Great-West Lifeco Inc.

Second Quarter 2024 Results

Conference Call Transcript

August 7, 2024

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See also "Important Note Regarding Sustainability Disclosure" in the Company's Q2 2024 MD&A.

Other than as specifically required by applicable law, the Company does not intend to update any forward-looking information whether as a result of new information, future events or otherwise.

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Operator:
Welcome to the Great-West Lifeco Second Quarter 2024 Results Conference Call.

As a reminder, all participants are in listen-only mode and the conference is being recorded. After the presentation, there will be an opportunity for analysts to ask questions. To join the question queue, you may press star, then one on your telephone keypad. Should you need assistance during the conference call, you may signal an Operator by pressing star, then zero.

I would now like to turn the conference over to Mr. Shubha Khan, Senior Vice President and Head of Investor Relations at Great-West Lifeco. Please go ahead.

Shubha Khan:
Thank you, Operator. Hello, everyone, and thank you for joining the call to discuss our second quarter financial results.

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As many of you already know, this is my first time hosting Great-West Lifeco's quarterly results call since I joined the Company earlier this summer. It's a pleasure to welcome many familiar faces on today's call. I look forward to working with you all.

Before we start, please note that a link to our live webcast and materials for this call have been posted on our website at greatwestlifeco.com under the Investor Relations tab.

Please turn to Slide 3.

I'd like to draw your attention to the cautionary language regarding the use of forward-looking statements which form part of today's remarks, and please refer to the Appendix for a note on the use of non-GAAP financial measures and important notes on adjustments, terms, and definitions used in this presentation.

Please turn to Slide 4.

To discuss our results on today's call, we have our President and CEO Paul Mahon; our Group CFO Jon Nielsen; David Harney, President and COO, Europe, and Capital and Risk Solutions; Fabrice Morin, President and COO, Canada; Ed Murphy, President and CEO, Empower; Linda Kerrigan, Senior Vice President and Appointed Actuary; Jeff Poulin, Executive Vice President, Reinsurance; and Raman Srivastava, Executive Vice President and Chief Investment Officer.

We will begin with prepared remarks, followed by Q&A.

With that, I'll turn the call over to Paul.

Paul Mahon:
Thanks, Shubha, and it's great to have you here.

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I'm very pleased to report strong results for the second quarter, which builds on our performance over the last 12 months. As we work to strengthen our business and deliver for our customers, we continue

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to create sustainable, profitable growth for our shareholders with a fourth consecutive quarter of record base earnings. In the second quarter, both base and net earnings exceeded $1 billion for the first time. This positive momentum is backed by clear strategies, disciplined decisions, and focused execution from our teams across Lifeco. These results have been supported by equity market tailwinds, partially offset by headwinds facing many of our businesses, including regulatory and policy changes, an inflationary environment, and shifting interest rates.

We are executing against our ambitions in the U.S. with focused investments to deliver scale and build new capabilities, which are fuelling an engine for sustainable growth. In line with the target we provided in early 2024, Empower continues to report double-digit earnings growth, driving a nearly 200 basis point increase in the U.S. segment ROE in just the past 12 months. Our U.S. segment is on course to become the largest within the portfolio this year.

Overall, the portfolio continues to create value for shareholders. We're operating at the top end of the range of our medium-term objective for base ROE despite the full impacts of the newly implemented global minimum tax. In light of the market volatility we've seen in recent days, it bears noting that the earnings mix of our business is diversified across our geographies and value drivers, and in our insurance business, we run a well matched book, removing a lot of the sensitivity to market movements. We also remain in a position of financial strength with building regulatory capital levels. This provides additional downside protection, as well as substantial flexibility to take advantage of future opportunities as they arise. We are well equipped to navigate the current market environment.

Please turn to Slide 7.

This quarter's results continued to deliver strongly against our medium-term objectives. Base earnings of $1 billion and base EPS of $1.11 both increased 13% over the prior year. Base ROE increased to 17.2%, up over a full percentage point from the prior year, and book value per share also increased 9%. We've maintained a comfortable leverage ratio and our regulatory capital position is strengthened, with our LICAT ratio increasing one point over last quarter.

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In Canada, we remain committed to driving growth and unlocking value for our customers. Recent acquisitions, coupled with positive market performance, have accelerated growth in our Canadian Individual Wealth business. Net flows have improved despite the overall industry tend to outflows in segregated funds. As we discussed at our wealth focused Investor Day last year, our wealth strategy includes providing a full range of market-leading products and support for advisors and their customers. This approach will help us capture an increasing share of investable assets as they move from segregated funds to other wealth products. Further, we've remained focused on strengthening our seg fund value proposition and reinforcing the unique benefits that these products have for customers.

In Group Life and Health, our results continue to reflect our commitment to growing the business and deepening plan member relationships. Book premiums were up 17% year-over-year, supported by the addition of the public services healthcare plan and solid organic growth. The negative net cash change in book premiums for the quarter is a result of a single termination of a large administrative services-only plan.

In Insurance and Annuities, CSM declined largely due to insurance experience losses. As a reminder, given our focus on growing our wealth platform and extending our leadership in workplace, we do not consider CSM to be a key growth metric in Canada. We have maintained discipline in our approach to risk selection and pricing within the more capital-intensive insurance and annuities businesses. We continue to believe in the value of protection products and regularly review our non-par insurance book. We will take actions as appropriate to maintain its sustainability and stability.

Please turn to Slide 9.

At Empower, we delivered another strong quarter across both Workplace and Personal Wealth. In Workplace, average AUA was up 14% over last year due to sales and U.S. equity market performance. Net flows were negative this quarter, largely due to the anticipated one-time impact of terminations from the Prudential retirement business that we acquired in 2022. Excluding these shock lapses, the business had modest net outflows due to higher withdrawals by DC plan members, principally as a result of higher balances they have achieved over the past years from strong equity markets. While this is weighing on flows in the near term, Empower remains well-positioned to meet growing market demands for retirement solutions over time.

