S&P Global
Market Intelligence

Manulife Financial Corporation TSX:MFC

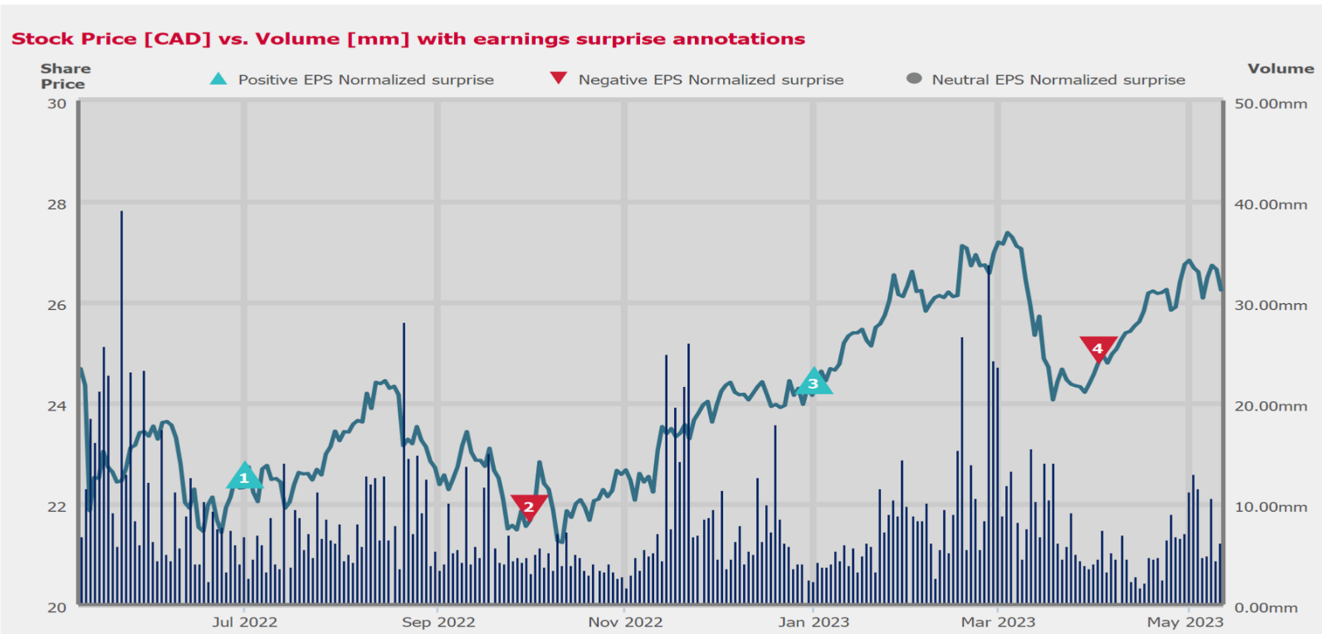
FQ1 2023 Earnings Call Transcripts

Thursday, May 11, 2023 12:00 PM GMT

S&P Global Market Intelligence Estimates

	-FQ1 2023-			-FQ2 2023-	-FY 2023-	-FY 2024-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	0.80	0.79	(1.25 %)	0.81	3.28	NA
Revenue (mm)	NA	NA	NA	NA	52626.13	NA

Currency: CAD
Consensus as of May-11-2023 2:32 PM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ2 2022	0.76	0.78	1 2.63 %
FQ3 2022	0.71	0.67	2 (5.63 %)
FQ4 2022	0.81	0.88	3 8.64 %
FQ1 2023	0.80	0.79	4 (1.25 %)

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Call Participants

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Presentation

Operator

Please be advised that this conference call is being recorded. Good morning, and welcome to the Manulife Financial First Quarter 2023 Financial Results Conference Call. Your host for today will be Mr. Hung Ko. Please go ahead, sir.

Hung Ko
Vice President of Group Investor Relations

Thank you. Welcome to Manulife's earnings conference call to discuss our 2022 comparative results under IFRS 17 and IFRS 9 as well as our first quarter 2023 financial and operating results. As this marks the first quarter of reporting under the new accounting standards, we are extended the call to 2 hours. Our earnings materials, including the webcast slides for today's call and IFRS 17 related reference materials, are available on the Investor Relations section of our website at manulife.com. We will begin today's presentation with an overview of our 2022 compared results under IFRS 17 and 9 by Roy Gori, our President and Chief Executive Officer.

This will be followed by Phil Witherington, our Chief Financial Officer, who will discuss our 2022 restated results, including the new DOE analysis, CSM movement analysis and our updated sensitivity disclosure. Please note that we are providing the 2022 comparative results for users to better understand and interpret our results under IFRS 17 and 9. This presentation will mainly focus on full year 2022 results, not period-over-period variance or comparing the results between the 2 accounting basis.

Following our 2022 comparative presentation, we will turn our attention to the first quarter of 2023, and Roy will provide an overview of our results and a strategic update. Phil will then discuss the company's financial and operating results in the first quarter under the new accounting regime. After the 2 steps of prepared remarks, we will move to the live Q&A portion of the call. We ask each participant to adhere to a limit of 2 questions, including follow-up questions. If you have extra questions, please requeue and we will do our best to respond to everyone.

Before we start, please refer to the slide containing the caution on forward-looking statements and non-GAAP and other financial measures within each of the respective presentations. Note that certain material factors or assumptions are applied in making forward-looking statements, and actual results may differ materially from what was -- what is stated. I also encourage you to take note of factors mentioned in our notes to reader slide, when interpreting our 2022 restated and 2023 financial results.

With that, I'd like to turn the call over to Roy Gori, our President and Chief Executive Officer. Roy?

Roy Gori
President, CEO & Director

Thanks, Hung, and thank you, everyone, for joining us today. Let me share with you a few highlights of our 2022 results under IFRS 17 before passing it to Phil to walk you through the details. While IFRS 17 does not impact the fundamental economics of our business or financial strength, the new accounting standards are expected to improve the stability of our financial metrics.

I'm pleased to confirm that our IFRS 17 transition impacts are consistent with the guidance we previously provided. On a restated basis, under IFRS 17, we delivered solid core earnings in 2022 and stable growth in adjusted book value, which incorporates the strength of our CSM. Our strategic priorities remain unchanged, and we're well positioned to achieve our medium-term financial and operating targets under the new accounting regime.

Turning to Slide 7. We delivered solid core earnings of $5.8 billion despite the claims experienced losses in our U.S. Life business due to COVID-19 and charges in our property and casualty reinsurance business due to Hurricane Ian. After adjusting for hedge accounting and ECL principles, we reported $3.5 billion of net income attributed to shareholders on a transitional basis for the full year. We believe our net income could have reached up to $4.7 billion in 2022 had we managed our investment activities aligned to the new accounting standards throughout the year. Phil will elaborate further on this in a few moments.

We delivered new business CSM of $1.9 billion in 2022, reflecting the profitable growth of our insurance businesses globally. We generated $1.3 billion of organic CSM and the total CSM balance ended at $17.3 billion on a pretax basis. Our adjusted book value per share grew by approximately 6% compared with the IFRS 17 opening balance and reached $29.42 at year-end 2022.

The new adjusted book value metrics incorporates the after-tax CSM balance into book value and reflects CSM's intrinsic connection to the value of our insurance businesses. And our capital remains strong with a LICAT ratio of 136% under IFRS 17, an increase of 5 percentage points relative to IFRS 4, reflecting a more stable capital ratio relative to interest rate movements under the new accounting regime.

On a comparative basis, the IFRS 17 transition impacts on our core earnings and balance sheet metrics as of January 1, 2023, were consistent with our previous guidance. I am incredibly proud of all of our colleagues who worked tirelessly to deliver a smooth transition.

Thank you. And I'll hand it over to Phil Witherington to provide an overview of our 2022 comparative results. Phil?

Philip James Witherington
Chief Financial Officer

Thanks, Roy. I'll start on Slide 10, which provides a snapshot of our key performance indicators for 2022 under IFRS 17 and IFRS 9. I'll focus on the metrics that are new or impacted by the new accounting standards throughout this presentation.

Turning to Slide 11. Throughout 2022, we delivered solid core earnings and stable growth in adjusted book value per share despite a challenging market and operating environment. This is consistent with our expectations as we believe the new accounting standards better align with the underlying economics of our insurance businesses.

Adjusted book value, in our opinion, reflects a company's overall financial position and is an important metric for valuation assessment. Our adjusted book value per share grew steadily over the past 5 quarters demonstrating the strength of our global franchise. Upon transition to IFRS 17, our LICAT ratio increased 5 percentage points to 136%, largely because the LICAT ratio under IFRS 4 was lowered by the impact of rising interest rates during 2022. We expect the LICAT ratio to be more stable and less sensitive to interest rate movements under IFRS 17 than the prior regime.

