Second Quarter 2020 Conference Call

July 23, 2020

CORPORATE PARTICIPANTS

Gary L. Coleman Globe Life Inc. - Co-Chairman & CEO

Larry M. Hutchison Globe Life Inc. - Co-Chairman & CEO

Frank M. Svoboda Globe Life Inc. - Executive VP & CFO

Michael C. Majors Globe Life Inc. - EVP of Administration & IR

Brian Mitchell Globe Life Inc. – EVP & General Counsel

CONFERENCE CALL PARTICIPANTS

Andrew Scott Kligerman Credit Suisse AG, Research Division - MD & Senior Life Insurance Analyst

Erik James Bass Autonomous Research LLP - Partner of US Life Insurance

Jamminder Singh Bhullar JPMorgan Chase & Co, Research Division - Senior Analyst

John Bakewell Barnidge Piper Sandler & Co., Research Division - MD & Senior Research Analyst

Ryan Joel Krueger Keefe, Bruyette, & Woods, Inc., Research Division - MD of Equity Research

Thomas George Gallagher Evercore ISI Institutional Equities, Research Division - Senior MD

PRESENTATION

Michael C. Majors - Globe Life Inc. - EVP of Administration & IR

Thank you. Good morning everyone. Joining the call today are Gary Coleman and Larry Hutchison, our Co-Chief Executive Officers, Frank Svoboda, our Chief Financial Officer, and Brian Mitchell, our General Counsel. Some of our comments or answers to your questions may contain forward-looking statements that are provided for general guidance purposes only. Accordingly, please refer to the second quarter earnings release we issued yesterday. Some of our comments may also contain non-GAAP measures. Please see our earnings release and website for discussion of these terms and reconciliations to GAAP measures.

I will now turn the call over to Gary Coleman.

Gary L. Coleman - Globe Life Inc. - Co-Chairman & CEO

Thank you Mike, and good morning everyone. I would like to start by saying that we are very pleased with the company's transition to primarily a remote workplace. While the COVID-19 pandemic continues to present challenges, our agents and employees have adapted very well to the current environment, and operations are running smoothly.

In the second quarter, net income was $173 million or $1.62 per share compared to $187 million or $1.67 per share a year ago. Net operating income for the quarter was $177 million or $1.65 per share, a per share decrease of 1% from a year ago.

On a GAAP reported basis, return on equity was 9.4%, and book value per share was $73.26. Excluding unrealized gains and losses on fixed maturities, return on equity was 13.6%, and book value per share grew 10% to $51.21.

In our life insurance operations, premium revenue increased 6% to $671 million, and life underwriting margin was $162 million, down 8% from a year ago. With respect to the premium revenue, we have been very pleased to see the persistency and premium collections improve since the onset of the crisis. However, the decline in margin is due primarily to approximately $22 million of incurred claims related to COVID-19.

For the year, we expect life premium revenue to grow approximately 5% and life underwriting margin to decline 1% to 3%, primarily due to the impact of COVID-19. At the midpoint of our guidance, we anticipate approximately $45 million in COVID-19 claims for the full year.

Health insurance premium revenue grew 6% to $283 million, and health underwriting margin was up 7% to $64 million. For the year, we expect health premium revenue to grow approximately 6% and health underwriting margin to grow 8% to 10%.

Administrative expenses were $62 million for the quarter, up 4% from a year ago. For the full year, we expect administrative expenses to grow approximately 5%.

I will now turn the call over to Larry for his comments on the second quarter marketing operations.

Larry M. Hutchison - Globe Life Inc. - Co-Chairman & CEO

Thank you Gary. I agree with Gary's comments regarding the company's response to the pandemic. The agencies continue to adapt to virtual sales appointments and recruiting, and we see clearly the consumers in our market have a heightened awareness of the need for life insurance.

I will now discuss current trends at each distribution channel. At American Income Life, life premiums were up 7% to $309 million, but life underwriting margin was down 4% to $93 million. Net life sales were $51 million, down 16%. While life sales were down for the quarter, we have seen an increase in agent activity. The rise in activity is not reflected in the second quarter sales due to the increased time for policies to be issued, resulting from changes in our underwriting procedures. These changes are designed to accommodate the virtual sales process, to work around limitations in obtaining certain data, and to protect the company from anti-selection. As we continue to work through this, our processing time will improve. This is incorporated in the full year's sales guidance I will provide later in the call.