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The expanded range of offerings introduced earlier this year provides Americans with even more options to secure the income stream they need in retirement and will bring more Americans into the retirement system. We continue to believe that we are well-positioned from a scale perspective to drive long-term growth in the DC business at Empower by gaining market share through differentiated customer experience while maintaining our cost advantage. The need for cost competitiveness and differentiated customer experience will drive more consolidation in the DC market, which we are uniquely positioned to benefit from.

Empower Personal Wealth also benefited from positive equity market performance, with average AUA up 23% over the past year. This business continues to see gains largely from the scale brought by the workplace business adding another $1.6 billion in net flows to the platform this quarter. Looking ahead, Empower remains focused on driving profitable growth and building on its recent success, and is well-positioned to continue this performance over the medium term.

Please turn to Slide 10.

We had great results in Europe where we delivered a sixth straight quarter of growth across all value drivers. These results are supported by a set of targeted strategies and focused action to strengthen our positions in Ireland, the U.K., and Germany. Average AUA across wealth and retirement businesses was up 15% year-over-year due to solid market performance and net inflows. We are continuing to deliver against our wealth strategy in Ireland, building out Unio to become a business of significant regional scale to provide more individuals with advice on managing their wealth.

In Workplace, we experienced solid sales and organic growth in Group Life and Health in both the U.K. and Ireland, with book premiums up 8% year-over-year.

In Insurance and Annuities, growth in the individual and bulk annuities in the U.K. helped drive CSM up 13% year-over-year. We see further opportunities for targeted growth in our bulks business this year, supported by disciplined pricing and risk selection, in line with our value creation objectives.

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Capital and Risk Solutions provided a consistent contribution to base earnings and remains an important source of diversification to the overall portfolio. Run rate reinsurance earnings were up slightly over last year as our short-term structured businesses continued to drive growth. These results are pre-tax and better reflect the underlying trend as they do not include the impact of global minimum tax. CSM remained relatively stable as we continued to approach our other reinsurance businesses with pricing discipline.

With that, I'll now turn the call over to Jon to review the financial results. Jon?

Jon Nielsen:
Thank you, Paul.

Please turn to Slide 13.

We continued to see strength in global asset markets in the second quarter, and macro factors continued to benefit our financial results, primarily as a result of higher interest rates in equity markets. Equity market performance supported growth in assets under administration within our wealth and retirement businesses, with average assets up 4% from the first quarter and 18% versus last year. Rising asset levels are positive for our clients who see their wealth growing. However, as clients have benefited from healthy market returns, we experienced increased withdrawals in dollar terms from our workplace savings plans, a dynamic we've seen play out at Empower, as Paul just noted.

Interest rates remained at elevated levels in the second quarter, easing somewhat on the short end of the curve as the Bank of Canada and ECB cut rates for the first time after a historic hiking cycle. Markets are expecting the U.S. Federal Reserve to cut four times in the second half of 2024. Against this backdrop, we continue to ensure that our fixed income holdings remain optimized for any changes in rates.

In terms of currency exposures to earnings, the U.S. dollar, euro, and British pound appreciated against the Canadian dollar both year-over-year and quarter-over-quarter, benefiting our results by 2% in terms of growth in base earnings.

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We delivered another record quarter for base earnings, which increased 13% year-over-year and 11% in constant currency. Both base and net earnings surpassed $1 billion in the second half. The results were driven by strong business growth in all segments, partially offset by the impacts of the global minimum tax, or GMT. Excluding the impacts of the GMT, base earnings grew 14% in constant currency in the quarter and 18% for the first six months of 2024. GMT reduced second quarter base earnings by $28 million. About 80% of this was within our Capital and Risk Solutions business and 20% within Europe. The effective tax rate on base earnings includes an approximate two percentage point impact related to the GMT, and this was in line with our expectations that we shared in previous calls. Our base return on equity for the quarter is slightly above the upper end of our medium-term objective of 16% to 17%, reflecting strong growth in base earnings and the continued focus we have on growing our capital-light businesses.

Turning to Slide 15.

Our Canada, U.S., and Europe segments delivered strong performances, with double-digit increases in base earnings year-over-year. Capital and Risk Solutions was impacted by GMT, but otherwise, posted solid underlying growth.

In Canada, base earnings increased 14%, driven by strong insurance experience, particularly in Group Life and Health; growth in fee income, reflecting the contributions from the ITC and Value Partners acquisitions. Non-directly attributable expenses were elevated by one-time and other items this quarter, tempering earnings growth in the segment. A more representative run rate for this line would be the average of the four quarters in 2023, with modest growth due to inflation and business volume. This aligns with the expense run rate that we are targeting for Lifeco overall.

In the U.S., Empower maintains strong momentum, with base earnings up 19% year-over-year in constant currency. Results reflected higher net fee and spread income resulting from rising equity markets, the realization of the expense synergies that we've articulated in prior calls, and a one-time true-up payment of $30 million from Prudential. Partially offsetting the strong earnings growth were impairments on two U.S. commercial mortgage loans totalling $40 million. Nevertheless, underlying earnings growth remains well within our 15% to 20% target for 2024. As a result, the ROE for this

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business has increased by nearly 200 basis points in the past 12 months alone and remains on track to reach our medium-term objective of 16% to 17%.

In Europe, base earnings increased 12% year-over-year in constant currency, driven by growth in net fee income, improved insurance experience, and higher expected insurance earnings from a growing annuities book. Within Capital and Risk Solutions, results were adversely impacted by the GMT, as we expected. Excluding this impact, base earnings growth was solid at 3% year-over-year in constant currency, with continued strength in our structured business. While we continued to see unfavourable claims experience in our U.S. traditional life portfolio, experience has improved meaningfully on a year-to-date basis. We've continued to monitor U.S. mortality rates post-COVID, and are maintaining pricing discipline in this segment of our business.

