of 2014, but it was going to level out in 2015. So one, it wasn't like 0 in the first quarter and $0.04 in the second, third and fourth. We had some in the first.

Operator

Tom Gallagher, Crédit Suisse.

Thomas George Gallagher
Crédit Suisse AG, Research Division

Kriss, one quick follow-up for you and then I had one on U.S. margins. The -- so the increased repatriation amount, can you just talk about planned uses of that? Is there the opportunity of potentially upsizing the buyback for this year? Or should we think about that more for paying an upcoming debt maturity?

Kriss Cloninger
President & Director

No, we've already provided for the upcoming debt maturity. We took care of that with the bond issue last year. This additional repatriation increases our financial flexibility. I think it gives us more confidence. We're likely to hit the high end of the target on the share repurchase this year. But quite frankly, we just decided it last week, and I really haven't had a chance to assimilate it with my treasury team here yet. But it increases our confidence we can hit the upper end of the share repurchase target. We already did $415 million worth of $800 billion to $1 billion target for the year. And we could have done more in the first quarter, but we wanted to keep some dry powder in case of market developments later in the year. So I don't know. Ken, do you have any...

Kenneth S. Janke
Former Executive Vice President and Head of Corporate Finance & Development

Tom, the only thing I'd add to that, it's more likely that the additional repatriation will be warehoused in Columbus on the U.S. segment, but we have more than adequate dividend capacity, if we elected later, to send it to the parent company.

Daniel P. Amos
Chairman & CEO

And the only other comment that I want to make is that we're well aware of how much shareholders feel about additional capital and that they'd like to see it in the share repurchase. So balancing that with what we've always said about the dividend will be continue the way we operate going forward.

Thomas George Gallagher
Crédit Suisse AG, Research Division

Okay, got it. And then my question on the U.S. is margins were strong there. Looks like it was coming from the reduction in the size of future policy benefit reserves, meaning there was some kind of reserve drawdown. Was that related to lapses? Or can you provide some color on what happened there?

Kenneth S. Janke
Former Executive Vice President and Head of Corporate Finance & Development

Yes, this is Ken. It was related to the change in persistency. That's what largely drove it. You saw that also reflected in higher debt amortization. We also had lower operating expenses, particularly general operating expenses. And you know we commented last year in the third quarter that we're undertaking some initiatives here to enhance our operations, particularly in an enrollment initiative right now. And we haven't seen a lot of expenses associated with that yet, so you'll see that increase as the year progresses. And the other thing that I'd note in there is you may remember last year we made some changes to our retiree medical and to moving from a defined benefit to a defined contribution plan for new hires. And as a result, a lot of that savings flows through the U.S. segment. And it's actually those savings that we had anticipated using as funding the initiatives that we're working on in the U.S. So again, our expectation would be that we would see higher benefits in the next several quarters, which is typically our seasonal pattern, and we'd also see greater spending on some of these strategic initiatives that we've outlined. The 2 highest priorities within those initiatives, I would say, other than the enrollment that I mentioned are the EVERWELL exchange platform and then building out the sales distribution at Aflac Group so that we can better penetrate the large case market.

Thomas George Gallagher
Crédit Suisse AG, Research Division

And just one last follow-up. Is the expectation that the higher lapses -- is that some -- you view that as a one-off? Or are you seeing any evidence that, that's going to remain elevated for a while?

Kenneth S. Janke
Former Executive Vice President and Head of Corporate Finance & Development

Well, we always see it a bit -- it's always a bit lower in the first quarter. It won't -- but it's something that we're carefully monitoring. We continue to see some mixed economic data, and we don't know to what degree that may be driving it. But it's something that we're watching very closely.

Operator

Seth Weiss, Bank of America Merrill Lynch.

Seth M. Weiss
BofA Merrill Lynch, Research Division

I have a question on the U.S. sales data and the change in recruited agents and producing agents. So I believe this is the first quarter in about 1.5 years where you've had an increase in recruiting agents, but the producing agent count continues to decrease rather sharply. Could you just comment a little bit on the dynamics of the producing and recruited agents?