Turning to Slide 12. Under IFRS 17, our Asia segment continues to be the largest contributor to total company core earnings despite the deferral of new business gains into CSM. Asia segment and Global WAM combined contributed more than half of our 2022 core earnings. Similarly, Asia generated the largest portion of our new business CSM for 2022 and represented more than half of the year-end with CSM balance.

In 2022, our CSM was amortized into core earnings at a rate of approximately 10%. The CSM is amortized into core earnings over time, growing CSM from the generation of profitable new business will support continued in-force earnings growth.

Slide 13 shows our drivers of earnings or DOE analysis, which replaces the SOE as 1 of the key tools we used to explain our results. I will focus on the core DOE view on this slide to demonstrate the elements within core earnings. The core net insurance service result of $2.9 billion represents earnings associated with providing insurance services to policyholders. Risk adjustment release contributed $1.1 billion to core earnings in 2022. We expect this amount to be stable and grow over time as we grow the business. CSM recognized for service provided or what we often refer to as CSM amortization contributed $1.8 billion to core earnings.

The sum of risk adjustment release, CSM amortization and expected earnings on short-term insurance business such as Canadian Group Benefits, represent the expected earnings on our insurance contracts, along with expected investment earnings in the net investment result. These results are expected to remain relatively stable with steady growth over the medium term as we continue to grow our insurance businesses.

The $208 million charge from the impact of new business was related to onerous contracts. It's not expected to vary significantly over time, but it could potentially be reduced through pricing actions. It's important to note that onerous does not mean that a contract is unprofitable, since it will still contribute to risk adjustment release over time and generate investment returns.

The insurance experience losses recognized in core earnings reflected the current period impact of the elevated mortality in 2022 due to the Omicron wave of the pandemic as well as the impact of Hurricane Ian on our property and casualty reinsurance business in the third quarter. It represents the difference between actual experience and expected claims experience. I will explain the full picture of insurance experience recognition under IFRS 17 in a few minutes.

We delivered a core net investment result of $3.1 billion in 2022, including $2.2 billion in expected investment earnings and $0.9 billion in expected earnings on surplus. These results reflect the book yield on our fixed income assets and expected returns on older and public equity, partially offset by the book yield on our insurance contract liabilities. Of note, the expected earnings on surplus do not reflect returns on seed capital investments as they were reclassified to Global WAM as part of the segment reporting changes.

In addition, the public equity portfolio related to surplus was reclassified as fair value through profit and loss as of December 31, 2022. A modest credit experience loss of $34 million represented the change in expected credit loss or ECL. Our result reflects the quality of our fixed income portfolio amid a challenging global macroeconomic environment in 2022.

Global WAM core earnings reflect minimal impact from the adoption of IFRS 17 with the only notable change being to update the capitalization and amortization of acquisition costs in the retirement business to reflect the directly related criterion of IFRS 9. Global WAM results were also restated to incorporate the segment reporting changes I mentioned earlier. Manulife Bank results were also largely unchanged under IFRS 17 and will continue to be reported on a stand-alone basis.

Other core earnings mainly reflect debt financing costs and nonattributed expenses. Total core earnings of $5.8 billion in 2022 were approximately 6% lower than under IFRS 4 within the guidance we provided previously, a high-level comparison of the differences is included in the appendix.

Turning to Slide 14. For the 2022 comparative results, we introduced the transitional net income metric that reflects the impact of hedge accounting and ECL principles as if the standards had allowed such principles to be implemented for 2022. This improves the comparability of our 2022 results to 2023 and beyond. The market experienced losses in 2022 were primarily driven by lower-than-expected returns on public equity, net realized losses on fixed income investments and foreign exchange-related impacts, partially offset by net gains from hedge ineffectiveness and derivatives that were not in hedging relationships.

Note that there are offsetting movements in other comprehensive income, or OCI, in relation to the realized gains or losses on fixed income investments and hedging effectiveness resulting in a largely neutral impact on shareholders' equity from these components.

We expect the magnitude of market experience impact to reduce going forward. First, the net realized gains and losses on fixed income assets in 2022 reflected the impact of our investment management approach under IFRS 4. We took actions in early 2023 to better align our investment activities to the new accounting standards, which are expected to lead to smaller realized gains or losses going forward.

Second, by applying IFRS 9 hedge accounting, a portion of the interest rate impact on our insurance liabilities is reflected in net income, largely offsetting the mark-to-market impact on our derivatives used for economic hedging. Some level of hedge ineffectiveness is expected, but it should reduce over time as we continue to refine our hedge accounting programs.

And finally, a large component of the other investment results reflects foreign exchange impacts. This is in part driven by the delinking of the assets and liability discount rates as part of IFRS 17 and IFRS 9 transition. Actions were taken in early 2023 to reduce the related foreign exchange accounting variability going forward. The changes in actuarial methods and assumptions reflect the same insurance experience study updates as under IFRS 4. I will provide additional details in a few minutes.

Turning to Slide 15. Reflecting the actions taken in the first quarter of 2023, this chart illustrates the potential impact to net income as we aligned our investment activities to the new accounting standards. These actions do not change the fundamental economics of our business. In addition, we plan to make further refinements to our investment activities to better reflect the application of IFRS 17 and IFRS 9. We expect net income will become more stable over time.

As Hung mentioned at the beginning, we have presented our comparative 2022 results as of the accounting standards that allowed hedge accounting and ECL principles to be implemented for 2022 and these results are reflected under the transitional column. The application of hedge accounting and ECL principles had a largely neutral impact on total comprehensive income and shareholders' equity, while the transitional net income is more representative of 2023 and beyond.

Turning to Slide 17. The movements in OCI on insurance contract liabilities and invested assets reflect the impact of interest rates and credit spreads, realized gains or losses from the sale of fair value through OCI fixed income assets, changes in certain insurance contract liabilities due to public equity performance and offsetting changes from ECL recognized in transitional net income.

As I mentioned earlier, these ECL-related items and realized gains or losses from fair value through OCI assets result in a neutral impact on shareholders' equity. The net impact of these movements on insurance contract liabilities and invested assets was relatively small as evidenced in our 2022 comparative results. We expect OCI will be less sensitive to risk-free rate movements under IFRS 17 as it better reflects the underlying economics, and you can see this from our restated interest rate sensitivities shown in a later slide.

The unrealized foreign exchange gains or losses of net foreign operations is equivalent to the cumulative currency translation adjustment or CTA that we reported under IFRS 4 of approximately $1.9 billion in 2022.

Slide 18 shows our CSM movement analysis, which is the key tool for understanding an insurance business' growth potential and future earnings capacity. We generated organic CSM growth of 7% in 2022, driven by resilient new business CSM results despite a challenging operating environment, interest accretion on the CSM and insurance experience gains, partially offset by $2 billion of CSM amortization, of which $1.8 billion was released into core earnings, while $200 million was related to participating policyholders and noncontrolling interests.

Excluding the U.S. variable annuity business that was reinsured in the first quarter of 2022, our total CSM balance decreased by 2% on a constant exchange rate basis for the year reflecting the impact of adverse public equity performance on our variable fee approach or VFA contracts.

Impacts from market experience and other items will vary from period to period. We believe organic CSM growth and the long-term trends in total CSM are more indicative of our underlying growth potential. The changes in actuarial methods and assumptions that impact the CSM will ultimately flow through core earnings as CSM amortizes into core earnings over time.

Slide 19 covers insurance experience in more depth. Under IFRS 17, insurance experience is reflected in both core earnings and CSM depending on the nature of the item. The portion recognized in core earnings is driven by claims experience variances between actual amounts paid in the current period and the expected claims. The portion recognized in CSM represents experienced variances that relate to future period impacts, including the lapse experience and changes in reserves caused by current period experience for contracts that have a CSM.

The elevated mortality experience from COVID-19 impacted our core earnings in CSM differently in 2022, particularly in our U.S. segment results. During the first quarter of 2022, this elevated mortality led to an adverse claims loss in our U.S. Life Insurance business, which was reflected in core earnings. It was partially offset by a corresponding reserve release, which impacted the CSM.

In addition, our U.S. long-term care business reported insurance experience gains in the CSM due to elevated mortality. 2022 results are not indicative of future experience given the impact of the pandemic. The combined impact on core earnings in CSM needs to be taken into consideration in order to understand the full picture. The benefit of our global diversified franchise is also reflected in these results.

Slide 20 shows the results of changes in actuarial methods and assumptions. The impact of assumption and methodology updates were largely the same as IFRS 4, except for those changes that no longer apply under IFRS 17. For example, under IFRS 4, updates to asset-related methods or assumptions would impact insurance contract liabilities. But under IFRS 17, these models are not used as discount rates are de-linked from asset returns.