We are strategically allocating capital to opportunities with strong returns and diversifications with our other segments. In addition to life and nonlife structured business, this includes property and casualty retrocession, which is approximately 10% of CRS earnings. Our exposure is primarily to natural catastrophe activity, which can be volatile from year-to-year. However, we have taken action over the last two years to significantly limit our risk. For example, it would now take $160 billion CAT event in Florida for our business to include the same $130 million loss that we saw for Hurricane Ian in 2022, and Hurricane Ian cost the industry about $70 billion to $80 billion. This is precisely why we do not expect to incur any losses related to the recent hurricanes Earl or Debby, and have yet to experience a loss triggering event this summer. Overall, we remain very comfortable with our risk exposures within CRS and see plenty of opportunity to continue generating attractive risk-adjusted returns in this business.

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Insurance service results were up year-over-year, reflecting favourable group experience in Canada, as well as Europe, as well as higher expected insurance earnings due to growth in our group businesses and structured business at CRS. The net investment result declined year-over-year as the benefits to earnings on surplus from higher interest rates and the addition of Franklin Templeton dividends were more than offset by the credit experience losses in the U.S. and lower trading gains in Europe. As I noted earlier, the negative credit impact relates to the impairment of two mortgage loans within the U.S. office portfolio. We continue to monitor our commercial real estate exposure closely. While we don't

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expect to be fully immune from headwinds in commercial property markets, we maintain a high-quality and well-diversified portfolio and do not expect losses of this magnitude to recur for the remainder of 2024.

Turning to Slide 17.

Net fee and spread income was up both year-over-year and sequentially, primarily to growth at Empower, reflecting higher equity markets, synergies from the Prudential acquisition, underlying business growth, and the one-time fee adjustment from Prudential. Non-directly attributable expenses at 318 were largely in line with the expected quarterly run rate we communicated last quarter, but included the one-time items in Canada that I previously mentioned.

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Within the quarter, net earnings were modestly below base earnings, as overall positive market experience and the favourable impacts of assumption changes in Management actions were more than offset by business transformation costs, ongoing amortization of intangibles, and the one-time GMT catch-up from the last quarter. Positive market experience was primarily driven by higher interest rates and credit spreads in Canada and the U.K., partially offset by lower than expected returns in both our Canada and U.K. property portfolios. The positive impact of $39 million from assumption changes in Management actions was mostly related to the finalization of the longevity reinsurance transaction that we completed in 2023, and you may recall from one of our previous calls. Business transformation costs moderated from quarter one, and were mostly attributable to the integration of the acquired Prudential operation, which was completed in May. We expect these costs to be negligible in the third quarter.

Turning to Slide 19.

We maintain a strong and stable balance sheet to ensure we are resilient through all market cycles. As Paul noted earlier, our business is well-diversified and the insurance book is well matched, limiting our sensitivity to market movements. In the Appendix to this presentation, we've included a table showing the immediate impacts of adverse movements and market indicators. I would note that both net earnings and balance sheet sensitivities have broadly declined over the past six months, and our

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balance sheet resiliency remains strong. Our strong regulatory capital levels provide an additional buffer against market related volatility.

In the quarter, our LICAT ratio increased to 130%, up 1% from the prior quarter. As a result of our ALM strategy and accounting policy choices, we've experienced a much more stable LICAT result under IFRS 17. This stability highlights the resilience of our balance sheet, which gives us the capacity to execute on strategic opportunities as they arise.

Our leverage ratio continues to decrease and now sits at 29%, down one point from a quarter ago on solid growth in shareholders' equity.

Our cash balance also grew, as strong earnings and capital generation within our businesses allowed for a flow of cash up to Lifeco. I note that there is some seasonality in our cash flow from quarter-to-quarter. Nevertheless, we expect to continue to deliver strong capital generation and for excess cash to build at Lifeco.

Overall, we're extremely pleased with the results of this quarter and for the first half of 2024.

With that, I'll turn the call back over to you, Paul.

Paul Mahon:
Thanks very much, Jon.

Please turn to Slide 20.

We've had a strong first half of the year, with base earnings growth above our medium-term objective of 8% to 10%. For the full year, we remain confident the portfolio will deliver at or near the high end of this range.

As we look beyond this year and into 2025, we're closely monitoring a number of externalities and potential headwinds, including evolving geopolitical trends, equity market volatility, and changes in interest rates. However, we remain well-positioned thanks to the diversification, strength, and resilience of our businesses. We have the right team to continue executing against a clear strategy and drive

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growth across all value drivers.. With plenty of momentum right across the business, we're looking forward to building on our track record and a strong close to the rest of 2024.

With that, I'll now turn the call back over to Shubha to start the Q&A portion of the call. Shubha?

Shubha Khan:
Thanks, Paul. In order to give everyone a chance to participate in the Q&A, we would ask that you limit yourselves to two questions per person and then re-queue for any follow-ups. Operator, we're ready to take questions right now.

Operator:
Thank you. We will now begin the analyst question-and-answer session. To join the question queue, you may press star, then one on your telephone keypad. You will hear a tone acknowledging your request. If you're using a speakerphone, please pick up your handset before pressing any keys. To withdraw your question, please press star, then two. We will pause for a moment as callers join the queue.

The first question comes from John Aiken from Jefferies. Please go ahead.

John Aiken:
Good morning. Thank you very much. A couple questions on Empower defined contribution, if I may. It looks like the participants have flat lined over the last several quarters. Does this relate to the terminations from Pru? If not, what's going on there, and when can we expect growth to resume within the number of participants, please?

Paul Mahon:
Thanks, John. I'm going to turn that one over to Ed to talk about participant dynamics and our anticipation in growing that. Ed?

Ed Murphy:
Sure. Yes. Thank you, Paul. Thanks for your question, John. In terms of participant growth, we did see, obviously, a lapse related to Pru, so we had participants coming off the platform associated with that

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loss, but if you look at the growth trajectory of the DC business, it's very, very strong, so consistently, we've grown our participants at a rate of twice the rate of the market. In some years, we've been growing at three times the rate of the market, but that's organically supplemented with M&A in the Mass and Pru acquisitions, but if I look at just sales in the defined contribution business, year-over-year, we're up 47%.

The small market, which represents all the growth opportunity, is up 35% year-over-year, so we're pretty sanguine about organic growth opportunities. Our pipeline is over $2 trillion, and the demand is very, very high, so we continue to see growth in all segments; not-for-profit, small market, large mega, our Taft-Hartley space, and the market, as we've discussed before, is consolidating, so if you look at the movement that's occurring when customers move from one provider to another, the top three to four players are capturing close to 70% of that business, and that's going to continue as the market shrinks.