The average producing agent count for the second quarter was 8,393, up 14% from the year-ago quarter and up 10% from the first quarter. Producing agent count at the end of the second quarter was 8,597. We continue to see a significant pool of high quality candidates due to current unemployment levels.

Overall, we are encouraged by our virtual sales and recruiting.

At Liberty National, life premiums were up 3% to $73 million, and underwriting margin was up 4% to $19 million. Net life sales declined 20% to $11 million, and net health sales were $4 million, down 30% from the year-ago quarter. The average producing agent count for the second quarter was 2,395, up 5% from the year-ago quarter and down 10% from the first quarter. The producing agent count at Liberty National ended the quarter at 2,379.

While we have seen an increase in individual sales, the worksite business is more challenging. While the persistency of the worksite business is stronger than anticipated, it is more difficult to generate sales activity. That being said, we expect to see improved sales throughout the rest of the year as agents continue to adapt to the virtual environment. As we gain momentum, we will benefit from the abundant recruiting opportunities currently available.

At Family Heritage, health premiums increased 7% to $78 million, and health underwriting margin increased 5% to $19 million. Net health sales were down 20% to $14 million. The average producing agent count for the second quarter was 1,248, up 15% from the year-ago quarter and up 2% from the first quarter. The producing agent count at the end of the quarter was 1,224.

As I indicated on our previous call, the agency owners have a very positive can-do attitude, and I am confident they will continue to recruit and encourage agents to sell.

In our direct to consumer division at Globe Life, life premiums were up 8% to $235 million, but life underwriting margin declined 28% to $28 million. Frank will further discuss the second quarter decline in underwriting margin in his comments.

Net life sales were $49 million, up 43% from the year-ago quarter. This is the largest sales quarter ever for direct to consumer. We have often said that times of crisis highlight the need for basic life insurance protection, and this has proven true with the pandemic. Application activity and sales were up across all direct to consumer channels. The capabilities we have built over the last several years that allow us to engage with consumers online and on the phone have positioned us to capitalize on the opportunity and provide much needed protection for working families.

At United American General Agency, health premiums increased 10% to $113 million, while margins increased 6% to $15 million. Net health sales were $12 million, down 28% compared to the year-ago quarter. While we have seen improving individual Medicare Supplement results over the last several weeks, it is always difficult to predict sales in this competitive marketplace. Group Medicare sales are even more volatile and are generally heavily weighted towards the end of the year.

While it is still difficult to predict sales activity in this uncertain environment, I will now provide full year projections based on knowledge of our business, and the current trends we are seeing. We expect the producing agent count for each agency at the end of 2020 to be in the following ranges: American Income, 8,550 to 8,850; Liberty National, 2,400 to 3,100; Family Heritage, 1,200 to 1,400.

Net life sales for the full year 2020 are expected to be as follows: American Income Life, flat to an increase of 8%; Liberty National, a decrease of 8% to an increase of 4%; and direct to consumer, an increase of 19% to an increase of 23%.

Net health sales for the full year 2020 are expected to be as follows: Liberty National, a decrease of 14% to a decrease of 2%; Family Heritage, a decrease of 5% to an increase of 3%; United American Individual Medicare Supplement, a decrease of 30% to flat.

I will now turn the call back to Gary.

Gary L. Coleman - Globe Life Inc. - Co-Chairman & CEO

Thanks Larry. Excess investment income, which we define as net investment income less required interest on net policy liabilities and debt, was $61 million a 5% decrease over the year-ago quarter. On a per share basis, reflecting the impact of our share repurchase program, excess investment income declined 2%. For the full year, we expect excess investment income in dollars to be down about 4% and be flat on a per share basis.

Now regarding investment yield.

In the second quarter, we invested $351 million in investment grade fixed maturities, primarily in the financial, municipal and industrial sectors. We invested at an average yield of 4.37%, an average rating of A- and an average life of 23 years. For the entire portfolio, the second quarter yield was 5.38%, down 12 basis points from the yield in the second quarter of 2019. As of June 30, the portfolio yield was approximately 5.36%.