In addition, different discount rates were applied in determining the present value of assumption and methodology updates under IFRS 17 since discount rates are now based on the characteristics of liabilities. The impacts are recognized in net income, OCI and CSM, specifically. Updates to future cash flows at locked-in discount rates are recognized in the CSM. The impact due to valuing the assumption changes under the current discount rates versus the locked-in discount rates is recognized in OCI and the impacts that are not absorbed by the CSM flow through net income, including instances, where the product group is onerous.

Slide 21 compares our interest rate-related sensitivities as of December 31, 2022, on both the old IFRS 4 and new IFRS 17 accounting basis. While our net income sensitivities are of similar magnitude, the OCI sensitivities to risk-free rates reduced significantly under the new accounting standards. Sensitivities for the new CSM metric are relatively modest.

Consistent with our previous disclosures, all the interest rate-related sensitivities assume a parallel shift in rates. Under IFRS 17, results can be different than the published sensitivities as exposures vary slightly across currencies and a long interest rate curves. In addition, our hedge accounting program could result in hedging effectiveness, which is recognized in net income. The impact on shareholders' equity is expected to be largely neutral due to the corresponding offsets in OCI.

Turning to Slide 22. Our public equity sensitivities on net income under IFRS 17 are comparable to those under IFRS 4. The sensitivities on OCI are driven by the changes in the present value of future fees on general measurement model insurance products, where policyholders invest in certain investment accounts.

These sensitivities on the CSM are related to VFA contracts. These amounts reflect any impacts that are not passed through to policyholders such as impacts on guarantees embedded in variable annuity or participating contracts or changes in shareholder profits on these contracts. In addition, changes in future annual return assumptions for public equities will not impact current period net income.

Turning to Slide 23. For [ALDA] sensitivities, the potential impact to net income from a 10% change in market value is largely comparable between IFRS 17 and IFRS 4. The sensitivities on OCI and CSM were modest as at year-end 2022. Notably, there will be no immediate impact to reserves, if we change our older return assumptions under IFRS 17 as it will flow through earnings over time, materially reducing potential net income volatility.

Turning to Slide 24. It's important to reiterate that the accounting changes do not impact the fundamental economics of our business or our financial strength, claims paying ability or dividend capacity. Our strategic priorities remain unchanged, and we're confident in achieving our 2025 targets.

Turning to Slide 25. Under IFRS 17, our core general expenses no longer include acquisition expenses. Acquisition expenses formed part of the new business CSM calculation and will be amortized through core earnings over time. An exception would be the acquisition expenses related to contracts measured using the premium allocation approach and onerous contracts. These contracts do not have any CSM and the acquisition expenses will flow directly to core earnings. As such, our core general expenses are lower under IFRS 17 and our restated 2022 expense efficiency ratio was 45.7%.

To provide a reference point closer to the expense efficiency ratio prior to the adoption of IFRS 17, we're temporarily introducing an additional efficiency ratio called the expenditure efficiency ratio for 2022 and 2023 only, which captures all expenditures including costs that are directly attributable to acquiring new business.

Our 2022 expenditure efficiency ratio was 52.8%, which includes all acquisition expenditures in the calculation. Given the change in accounting for acquisition expenses and the resulting decrease in expense efficiency ratio, we would explore potentially recalibrating our expense efficiency ratio target over time.

Slide 26 outlines our medium-term financial targets and compares our 2022 performance between the 2 accounting basis. The IFRS 17 metrics demonstrate reasonable consistency with our medium-term targets despite the challenging backdrop, highlighting both the resilience of our business and the appropriateness of the targets we have set.

In summary, IFRS 17 and IFRS 9 are expected to improve the stability of our core earnings, net income, book value and the LICAT ratio over the medium term. We're pleased with our 2022 restated results, which had solid core earnings, resilient new business CSM and stable growth in adjusted book value.

With that, we will now turn our attention to the first quarter of 2023. I'll hand back to Roy to kick that off. Roy?

Roy Gori
President, CEO & Director

Thanks, Phil. Yesterday, we announced our first quarter financial results, our first ever quarterly reporting under IFRS 17 and IFRS 9. We reported strong operating results against the challenging backdrop of market volatility, persistent inflation, continued recession concerns and stress in the banking sector.

Despite that, we delivered 11% growth in our core EPS to $0.79 per common share, reflecting strong core earnings of $1.5 billion and the impact of our share buyback program over the past year, which is supported by our strong capital position.

Our North American insurance businesses generated strong core earnings growth compared with the prior year quarter, and we're encouraged by the momentum building in Asia. Net income of $1.4 billion was in line with the prior year quarter. We also delivered core ROE of 14.8% this quarter, tracking well against our updated medium-term target of 15% plus. These strong results are a testament to the strength and global diversity of our franchise.

Turning to Slide 7. We delivered new business value of $509 million in the quarter. And in Global WAM, we generated net inflows of $4.4 billion, with positive contributions from all business lines and geographies. Our APE sales were $1.6 billion, supported by sales growth in Asia, which increased 5% from the prior year quarter, and we saw sales momentum building throughout the first quarter.

Of note, Hong Kong APE sales increased 26% from the prior year quarter, reflecting a return of demand from Mainland Chinese visitors, or MCV, following the border reopening between Hong Kong and Mainland China during the quarter. And our domestic Hong Kong business remained strong with a 21% increase in sales quarter-over-quarter.

Our sales in 2022 were resilient, though dampened in Asia as we continue to navigate the impact of COVID-19 in some markets. The rebound we delivered this quarter demonstrates the quality and diversity of our distribution platform and our ability to offer attractive products and solutions to customers as demand returns.

Turning to Slide 8. We continue to maintain a strong capital position, supported by a LICAT ratio of 138% and a leverage ratio of 26%. Our strong balance sheet gives us tremendous flexibility to navigate a challenging operating environment, while continuing to return capital to shareholders and invest in organic and inorganic growth opportunities.

We reported adjusted book value per share of $30.4, an increase of 9% from the prior year quarter. This 5-quarter trend in adjusted book value growth during a period with significant capital market movements and volatility illustrates the strength and stability of our book value under IFRS 17. It was also during a period when we returned significant capital to shareholders through dividends and share buybacks of $5.5 billion.

Turning to Slide 9. We are relentlessly focused on taking action to generate value for shareholders across all our businesses. In the first quarter, we continue to deploy capital and returned $1.1 billion of capital to shareholders through dividends and share buybacks. This adds to the $4.4 billion in 2022. And we remain active with share buybacks since receiving approval in February to repurchase up to 3% of our outstanding common shares.

In Asia, we are a top 3 Pan-Asian life insurer with strong digital capabilities. We are leveraging our Health and Wellness platform, ManulifeMOVE to drive incremental sales. We've seen strong adoption of our app with over 50% of in-force eligible customers activating the app, of which over 1/3 have made a subsequent insurance purchase.

In Global WAM, our diversified business by geography and business line, including our leading position as a global retirement solutions provider continue to deliver solid results amid a challenging market, generating strong net inflows of $4.4 billion, as I noted earlier. And our long-term investment performance remains solid with 65% of assets outperforming their peers or index over the past 5 years.

Our financial strength and stability are as important as ever as the macro backdrop remains uncertain. Our investment portfolio is high quality and well diversified. Of note, 96% of our bonds are investment grade and 71% are rated A or higher. Our long-term investment approach has served us well in the past, and we expect it to continue to do so. And our sensitivity to market movements has also greatly reduced, since the global financial crisis and will further reduce under IFRS 17.

Finally, we released our 2022 embedded value report yesterday. Our embedded value of $63.9 billion or $34.29 per common share grew $0.94 per share in 2022, supported by robust organic growth of 11.7%. We believe that embedded value continues to be an important valuation metric and should be considered alongside adjusted book value. I'm confident that as we execute on our strategy and prioritize actions that generate shareholder value, we will see this result in strong total shareholder return.

Thank you. And I'll hand it back to Phil, who will review the highlights of our first quarter financial results. Phil?

Philip James Witherington
Chief Financial Officer

Thanks, Roy. I'll start on Slide 11 that shows a snapshot of our financial KPIs for the first quarter of 2023. We've started the year with strong results, including core EPS growth of 11% and adjusted book value per share growth of 9%. Although total APE sales declined modestly from the first quarter of 2022, we've delivered 5% growth in Asia, reflecting sales momentum that built progressively through the first quarter.

