

FBL Financial Group, Inc.
4Q17 Conference Call



Jim Brannen
Chief Executive Officer

Thanks, Kathleen. And thank you to everyone on the call. I'm glad you are able to join us today.

FBL Financial Group reported solid earnings for the fourth quarter of 2017. Net income totaled an unusually high \$4.33 per share and non-GAAP operating income was \$0.99 per share. Net income was impacted by solid earnings and large adjustments due to tax reform. We will discuss those in detail later. We had expected somewhat stronger non-GAAP operating earnings for the fourth quarter, but a one-time item drove results somewhat lower than anticipated. Full year 2017 results, however, were at record highs with FBL Financial Group reporting 2017 net income of \$7.75 per share and non-GAAP operating income of \$4.32 per share.

Don will review the financial results in detail as well as the impact of tax reform. I'll focus my comments on sales, our Farm Bureau Financial Services agency force and the new wealth management initiative.

Total premium collected for the fourth quarter of 2017 was \$154 million.

Annuity premium collected for the fourth quarter totaled \$68.5 million, a decline from the fourth quarter of 2016. Full year annuity premium collected declined 19% and was

impacted by a combination of lower interest rates, increased regulation, the relative attractiveness of the equity markets and our increased focus on life insurance. And I am pleased that fourth quarter annuity premium collected increased 18% from the third quarter of 2017. This reflects an increase in both fixed rate annuities and indexed annuities. In September 2017 we introduced a flexible premium indexed annuity. This product replaced our single premium indexed annuity product. The ability to make additional contributions into their indexed annuity contracts has been an attractive option for our clients.

Life premium collected for the fourth quarter of 2017 totaled \$72.4 million and was essentially flat compared to a very strong fourth quarter of 2016 and up slightly compared to the third quarter of 2017. Overall 2017 was a positive year from a life sales perspective.

Full year life premium collected grew 4% in 2017. We experienced strong growth in universal life insurance sales. We also had a positive reception to our accelerated underwriting pilot program. A renewed focus in 2017 was to increase the number of life applications, and I'm pleased with the results. Life applications rose by 5.5%, which means we're reaching more clients with products they need. In addition, these life sales position us for a long term profit stream and allow us to continue to grow earnings from sources other than spread income. It is positive to have a balanced book of life and annuity business, particularly with a year like 2017, where we were able to focus more on life sales.

Turning now to our agency force. As of year-end 2017, we had 1,840 exclusive agents and agency managers, a decline from year-end 2016. While many of our markets grew agents as planned, and top line recruiting was strong, we experienced higher than average tenured agent attrition in a few markets. This drove the majority of the decline. We have taken steps to address this issue, and expect to resume growing the agency force.

Last month I met with agency leadership at our annual sales kickoff meeting. I am optimistic about our prospects for 2018 because of our focus on agent support, new products, digital strategy, increased advertising and our newest initiative, wealth management.

As you recall, on last quarter's call, I mentioned that we are adding advisory capabilities through a newly formed Registered Investment Advisor.

We have four phases related to this initiative. The first phase, occurring this quarter, is to introduce a new mutual fund platform to our exclusive agents. Early reaction to this from our agents has been extremely positive. Many of our agents are already registered representatives, but for those who are not, we have seen an increase in additional agents seeking securities licensing. Phase 1 of this rollout includes required online training for our agents as well as classroom instruction.

The second phase of this initiative will be to convert our existing mutual fund business – nearly \$1 billion of mutual fund assets – to the new platform.

The third and fourth phases include introducing financial planning and a managed account platform to our agents as well as adding the role of a Farm Bureau wealth management advisor to our distribution system.

Once fully implemented, we expect this initiative will allow our agents to add more value, enhance the customer experience and further strengthen the agent/customer relationship.

There will be costs associated with the build out of the initiative – estimated to be a couple of pennies per share each quarter of 2018 – to be included in our Corporate & Other segment. Ultimately, we expect our wealth management initiative to add a diversified earnings stream to FBL Financial Group given the fee-based nature of this business.

To conclude, 2017 was not without its challenges, but I am pleased with our accomplishments – record earnings, growth in life sales, and introducing our wealth management initiative. Most importantly, I am proud of the meaningful work we do to protect the livelihoods and futures of our clients. I am confident in our future as we move forward in 2018.

Now I'll turn the call over to Don Seibel to review our financial results. Don.



Don Seibel
Chief Financial Officer

Thanks Jim. I also want to welcome everybody on the call.

I'm glad to be here today to discuss our fourth quarter earnings results with you. I'll begin my comments by discussing the impact of tax reform on our financial results.

The Tax Cuts and Jobs Act of 2017 enacted December 22 reduced the federal statutory tax rate from 35% to 21%, effective for 2018. This resulted in an \$85.8 million, or \$3.42 per share, benefit to earnings in the fourth quarter of 2017. This benefit is due to the remeasurement of net deferred tax liabilities using the reduced corporate income tax rate. This was a one-time, non-cash accounting adjustment. Given its non-recurring nature, this one-time gain is excluded from non-GAAP operating income.

Going forward, we estimate FBL's effective tax rate to be approximately 17% to 20% in 2018. This compares to our effective tax rate prior to tax reform of 31.7% for 2017.