Kenneth S. Janke
Former Executive Vice President and Head of Corporate Finance & Development

Yes. Let me start, and I'm sure Dan is going to want to add something to this as well. We have really been focusing the career side of our sales force, meaning our sales management throughout the country to focus on the recruiting activity. And the 3% increase that we saw in the first quarter, I think, is just a reflection of, really, a redoubled effort on recruiting. What we need to do is -- the process is to bring new recruits in and then have them convert to producing agents. And you get that through training and the mentoring through the coordinator system. And that's the number that we're really focusing on turning. We haven't seen it yet, but we've seen other activities, for instance, improvements in the number of new payroll accounts that we think will lead to better producers as we go forward.

Daniel P. Amos
Chairman & CEO

Yes. I think -- I've been now watching the U.S. in getting very actively involved for the last 9 months or so. And we've created some short-term disruption for what I believe will be long-term growth. The segmentation of the way we do business to where our field force is concentrating on 100 or less, our core broker, which is more brokers that deal with what I'd call community brokers and then national brokers and our ability to pay higher commissions to the management team for 100 or less, I think, is going to be very positive now. The way we do it is, it's not on first-year commission, it's on renewal commission. So they actually won't see the benefits until January of next year. I mean, it's kind of like me telling you, I'm going to give you $100 versus handing it to you. And so, it has a little slower impact even though we're showing it to them on statements of what it will be and things of that nature. It takes a little while. But I do believe that there is great opportunity there for us, and I think the second quarter will still be down slightly. I want to be clear on that. But I think the second half, I'm expecting it to be up. All that being said, we've got to execute well. We've got some problems on our own that we're working on. But I am encouraged because I believe with change comes disruption, but it also offers opportunity. And I believe there's a lot of opportunities for us and we're working hard on doing that. And I believe, ultimately, we will prevail and see stronger growth, especially in the larger than 50 accounts, because I think our individuals will continue to grow that business for us. But it'd be actually easier to grow accounts 50 or more if we didn't have the field force. But I've to deal with the field force who are so important to us, and they are key to our growth. But I have to work that through, and it's just taken some time. But I have been -- and talk to the vast majority of our field force. I'd say 80% to 90% of the field force I've been in front of, talked to and -- I'm encouraged by what I'm seeing, but it's slower than I want it to be. I'm frustrated that it's taken longer than it is. But I do believe the fundamentals are there. And I could talk on and we'll cover it in more detail at the FAB Meeting, but just because of a lot of financial questions, you want I'll limit to that, but if you want to ask more, I'd be glad to answer.

Seth M. Weiss
BofA Merrill Lynch, Research Division

Okay. And I appreciate that commentary. If I could just ask one follow-up maybe just on Japan and Japan Post. And I believe, this quarter, in terms of talking about the Japan Post ramp-up, this is the first time that, just in your prepared script, you've linked the 2% to 7% increase in sales with the ramp-up of sales representatives in the 3,000 Japan Post offices. I'm just trying to reconcile those comments with Toru's comments that the rollout was slightly slower than expected. So maybe if you could comment on that and if there's actually a specific number of Japan Post cancer sales that's built into that 2% to 7% guidance number.

Daniel P. Amos
Chairman & CEO

Oh, absolutely. There's a number built into the 2% to 7% with Japan Post, but they have specifically asked us not to discuss that and we have to adhere to their request. But most definitely, and -- I believe they will achieve what they've told us. I generally find that to be true with all Japanese corporations. I saw it with Dai-ichi Life. I saw it with the bank channels. I've seen it with all the groups that we've dealt with that they come very close to meeting or exceeding the objectives that they've set forth. Saying that, remember, all the new objectives were reset effective April 1, with it being a new year for them. And so, I do expect them to make those numbers because they're committed to it. They see it as a positive for them, not just for us, as they make decisions on what they're going to do in terms of going public or whatever. It's a big benefit to both us and to them. So -- go ahead, Robin.

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

And I would also remind you that the number of Post offices almost doubled in March. So that's just the curve where we went from 1,500 Post offices to 2,980.

Operator

Our next question comes from Yaron Kinar, Deutsche Bank.

Yaron Joseph Kinar
Deutsche Bank AG, Research Division

Going back to that last discussion above the cancer product sales in Japan Post, I guess, I'm still having a little difficulty reconciling a few of the previous statements, where, on the one hand, we have the 2% to 7% growth guidance still intact; on the other hand, I think -- or was it in the past was that the EVER product [indiscernible] the impact from the August launch would wane by the second half of this year. And I believe, Dan, you also said that the cancer sale rollout will be gradual. I just -- I have a very difficult time getting to, let's say, the midpoint of that 2% to 7% growth range without a much more substantial growth in cancer products and would be thankful for any additional color you could offer there.