I'll now highlight the key drivers of our first quarter performance. Slide 12 shows our drivers of earnings analysis for the first quarter of 2023 compared with the prior year quarter. Our core net insurance service result increased 10% driven by improved insurance experience and a reduction in onerous losses from new insurance business, partially offset by lower CSM recognized for service provided or CSM amortization.

The improved insurance experience largely reflects the nonrecurrence of excess mortality claims related to COVID-19 in our U.S. Life Insurance business and the decline in CSM recognized for service provided reflects slower amortization of CSM for certain variable fee approach or VFA contracts due to the impact of higher interest rates and the U.S. variable annuity reinsurance transactions in 2022.

The core net investment result increased 14% from the prior year quarter, driven by higher expected investment earnings, which reflects both portfolio growth and higher reinvestment yields. In addition, higher interest rates contributed to higher earnings on surplus assets. This was partially offset by an increase in the ECL provision, which I will elaborate on in a moment. The decrease in Global WAM core earnings reflects a decline in net fee income driven by lower average AUMA and higher general expenses.

Slide 13 shows our 5 quarter change in ECL trend. As I noted earlier, we expect the ECL to remain relatively stable in most market environments. This is illustrated throughout 2022, where the overall change in ECL was a modest $34 million pretax charge despite a backdrop of market volatility and significant equity market declines. Under IFRS 9, we measure ECLs using a 3-stage approach.

Stage 1 comprises all performing financial instruments that have not experienced a significant increase in credit risk since initial recognition. ECL for Stage 1 instruments represents the potential default over the next 12 months. The vast majority of our financial instruments subject to credit exposure are classified as Stage 1.

Stage 2 comprises all performing financial instruments that have experienced a significant increase in credit risk or have become 30 days in arrears on interest or principal payments. When an instrument has moved to stage 2, full lifetime ECLs are recognized based on a probability of default. Stage 3 comprises financial instruments identified as credit impaired. Similar to Stage 2, full lifetime ECLs are recognized though the probability of default is set at 100%. The majority of the $141 million pretax charge in the first quarter related to certain commercial mortgages, primarily in the U.S., moving into Stage 3.

The change in ECL related to other factors was modest in the first quarter. Our commercial mortgage portfolio is diversified and has performed well through previous economic cycles. In the first quarter, we moved certain loans to Stage 3 as part of our regular diligence and credit review process that takes into account property values, cash flows and other considerations.

With office real estate under some cyclical and secular pressures, there could be further declines in this asset class if conditions in the macro environments deteriorate further. However, since our credit provisions reflect current market dynamics, we would not expect future provisions of a similar magnitude to those we have seen in the first quarter, if current conditions continue to prevail.

Slide 14 shows our earnings reconciliation to net income attributed to shareholders for the first quarter. Net income improved by $81 million from the prior year quarter transitional net income, reflecting strong core earnings growth of 6%, partially offset by unfavorable market experience.

Market experience was a net charge of $65 million in the first quarter. This included a $364 million charge from lower-than-expected returns on alternative long-duration assets, largely related to real estate and private equity. We have decades of experience managing a diversified older portfolio. While performance can vary from quarter-to-quarter, since 2005, inclusive of our first quarter 2023 performance, our actual average annualized returns have been in line with our current expected return.

We also reported a $31 million net realized loss from the sale of fixed income assets, which are classified as fair value through OCI. This was partially offset by a $108 million gain from higher-than-expected returns on public equities, a $93 million gain from derivatives and hedging effectiveness and a $129 million gain from other market experience, including favorable foreign exchange impacts.

Slide 15 shows our earnings by segment and return on equity. Core earnings in our Global WAM business decreased by 20%, driven by the factors I noted earlier. Core earnings in Asia decreased by 1%, driven by slower amortization of CSM and less favorable claims experience. This was largely offset by higher expected investment income and lower nonattributable maintenance expenses. Core earnings in Canada increased by 6%, reflecting improved insurance experience, higher expected investment spreads and higher Manulife Bank earnings, partially offset by slower amortization of CSM.

Core earnings in the U.S. increased by 23%, reflecting improved insurance experience, increased expected investment earnings and lower onerous losses on new insurance business. This was partially offset by an increase in the ECL provision and lower CSM recognition related to the variable annuity reinsurance transactions in 2022 and slower amortization of CSM.

The core gain in Corporates and Other increased by $74 million compared with the prior year quarter, primarily driven by higher yields on fixed income investments and surplus, net of higher cost of debt financing, and we delivered core ROE of 14.8%, which is tracking well against our medium-term target of 15% plus.

Turning to Slide 16, which shows our APE sales, new business value generation and new business CSM. In the first quarter, we generated APE sales of $1.6 billion, down 3% from the prior year quarter as growth in Asia was offset by a decline in North America. In Asia, APE sales increased 5%, driven by higher sales in Hong Kong, reflecting a return of demand from MCV customers following the reopening of the border between Hong Kong and Mainland China.

In Canada, APE sales decreased 19%, driven by lower segregated fund sales, due to the impact of market volatility and variability in the large case group insurance market. APE sales in the U.S. decreased 22%, reflecting the adverse impact of higher short-term interest rates and equity market volatility on consumer sentiment.

In addition to new business CSM, which I will comment on in a moment, we believe that NBV continues to be a relevant metric for assessing the intrinsic value of new business in a given period. We reported new business value of $509 million in the first quarter, a decline of 5% from the prior year quarter.

In Asia, NBV decreased by 4% as the impact of higher sales was more than offset by less favorable product mix. In Canada, NBV decreased 12% due to lower segregated fund and group insurance sales, partially offset by higher margins in individual insurance and annuities. And NBV in the U.S. increased 6% as pricing actions and favorable product mix more than offset the decline in sales volumes.

New business CSM in the first quarter was $442 million, which declined 13% from the prior year quarter. In Asia, new business CSM decreased 9% due to similar factors that I referenced for NBV. In Canada, new business CSM decreased 25%, driven by lower segregated fund sales and less favorable product mix in individual insurance.

And in the U.S., new business CSM decreased by 20%, consistent with lower sales. Overall, our first quarter new business CSM performance was dampened by less favorable product mix in Asia and Canada and lower sales in North America. As the operating environment normalizes and our sales momentum continues to build, we expect to achieve our 15% medium-term growth target for new business CSM.

Slide 17 illustrates the changes in CSM balance. During the first quarter, the contribution from new insurance business and expected movements related to finance income or expenses also referred to as interest accretion exceeded the CSM recognized for service provided also referred to as CSM amortization.

Insurance experience reported through the CSM was a modest charge of $30 million driven by unfavorable lapse experience in Asia, partially offset by favorable experience in Canada. Insurance experience in the U.S. was neutral. Overall, we generated organic CSM growth of 1% or 4% on an annualized basis during the first quarter. And the impact of new insurance business grew 3% compared with the fourth quarter of 2022. Inorganic movement in the CSM was a modest $57 million increase. Compared with the 2022 year-end balance, our total CSM balance increased 1%.

Turning to Slide 18. Our Global WAM business recorded net inflows of $4.4 billion with positive contributions from all business lines and geographies in the first quarter. In retail, net inflows were $0.8 billion compared with net inflows of $4 billion in the prior year quarter. The decrease reflected lower investor demand and continued market volatility and higher interest rates.

In Retirement, net inflows were $1.2 billion compared with net inflows of $2 billion in the prior year quarter, primarily driven by higher planned redemptions and lower new pension plan sales partially offset by higher member contributions and lower member withdrawals.

Institutional Asset Management business recorded net inflows of $2.5 billion compared with net inflows of $0.9 billion in the prior year quarter driven by new product launches in Mainland China, totaling $1.6 billion. Our core EBITDA margin decreased to 22.4% in the quarter, reflecting the factors I noted earlier on core earnings as well as the modest impact from the acquisition of full ownership in Manulife Fund Management in Mainland China as its general expenses are now consolidated.

Overall, Global WAM's average AUMA decreased by 7% compared with the prior year quarter, driven by the unfavorable impact of markets in 2022. Net fee income yield of 44.6% improved from the prior year quarter, reflecting higher fee spread on deposit products.

Turning to Slide 19. We continue to maintain a strong balance sheet and capital position, which supported our continued active capital deployment. During the quarter, we repurchased 0.8% of our outstanding common shares for $400 million.

At the end of the quarter, we had $23 billion of capital above the supervisory target and our LICAT ratio of 138% remains strong. The 2 percentage point increase from our LICAT ratio as of January 1 this year was primarily driven by the issuance of $1.2 billion of subordinated debt, partially offset by the impact of share buybacks.

Our financial leverage ratio increased by 0.9 percentage points from the prior quarter, driven by the subordinated debt issuance. In April, we announced our intention to redeem $600 million of subordinated debentures on May 9. The impact of these redemptions will be reflected in the LICAT and leverage ratios for the second quarter of this year. We've reflected the impact in the pro forma metrics on this slide, all else being equal.

