

REFINITIV STREETEVENTS

EDITED TRANSCRIPT

CNO.N - Q2 2023 CNO Financial Group Inc Earnings Call

EVENT DATE/TIME: AUGUST 01, 2023 / 3:00PM GMT

CORPORATE PARTICIPANTS

Adam Auvil *CNO Financial Group, Inc. - VP of Corporate Development*

Eric Ronald Johnson *CNO Financial Group, Inc. - CIO*

Gary Chandru Bhojwani *CNO Financial Group, Inc. - CEO & Director*

Karen Jeannine DeToro *CNO Financial Group, Inc. - Chief Actuary*

Paul Harrington McDonough *CNO Financial Group, Inc. - CFO & Executive VP*

CONFERENCE CALL PARTICIPANTS

Erik James Bass *Autonomous Research US LP - Senior Analyst of US Life Insurance*

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

Ryan Krueger

Scott Gregory Heleniak *RBC Capital Markets, Research Division - Assistant VP*

Suneet Laxman L. Kamath *Jefferies LLC, Research Division - Equity Analyst*

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

Wilma Carter Jackson Burdis *Raymond James & Associates, Inc., Research Division - Research Analyst*

PRESENTATION

Operator

Good morning, and a warm welcome to the CNO Financial Group Second Quarter 2023 Earnings Call. My name is Candy, and I will be your moderator for today's call. (Operator Instructions)

I would now like to hand the conference call over to our host Adam Auvil. Please go ahead.

Adam Auvil - CNO Financial Group, Inc. - VP of Corporate Development

Good morning, and thank you for joining us on CNO Financial Group's Second Quarter 2023 Earnings Conference Call. Today's presentation will include remarks from Gary Bhojwani, Chief Executive Officer; and Paul McDonough, Chief Financial Officer. Following the presentation, we will also have other business leaders available for the question-and-answer period.

During this conference call, we will be referring to information contained in yesterday's press release. You can obtain the release by visiting the media section of our website at cnoinc.com. This morning's presentation is also available in the Investors section of our website and was filed in a Form 8-K yesterday.

We expect to file our Form 10-Q and post it on our website on or before August. Let me remind you that any forward-looking statements we make today are subject to a number of factors, which may cause actual results to be materially different than those contemplated by the forward-looking statements.

Today's presentations contain a number of GAAP measures, which should not be considered as substitutes for the most directly comparable GAAP measures. You'll find a reconciliation of non-GAAP measures to the corresponding GAAP measures in the appendix.

Throughout the presentation, we will be making performance comparisons, unless otherwise specified, any comparisons made will be referring to changes between second quarter 2023 and second quarter 2022. And with that, I'll turn the call over to Gary.

Gary Chandru Bhojwani - CNO Financial Group, Inc. - CEO & Director

Thanks, Adam. Good morning, everyone, and thank you for joining us. We delivered a solid performance in the second quarter. Operating earnings were \$0.54 per share.

The fundamentals of our business remain sound, including double-digit sales production across multiple product categories, a strengthened capital position and strong free cash flow generation.

Another quarter of strong new money rates drove continued improvement on the earned yield on investments allocated to insurance products. Variable investment income improved sequentially. Elevated health claims impacted results in the quarter. We expect this to moderate in the second half of the year. Paul will touch on this during his remarks.

Both our Consumer and Worksite divisions once again delivered strong sales production and agent results in the quarter. Total new annualized premium was up 11%. We reported double-digit sales growth in field life sales, Medicare supplement, supplemental health and the worksite insurance sales.

Capital and liquidity improved and remained above target levels even after returning \$47 million to shareholders. This demonstrates the strong cash flow generation of the enterprise. Our high-quality investment portfolio continues to produce stable core investment income. Book value, excluding AOCI, was up to \$32.34 per share.

Turning to Slide 5 and our growth scorecard. Life and Health production was strong in the quarter and client assets in our broker-dealer and advisory services were up nicely. Our broad product portfolio and balanced business model continue to provide strength, stability and resilience to our overall results. I'll discuss each division in the next 2 slides.

Beginning with the Consumer division on Slide 6. Sales production was strong, continuing the growth momentum from the first quarter. Life and health NAP was up 9%. Life production was up 7%. Field life sales were up 20%, demonstrating the strength of our captive agent distribution and broad product portfolio to quickly respond to evolving customer needs.

Our D2C life channel was down 1% on a strong comparable, but contributed to overall life sales growth through shared lead generation. 1/3 of field life sales in this quarter originated from a D2C customer lead. This illustrates the value of our integrated distribution model.

During the second quarter, we also implemented accelerated underwriting on our simplified life product to address a growing market demand. This real-time underwriting solution gives customers an instant decision on their application as they sit across the kitchen table from their agents.