Daniel P. Amos
Chairman & CEO

Well, what I would say is the actual number of accounts or Post offices does not totally give you a number because 1 office in Shinjuku is bigger than 100 offices in another location. So total number of offices won't directly tell you. But symbolically, it begins to set the pattern for what we're talking about, that we have doubled and that we're on the road to do this. You -- so the other thing that Toru mentioned is, is it's not just the Post office, but also the sales organization of the Post office eventually selling with us and when it will come online and how they'll do it. They got -- which is compote [ph], they have an enormous sales force that is very, very strong in dealing with the consumers and exactly how that will come on. And all I can really tell you is, is what I've said in the fourth quarter is, is that we absolutely expect to achieve that number. And I wish I could give you more color on it, but that's part of doing business in Japan. As you may know or not know, one time, people of other companies discuss something that was told not to do, and it created enormous problems between the 2 companies. So we don't want any problems because we are working so well with them and appreciate. But we -- let me be clear, we don't get to go at our pace. We have to go at their pace, but their pace and our pace are the numbers reflected in the sales targets that I gave you.

Yaron Joseph Kinar
Deutsche Bank AG, Research Division

Okay. And then, one follow-up on U.S. sales and persistency. Usually, when I look at persistency coming down, it's some indicator of more shopping around and turnover. And yet, sales still seem to be a bit lower, so you're not benefiting from lower persistency on the other end. Could you maybe add some color there on what's hindering sales at this point?

Daniel P. Amos
Chairman & CEO

Say that one more time.

Yaron Joseph Kinar
Deutsche Bank AG, Research Division

Sure. In the U.S., I'm looking at persistency rates. They've come down a bit even when you adjust for seasonality. Usually, when you see some lower persistency, it's -- it often comes in with a bit more sales just because you see more turnover in accounts and more shopping around. And yet, we haven't really seen that in the sales numbers this quarter. So I was curious, maybe you could give us a little more color on what's been holding back sales.

Daniel P. Amos
Chairman & CEO

Well, part of it is recruiting from the year before. There's no doubt in my mind that the recruiting has hurt us to a great degree because there is an enormous correlation between the number of new accounts. I mean, the number of new recruits and the number of new accounts they open. And so, Tom, our Director of Sales, has really been concentrating on ramping up the number of people that we hire. Also, one of the things is simply putting in these new programs and the separation. We've had meetings that have disrupted us to a degree in terms of just short-term sales. But putting excuses aside, I just don't think we've done a good enough job, and we've got to do better. I'm not going to go blame a bunch of stuff except us, and we're going to pick it up, and we've got little problems here and there on everything. But

I believe the economy is no worse than it was, if not a little bit better. I believe the accounts over 50, they've adjusted pretty much, and there's no major change there. There -- it seems to be a little bit of problem with the accounts of 50 and less because they are uncertain to some degree. And of course, that's where we write the majority of the business. But overall, I think we should be doing better, and I'm going to be expecting more in the second half.

Yaron Joseph Kinar
Deutsche Bank AG, Research Division

Okay. So the 0% to 5% growth target or guidance is still intact?

Daniel P. Amos
Chairman & CEO

I still believe in that. And as I said, I look for the fourth quarter to -- I mean, second quarter to be down slightly. So I don't want to mislead you. [indiscernible] it would be hard to live with it, end of second half, I warn you now. You don't have to tell them. They know it.

Operator

Our next question comes from Erik Bass, Citigroup.

Erik James Bass
Citigroup Inc, Research Division

I just have a couple of follow-ups on sales in Japan. I guess, first, could you talk a little bit about the product cycle in Japan and if that's shortening at all? And I guess, I was surprised a little bit by the sharp sequential drop-off in medical sales, as I would've thought that this product, in many ways, is opening a new market for you. So it might have had a little bit of a longer sales cycle. And then, secondly, just on Japan Post, do you get any sense that agents may be waiting to push the cancer product until the Post-exclusive product is rolled out later in the year?

Daniel P. Amos
Chairman & CEO

I can answer these, but I'm going to let Japan answer, whoever wants to.