Slide 20 shows the summary of our financial performance for the first quarter and our medium-term financial targets. We're pleased that our core EPS growth and core ROE were tracking well against our medium-term targets. While our CSM growth metrics were dampened by factors such as lower sales and market volatility, we view these as temporary headwinds and remain confident in our ability to deliver on both new business CSM and CSM balanced growth targets over the medium term.

This concludes our prepared remarks. Before we move to the Q&A session, I would like to thank you all for joining us for this milestone quarter, which we reported under IFRS 17 and IFRS 9 for the first time. As a reminder, we ask each participant to adhere to a limit of 2 questions, including follow-ups and to requeue, if they have additional questions.
Operator, we will now open the call to questions.

Question and Answer

Operator

[Operator Instructions] Our first question is from Gabriel Dechaine from National Bank Financial.

Gabriel Dechaine
National Bank Financial, Inc., Research Division

A couple of things. Phil, can you just repeat, I guess, the comments you made around sales and other drivers that would get your CSM growth back to -- on track to the 8% to 10% target?

Philip James Witherington
Chief Financial Officer

Yes, happy to. Thanks for the question, Gabe. This is Phil. So the guidance we've issued on new business CSM, 15% over the medium term. I will highlight what I highlighted a few moments ago, which is we've been operating in a really tough environment over the course, not really just the past 12 months, but the past couple of years. And so the contribution to the CSM through new business growth has been lower than what we would typically expect.

But I will highlight that when we look at new business CSM generation, each quarter, it's typically been around $450 million to $500 million and very stable. And then when we look at the first quarter of this year relative to the fourth quarter growing at 3%, so I think that's an encouraging sign that the corner has been turned on new business generation.

In terms of what gets us back to that 15% growth that we would expect over the medium term, it's really a reactivation of the normal level of sales growth in Asia will be the most important driver as well as, I think, improved customer sentiment, consumer sentiment in both the U.S. and Canada. And I think that consumer sentiment is a really important point in the first quarter and looking at the end of last year as well. It's been a very difficult operating environment.

Stepping back, looking at the CSM more broadly, it's really important to look at the organic CSM growth. And when you look at 2022, the organic CSM growth was 7%, which even in a tough environment, I find that encouraging.

Roy Gori
President, CEO & Director

Gabriel, just a couple of other thoughts I would add. I think Phil has covered it well. But we did deliver resilient new business CSM growth throughout 2022, $1.9 billion, in fact. And we're really encouraged that we're getting sales momentum back across all of our franchise.

In fact, our APE sales quarter-on-quarter grew 22% in Q1 versus Q4 and Asia grew 28% quarter-on-quarter. And throughout the first quarter, we saw consistent and stable increase in sales momentum, which came off the back of the restrictions being lifted. So yes, a tough environment as it relates to restrictions, but we're really actually quite encouraged with the momentum that we saw in Q1 and that's continued since Q1.

Gabriel Dechaine
National Bank Financial, Inc., Research Division

Okay. That's a fulsome answer. And then my next question is on the property portfolio and the commercial mortgage portfolio, twofold, I guess. We've had a couple of quarters now of marks on the property portfolio. Have you gone through the whole portfolio? And what kind of changes to cap rates have you done specifically on the office, which is the biggest chunk of that portfolio?

And then if I understand you correctly, this ECL provision on commercial mortgages, you're saying if market conditions stay the same, you don't expect much more of that. I mean, that seems like a pretty confident outlook there?

Scott Sears Hartz
Chief Investment Officer

Sure. Thanks, Gabriel, for the question. This is Scott. So starting with the real estate portfolio, Yes. We have external appraisers value that every quarter on over 95% of the portfolio. So we do feel like our marks are up to date. In the quarter, we did see, as Phil mentioned, a $360 million loss on all the meaning our returns were below expectations. About 2/3 of that did come through on real estate. And real estate, it's total return for the quarter was about minus 0.6%. So again, below the long-term expectation that resulted in that loss.

In the fourth quarter, we saw a larger loss. We saw a minus 5% return on the portfolio. So we have seen values come down in our North American office. Values are down about 25% from their peak. So we think we are reflecting current market conditions. But we do -- if headwinds continue, we will expect a little bit of a drag further on that.

I think it will be a challenge to meet our expected returns on our office real estate. I will say that office -- North American office, which is the most concern, the investment properties represent about 1/3 of our total real estate and that leads to about 1% of total assets.

On the ECL, moving over to the ECL, yes, we put up a decent provision on our commercial mortgage portfolio. That was all coming out of office, as you might expect. And we've been through that portfolio in some detail and try to -- again, have tried to reflect sort of current valuation. So again, on the office, we see values down about 25% from where we originally underwrite them. But that will vary a lot. And in certain really weak markets, certain parts of San Francisco and Chicago, we're seeing much larger drops in value. And so while we don't actually have any properties in arrears, these are all forward-looking assumptions, we do -- most -- a lot of that provision did come out of the Chicago area on a couple of properties.

But again, we think we've reflected sort of current valuations. So if markets sort of stabilize from here, I think we feel pretty good. We probably will have some more provisions, but not to that extent. But if markets continue to deteriorate, we should expect to see continued provisions.

Philip James Witherington
Chief Financial Officer

Thanks, Scott, and this is Phil. Could I just also supplement 1 point. Gabe, you were specifically talking about, where the current market conditions are reflected, and we're satisfied that current market conditions are reflected in our ECL provision. So unless there is a further material deterioration, we wouldn't expect charges of a similar magnitude to those we've seen in the first quarter.

By moving the properties that Scott referenced into Stage 3, we're assuming a 100% probability of default in a full lifetime ECL.

Gabriel Dechaine
National Bank Financial, Inc., Research Division

Those have actually defaulted, right? Or is it just an assumption you've made?

Philip James Witherington
Chief Financial Officer

They actually haven't defaulted. We're applying a level of conservative professional judgment when we've made that change.

Operator

The following question is from Meny Grauman from Scotiabank.

Meny Grauman
Scotiabank Global Banking and Markets, Research Division

Just a follow-up on the ECL in terms of some of the detail you provided, you talked about the properties generally being around the Chicago area. Is there anything unique about that property market that's different as you look across your portfolio? Just curious about that to storm?

Scott Sears Hartz
Chief Investment Officer

Sure, Meny. Thanks for the question. It's Scott again. Yes. I would say it's a bit unique. And it's not even -- in various cities, there are certain areas that are not doing well on certain areas that are in Chicago, they're actually are -- there's a vibrant area called the Fulton market area, where more in the central loop area. And while the buildings are good-looking Class A buildings, it's not been, where companies have wanted to lease.

And so we've seen in a couple of cities, and I did reference San Francisco and Chicago, in particular. And in San Francisco, we really don't have any loans to buildings in the areas we see particularly depressed. Whereas in Chicago, we do have a couple of buildings and that led to the bulk of the Stage 3 provision.

Meny Grauman
Scotiabank Global Banking and Markets, Research Division

Got it. And then I just wanted to ask about Asia. We saw sales improve and you provided some commentary. There's some mixed sort of reports that I'm reading in terms of people and other companies talking about a reopening bump in China, but it seems like there's some sense that maybe that is waning and the recovery is slowing in China.

I'm just curious, your thoughts about how the recovery progresses from here. Obviously, we saw the good sales results from the quarter. I'm wondering what you're seeing now that we're into the new quarter and just your overall outlook in terms of the pace of recovery there and in Hong Kong?

Damien Allen Green
Executive Director

Yes. Thanks, Meny, for the question. It's Damien here. So yes, happy to cover these off and give you a sense of how things are tracking currently as well. Firstly, for the first quarter, the constraining impact of the pandemic on our Asia segment began to turn around very sharply from late in the first quarter. And in particular, we were very encouraged by the return in excellent sales growth momentum in key markets from March.

You've seen what we've disclosed on Hong Kong, but overall, I think March has enabled us to deliver year-on-year growth number of 5% APE, which Roy mentioned, albeit with a modest decline in NBV. Now underlying the headline results that you see here in terms of core earnings, APE and NBV, we did see a resurgence in business momentum, not just in Hong Kong, but also in China.

We saw very robust double-digit growth in new business value in China and APE in China, along with a robust growth in Hong Kong led predominantly by our Mainland Chinese Visitor sales hitting all-time record high actually in line with our strategy. So China is more than a bump.

And what we're observing, I'm really pleased to see that this momentum is continuing in the second quarter in both China and Hong Kong, if not accelerating. Our Mainland Chinese Visitor sales in Hong Kong are currently over 2x our pre-pandemic average that trend is continuing, and we're seeing continued acceleration in terms of volume and value in China. Thanks, Meny.