We are currently evaluating the impact of tax reform and how the lower tax rate will affect our business going forward. As we assess opportunities, we will consider possible benefits for a variety of constituents, including policyholders, shareholders and employees.

Now I'll turn to financial results for the quarter. As Jim indicated, net income for the fourth quarter of 2017 was \$4.33 per share. This includes the large benefit from tax reform as well as net realized losses on investments and the change in net unrealized

gains and losses on derivatives. Excluding these items, non-GAAP operating income for the fourth quarter of 2017 was \$0.99 per share.

Non-GAAP operating earnings for the quarter were below our expectations. These results, however, allowed FBL to end the year with record full year non-GAAP operating income.

The results for the fourth quarter were negatively impacted by:

- \$0.04 per share of higher than expected mortality experience; and
- A one-time \$0.10 per share reduction of income due to the correction of product charges on a closed block of universal life business.

These negative items were partially offset by the benefit of investment prepayment fee income totaling \$0.13 per share. In this low market interest rate environment we have averaged approximately \$0.06 per share per quarter from this source of income.

Next, I'll focus my comments for the quarter on each of our segments.

Looking at our Annuity segment, it is performing well and continues to grow. Annuity pre-tax non-GAAP operating income increased in the fourth quarter of 2017 compared to the prior year, primarily due to the benefit of other investment-related income.

There is continued pressure on annuity spreads. At December 31, 2017, the spread on our individual annuity business was 194 basis points, six basis points below target for this business. We've been active in managing this business and lowering crediting rates where appropriate. We recently decreased crediting rates on a portion of this business by 25 basis points, subject to guarantees. But this has not been enough to offset the decline in yields on investments backing this business due to the maturity of higher yielding assets and purchases of lower yielding assets. Competitive pressures make it difficult to be aggressive in taking further rate actions. At year-end 2017, we had 32% of our annuity business receiving a crediting rate above the minimum guarantees.

Next I'll comment on the results for our Life Insurance segment. In the fourth quarter of 2017, this segment also experienced a benefit from other investment-related income but this was more than offset by the correction of product charges that I previously mentioned. In addition, death benefits for the Life Insurance segment were slightly elevated this quarter primarily due to an increased number of claims.

I am pleased to say that spreads for the Life Insurance segment increased in the fourth quarter, but remain below our targets. The point-in-time spread on our universal life business was 143 basis points at December 31, 2017, below our target for this business of 147 basis points. Yields on investments backing this business declined due to the maturity of higher yielding assets and purchases of lower yielding assets. But this was more than offset by a variety of crediting rate changes we made. It is difficult for us to lower crediting rates further as we now have only 5% of the universal life business receiving a crediting rate above the minimum guarantees at December 31.

Results for the Corporate & Other segment were solid for the fourth quarter of 2017. This segment benefited from the positive impact of equity markets on separate account performance. This segment also experienced slightly elevated death benefits on our closed block variable universal life business. By their nature, death benefit levels can vary from quarter to quarter.

Turning to investments, in the fourth quarter of 2017 the average tax-adjusted yield on investments acquired backing our long-term business was 3.92%. During 2017 we found value in structured product and commercial mortgage loans. Fixed maturity security acquisitions in 2017 had an average life of 12 years and were of high quality with 76% designated NAIC 1 and 23% designated NAIC 2.

While U.S. Treasury yields have increased, the investment environment remains challenging. The Treasury curve continues to flatten and corporate spreads continue to tighten relative to Treasuries.

Next, I'll comment on capital levels. At year-end 2017, our subsidiary, Farm Bureau Life, had an estimated company action level risk based capital ratio of 552%. This is a decrease from September 30 due the impact of federal tax reform. On a statutory accounting basis, Farm Bureau Life revalued its deferred tax asset using the reduced corporate tax rate. In addition, our low income housing tax credit investments incurred a charge from lower future tax benefits due to federal tax reform. These items reduced surplus, lowering the RBC ratio by 27 points.

Despite this decrease, Farm Bureau Life continues to have an excellent capital position. Using 425% RBC as a base, Farm Bureau Life had excess capital of approximately \$160 million at December 31, 2017. Additionally, we estimate that we have approximately \$40 million of excess capital at year-end 2017 at the holding company level.

As we review our options for deploying our current level of excess capital, we consider

stock repurchases, our regular quarterly dividend and the payment of special dividends. We expect future stock repurchases to be limited as we are constrained by our limited public float.

Our board of directors reviews the dividend rate regularly and is committed to having an attractive dividend yield, given our strong and consistent operating results. We also view the payment of special dividends, on occasion, as an attractive option for distributing a portion of our excess capital. Our board will next review the payment of dividends when it meets in March.

In closing, 2017 was a strong year for FBL Financial Group. Despite some fluctuations on a quarter to quarter basis, FBL achieved record full year net income and non-GAAP operating income. The environment for life insurers remains challenging, but during 2017 we were able to grow our business, deliver record financial results and return \$81 million in dividends to shareholders. We move forward in 2018 with financial discipline to continue to profitably grow our business while maintaining a strong financial foundation.

I'm pleased to have been able to share these results with you. We will now turn the call over to the operator and open it up to any questions you may have.