Invested assets were $18.2 billion, including $16.7 billion of fixed maturities at amortized cost. Of the fixed maturities, $15.9 billion are investment grade with an average rating of A-, and below investment grade bonds are $772 million compared to $740 million at March 31. The percentage of below investment grade bonds to fixed maturities is 4.6% compared to 4.5% at March 31. Overall, the total portfolio is rated BBB+, same as a year ago, and we have net unrealized gains in the fixed maturity portfolio of $3 billion.

Bonds rated BBB are 56% of the fixed maturity portfolio. While this ratio is in line with the overall bond market, it is high relative to our peers. However, we have little or no exposure to higher risk assets such as derivatives, equities, residential mortgages, CLOs and other asset backed securities. We believe that the BBB securities that we acquire provide the best risk adjusted and capital adjusted returns due in large part to our unique ability to hold securities to maturity regardless of fluctuations in interest rates or equity markets.

Because we invest long, a key criterion utilized in our investment process is the ability of an issuer to survive multiple cycles. This is particularly true in the energy sector. Our energy portfolio is well diversified across subsectors and issuers. It is heavily weighted towards issuers that are less vulnerable to depressed commodity prices. As we discussed on our last call, approximately 57% of our energy portfolio is in the midstream sector and 34% is in the exploration and production. Less than 10% of our energy holdings are in oilfield service, refiner and drill sectors. The composition of our energy portfolio was essentially unchanged during the second quarter, the fair value increased by approximately $320 million. While we have no intent to increase our holdings in this sector, we are comfortable with our current energy holdings.

Finally, lower interest rates continue to pressure investment income. At the midpoint of our guidance, we are assuming an average new money rate of around 3.3% to 3.4% for the second half of the year. For the full year, that would translate to an average new money rate of 3.76% compared to 4.47% for 2019. While we would like to see higher interest rates going forward, Globe Life can thrive in a lower for longer interest rate environment. Extended low interest rates will not impact the GAAP or statutory balance sheets under the current accounting rules since we sell non-interest sensitive protection products. Fortunately, the impact of lower new money rates on our investment income is somewhat limited as we expect to have an average turnover of less than 2% per a year in our investment portfolio for the next 5 years.

Now I will turn the call over to Frank for his comments on capital and liquidity.

Frank M. Svoboda - Globe Life Inc. - Executive VP & CFO

Thanks Gary. First, I want to spend a few minutes discussing the available liquidity and capital position at the Parent Company. The Parent ended the second quarter with liquid assets of approximately $635 million. This amount is higher than normal due to year to date share repurchases of $139 million being less than the $280 million of excess cash flows available to the Parent through June, the $150 million increase in commercial paper borrowings taken to enhance our liquidity position, and the receipt of the $300 million term loan issued by members of our bank line. The company did not repurchase any shares in the second quarter.

In addition to these liquid assets, the Parent Company will still generate additional excess cash flow during the remainder of 2020. The Parent Company's excess cash flow, as we define it, results primarily from the dividends received by the Parent from its subsidiaries, less the interest paid on debt and the dividends paid to Globe Life shareholders. Keeping our common dividend rate at its current level for the remainder of this year, we anticipate the Parent Company's excess cash flow for the remainder of the year to be in the range of $95 million to $105 million. Thus, including the roughly $635 million of liquid assets available at the end of the second quarter, we expect the Parent Company to have around $730 million to $740 million available during the remainder of this year. I will discuss in a little more detail in just a few moments, but we believe this amount of available assets is more than necessary to support the targeted capital levels within our insurance operations. Given that the Parent still has ready access to the commercial paper market, the ability to issue, if necessary, commercial paper through the government's new commercial paper funding facility, and the ability to issue long-term debt in the public debt markets, we have substantial flexibility over the remainder of the year.

Now regarding liquidity and capital levels at our insurance subsidiaries.

In the current environment, we have been keenly focused on liquidity and capital within our insurance operations. With respect to liquidity, our insurance company operating cash flows continued to be very strong. In general, while we do expect higher COVID related life claim payments over the course of the year, these higher claims are expected to be largely offset by higher premium collections and lower health claim payments. We do not see any issues with their ability to fund all remaining dividends payable to the Parent during the remainder of 2020, and we anticipate our insurance operations will generate enough excess cash flows to acquire over $650 million of invested assets to fund future policy obligations.