Tohru Tonoike
Vice Chairman of Aflac Japan

Yes. I'll talk -- about the medical products -- you asked. If the product cycle is shortening in Japan and -- yes, that might be true to some extent, but we don't see the big difference in the period which the new product continues to be successful. Although I think we are still in that -- within the period, in which the sales is still good. So like I said, we see some decline in that -- from the fourth quarter last year to the first quarter this year. But still, close to 20% of growth is a good number and we've been maintaining that growth rate as long as possible. The competition is very hard. That is true. But I think we are very competitive in that, and we will be able to maintain our share in that. And also, the Japan Post, it is true that Japan Post wants to see the special products for them, but that doesn't hold them back from selling that -- the existing products now. They know, as I told you before, that from the April 1, the sale of the cancer product is included in their annual business plan. So they have a good reason to, say, make efforts to sell the cancer plan today. So if we can offer them the new products specific to them, that would be nice. But even now, they are working very hard to expand their cancer business within their network.

Paul Shelby Amos
Former Director

Yes. And one thing -- this is Paul. One thing I'd like to chime in and say, we're spending a good bit of time and resources on helping Japan Post get up to speed. You'll remember back when we did the bank channel years ago, it took us extended effort and that was for a smaller rollout in terms of total number of branches in the initial rollout. Here, we're rolling out a massive number of larger offices in a short period of time. In fact, as of April 1, we've shifted 52 people over to work full time on helping the Post offices get up to speed. Now we know that's going to be a gradual ramp-up, but we're continuing to stay in front of each of the Post offices and their sales staff to make sure it's the most effective possible. In terms of product development, the reality is that we continue to keep our product development cycle moving as fast as possible. As you think about -- we've launched our medical plan last year. We plan to launch another third sector plan this year, if at all possible, and we continue to negotiate with the government and other people to make sure that happens, potentially, in the latter half of this year.

Erik James Bass
Citigroup Inc, Research Division

Great. And if I could just ask one quick one on the investment portfolio. Just what are you targeting now as a percentage of Japan cash flows to invest in U.S. dollar securities for 2014? And then, should we still assume that that's primarily corporates at this point? Or are you expecting a broadened asset classes over the course of the year?

Daniel P. Amos
Chairman & CEO

Before Eric answer that -- and this is Dan, and I want to make one other comment. What -- with products changing so fast, which they are faster, that's the reason we need these additional funds for the computer updates because things are changing new bells and whistles on products, new ways of doing things. So I just want to reiterate, as you talk about these changing products and moving faster, that's one reason the expenses have gone up in our IT systems to be able to do that. So now, Eric, sorry.

Eric M. Kirsch
Global Chief Investment Officer and Executive VP

Thank you, Dan. No problem. Relative to 2014, looking at the entire year and primarily focused on the Japan portfolio, we would expect, as a percent of all Japan cash flows, the U.S. dollar allocation to be in the 35% to 40% range. It could go higher depending on market conditions and our tactical decisions, but we would expect that and the remainder to be in JGBs. Relative to new asset classes, we are ramping up those efforts. That's always been part of our plan. I would acknowledge, because of the volatility last year, particularly with interest rates, we focused most of our resources and attention there. So the concept of the outsourcing and new asset classes did get slowed down, but we're ramping up those efforts again this year. Having said that, it takes months of research of different asset classes, the ones that fit our risk appetite. It takes working with our partners in accounting and finance to get prepared for that. So in terms of actual implementation and new assets, something could happen. But it would be more likely to be towards the end of the year. But I would certainly expect, in '15, you'll hear more about that with respect to new asset classes. And finally, on the U.S. dollar allocation -- and I think last quarter, we talked about this. And certainly at FAB, I'll talk about this. No, it's not going to be all in corporate securities. We broadened out our investment capability, and we're thinking more tactically around markets. So when we think of the U.S. allocation, corporates, fundamentally, are very sound, as you all, I think, would appreciate and agree from a credit standpoint. However, from a spread standpoint, technically speaking, they're at all-time lows. They continue to get tighter because demand in the market for yielding assets is very, very high. But because of that, we're actually using a mix of U.S. Treasury securities and corporates in our U.S. dollar allocation with the thought being we'd rather leave some dry powder for a later day. Now we're going to meet our NII budgets, which we have an eye on as well. But within that, we're going to use our discretion in terms of where markets are, spreads are, yield levels are to make tactical decisions within the asset class of U.S. dollars or, frankly, between U.S. dollars and JGBs as well. So that will develop throughout the year. By then, I'll give you a good roadmap of our expectations, absent any big volatility in the market that could change that.