Operator

The following question is from Tom MacKinnon from BMO Capital Markets.

Tom MacKinnon
BMO Capital Markets Equity Research

Two questions. First of all, I think as historically, you used to talk about when you did the valuation on your ALDA assets. Obviously, you can't go through every single property thoroughly every quarter that you may have done some thorough valuations for maybe 1/3 of the portfolio at a certain quarter. And then provided some blanket adjustments for the rest of it and then continue on that kind of cadence over the next couple of quarters.

Is that still the case? Doing a deep dive into evaluation on every 1 of these properties for each quarter, it sounds like a pretty arduous task. So maybe you could shed some color as to how you do those marks and I have a follow-up.

Scott Sears Hartz
Chief Investment Officer

Sure, Tom. Thanks for the question. No. On the commercial real estate portfolio, for quite a while now, we get quarterly external appraisals on virtually the entire portfolio. There are a few small buildings that we would do less frequently, but the coverage is over 95% of the portfolio.

So we do feel like we are up-to-date with current market conditions. I would say in our timber and agricultural portfolios, we do, do kind of a rolling appraisal throughout the year. And if we ever saw significant weakness, we will then accelerate that, but that is a part of the portfolio that acts more the way you would suggest that it's -- each quarter, we will revalue about 1/4 of the portfolio.

Tom MacKinnon

BMO Capital Markets Equity Research

And then what about private equity? What's the process there?

Scott Sears Hartz
Chief Investment Officer

Sure. So private equity, most of our private equity is held in private equity funds. So we're getting valuations from the general partners of those funds. And those are typically lagged about a quarter. So normally, in the first -- our first quarter results would reflect the fourth quarter returns on those and the year-end NAVs.

I would point out that the fourth quarter is the quarter that private equity firms typically get those results audited. They don't get audited every quarter, although they do appraise -- they do value them every quarter.

And because of that process, they're a little later in getting them to us. So we typically do see results being a little bit lower because about half of our private equity funds, we actually did not have fourth quarter results on. So we assumed a 0% return. We've made an estimate that if we actually had those valuations, results would have been $100 million higher or better for the quarter.

Tom MacKinnon
BMO Capital Markets Equity Research

Okay. And then a question for perhaps Phil. If we look at Slide 12 of the Q1 deck, my question is just with respect to -- that's the drivers of earnings there. And the ones that should be fairly consistent being the risk adjustment release, the CSM recognized and the expected earnings on short-term insurance business. If I look at the kind of -- some of those 3 were down year-over-year. We're -- and we're down actually year-over-year on that in Canada as well as the U.S., I get the U.S. might be a little bit variable annuity related, we're down year-over-year in Canada. In fact, Canada, that's the lowest of the last 5 quarters, and we're down year-over-year on that metric in Asia as well.

So if this is supposed to be the good steady Eddie in terms of net insurance service results on a core basis, why are these numbers not kind of trending up nicely? I mean, albeit we only have 5 quarters to look at here?

Philip James Witherington
Chief Financial Officer

Thanks, Tom. This is Phil. I'll make a start. I may hand over to Steve Finch to provide any thoughts as well. But just -- to start with, risk adjustment release and the impact of short-term insurance business, it's actually been very stable quarter-on-quarter. So -- and that's typically what we would expect to see for these businesses. And over the medium term, of course, we would expect them to grow as our portfolio grows.

The CSM amortization that you see coming through or so-called CSM amortized for service provided, that has gone down year-on-year, and that's really reflecting -- I suppose a couple of things. One is that the pace of amortization has slowed in a higher interest rate environment, but also the CSM balance has not actually grown as quickly as we would -- as much as we would typically expect it to have grown, and that's coming to my comments a little earlier on the new business CSM generation. It's been a really tough environment, operating environment. But we expect to get back to 15% growth in new business CSM, 8% to 10% growth in CSM balance over the medium term.

And then on experience gains and losses, that 1 is a favorable movement period-over-period. And as I referenced in the remarks earlier, that's really driven by the nonrecurrence of the U.S. life losses that we saw in the first quarter of last year, and that was related to the Omicron wave of the pandemic, for which there was an offset that shows up in the CSM movement, CSM experience, favorable CSM movement in the CSM balance.

Steve, did you have anything to supplement?

Steven Andrew Finch
Chief Actuary

Yes. Just 1 thing I'd highlight, in addition, Phil, is the slower CSM amortization that you referred to in your opening remarks, that is -- that's 1 place that interest rate impact. So higher interest rates have slowed the amortization on certain VFA contracts. However, we need to take a step back and look at the overall impact of interest rates, higher interest rates, which is benefiting the company through 2022 and in Q1, and that's coming through in terms of higher interest on surplus from higher yields.

And Phil, as referenced before, that's worth in 2022, about $170 million pretax. And then the CSM amortization slowdown, that's being offset in the segments, not equally by segment, but offsetting the segments, again, due to higher reinvestment yields. So that's being offset. And Q1 is a good base to look at going forward in terms of the CSM amortization. We would expect these line items to grow as the business grows. And the last thing I'll point out is, in Q1 '23, our CSM amortization on an annualized basis is 10%, consistent with the guidance that we've provided.

Operator

The following question is from Doug Young from Desjardins Capital Markets.

Doug Young
Desjardins Securities Inc., Research Division

Damien, hoping we can maybe drill down a little bit more on what you're seeing in some of the markets. And so maybe I'll take Hong Kong. I mean, sales absolutely picked up, but it sounds like it's more a lower-margin product through MCV. Are you starting to see a shift in mix back to more profitable products? And/Or do you see line of sight to have a better mix coming through over the next year?

And then maybe kind of winding that into the CSM, I mean how important is that, Phil in terms of improved mix to drive CSM growth and new business, CSM growth more in line with what your expectations are?

Damien Allen Green
Executive Director

Yes. Thanks, Doug. Let me jump in on part 1 there, and Phil can supplement on the second part of your question. So as I mentioned in the first quarter, overall, we saw some really positive developments in Hong Kong in terms of business momentum and business growth. And I think we'd referenced a strong double-digit APE growth year-on-year, quarter-on-quarter, driven by Mainland Chinese Visitor business.

Now what we saw in terms of new business value there was the result that you've pointed to with a slight reduction year-on-year in new business value was predominantly the result of channel and product mix associated with demand that emerged from Mainland Chinese Visitor customers for savings products, which was reported across the industry, and it's a major player that we experienced that too. You will see some adjustments to our portfolio mix and margins as we continue to execute on our strategy. So yes, you will see us continue to improve margin in Hong Kong.

What I would say, just in general terms, it's worth noting that the Mainland Chinese Visitors sales that we have generated almost purely incremental for us in Hong Kong, but not cannibalized other high-margin products. They do have robust margins, and they've clearly generated positive absolute NBV for us.

Thanks for the question, and I'll hand over to Phil.

Philip James Witherington
Chief Financial Officer

Great. Thanks, Damien. And Doug, thanks for the question or at least the second half of the question for me. What do we really need to drive that CSM balance higher? I don't think it's either more volume or improved mix or margin. I think it's a combination of both.

And we've seen a turn in the first quarter in volume momentum. And Damien referenced that, that really kicked in from March, which I think does indicate -- that does -- it's a good indicator for what might happen for the rest of the year, and it is certainly demonstrating the strong sequential performance as we look at month-by-month in Q1.

And that momentum is particularly strong in Hong Kong from -- and China and the Mainland Chinese Visitor components in Hong Kong as well as the domestic business is visible there. But it's worth recognizing as well that other markets within Asia continue to see, I would say, a bumpy emergence from the pandemic, and Vietnam is an example of that, that it continues to be a tough market, but we expect these to come back during the course of 2023. That will help with strong momentum that then helps with the CSM balance build that then feeds into CSM amortization into the income statement and supports core earnings growth.

Roy Gori
President, CEO & Director

Doug, just Roy here, just a couple of quick adds. We did see in Q1 annualized organic CSM growth of 4% as well as annualized total CSM growth of 4%, and that's despite some of the challenges on sales. And as we see that sales momentum pick up, not just in Asia but across all of our franchise, getting back to new business CSM growth at 15% and then total CSM balance growth of 8% to 10% is definitely still something we feel very confident about and certainly through our medium-term focus and targets, that's where we'd like to be, and we see ourselves.

Doug Young
Desjardins Securities Inc., Research Division

Maybe a follow-up, Roy? Is that something you feel confident about getting this year? Or is that a multiyear kind of evolution?