Now with respect to capital.

As discussed on previous calls, Globe Life targets a consolidated company action level RBC ratio in the range of 300% to 320%. At December 31, 2019, our consolidated RBC ratio was 318%, near the high point of our range. Taking into account the downgrade and credit losses that have occurred through the end of the second quarter, we estimate this ratio has declined slightly to approximately 312%. At an RBC ratio of 312%, our insurance subsidiaries have approximately $60 million of capital over the amount required at the low end of our consolidated RBC target of 300%. This excess capital, along with the $730 million to $740 million of liquid assets that we expect to be available at the Parent, provide nearly $800 million of assets available to fund future capital needs.

As we discussed on the last call, the primary drivers of additional capital needs from the Parent are lower statutory income due to COVID-19 related factors, lower statutory income due to investment portfolio defaults or other credit losses, and investment downgrades that increased required capital. At this time, we anticipate that our 2020 statutory income, before any realized gains or losses, will be approximately the same as 2019. Thus, we believe our capital needs will be largely dictated by the amount of downgrades and future credit losses on our investments. To estimate the potential impact of these items, we have modeled several scenarios that take into account consensus views on the economic impact of the recession. The strength and timing of the eventual recovery and a bottoms-up application of such views on the particular holdings in our investment portfolio. We have also analyzed transition and default rates as published by Moody's and evaluated the impact to our RBC ratios, should we experience the same transition and default rates as were experienced in 2001 and 2002 as well as from 2008 to 2010. Under these various scenarios, we estimate our RBC ratios would be reduced from year end 2019 levels in the range of 35 to 60 points over 1 or 2 years, requiring an additional $100 million to $230 million of capital to maintain a 300% RBC ratio. Our base case assumes $60 million in total after tax credit losses, plus over $2.3 billion of downgrades to our fixed maturity portfolio.

Through the second quarter, we have experienced $31 million in losses and $860 million of downgrades, mostly from category NAIC 1 to NAIC 2. The range of potential capital needs is consistent with the range indicated on our last call and is well below the amount of liquidity available at the Parent Company. It is important to note that Globe Life statutory reserves are not negatively impacted by the low interest rates or the equity markets, given our basic fixed protection products. Furthermore, the current interest rates do not have any impact on our statutory reserves, given the strong underwriting margin in our products. In the aggregate, our statutory reserves are more than adequate under all cash flow testing scenarios.

Given the level of liquidity available at our Parent Company versus the potential capital that may be needed within our insurance companies, we anticipate being in a position to restart our share repurchase program during the third quarter at levels consistent with those expected at the beginning of the year.

At this time, I would like to provide a few comments relating to the impact of COVID-19 on our second quarter results.

As noted by Larry, life underwriting margin declined at both American Income and direct to consumer during the quarter. These declines were primarily due to higher COVID-19 policy obligations. During the quarter, we estimate that American Income incurred an additional $7 million relating to COVID claims, and that direct to consumer incurred an additional $11 million. Absent these additional losses, American Income's underwriting margin would have been 32.7% of premium for the quarter and would have grown by 4%.

In the direct to consumer distribution, absent the estimated policy obligations due to COVID, their underwriting margin would have been 16.8% of premium for the quarter and would have grown by 3%. In total, for our life operations, we estimate that our total incurred losses from COVID deaths in the second quarter were $22 million. Absent these additional losses, our total life underwriting margin would have been approximately 27.4% of premium, up 4.9% over the year-ago quarter.

Finally, with respect to our earnings guidance for 2020.

We are projecting net operating income per share will be in the range of $6.80 to $7.04 for the year ended December 31, 2020. The $6.92 midpoint of this guidance reflects a $0.02 increase over the midpoint of our previous guidance of $6.90. The $0.02 increase at the midpoint is primarily attributable to lower borrowing costs associated with our short-term debt.

As Gary previously noted, at the midpoint of our guidance, we now expect our life premiums to grow in 2020 by around 5% and our total health premiums to grow by 6%, both higher than indicated in our previous guidance. Our total premium income is anticipated to be approximately 5% higher than 2019 levels.