We expect roughly 60% of our underwritten life business to be eligible for this new process. Health NAP was up 12% in the quarter, driven by strong sales growth in Medicare Supplement and supplemental health. Medicare supplement was up 29% as consumers gravitated towards these plans, continuing this positive trend from the last several quarters.

Our new more competitive Medicare supplement plans continue to perform well with customers, and we have experienced the balancing of our Medicare product sales as a result. As a reminder, we offer 2 types of Medicare products in our portfolio. Medicare supplement products that we manufacture and a broad offering of third-party Medicare Advantage and Part D prescription drug plans for which we collect ease.

By offering both Medicare Supplement and Medicare Advantage products, we can provide more coverage options for customers to choose from and respond immediately to shifts in the health care preferences of our middle-market consumers.

Supplemental health plans were up 12%, the fourth consecutive quarter of double-digit growth. This product continues to benefit from growth in our producing agent comp.

Annuity account values were up 4% year-over-year. Annuity collected premiums for the quarter were the third highest ever posted for this product line, which is significant given the tough comparable. Persistency remains within expected ranges. Additionally, we have experienced a modest shift towards fixed interest plans due to the higher interest rate environment.

As noted previously, our captive distribution model and the long-term relationships our agents build with customers provide stability to this block.

Client assets in brokerage and advisory were up 14% year-over-year to a new high of \$2.9 billion. We increased net inflows in new accounts, which strengthened the quarter strong returns that our customers captured from improved market conditions in the quarter.

When combined with our annuity account values, our clients entrust us with more than \$14 billion of their assets. Our diverse and integrated distribution model remains a differentiator for CNO. We marry a virtual connection with our established in-person agent force who serve more than 230 communities nationwide. We market nationally and complete the last mile of the sale locally.

The strength of our agent force remains a key enabler of sales growth in the Consumer division. Agent recruiting is a leading indicator of future sales growth, and we were very pleased with our performance in the quarter. Recruiting was up 27%, which represents our best overall recruiting quarter since late 2020. This recruiting momentum has led to growth in our producing agent count, which was up 8%.

Based on this trend, we expect the agent force to continue to grow in the second half of the year. Veteran agent retention and productivity remain strong. Our registered agent count increased 3% from prior year. As economic uncertainty persists, demand for securities professionals remain high. This is especially critical for middle income consumers. Expanding our bench of registered agents is key to how we serve our middle market with both insurance and financial protection products.

Turning to Slide 7 and our Worksite division performance. Life and Health insurance sales were up 31% this quarter, exceeding prepandemic sales levels for the first time. This is the ninth consecutive quarter of worksite insurance sales growth. As a reminder, immediately prior to the onset of the pandemic, our Worksite business posted record sales production with 8 consecutive quarters of growth prior to the first quarter of 2020. Achieving this result marks a significant milestone in the return to growth trajectory for our Worksite division. Importantly, sales from new broker relationships positively contributed to sales performance in the quarter. Expanding our broker sales pipeline remains a strategic initiative for both our national and regional worksite markets.

We recently launched several pilots designed to increase broker engagement. We are very pleased with the early results. Key indicators of the health of our Worksite business continue to trend positively in the quarter. Retention of our existing employer customers was strong, employee persistency within these employer groups was stable and collected premiums within these employer groups was also stable. Total producing agent counts were up 32% and agent productivity remained strong.

Among our first year agents, producing agent counts were up 94% and productivity in that cohort was up 64%. As a reminder, agents must reach a certain level of production to be considered a producing agent. Our successful worksite agent referral program and enhancements to our new agent onboarding program are credited for driving these meaningful agent productivity gains.

Product refreshment remains an important component to accelerating worksite growth. In early June, we introduced a new accident insurance product available for both individual and worksite sales. Sales in the first month are off to a solid start, representing nearly 10% of the total NAP in the quarter.

As I shared last quarter, we are squarely focused on 3 strategic work site growth priorities as we look to the second half of 2023 and beyond. Continuing the integration of our worksite capabilities under a single optimized brand; expanding distribution capabilities in our national and regional employer markets through new broker relationships and strategic alliances and accelerating momentum in agent recruiting to grow producing agent counts.

And with that, I'll turn it over to Paul.

Paul Harrington McDonough - CNO Financial Group, Inc. - CFO & Executive VP

Thanks, Gary, and good morning, everyone. Turning to the financial highlights on Slide 8. Operating earnings in the period reflect continued growth in average net insurance liabilities, driven by growth of the business, continued improvement in the earned yield on the assets supporting those liabilities, driven by improved new money rates in the last several quarters that have exceeded the portfolio yield and continued disciplined expense management. We expect these favorable trends to continue.

Offsetting these favorable dynamics in the quarter were elevated health claims impacting our long-term care and net sub margins, favorable LDTI related impacts in the prior year period in our life margin and lower variable income from alternative investments and from calling prepayment activity in our bond portfolio.