Roy Gori
President, CEO & Director

Yes. Well, the target, as you know, is a medium-term target. And obviously, in the short term, we could and would possibly see some headwinds or challenges. But again, for us, as we look to the rest of this year, we feel reasonably optimistic that we're going to get back on track. That's what I'd broadly leave you with.

Doug Young
Desjardins Securities Inc., Research Division

And then -- okay. Then, Steve, on the long-term care insurance, I saw that there was some favorable experience that flowed through the CSM. Can you kind of elaborate what that was? You didn't mention anything in the driver of earnings insurance experience around long-term care insurance. So I assume there's nothing in there. But I think there was favorable experience going through this [indiscernible] and long-term care insurance, but I think there was negative lapse experience on the U.S. Life product. Just trying to get a sense of the moving pieces there.

Steven Andrew Finch
Chief Actuary

Sure. Yes. Thanks. So what we're seeing in the U.S., I'll speak broadly, but it will get to those questions is, we are seeing higher levels of mortality rates. So consistent with population mortality trends, higher mortality rates. In our U.S. Life business, we reported a gain all-in from mortality. And I've talked in previous quarters about variability in large cases. It was favorable this quarter. .

However, we did see that elevated mortality result in gains in long-term care. So it came through in the long-term care line. That's going through the contractual service margin. We did also see lower -- and that was offsetting some of the trends that we've been seeing on the U.S. Life lapse losses. So the LTC and the life lapse losses were fully offsetting in the quarter. And then the last thing that we saw on LTC was continued lower incidence versus what we would typically expect in Q1. We typically see some seasonally higher incidents, but we did not see that in Q1 this year. So favorable quarter on LTC experience and favorable on U.S. life mortality.

Operator

Our following question is from Mario Mendonca from TD Securities.

Mario Mendonca
TD Securities Equity Research

So I appreciate your comments about the -- all the return assumptions being broadly in line since 2005. But I think investors generally wouldn't invest on 18-year averages. So maybe you could help me think through what kind of variability has there been in these older returns in any given year around -- relative to the expected? And maybe if you could help us think about that variability relative to expected in the context of the company's pretax earnings.

What I'm really trying to understand is does -- could this variability in any given year cause swings in pretax earnings of 15% or 20%? Understanding that over the very long term, it all sort of averages out. I'm sure you understand where I'm going with this. Can you help me think through that?

Scott Sears Hartz
Chief Investment Officer

Mario, maybe I'll start, and Phil can put it in context for our overall earnings. But you're right, all the -- it's most important to us, we're backing really long-term liability. So the long-term return is the most important thing to us, but we -- no one likes variability in the short run. And although in the short run, I would say, if you look over the last 3 years, right through the pandemic, we have achieved our long-term returns. So it's -- recently, we've achieved it. And in the long term, we've achieved it. But there will be variability quarter-to-quarter.

And in recessions, we're going to underperform. But in recessions, the fixed income book will underperform as well. We'll have ECL charges that will underperform. As we've looked at it, we do try to construct a portfolio that's as low vol as we can get. We do that in a couple of ways. One is within each category of our 6 ALDA categories, we do try to stay at the low end of the risk return spectrum, and we could give you many examples of that.

And the other thing is we have 6 different categories, and they're not all correlated. Agriculture in particular, is actually somewhat negatively correlated with the rest. So it all brings down the volatility. If you look at our history and the volatility of it, it's about 1/4 of the volatility of public equity portfolio, so about a 4% standard deviation. And if you look over that long history, there's only been 1 year, where we've actually had a slight negative return that was in the financial crisis. And then the following year, it rebounded and recovered all of those losses.

And maybe the final point I'd leave you with is, one of the things we like about the ALDA portfolio is we'll see variability largely just based on valuations. Like right now, we're seeing commercial real estate getting valued down because cap rates are rising. But that implies higher returns in the future. It's valuation changes. It's not real losses that are gone forever, like you would experience in a credit portfolio below investment-grade credit portfolio. When you take those specific provisions, they ultimately end up in realized losses.

With that, I might turn it to Phil, if you want to add anything?

Philip James Witherington
Chief Financial Officer

Sure. Thanks, Scott. And just add a couple of things. One is the transparency of our new disclosure here, because I think this helps put into context what we've actually seen in terms of all the variants to expected long-term assumptions over the 5-quarter period that we've released today or released yesterday evening. It's on the first numbers page of the SIP, and we've included this new disclosure so that in dollar terms, you can actually see the variance, not just in total for investment experience, but break it down by components of that investment experience, including older specifically.

And that -- so that the $364 million adverse variance to long-term assumptions that Scott referenced earlier, that's in Q1. And if we look at full year '22, it was really modest at negative $32 million. And I think the overall diversification of the portfolio is important there.

The second point that I'll mention is that we have continued to provide sensitivity disclosures, arithmetic sensitivity disclosures that show what the impact of a 10% shortfall in investment return would do to the ALDA portfolio. And that was included in the 2022 deck that I ran through earlier this morning, and it's included in our Q1 disclosures as well.

Mario Mendonca
TD Securities Equity Research

Okay. Let me add follow-up then with this. So all the -- to be perfectly represent how [indiscernible] insurance company operates for long-term value creation is sort of disconnected with the way investors look at companies generally. I appreciate that it makes a lot of sense for Manulife, it may not make a lot of sense from your investors though. So I'm going to ask the question in a slightly different way.

What are the expected returns that make it into your earnings for ALDA relative to the expected returns on all your other invested assets? I'm trying to understand how valuable ALDA is to your expected returns. And I'm trying to weigh that against this increased volatility.

Philip James Witherington
Chief Financial Officer

Yes, yes. Thanks, Mario. Thanks for the clarification of that. So ALDA if you look at ALDA expected returns as a proportion of our overall core investment returns, it's about 1/3. And when you look at investment returns as a component of our overall earnings, it's about half. So on that basis, ALDA would represent approximately 15% of our -- the core earnings in a typical year.

Mario Mendonca
TD Securities Equity Research

But could you talk about what your expected return is on the ALDA relative to your expected return on everything else?

Philip James Witherington
Chief Financial Officer

Yes. So the expected -- long-term expected return on ALDA is a weighted average between 9% and 9.5%. That's effectively the same as it was under IFRS 4. We haven't changed our expected long-term assumptions as we've made the transition to IFRS 17. I think that covers what you were guessing at there, Mario.

Roy Gori
President, CEO & Director

So, I'll just add a couple of comments as well. And Scott, you might want to chime in as well. And that is to say that ALDA is not something new for us. It's something that we've have clearly, a lot of experience in, and it's something we've been focused on for more than 20 years diversed portfolio, as Scott mentioned earlier. And the returns really have actually performed very, very well and certainly to our expected assumptions. So we see this as a competitive strength. We see many of our competitors looking to develop this capability. In fact, some of them are actually using us to manage their portfolios. And the long-term liability match is certainly something that we think is a source of value.

But Scott, you might want to chime in as well.

Scott Sears Hartz
Chief Investment Officer

Yes, Mario, to get at like where that sits relative to fixed income, if you look at sort of long rates around 3.5% and maybe investment grade 150 basis point spread, you're at 5% for investment grade. If you do below investment grade, you'll get above that, you still won't get to the ALDA returns.

When rates were really low, there was a bigger spread. I think with rates coming up, inflation coming up, frankly, it gives us more confidence that we absolutely will achieve those returns. The low inflation was a bit of a headwind for a real asset portfolio. So it does give a decent amount of incremental return. As Roy pointed out, we do see peers moving into this space. We still will stand out relative to peers in terms of having more. And again, importantly, I think while you will see more variability than a fixed income portfolio, in a bad cycle, like we saw in the GFC, we took a bunch of credit losses, and those don't come back, whereas the ALDA got valued down, but rebounded in subsequent years. And that's part of why we really like the category.

Mario Mendonca
TD Securities Equity Research

The bottom line, the 400 basis point extra spread in your mind is worth that added volatility and that's the message you'd want to offer to investors that don't like the ALDA. Is that right?

Scott Sears Hartz
Chief Investment Officer

It's -- that's a little oversimplification. I would suggest, I think there's a diversification element to the basic credit risk that underlies that 5% return that's also a reason to be in this space.

Operator

Our following question is from Nigel D'Souza from Veritas Investment Research.

Nigel R. D'Souza
Veritas Investment Research Corporation

I wanted to touch on earnings on surplus. I believe Phil mentioned the pretax annualized run rate of $170 million. But I think, he also mentioned that [indiscernible] top booking are now under global plan. And when I look at IFRS 4 versus IFRS 17, I assume that's driving the step down in earnings on surplus on a comparative basis. .

Just trying to get a sense of the run rate effect going forward. Your yields have come down a bit on long-term bonds in Q2. And I think you also mentioned there's a change from mark-to-market gains between OCI and fair value to P&L that shows up in earnings on surplus. Just wondering if you could expand on that?