John Aiken:
Thanks, Ed, and that leads into my second question. Obviously, with the strength in your LICAT ratio, leverage ratio coming down, everything else like that, you've got a lot of dry powder and you talk about strategic objectives, but of course, Empower has been part of the consolidation in the industry. Is the dislocation of these plans or these numbers on an organic basis enough, or do you still expect to be able to pursue opportunities for additional acquisitions, be it today, tomorrow, or somewhere down road?

Ed Murphy:
Well, I think...

Paul Mahon:
You're on a roll, Ed, you take that one.

Ed Murphy:
Okay. No, I was just going to say, I think organically, if you look at the market, the market's turning about 5% to 6% a year, so our ability to capture our fair share of the plans that are in motion is very, very high, so we're going to continue to see solid organic growth. We'll continue to grow the business organically at a rate faster than the market. I'm convinced of that. We have a superior value proposition.

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We have the scale. We have a cost advantage. On the inorganic side, there will always be entities that are looking to exit the business, and I think as Paul and I have shared with you in the past, we'll be opportunistic there. We definitely see opportunities, and what typically we're looking for is, obviously, scale benefits, but also capabilities that allow us to extend our reach, to append to our existing offerings, and then, of course, the human capital dimension. We've acquired some great talent through these acquisitions, so the short answer is I think we're going to be thoughtful and smart and strategic and opportunistic as these situations present themselves.

John Aiken:
Thank you. I'll re-queue.

Operator:
The next question comes from Mario Mendonca with TD Securities. Please go ahead.

Mario Mendonca:
Good morning. Can I have you stick with the U.S.? The net fee and spread income this quarter is $460 million. Now, I appreciate that there's $30 million or $40 million in there for the fees from Pru, but that improvement from one quarter to the next, I know it's net, so it reflects not just the revenue side, but expense savings, but perhaps you could help me understand that delta from Q3 to Q1 rather to Q2, that significant increase, the extent to which it was driven by the top line, or perhaps it was mostly driven by expense savings at Pru. Just help me understand that delta, please.

Paul Mahon:
Thanks, Mario. I'm going to ask Jon to take that one.

Jon Nielsen:
Yes, Mario. Thanks for the question. Obviously, the one-time fee adjustment from Pru, I think, is well articulated in the material, so that's part of it. The other thing is the, as you call out, fairly flat expense levels with the synergies coming through. We're now on track. The full $180 million of synergies that we called out on the acquisition have been delivered. There's a small piece that didn't come through as we finished the integration in the middle of the quarter that you'll see come through further in the third quarter in terms of those synergies, as well as other cost actions that we take regularly to continue to

drive that scale advantage, so that has an element of effectively growing being a driver in terms of that growth in fee and spread income levels.

The other part is obviously the strong markets that we experienced over the last months and some growth in overall assets under management. As Ed said, we've had a strong pipeline of plan sales, small amount of net outflows that were, call it, unrelated to the Prudential acquisition and priced in, so those were the main contributors of that strong result. The one-off item in terms of the future is the part that you would assume wouldn't recur as we look forward and then factor in that scale and further synergies to come.

Mario Mendonca:
From your answer, I take it that $462 million, of course, adjusting for the one-time payment from Pru, that $462 million adjusted for that is a reasonable run rate for this company, assuming—I appreciate that markets and rates will have their say, but assuming those are stable, this looks appropriate as a run rate for the Company?

Jon Nielsen:
Yes, and overall, we're really happy with the total result of Empower and think the run rate's going to be, now that we're through the integration, a little easier for you to get your hands around. If you look at Pages 23 to 25 of our Supplemental Information Package, it gives more detail below the surface on that number, and as a number of the analysts have suggested, we may look at making it a little easier for you to get below the surface in our disclosures as we look forward, Mario.

Mario Mendonca:
Yes, and then my second question is, I think you addressed this in your opening comments about the non-attributable expenses in Canada being somewhat elevated. What was your point there? I think the point you made is that you you'd have us look at the average of 2023 as a better run rate?

Paul Mahon:
Yes. Jon, why don't you start and then you can pass it over to Fabrice?

Jon Nielsen:

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Yes. Yes. That's what I would say is we're looking at overall being fairly neutral in that line item or flat year-over-year, maybe some modest inflation both at Canada and Lifeco. Let me have Fabrice give you a little colour on what came through or the quarter in Canada.

Fabrice Morin:
That's right. In the non-directly attributable expenses, we have a few one-time items that we don't expect to recur to the tune of around $15 million, so if you look at a run rate for 2023, that's probably close to the run rate that you should expect there.

Mario Mendonca:
Sure, that's makes sense. Thank you.

Paul Mahon:
Thanks, Mario.

Operator:
The next question comes from Doug Young with Desjardins Capital Markets. Please go ahead.

Doug Young:
Hi. Good morning, and I do appreciate you've given some sensitivities to the market movement on Slide 24. I'm just curious if you can walk through and help me understand what lower—how we should be thinking about the impact from lower rates on your base earnings, which there is not sensitivities provided to that line item. If you can walk through some of the areas where we should be thinking that impact would flow through, and I assume if you've got a steeping yield curve, that's one outcome, but if it's a flat and parallel move, that's another. Just trying to visualize this.

Paul Mahon:
Okay. Jon, do you want to take that?

Jon Nielsen:
Yes. Thanks, Doug. Obviously, we've given you the sensitivity to rate in terms of our net profit, LICAT, and so forth, but let me give you a sense on base earnings. This does impact the number of lines within the DOE, not just surplus earnings, the spread earnings, but also, to a certain degree, there is some

impact in our group insurance experience as it relates to our long-term disability business where there's some duration in terms of claims. Also, net fee and spread income in terms of—if you think of our wealth and retirement businesses, if you think of the portfolio, our clients have a diversified portfolio, so think about that portfolio being about 30% in fixed income, so a rate decline obviously then impacts our fee income as well. If you aggregate those impacts in terms of—give you a sensitivity to base earnings that we would expect in a year, about 50 basis point decrease in rates, call it about 1% impact on our base earnings from negatively, so all those movements provide some offsetting, and you can think of it about 1% of our base earnings for 50 basis points, Doug.