Operator

Our next question comes from Steven Schwartz, Raymond James.

Steven David Schwartz
Raymond James & Associates, Inc., Research Division

Looking at U.S. sales, some follow-ups. Dan, can you pinpoint maybe what territories or what areas of the country that you found to be most disappointing when looking at the sales in the quarter?

Daniel P. Amos
Chairman & CEO

I was trying -- I'm sitting here trying to -- in my mind, break it down. I think 4 are up and 4 are down. I know the Southeast is down, and I know that the North is up, the way we do it. I can't remember any of the specifics, but I do know those 2 particular ones. I know the Pacific, the number of recruits is way up, and we're expecting that to continue. We've had a couple of management changes. So that impacts us, too. But I'm trying to think of anything else. But it's more of just -- I look at more of the states than I do the territory itself in what's going on from that perspective. And the place we've got to see growth has got to be California and New York, Florida, Texas. The same states you think of in terms of winning a presidential election, it's the big state with the population. It's not going to be the Georgia. I mean, our highest penetration in population is South Dakota. They're not going to carry us over. They're a great state, and they're good example, thereby, to look to. And they -- that area of the country is doing very well. So I can mention them when I think about it. But it's got to be these metropolitan areas that have got to pull us for future growth. So I'll give you more detail about it at the Analyst Meeting. I'll break that out, get it broken out for you where you'll know more. But I apologize, I don't know more than that.

Steven David Schwartz
Raymond James & Associates, Inc., Research Division

That's okay. Just I know you don't want to lay blame anywhere, but you got to wonder about the -- I got to wonder about the weather. Also, on the number of agents, so one thing I noticed, maybe you can talk about this -- and I realized licensed sales agents isn't a key parameter, but it -- they did fall dramatically despite the increase in recruiting. And I'm wondering if there was a change there, if there was a culling or anything like that going on.

Kenneth S. Janke
Former Executive Vice President and Head of Corporate Finance & Development

Steven, this is Ken. We did have a culling. We periodically do purge our agent records for non-producers. We also had some that fail to take required training, and those are naturally purged as well. So it was kind of a -- it was a cleanup, if you will, of the ranks. And we don't do it annually. We do it periodically. And because of that, it does get noticeable.

Operator

Our next question comes from Mark Finkelstein, Evercore.

A. Mark Finkelstein
Evercore ISI, Research Division

Kriss, if you said it, I missed it, I apologize. But what is the ratio of repatriation to expect at year end FSA earnings with JPY 127 billion of repatriation?

Kriss Cloninger
President & Director

We had a gain on the reinsurance transaction during the FSA fiscal year ending March 31, 2014 that will be included in FSA earnings. The repatriation of JPY 127 billion, let's see, it's probably going to end up being around 80% again, including the reinsurance gain. But it will be close to 100%, excluding the reinsurance gain. Again, I want to reiterate that I'm more focused on SMR than FSA earnings. But those are the order of magnitudes of the repatriation relative to earnings.

A. Mark Finkelstein
Evercore ISI, Research Division

I guess, the question then becomes -- and maybe this is early and you'll talk about it more in a few weeks. But I mean, are we hitting upon a new normal or a higher kind of standardized level for repatriation that we should be thinking about?

Kriss Cloninger
President & Director

Well, I hope so. It's my intent to continue to decrease the difference between the FSA reported earnings and, say, U.S. statutory earnings, where U.S. statutory earnings are increasing at a more rapid pace than FSA earnings. I'll talk some on the road about the difference between FSA and Stab reserves and how the more conservative assumptions and the like underlying the FSA reserves and the fact that we have to post full strength. And that level of reserves, on an FSA basis, drags down our FSA earnings in the year. We write a lot of new business, and statutory gives us a little bit of break through an actuarial technique called preliminary term. We've just seen significant increases in FSA reserves over Stab reserves, and I think the Stab reserves were satisfied that those are adequate from an economic point of view and probably more than adequate from an economic point of view. So I'm working toward reducing the difference between Stab and FSA reserves, which improves -- will improve our ability to repatriate.

A. Mark Finkelstein
Evercore ISI, Research Division

Okay. And then, just finally, any additional updates or progress on, I guess, release -- reducing that statutory strain potentially through internal or external reinsurance agreements?