On our last call, we indicated the midpoint of our guidance assumed approximately $25 million of additional claims related to COVID-19 on an assumption of around 80,000 deaths. That was based on some early assessments of infections, death rates and the ages impacted. Since the first quarter, more granular data regarding infection and projected deaths in various geographies has become available. In addition, better projection models are available that project death by state. We have utilized these models along with our experience to date and applied them to our mix of business by state and the attained ages of our policyholders to refine our estimate.

We now estimate that in 2020, we will incur COVID related life claims of approximately $2 million for every 10,000 U.S. deaths. At the midpoint of our guidance, we estimate approximately $45 million of COVID related life claims for the full year 2020. These additional life claims are expected to reduce our 2020 earnings per share by approximately $0.33 on an after-tax basis.

With respect to our health claims, due to lower than expected utilization rates, we now estimate that our supplemental health benefits will be approximately $8 million lower than what we expected at the beginning of the year. Taking into account the higher COVID life obligations, we expect the life underwriting margin for 2020 as a percentage of premium to be approximately 26.1% at our midpoint, down from the 27.4% expected on our last call. Absent the higher policy obligations, the life underwriting margin percentage would be similar to the percentage for the full year 2019. The health underwriting margin as a percentage of premium for 2020 should increase to approximately 23.2%.

Those are my comments. I will now turn the call back to Larry.

Larry M. Hutchison - Globe Life Inc. - Co-Chairman & CEO

Thank you Frank. Those are our comments. We, will now open the call up for questions.

QUESTIONS AND ANSWERS

Erik James Bass - Autonomous Research LLP - Partner of US Life Insurance

Hi, thank you. I was hoping you could provide a bit more detail on the health results this quarter. And I know you just gave some detail, but if you could give a little bit more on how much impact you did see from direct COVID related claims? And how much benefit you saw from lower normal course activity?

And am I correct from your comments that you are assuming the lower levels of utilization continue through the second half of the year?

Gary L. Coleman - Globe Life Inc. - Co-Chairman & CEO

Eric, we experienced about a $900,000 positive impact in the second quarter. Now that will grow as -- towards the end of the year, we expect to be closer to $8 million positive in the remainder of the year. Excluding the $900,000 or so for the second quarter, our policy obligations, would have still been up slightly and -- but that is offset a little bit by the fact that we had to lower non-deferred commissions and amortization. So again, it had a little impact in this quarter. We will see more of that as we go through the remainder of the year.

Erik James Bass - Autonomous Research LLP - Partner of US Life Insurance

Got it. And that is an $8 million net benefit, so offsetting any higher claims with the better utilization?

Gary L. Coleman - Globe Life Inc. - Co-Chairman & CEO

Right.

Erik James Bass - Autonomous Research LLP - Partner of US Life Insurance

Okay thank you. And then on the buyback, just to make sure I am thinking of it correctly. When you say resuming to the levels you would have expected at the beginning of the year, does that mean that for 2020, overall, you expect to get to the same level that you had anticipated coming into the year and realizing you did more in the first quarter of the year? That it would be sort of a normal run rate in 3Q and 4Q?

Frank M. Svoboda - Globe Life Inc. - Executive VP & CFO

Yes, Eric. We anticipate starting with repurchase levels, probably in that $90 million to $100 million per quarter range. That is where at the beginning of the year, we would have thought we would be on kind of a per quarter basis. And then following our historical practice, we would -- our repurchases normally occur over time and somewhat ratable over the course of the quarter. And then remember that we would be under no mandate to spend any specified amount. So that really gives us the flexibility to slow it down if economic conditions were to deteriorate over the course of the remainder of the year or if everything looks good, if you will, by the end of the year, and the economy is not -- is performing basically as consensus would indicate it. We do think ultimately that the total level of repurchases by the end of the year should be pretty close to what we had thought, somewhere in that $375 million to $385 million of excess cash flow that we would have for 2020. Given that we have already spent $140 million in the first quarter, we could see if everything works out that we'd be at that $200 -- not to exceed that $240 million level.

Erik James Bass - Autonomous Research LLP - Partner of US Life Insurance

Got it, thank you very much.