Doug Young:
That's helpful, and on the earnings on surplus, because you did shorten up the duration of your fixed income portfolio, is there a meaningful impact to that line item? Can you remind us what the duration of that portfolio as well?

Jon Nielsen:
Yes, it varies by segment, and this is something that we're always optimizing, in particular as we look forward to some upcoming changes in terms of LICAT, something that we're always going to look to optimize, so it varies by country or by segment. You can think of it as around half of that earnings sensitivity that I shared with you comes from the surplus piece, and the other impacts, positive and negatives, are the residual, and I would call it a two- to three-year duration on average across, not equal in each segment, because we manage ALM by business unit, but you can think of it in those types of terms.

Doug Young:
Perfect, and then just lastly, in the CSM, there was negative insurance experience and it related to claims volatility on the longevity business in Europe and the CRS. I'm just hoping you can flesh this out and maybe dumb it down for me as to what drove that?

Paul Mahon:
I'm going to actually ask Linda Kerrigan to take that one. Linda?

Linda Kerrigan:

Yes. The longevity was really across the overall Lifeco CSM insurance experience, so you did see negative experience in the insurance experience across Lifeco, and longevity was in a large part the driver of that. We do take a very disciplined approach to our longevity risk, both in terms of underwriting, pricing risk, and we do have good diversification in our portfolio between a mortality and longevity risk, but you can just get a volatile claims quarter, and that's really what we're seeing this quarter in terms of the longevity experience.

Doug Young:
Nothing you'd call out? Just volatility in this particular quarter, and that didn't go through earnings? It went through the CSM as per just the mechanics of it? Is that simple way to think of it?

Linda Kerrigan:
That is. Exactly.

Doug Young:
Okay, appreciate the colour. Thank you.

Paul Mahon:
Thanks, Doug.

Operator:
The next question comes from Paul Holden with CIBC. Please go ahead.

Paul Holden:
Thank you. Good morning. I want to ask a question on Europe. You announced a number of profit improvement strategies, I think, in 2023. We've seen very good earnings growth out of the segment now for two consecutive quarters. Wondering how you're thinking about how far along are we in that path in terms of profitability improvement? How would you frame it, whether it's from an ROE perspective or a growth perspective, and I'm trying to really get at how much more is still to come?

Paul Mahon:

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Yes, I'll start off with that one and I'm going to turn that to David Harney to provide a little more colour, so the actions we took in the latter part of 2023, in part, were cost driven, but a lot of it was actions to try and strengthen capital and cash generation as well, so it was kind of a balance of those two things, and the actions we took, if you think about it, in part, we're pulling back in some businesses that we did not think were long-term sustainable, and notwithstanding that, pulling back from businesses we've seen growth, so maybe, David, you can provide a bit of colour and a little perspective on that and how the expense actions will play out.

David Harney:
Yes, so, yes, I think that's a pretty good answer, Paul. Look, we've seen good sort of top line experience in Europe over the last six quarters, and the actions we took at the end of last year have translated that into the bottom line earnings growth that we're seeing in this quarter, so, like I say, overall, this quarter is probably a good indication of Europe going forward, so the expense actions we've taken have translated wealth and retirement top line growth into earnings growth, and then some of the actions that we've taken have positioned us well on the insurance and annuity line, particularly for changes that have happened in the U.K. that the PRA have implemented around fund reinsurance and capital requirements. The actions that we've taken there have positioned that product line pretty well going forward, so overall, a good quarter for Europe and a pretty good indication, I think, of potential going forward.

Paul Holden:
Okay, so I get the impression then that most of the benefits have been realized and are flowing through?

David Harney:
Yes. I think the actions we've taken are—they're on the capital side to position us for growth on the annuity side, so we're pretty happy on that segment, and then I think the cost actions, they will continue to moderate expense growth in Europe, so we'll continue to see growth in, I think, wealth and retirement segment as we true into the bottom line results, so I think the actions will continue to moderate expense growth, so, overall, it positions Europe pretty well, and this quarter is a good

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indication of potential going forward.

Paul Mahon:
Yes. The way to think about it, Paul, would be that we're not taking a major cost initiative over a short period of time. There's plans over a number of quarters to come, and it's really just to hold expense growth at a lower rate, and we're really looking to continue to strengthen our earnings base.

Paul Holden:
Okay. That's great. Thank you. Second question, Paul, in your opening remarks, you mentioned competitive pricing environments and remaining disciplined, both from a pricing and capital perspective in the individual insurance business in Canada, so really curious if you can follow up on that question just in terms of the competitive pricing dynamics you're seeing? Give us a sense of how competitors are reacting within any particular product lines where competitive intensity has increased.

Paul Mahon:
Good question. I'll start off at a high level. I think that was, to a large extent, a general statement in the fact that we look at products through a very disciplined lens when we see—for example, if I think about some of the actions that some competitors have taken with longevity pricing, we've held our powder dry. We want to make sure that we understand the impacts of a post-COVID environment, and what does a real stable environment look like going forward, so that was more of a general term, but as it relates to Canada, I think Fabrice can provide you with some insights into the way we think about the market and its competitive dynamics. Fabrice?

Fabrice Morin:
Thank you, and thank you, Paul, for your question. We're pleased with our sales results and our business performance and individual insurance in Canada. A lot of growth at the market level is in participating whole life insurance, which has slightly different dynamics. We remain disciplined in the way we approach the participating whole life insurance market. In the non-participating side, we're pleased with the results as well, balancing that pricing discipline, but also the volume in the market. We have, over the past several quarters, changed some of our product structures in Canada to limit the risk that we have, some of the long-term risk that we have into these products. We've also limited our appetite to some of the very long tail risk that exists in some versions of permanent products on the non-participating side, so, overall, individual insurance is a very competitive market in Canada. We

continue to be focused both on growing our presence, but also on pricing discipline and risk discipline overall.