Kriss Cloninger
President & Director

Well, we'll probably have reinsurance as a significant tool to help us reduce the change in the difference between FSA and Stab. I'm going to give you some additional information on -- at FAB about that, what the progressions are. But roughly, the projected increase would be about JPY 60 billion next year in the difference and I think I can use some techniques to manage that difference down and to allow more of that to flow to FSA earnings. But again, I'm focused on the SMR more than earnings, but I am trying to manage our ability to repatriate up by creating a stronger and a more stable solvency margin, one that's less subject to volatility. And I think the reinsurance agreement we did this year, the other actions we took to minimize volatility in SMR, give you an indicator as to why we were comfortable increasing repatriation this year. And that is one of our management objectives.

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

I think we're coming close to the top of the hour, so we have time for one more question.

Operator

Our next question comes from the Suneet Kamath, UBS.

Suneet Laxman L. Kamath
UBS Investment Bank, Research Division

I just wanted to go back to one of the responses to a previous question. Dan, I think, in describing the U.S. sales force and all the dynamics, you made a comment, I'll try to paraphrase it, something like it would be easier to grow in the 50 and over market without the field force. And I didn't quite understand what you meant by that. Can you just describe that in a little bit more detail?

Daniel P. Amos
Chairman & CEO

Sure, I'd be glad to. What I'm saying is, is that our field force is key to our business. And as we deal with larger accounts, brokers don't like to necessarily deal with our field force. But our field force is what built our company, and we have to keep them. So there's conflict between brokers and field force. So I'm trying to constantly keep the field force writing the accounts of 100 or less, especially new people that are getting in the business. And I'll give you this example, it's kind of corny, but it's a true story -- I mean, a true example. If I said to you I'm going to take you fishing, and I'm going to take you and you can fish in this lake and you will catch all the fish you want, but none of them will be bigger than a pound. But you'll leave with all you want, or I'll take you over here and you can fish in this lake and you can catch a few, but there's a 10 pounder in there." Almost everybody wants to go to the lake and try to catch the 10-pounder. That's true with the sales force. You hire a new person. They all want to go land the big account. But the fact is, they'll make a living and they'll be able to eat and do what they need to do while writing the 1-pounders or the small accounts. And trying to create that wedge creates conflict in trying to keep them to do that. Because most of the time, our associates are going to do great with the 50 or less or 100 or less. But they're not going to land the big ones. But brokers tend to land the bigger ones. So there's a disruption before we just say go out and call on anything you want, do whatever you want to do. And now, we try to move them to the younger through -- I mean, smaller accounts through compensation. So that's what I'm talking about.

Suneet Laxman L. Kamath
UBS Investment Bank, Research Division

Got it. Okay. And then, my follow-up is just -- if I think back to the history of AFLAC U.S., when you've had these sort of issues in terms of managing the field force, my recollection is it always seems to take a little bit longer to correct than maybe some of us think. Do you think that is potentially the case this time, or do you think that you could really get on top of this and really get to that 0% to 5% for this year?

Daniel P. Amos
Chairman & CEO

Well, I wouldn't say it if I didn't think it. I think it's going to be tough, but I've always found a way to win, and my age makes no difference. I'd say I'm working harder. And actually, I'm enjoying it. There's -- a lot of the strategies we're putting in place or doing were carryover for things that have been going on in the past. It's just the changing environment. It's not that our strategies were wrong, it's just things are changing. So I still believe in it or I'd tell you. I mean, that's why I said that second quarter is going to be down slightly. So I'll give you more insight into that at the FAB Meeting. But again, I believe with change comes opportunity. And I wouldn't swap our U.S. market and our potential for anybody else out there. I mean, I don't want to be in the life insurance. I don't want to be in the property casualty. I still think our markets got the biggest potential, and I think we're in the right place. And the final thing I'll say as we're ending this call is we have a written trashy [ph] business either. The one thing that's the undercurrent of everything we're doing right now is, look at the margins, look at the business we're writing, we're making sure that what we put on the books is good business. And you don't have to come back 3 years from now and say, "Yes, you wrote all those sales increases, but they didn't end up being profitable." And we're not doing that. So we're being cautious in making sure, as we take on new markets and new things, that we ultimately protect the shareholders and make sure we give a good value to the policyholders.

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

Thank you, everybody, for joining us. If you have further questions [Audio Gap], and we have to all -- to see you all at our Analyst Meeting on May 22. Thanks so much. Bye-bye.

Operator
This concludes today's conference call. Thank you for participating. You may disconnect at this time.