Philip James Witherington
Chief Financial Officer

Yes, happy to do that. This is Phil, Nigel. So where I'll start is earnings on surplus. And your memory is largely correct. Last year, what we said, we said in Q4 that the benefit we've seen from higher rates in earnings on surplus was $170 million. If we look now at the first quarter and the benefit that we see from higher rates in Q1 '23 relative to Q1 '22, that's a benefit of $80 million in the quarter.

And that's a net number. So that's the improvement that we see in the yield and the investment portfolio less the higher cost of -- to the higher cost of debt. So we are seeing the benefits of higher rates flowing through earnings on surplus.

The second component of your question there relating to seed capital. You're right, we have reallocated seed capital to Global WAM, it makes sense that we do that. That's where the seed capital is managed. The balance is actually slightly lower in Q1 than where it had been at the end of the year. There's some seed capital repatriation. So the current seed capital balance is around $1.2 billion. And that gives a good indication is the balanced portfolio between equity returns and fixed income and balanced portfolios. That gives us a good indication of what you'd expect the return to be in any particular quarter.

The return will be stable in core earnings because we're using expected long-term returns to determine the core earnings amount. But then any variance to actual fair value will be disclosed separately outside of core earnings within the G WAM segmental results.

And in the first quarter, you see a core gain of $28 million from the impact of seed capital -- sorry, $28 million versus $36 million in '22. So it's actually come down because the seed capital balance has come down slightly. And in Q1 this year, the favorable fair value adjustment that you see outside of core earnings is $10 million for G WAM.

Scott Sears Hartz
Chief Investment Officer

Phil, it's Scott. I might add to that, as you look at rates and the question around long-term rates have come down a little bit, what really drives on the fixed income part of surplus is the cash has a higher earnings rate and short-term rates really have not come down, and you can see cash balances on our balance sheet. For longer-term rates, which have come down a little bit here, it's really a matter of where they are relative to the book yield on the portfolio. And the book yield is still much lower than kind of current rates. So as portfolio turns over, that will still increase income given, where current rates are relative to book yields.

Philip James Witherington
Chief Financial Officer

And Nigel, I realized I didn't answer the component of your question relating to the run rate. I think the Q1 run rate that you see on [IOS] $283 million in the drivers of earnings analysis, that's a good reference point, good run rate reference point for future quarters.

Nigel R. D'Souza
Veritas Investment Research Corporation

Okay. That's helpful. And then my second question was on Global WAM's core EBITDA margin. I noticed you have pointed to a decline in AUM year-over-year, but you also had to offset with higher fee yields. So just trying to get a sense of what's the variable components expense this year, because I would assume that some variable costs would have declined as well, but it does not seem to be the case. And in terms of the margin going forward, is it fair to assume that if you return to the previous AUM level, the core EBITDA margin will also [indiscernible] back. Do you think to be subtle?

Paul Raymon Lorentz
President and CEO of Global Wealth & Asset Management

Yes. Thanks, Nigel. It's Paul here. Yes, so the decline year-over-year, the impact of that was from markets, if you recall, markets continued to decline from Q1 last year for the remainder of the year, and there is some expenses in there. But if you look at the core earnings decrease of 20%, the majority of that was from markets in isolation.

There is a component on expenses. Expenses were up from last year. Some of that is good expenses from my perspective. And that is we're seeing sales activity pick up quite a bit from where we were last year that is driving higher travel and entertainment expenses from what we would have seen last year, that's typically a leading indicator of good sales momentum for us. So considering we started the quarter with positive flows and are seeing that, it's not something we really want to pull back on too much because that should translate into higher flows AUM and ultimately, earnings.

The other thing I would call out is that there's also an impact this quarter from the consolidation that Phil talked about as it relates to our China acquisition, now called Manulife Fund Management. Previously, we reported 49% of flows and AUM, but for earnings, we reported as an equity pickup. So earnings came in directly in the core earnings line.

Now with the full consolidation, we're reporting 100%, but we're showing the earnings and the income statement in each of the line items. So you are seeing revenue come through in expenses. That is a compression on the margin in the short term. And so that is having an impact year-over-year.

But just a couple of points on that 1 I'd make. The first is we're already starting to see some positive momentum of the acquisition and the new leadership team we put in place of the positive flows in the quarter, $1.8 billion came from China in Q1, and a lot of that was driven by a very large fundraise they were able to complete.

The second comment I'd make is, while it was a compression on the margin year-over-year, it's a net positive contributor to earnings. So we do expect this to be a tailwind over the long term. So the way we look at it and how we're looking at it is we were at 28% just over a year ago, and we've had a significant market pullback. So as we look forward on this, assuming markets recover, our track record on net flows, our stable net fee income our ability to manage expenses, we feel quite confident we're going to get that back and are still feel confident in our ability to deliver the 30% over the medium term.

Operator

Our following question is from Lemar Persaud from Cormark Securities.

Lemar Persaud
Cormark Securities Inc., Research Division

Hopefully, just a quick 1 for me. Just wrapping up some of the earlier comments on Asia, particularly as it relates to new business CSM growth. Would it be fair to suggest that you need both better product mix and for Asia, other to accelerate to get to that 15% new business CSM growth target? So the recovery in Hong Kong that we're seeing isn't going to be enough in it of itself to drive that strong momentum needed to get back into the 15% range. So we need to see like Vietnam and some other geographies kind of recover to drive that? Is that a fair characterization?

Philip James Witherington
Chief Financial Officer

Yes. Lemar, this is Phil. I think that is a fair characterization. We need a recovery of both volumes and along with improved product mix and strengthened margins. But it's really important to note on this that as volume improves, that naturally helps to improve our margin because the component of our cost base is fixed. .

So a really important driver here is making sure that as markets come out of the pandemic, we do get back to normal rates of production, normal rates of growth. And we're really confident that, that will happen. I don't know whether you have anything you'd like to add to that, Damien.

Damien Allen Green
Executive Director

No, that's great, Phil. One small thing in regards to Hong Kong, we are expecting customer demand in the first quarter impacted new business CSM around a preponderance and focus from customers on -- we are expecting that to diversify in coming quarters. Our customer research on Mainland Chinese Visitor customer suggests a growing demand for health and critical illness coverage. So we do expect to see improved margins there as well, which will flow new business CSM and NBV.

Roy Gori
President, CEO & Director

Lemar, 1 of the big advantages that we have in Asia, apart from being 1 of the top 3 fastest-growing Pan Asian players is that we have actually a very diverse business. And the diversity spans not just geography, but also product lines and channels. We've got a strong agency force, a really strong banker capability. We've got 100 bank partners, 10 that we work with exclusively, which gives us access to more than 35 million customers. So again, we're really optimistic about our Asia franchise.

Obviously, '22 has been challenged because of sales volumes, and we saw that recover somewhat in the first quarter. But we're still very bullish about the opportunity that we see across Asia and the low penetration rates, which put us in a tremendous position to capture outsized growth for the years ahead.

Operator

[Operator Instructions] Following question is from Tom MacKinnon from BMO Capital Markets.

Tom MacKinnon
BMO Capital Markets Equity Research

Yes. Just a point of clarification here. Phil, I think you said the all the returns would be about 1/3 of the core net investment result. I think that's on a gross basis, but not on a net basis because as you know, the core net investment results would have the finance expense associated with the unwind, I guess, of the discount on the insurance contracts. So I think your comment was related to on a gross basis and on a net basis. Is that correct?

Philip James Witherington
Chief Financial Officer

Tom, it's actually with respect -- it's on a net basis that we're making that comment. The -- we're not -- we don't have -- the way in which we determine our discount rate that then drives the -- naturally the underwind of the discount and the interest accretion on liabilities, that we don't differentiate based on the asset portfolio. It's based on the characteristics of the liability. So it's uniform across the portfolio. So when we're referencing 30%, we're referencing that net number. But happy to give you a call and walk you through that, Tom.

Tom MacKinnon
BMO Capital Markets Equity Research

It looks like you're just kind of apportioning that to each 1 of those categories, and then that -- you would happen that as a third. Okay. So that in my example that I just said that you would have the same on a gross and a net basis, because all you're doing is a portioning that expense to those various investment categories. Is that correct?

Philip James Witherington
Chief Financial Officer

Correct.

Operator

So, we have no further questions registered at this time. I would now like to turn the meeting back over to Mr. Ko.

Hung Ko
Vice President of Group Investor Relations

Thank you, operator. We will be available after the call if there are any follow-up questions. Have a good day, everyone.

Operator
Thank you. The conference has now ended. Please disconnect your lines at this time, and we thank you for your participation.