Paul Mahon:
Yes, and Fabrice, would it be fair to say that there's been no acute change in the competitive dynamic? It's more the fact that we're really trying to look at it through both a sales and a risk lens.

Fabrice Morin:
Absolutely.

Paul Holden:
Okay, that's helpful. I will leave it there. Thanks.

Operator:
The next question comes from Meny Grauman with Scotiabank. Please go ahead.

Meny Grauman:
Hi. Good morning. I just wanted to ask about insurance experience higher than what we saw in Q1. It's always hard to forecast. We saw favourable experience in Canada, not so much in the U.S. traditional life. Just wondering if you could give us a bit of sense of where to expect insurance experience to go from here, and then in terms of the specific dynamics in terms of what's happening in Canada specifically, and how persistent you see that?

Paul Mahon:
Yes, so Meny, I think you actually make a good point with your question is the fact that we've got a diversified book of insurance risk, so we see what we have going on with traditional life in the U.S. We see the strength of LTD in Canada, and that's the benefits of diversification. At any given point in time, we're going to see different dynamics in different segments, different markets, and we're seeing a net benefit, but I go back to the fact that we focus on discipline in pricing, discipline in claims management, and if you maintain that focus, then it can be a contributor, recognizing that you're going to have cycles and volatility, so I'll turn it over to Fabrice, maybe, to get into a bit of the Canadian dynamic.

Fabrice Morin:

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Thank you, Paul, and thank you, Meny, for your questions. We're very pleased with the insurance experience this quarter. It's a good quarter for us. The insurance experience is mainly driven by our workplace long-term disability, but also driven in part by our workplace health experience, and also significant improvement in individual mortality experience, which has been a drag in some of the past years since COVID.

As I think long-term, the stability, typically these cycles are more than one quarter long in nature. They can be long cycles. We see this experience at the industry level. They're driven in part by the external market environment on disability, as Jon was mentioning earlier, and I'd reiterate the point that Paul made. We believe we have a very strong franchise in workplace, especially it relates to our disability operation. It's about the underwriting, first of all, making sure we choose our risk carefully. We price our risks carefully. Then it's about doing what's right to support these individuals facing disability situations and help them overcome these situations and get back to work, and that's what our business is focused on, and we have, over the years, been able to achieve good results. We're careful in how we bake these results into our expected profit. We grow our expected profit relatively in line with the growth of our insured book growth, so I think we're conservative with we're approaching that.

Meny Grauman:
Thanks for the detail.

Paul Mahon:
Thanks, Meny,

Operator:
The next question comes from Tom MacKinnon with BMO. Please go ahead.

Tom MacKinnon:
Yes. Thanks. Good morning, everyone. First question just with respect to Empower defined contribution net flows. Even excluding the impact of shock lapses, we're still in net outflows here, and you talk about one of the reasons is because just higher account balances here, so you're getting increased withdrawals reflecting that, so why is that? Does that imply that as markets do better, you're going to have more net outflows in DC? Am I reading that correctly here? Is it a function of planned demographics? Maybe you can help us understand that. Thanks.

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Paul Mahon:

Yes. Tom, I'll start off maybe at a high level, and then Ed can get into the dynamics that we saw this quarter and our perspectives on the fact that we actually still view this, notwithstanding all of those movements and dynamics, to be a potential growth engine for us, so the reality is there are demographic headwinds if you think about an aging population, you think about the wealth that someone who's nearing retirement has versus a new plan member entering early on in their career, and when you think about it, the money that rolls into an IRA is someone who's built up their wealth, the money that someone's contributing based on their paycheck early in their career would be different, so you've got that dynamic, but that's, frankly, one of the reasons why we love the consolidation opportunity we have in this market. It's a market that has that dynamic, and if you have scale and if you have differentiated capabilities, you can win on the organic growth side and then you can be a winner on the acquisition side, and that's a lot of opportunity to offset what is more of a fundamental dynamic that would be happening on a population basis, so I'll turn it over to Ed maybe to talk about the dynamic we saw this particular quarter. Ed?

Ed Murphy:

Sure. Yes. I think there's two elements, Tom, in terms of the way to think about this. There's plan level flows, which were positive, which I think speaks to the comments I made earlier about the demand that we're seeing and the growth that we're seeing, and our net participant growth will be at budget or exceed budget in that regard, so we're seeing good flows at the plan level. On the participant side, it's up about 5% in terms of participants taking distribution, but it's driven more by rate than volume. Balances are up 35% due to higher markets, as you referenced, and so while distributions are higher, on the flip side, our rollover sales are higher. They're up 28% year-over-year, so as there is dislocation and people are leaving, our ability to capture some of those assets on the wealth side has certainly worked to our advantage.

Yes, there's a demographic trend playing out here. We've been in a high inflationary environment, so in some instances, the distributions people are taking are a little bit higher to augment other income that they have to address any challenges they have with expenses and the like, but there's also a lot of growth on the participants side, and if you have—what I would say is—just a couple of key points I would make there.

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One is you have 18 million participants and there's a large subset of those that are continuing to contribute to their plans, and we're seeing savings rates continue to increase. They've levelled off a little bit because of the economy, but over the last few years, savings rates have continued to rise, and that's in part due to the way that we engage the participants. The second thing I would say is we've got public policy and regulatory policy in the U.S. that's very constructive around new plan formation, so it took the industry 40-plus years to get to 700,000 defined contribution plans in the country, and Cerulli, independent third-party research company, estimates it's going to grow to a million by 2028, so you're going to have 300,000 new plans, and we have a product to address that opportunity in the marketplace.

There's 40 million Americans today that work for small companies that are not covered by workplace savings, so we see a lot of opportunity to drive flow, and as we've referenced earlier, we have the scale and the competitive pricing and the product capabilities to be able to take advantage of that, so, in summary, I would say the dynamic isn't so much that there's a higher volume of people taking distributions. It is a factor of higher balances due to market growth, and in some cases, the distributions that they're taking are higher. Instead of taking a third of the account, they might take a half of the account or two-thirds of the account, so hopefully that helps.