Ryan Joel Krueger - Keefe, Bruyette, & Woods, Inc., Research Division - MD of Equity Research

Hi, thanks good morning. In terms of your short-term debt, I guess at what point would you -- given how low rates are and spreads at this point? At what point would you consider issuing long-term debt and repaying some of the short-term debt for a more permanent capital solution?

Frank M. Svoboda - Globe Life Inc. - Executive VP & CFO

Yes, hi Ryan, it is a good question. And the debt capital markets really are very favorable right now. And obviously, rates have come down significantly over the last couple of months. We have been in quite a few conversations with several of our bankers. And assuming that the market conditions do continue to be favorable, we will be considering issuing some long-term senior debt here in the third quarter or at least relatively soon. And then we would anticipate using the proceeds of that to refinance that $300 million term loan that we did take out earlier in the year.

Ryan Joel Krueger - Keefe, Bruyette, & Woods, Inc., Research Division - MD of Equity Research

Got it thanks, and then I guess just on the direct to consumer business, given the level of growth you are experiencing at this point, would you expect there is any positive from a scale standpoint if that continues to grow at this level?

Larry M. Hutchison - Globe Life Inc. - Co-Chairman & CEO

I think the question is – I would answer it this way. For direct to consumer business, our marketing costs are mostly fixed. So sales that are greater than those planned, generally provide additional margin, which could help offset the higher mortality cost.

Ryan Joel Krueger - Keefe, Bruyette, & Woods, Inc., Research Division - MD of Equity Research

Got it, thank you.

John Bakewell Barnidge - Piper Sandler & Co., Research Division - MD & Senior Research Analyst

Yes hi, what percent of insurers went through a job loss during the quarter?

Larry M. Hutchison - Globe Life Inc. - Co-Chairman & CEO

I do not think we have that information available to see what percentage of our insurers -- what we know is that our persistency was actually better than expected during the quarter.

Frank M. Svoboda - Globe Life Inc. - Executive VP & CFO

Yes. The other thing I would add to that is that it was, as Larry said, we have actually seen fewer claims and greater persistency, which, in our minds, kind of reiterates kind of a view of the importance of life insurance to our policyholders. But we also saw the situation where our policyholders were accelerating their premiums. So rather than seeing higher lapses, we have actually seen acceleration of premiums, people paying a little bit ahead of time on their policies.

John Bakewell Barnidge - Piper Sandler & Co., Research Division - MD & Senior Research Analyst

Okay. And then my follow-up. Given the challenges being seen in Texas with COVID right now, can you remind me what percent of your in force life business is in that state?

Frank M. Svoboda - Globe Life Inc. - Executive VP & CFO

I do not think I have that in front of me. We will have to get back with you on that one.

John Bakewell Barnidge - Piper Sandler & Co., Research Division - MD & Senior Research Analyst

Alright, great thanks.

Thomas George Gallagher - Evercore ISI Institutional Equities, Research Division - Senior MD

Thanks, how are you protecting against potential adverse development on life sales and the direct to consumer business during the pandemic? I know a number of other companies, admittedly, their more selling to the affluent market, but they have pretty dramatically slowed sales deliberately. So just curious how you are thinking about that. I know you mentioned there has been some changes to underwriting.

And then I guess just a related question to that. It looks like the majority of COVID related impacts were felt in that segment. Have you looked at whether any of the recent sales have been the cause of the -- the near-term mortality? Or is it more older policies?

Larry M. Hutchison - Globe Life Inc. - Co-Chairman & CEO

This is Larry. We monitor the incoming insurance applications for indications of change in the risk profile. This monitoring includes things like age, amount of insurance and geography. And at this point, we have not seen a material change in the risk profile, and we are very comfortable with the sales to date. We still have the ability to put other marketing or underwriting limitations in place, should we observe changes in the incoming applications that could have a negative effect on our profitability.

Gary L. Coleman - Globe Life Inc. - Co-Chairman & CEO

And Tom, as far as the COVID claims, they are not policies that were issued in 2020 and there were very little issued in 2019. The claims have really been spread out through policies issued and prior to 2019, fairly evenly throughout the years. But it has not come from the -- either 2019 or 2020.

Thomas George Gallagher - Evercore ISI Institutional Equities, Research Division - Senior MD

Got you. And what are – you had mentioned you have implemented underwriting changes. Any -- can you elaborate a bit as to what you have changed on the underwriting side?