Tom MacKinnon:
Yes, that's good, and then follow-up questions with respect to operating expenses at Empower DC. Generally, they've gone up quarter-over-quarter. This quarter, they came down substantially quarter-over-quarter. Was Q1 elevated? I'd assume that, or did some of these synergies from the Pru thing come in, in an uneven fashion? Is there anything in the quarter that would—how should we would be thinking of that one just going forward, those operating expenses? Just kind of inflation?

Ed Murphy:
We did have $20 million of synergies related to the Pru acquisition that hit in Q3, and I think we referenced that there's another $8 million or so in Q3, but even if you adjust for that, on the workplace side, the expense growth year-over-year is pretty benign. The real investment that we're making is in Empower personal wealth where we're making pretty meaningful investments in technology, distribution, and product capabilities.

Tom MacKinnon:

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How should we be thinking about those operating expenses going forward then? Just growing at an inflation plus something?

Ed Murphy:
Yes. I think that's fair. I think on the workplace side, we think about it in that 3% to 4% range. We have a lot of benefit coming to us based on the scale advantages that we have, but we also have 12,000 associates, and we provide merit increases to people every year, but we're also continuing to find ways to drive increases in productivity. I think we've referenced the full potential program of what we've done from a transformational standpoint, but I think that expense growth rate that I referenced is probably in line for workplace, and then you'll see higher operating expenses in the wealth business. It's still an investment business for us. We're still focused on integrating to a single tech stack and growing our advisor distribution sales force and the like.

Tom MacKinnon:
Okay. Thanks very much.

Ed Murphy:
Sure.

Paul Mahon:
Thanks, Tom.

Operator:
The next question comes from Gabriel Dechaine with National Bank Financial. Please go ahead.

Gabriel Dechaine:
Hi. Good morning. Question on those commercial mortgage impairments. Not trying to make a mountain out of a molehill here, the two of them, and the numbers overall weren't that big in the context of your portfolio. My question, though, is just how to see these things coming, which sounds silly, but if I look at your Q4, your Q1 slide deck, I see no mortgages, commercial mortgages in arrears, so I'm wondering what the disconnect might be there or if I'm misinterpreting something, and then related to that, you might not have stuff in arrears or whatever, but do you maintain a watch list, and if so, how is that fluctuating and where might it be fluctuating?

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Paul Mahon:
Okay. Thanks, Gabe. I'm going to turn that one over to Raman and he can speak to that.

Raman Srivastava:
Yes. Thanks, Gabe, and thanks for not making a mountain out of it, so I guess a couple of comments to answer your question, so just on the particular quarter, as Jon mentioned, this was driven by two mortgages. One was actually one we impaired in Q4 of '23, and we just got the final terms and that related to a further impact, and that was one of our largest ones, if you might recall, and the second was more of an idiosyncratic event related to a second mortgage, and I think just to your question, that's how you would think about these things going forward. They tend to be tenant-related, one-off, idiosyncratic events that affect a particular mortgage.

I'd remind you, if you think about our book, we benefit from geographic diversification, the fact that we have an LTV cushion across the book, good debt service coverage ratios, etc., so these, when they do happen, and we don't expect we'll be immune, but we have pretty good visibility there that we expect impacts to be modest over the balance of this year, and that relates to your question about the watch list, so if we think about that, we do think for the foreseeable future over the course of this year, we expect impacts to be modest. Headwinds still exist. Just don't forget there's headwinds in the office sector, but as Jon noted in his opening remarks, if you look at what's priced into the market in terms of rates, the fact that we have 100 basis points or so priced into the market in terms of rates coming down, that's helpful to the real estate market in general.

Gabriel Dechaine:
Yes. Okay, so, just, if I understand you correctly, you do have a watch list, as I imagine you would, but based on that watch list, you're not expecting any significant losses this year, and then as far as the language around arrears goes, it sounds like one went straight from performing to impaired this quarter, so you didn't even have it categorized in arrears prior to that? I'm just missing the point a little bit here.

Raman Srivastava:
Well, yes, so I think the watch list would reflect—we do have a watch list and it reflects loans that we have concerns on, and we do have—so, for example, you might have a tenant that unexpectedly declares bankruptcy, so then you—things happen, but in general, if you look at our outlook for the

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balance of this year, we expect those impacts to be modest based on visibility we have at this point in time.

Gabriel Dechaine:
Okay. All right. I might want to talk about that offline. Thanks. Have a good one.

Paul Mahon:
Thanks, Gabe.

Operator:
The next question comes from Darko Mihelic with RBC Capital Markets. Please go ahead.

Darko Mihelic:
Hi. Thank you. Two really quick questions. I just wanted to go back to the answer you provided to Meny on the experience gains in Canada. While I understood the answer, in your written materials, it says that there was management actions that helped with experience, so I wonder if you can just touch on that, and at what point do these experience gains prove to be consistent enough for you to change either the CSM or the risk adjustment?

Paul Mahon:
Jon, do you want to start with that or are you going to turn it—okay. Yes, so this, over to you.

Jon Nielsen:
I can take this one, so the experience gains that we see in Canada are mainly related to our PAA business, which would be a business that doesn't have reserves associated with it. It's our workplace business in Canada, so in this case, management action would refer to pricing action and the way we cautiously manage our book. I mentioned earlier the fact that there's some macro factors related to the experience. There's the disability in particular sensitive to rights, so we need to be careful. As rate comes down, the cost of providing disability can go up, and as rate goes up, the cost of providing disability goes down, so we continue to be very cautious in the way that we manage our pricing in the volatile rate environment. That's what the management action would refer to.

Darko Mihelic:

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Okay. That's very helpful. Thank you, and just a follow-up question, Paul, in your opening remarks, you said something that caught my attention. You said that you were looking to strengthen the seg fund value proposition. Others might say that distribution is really the way to sell seg funds, so what is it specifically about the seg fund that you are targeting with respect to this, especially the ones that you're selling?