Larry M. Hutchison - Globe Life Inc. - Co-Chairman & CEO

On the direct to consumer, we have limited the amount of insurance in the upper ages. We have also discontinued some add-on insurance in those upper ages.

And additionally, we have temporarily stopped issuing policies to applicants with certain underlying health conditions. So that is 3 of the specific items we have taken steps in our underwriting process.

Thomas George Gallagher - Evercore ISI Institutional Equities, Research Division - Senior MD

Okay thanks, and then the $22 million of adverse COVID mortality in the quarter that you highlighted, can you quantify how much of that was claims received versus IBNR?

Gary L. Coleman - Globe Life Inc. - Co-Chairman & CEO

It is about half... go ahead Frank.

Frank M. Svoboda - Globe Life Inc. - Executive VP & CFO

Sorry, Gary. Out of the $22 million, we have paid roughly $10 million to $10.5 million of that has been paid in actual cash.

Thomas George Gallagher - Evercore ISI Institutional Equities, Research Division - Senior MD

Okay thank you.

Andrew Scott Kligerman - Credit Suisse AG, Research Division - MD & Senior Life Insurance Analyst

Hey good morning. I wanted to ask first about the direct to consumer sales outlook. I think you are guiding to 19% to 23% for the year after a 43% quarter that you had year-over-year. So why not go a little bit higher on that sales growth outlook?

Larry M. Hutchison - Globe Life Inc. - Co-Chairman & CEO

Well, if you remember, in the first quarter, we were basically flat and we are up 43% in the second quarter. As we look at our different channels, we think sales will be up across all channels in the third and fourth quarter. We just don't think the sales increases will be as robust in the third and fourth quarter as they were in the second quarter.

Andrew Scott Kligerman - Credit Suisse AG, Research Division - MD & Senior Life Insurance Analyst

Got it, got it, got it. Okay. And then with the health utilization, and it looks like the margins were pretty stable year-over-year, but shouldn't -- and your guidance seems to imply that the utilization even gets lower, whereas I guess, conceptually I think the utilization might pick up, just given that in the second quarter policyholders probably could not get to the doctor's office. They may have had issues filing claims. So why might you think that the underwriting margin in health should improve as we go through the balance of the year?

Gary L. Coleman - Globe Life Inc. - Co-Chairman & CEO

Well, offsetting the benefit we will get from the COVID claims is, in the Med-Sup business we have seen increasing claims there. And we noted that last year in 2019 we had requested rate increases. Well, the higher claims continued, at least into the first quarter of this year. And we have not yet gotten the full benefit of rate increases. So the combination of those 2 things has caused us to see an increase in the policy obligations on the Med-Sup business, and that's offsetting a little bit of the favorable benefit that we are getting from the COVID. We will still have a slight benefit, but it won't be the full COVID benefit.

Andrew Scott Kligerman - Credit Suisse AG, Research Division - MD & Senior Life Insurance Analyst

I see, I see. And then maybe just with regards to your guidance of $6.80 to $7.04, you have really narrowed in the band. The midpoint is slightly higher. The quarter looked great. I mean just so much stability in so many different places what is giving you that confidence to narrow the band so much on the guidance?

Frank M. Svoboda - Globe Life Inc. - Executive VP & CFO

Yes. We really just do -- we feel much better about the -- where the impact of the COVID related claims might be. We are able to do just a better job modeling to where we have a decent sense of where that will turn out for us. So as we do think about the range, we kind of typically have a $0.10 or so range this time on this particular call, kind of historically, we are expanding it greater than what we typically have just because of some of the uncertainty around the ultimate COVID life claims. But at this point in time of the year, new money rates on our investments do not have that much impact on the overall GAAP earnings, the amount of sales between now and then does not have as significant of an impact. So our primary variable really is around what happens with our COVID claims at this point in time.

Andrew Scott Kligerman - Credit Suisse AG, Research Division - MD & Senior Life Insurance Analyst

Got it. Maybe just throw in one last question. Recruiting going forward, you mentioned on the call that you are seeing a lot of high quality recruits. What are you thinking as we kind of get into the back half of the year? I mean, can we see the kind of recruitment increases that we saw in the first quarter?