Paul Mahon:
Yes. Well, seg funds have some unique characteristics that are very helpful and powerful for small business owners and families and when people are looking for levels of protection, and I'll let Fabrice speak to the actions we're taking, because we think it's—while we think a diversity of products is really important to meet a range of needs, we think seg funds have a strong place relative to our customer base. Fabrice?

Fabrice Morin:
Seg fund is a great vehicle. It's a great technology used in the right situations at the right price. We believe it can grow. It's a very small share of the wealth market in Canada right now, and it has room to grow if it's well-positioned. Some of these unique characteristics that Paul referred to, they come with some guarantees variable by product. They offer creditor protection, no probate fee, confidentiality. No other wealth product offers these characteristics that are very relevant to some Canadians and specific situations, as Paul mentioned, business owners, in particular. Many advisors we work with are well aware of these characteristics and promote these products appropriately, and we continue to develop our market relationships to make sure that these products are available to all Canadians who need them. There's a big opportunity in the Canadian marketplace where not all one advisor needs to be insurance licensed to be able to distribute these products. Not all advisors have access under a platform to these products at the relevant licenses, so our focus on our wealth strategy is to provide the full range of products, not only seg funds, but mutual funds, securities, managed portfolios, and the acquisitions that we've done last year, and we're committed to bringing this full range of products to entrepreneurial advisors in this country.

Darko Mihelic:
How quickly can these products be rolled out for you?

Fabrice Morin:

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What I would say here, and you might see the outflows that we see in seg funds, and many of our peers, especially those that have mature blocks like us, would see outflows in the current period. We've seen elevated outflows since interest rates went up. That's true across the wealth marketplace, and it's especially true for a seg fund given the makeup of clients that are into these products. There's cyclicality into that, we believe, and we've seen some improvement lately in the flow situations for a seg fund, so the comments that I made earlier relate to the longer term prospects and actions that we have in the short to medium-term. Of course, there's volatility into the flows that we see on these products given the market situation, and that's what we have been seeing over the past two years to three years.

Darko Mihelic:
Okay. Thank you.

Paul Mahon:
Thanks, Darko.

Operator:
The next question comes from Nigel D'Souza with Veritas Investment Research. Please go ahead.

Nigel D'Souza:
Good morning. Thank you for taking my question. I wanted to circle back to Empower. I believe you outlined some revenue synergies that you expect to realize by end of this year. Just wondering if you could expand on what's driving those revenue synergies, and is there potential for more down the line?

Paul Mahon:
Nigel, I'm going to turn that one over to Ed. I think what he's referring to there is the continuing rollover opportunity that we see across the Empower platform with $90 billion of money in motion each year, but Ed, over to you.

Ed Murphy:
Well, yes, I was referring to—when I made the comment about additional synergies in Q3, I was specifically referring to the Prudential acquisition, that there's some follow-on synergies that will hit in Q3, about $8 million.

Nigel D'Souza:

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Okay, and then if I could…

Paul Mahon:
No, I was just going to say, Nigel, so, yes, so Ed talked about the Q2 synergies, the tailing remaining synergies associated with Pru in Q3, and then the long game for us is the significant opportunity for growth on the wealth side, and to a large extent—I made a comment in my opening remarks and Ed did as well that as we've grown the client-based 18 million participants, there's significant money in motion, and it's, frankly, a synergy associated with having grown the significant Empower workplace business, which essentially is a significant opportunity for us to grow the wealth business off the back of that, so that's the longer game here.

Nigel D'Souza:
Okay. That's helpful. I understand. I'll keep it there. That's it for me. Thanks.

Paul Mahon:
Thanks, Nigel.

Operator:
Once again, if you have question, please press star, then one. The next question comes from Mario Mendonca with TD Securities. Please go ahead.

Mario Mendonca:
Hi. I know we're over, so I'll be quick. On Page 9 of the presentation, you offer definitively that the shock lapses are now complete. How do you get confident on something like that, considering I don't imagine Great-West Life controls the pace of shock lapses? Folks lapse when they lapse, so how can you be so declarative in that respect?

Paul Mahon:
Yes. Well, so, we've actually—Mario, I'm going to turn it to Ed to talk specifically about the Empower book, but when you do an acquisition, you go out to all your clients, you establish the potential clients, right, because you have to actually have to get their commitments. They're going to change carriers. They're going to move off of the platform of the carrier that they were on, and they're either going to

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come to your platform or they're going to go to another one, so every one of those clients is going to make a commitment one way or another to join Empower or go elsewhere, and we saw the same dynamic when we did our roll up in the Canadian market, so to a large extent, all of the clients have made those decisions. Ed, is there anything else you could add to that?

Ed Murphy:
No. I think that's the response. They've all made the decision. They've come over to our platform, so now it just becomes part of our normal operating business, and we would just think about attrition, if you will, in the context of our normal business, which our retention rate is in the 97% to 98% range.

Mario Mendonca:
That's clear. Thank you.

Jon Nielsen:
Maybe just to add, the notice period on that would be 12 months-plus, so you have a pretty good—we had a pretty good outlook of when these would happen, and if you step back, Mario, we price the transaction at a certain level of retention and we outperform that by a few percentage points, and we think both the last two transactions ended up at a point far better than other integrations that have occurred in the market, so we're really pleased that we now closed the integration of the Prudential business really positively.

Ed Murphy:
Yes. I'd just put a finer point on it. I mean we budgeted 82% revenue retention. We came in north of 86%, so that's world class in terms of what we see in the industry, and it was similar to MassMutual, frankly.

Mario Mendonca:
Got it. Thank you.

Paul Mahon:
Thanks, Mario.

Operator:
This concludes the question-and-answer session. I would like to turn the conference back over to Mr. Khan for closing remarks.

Shubha Khan:
Thanks, everyone, for joining us today. Following the call, a telephone replay will be available for one month and the webcast will be archived on our website for one year. Our 2024 third quarter results are scheduled to be released after market close on Wednesday, November 6, with the earnings call starting at 10 a.m. Eastern the following day. Thank you again, and this concludes our call for today.

Operator:
This brings to a close today's conference call. You may disconnect your lines. Thank you for participating and have a pleasant day.

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