Larry M. Hutchison - Globe Life Inc. - Co-Chairman & CEO

Year-to-date, recruiting at American Income is up about 17%. And what is really driving that is the -- not just the unemployed, but the underemployed. There are a number of people that are unemployed or looking for a better opportunity. So in the second half of the year I think we will have strong recruiting in all 3 agencies. The development of virtual recruiting is really another impetus as we have developed virtual recruiting it's strengthened the recruiting process in all 3 agencies because we can reach more people that are interested in the career and the virtual selling has been a positive because it appeals to more people because they have more flexibility when they set appointments to make presentations. So I think the second half of the year will have strong recruiting, just like the second quarter.

Andrew Scott Kligerman - Credit Suisse AG, Research Division - MD & Senior Life Insurance Analyst

Excellent, thank you so much.

Jamminder Singh Bhullar - JPMorgan Chase & Co, Research Division - Senior Analyst

Hi, good morning. I had a question first on sales through the agency channel. Can you talk about what -- how the quarter sort of progressed? So at American Income, Liberty and Family Heritage as well, like did you see an improvement in your sales as you went through the second quarter? Or were they fairly stable throughout the quarter?

Larry M. Hutchison - Globe Life Inc. - Co-Chairman & CEO

Yes, we saw a real improvement as we worked through the quarter. At the beginning of the quarter, really for all agents, not just new agents, but all agents were making a transition from in-person sales to virtual sales. Of course, that was the easiest in American Income because they sell individual products in urban areas using union and nonunion leads. So the transition there to virtual sales, necessary training happened fairly quickly. At Liberty National and Family Heritage, they do not have the same lead sources. Their lead sources have traditionally been more in person so it is a little slower process. But by the last 2 weeks of the second quarter, we saw submitted business roughly equal to what it was for the same period of time in 2019.

Jamminder Singh Bhullar - JPMorgan Chase & Co, Research Division - Senior Analyst

And then on direct response, how much of a benefit do you think you are getting from people just being home and not being, sort of, comfortable meeting with an agent and seeing higher response rates versus maybe more of a sustainable change in response rates and sales trends in that business?

Larry M. Hutchison - Globe Life Inc. - Co-Chairman & CEO

Well, the pandemic really increased the awareness and the need for life insurance, and the increase is across all 4 channels. It really -- we could immediately meet that need because we were not constrained by having to train agents or change to virtual. The investment we have made over the last couple of years particularly in the Internet and our inbound phone call center, has really paid off because they immediately were able to meet the increased demand for life insurance.

Jamminder Singh Bhullar - JPMorgan Chase & Co, Research Division - Senior Analyst

And then just lastly, it does not seem like the A.M. Best impact or the action last week on the downgrades is having an impact on how you are thinking about capital, but do you see that impacting either your business in any way, or has that gone into your thinking in terms of capital deployment?

Frank M. Svoboda - Globe Life Inc. - Executive VP & CFO

Yes. Jimmy, it really has not too much -- we really do not think that it will have that much effect on our overall marketing efforts, just given the kind of the nature of our products. And then as you kind of mentioned, it really won't have an impact on our cost of capital at all. So we are not -- while we would rather have had it not happen, we really do not see it having a meaningful impact on our business.

Jamminder Singh Bhullar - JPMorgan Chase & Co, Research Division - Senior Analyst

Thank you.

Frank M. Svoboda - Globe Life Inc. - Executive VP & CFO

Larry, one thing I would like to follow-up on John’s question regarding amount of exposure to the state of Texas. I did come across that. We have about 7.5% of our total face amount of our policies in force within the state of Texas.

Larry M. Hutchison - Globe Life Inc. - Co-Chairman & CEO

Yes, it varies by company. At American Income, Texas is less important than some other states. If you are talking overall, I agree with that. But Texas, I believe, is the largest state for direct to consumer.

Frank M. Svoboda - Globe Life Inc. - Executive VP & CFO

Right, I do not have it broke down by company.

Operator

At this time, we have no persons in the queue.

Michael C. Majors - Globe Life Inc. - EVP of Administration & IR

All right. Thank you for joining us this morning. Those are our comments, and we will talk to you again next quarter.