From a capital perspective, we generated strong free cash flow in the period, completed \$30 million of share repurchases and increased both RBC and holdco liquidity as compared to March 31, all of which reflects continued capital management discipline.

Turning to Slide 9. Insurance product margin was down in the quarter, which was driven by a number of factors. First, as just mentioned, we experienced elevated health claims in our long-term care and Medicare supplement businesses.

It's worth noting that even at these levels, we are not running unfavorable to pre-COVID claims experience. Even so, we expect these claims to moderate in the second half of the year based on leading indicators and as a result, did not change any of our go-forward assumptions.

Second, in 2Q of last year, there was a larger than typical reduction in claim liabilities in our traditional life business due to the work down of the backlog of claims that were in the course of settlement. The claim payments also had an approximately \$10 million positive impact on the change in the liability for future policy benefits calculated under LDTI. This is the primary driver of the negative variance in 2Q '23 compared to 2Q '22. The margin in the current period is more reflective of our run rate expectations.

And third, the margin in our annuities -- in our other annuities business varies based on our mortality experience, which was more favorable in the prior year period. There's no change to the favorable long-term view we have on any of our product lines.

Turning to Slide 10. The new money raised in the quarter was 6.32%, up from 5.53% in the prior year period and largely flat versus 6.34% in the first quarter of this year. This is the fifth consecutive quarter with new money rates in excess of the average yield on our allocated investments, which increased to 4.65% in the quarter, up 11 basis points year-over-year and 3 basis points sequentially.

This marks the fourth quarter of sequential improvement in the second quarter of year-over-year improvement in net yield. The increase in yield along with growth in net insurance liabilities and the assets supporting them, contributed to a 5.4% growth in net investment income allocated to products.

Investment income not allocated to products fell in the quarter, driven by a decline in income from alternative investments and from call and prepayment activity. These sources of income are by definition, volatile, particularly income from alternative investments, which was above our long-term run rate expectation in 2Q of last year and below that expectation in 2Q of this year.

Our new investments in the quarter comprised approximately \$590 million of assets with an average rating of AA- and an average duration of just under 7 years. Our new investments are summarized in more detail on Slides 21 and 22 of the presentation.

Turning to Slide 11. Approximately 97% of our fixed maturity portfolio at quarter end was investment-grade rated with an average rating of A, reflecting our up-in-quality actions over the past several quarters.

In the last 12 months, the allocation to single A rated or higher securities is up 470 basis points. The BBB allocation is down 330 basis points, and the high-yield allocation is down 140 basis points.

Last quarter, we shared additional disclosures on our commercial real estate portfolio. This asset class continues to perform well. We have, again, included metrics on these investments in Slides 23 and 24 of the presentation.

Turning to Slide 12. We ended the quarter with a consolidated RBC ratio of 386% and Holdco liquidity of \$176 million. Both improved relative to March 31 of this year and both comfortably above our targets of 375% and \$150 million.

A portion of the improved capital position relates to a sale leaseback program, which resulted in a \$43 million reduction in non-admitted assets and corresponding increase in total adjusted capital in the quarter.

Turning to Slide 13. Based on the lower alts in the first half, an elevated long-term care in Med Sup claims in 2Q, we are adjusting our full year 2023 operating earnings per share forecast to a range of \$2.65 to \$2.85. There is no change to our other earnings-related guidance. So we still expect our full year expense ratio to be in the range of 19.0% to 19.4% and our effective tax rate in the range of 23.0% to 24.8%.

With respect to capital, we affirm our target consolidated RBC ratio of 325% and minimum Holdco liquidity of \$150 million and our target leverage of 25% to 28%. We are revising our expected full year excess cash flow to the Holdco to a range of \$180 million to \$200 million, so raising the low end of the range by \$10 million with no change to the high end of the range.

Regarding our planned formation of a captive Bermuda reinsurance company in the third quarter of this year, we continue to work through the regulatory approval process, and we'll provide an update once that process has been completed and the treaty has been initiated.

And with that, I'll turn it back to Gary.

Gary Chandru Bhojwani - CNO Financial Group, Inc. - CEO & Director

Thanks, Paul. Last month, we published our fourth annual corporate social responsibility report, which highlighted 6 focus areas that are most relevant to our business and the recent progress on our commitments.

As I've shared before, the core of our business is helping people. It's [what we do] every day. For that reason, corporate responsibility is embedded in our day-to-day operations. Our success as a company is tied directly to the well-being of our associates, agents, customers and communities. I invite you to download our report to learn more about our program and commitments. You can find it on our website.

As we look to the second half of 2023, I am pleased by our continued strong sales production and the progress we've made against our strategic priorities. Our capital position, liquidity and the cash flow generating company -- power of the company remain robust.

We thank you for your support of and interest in CNO Financial Group. We will now open it up for questions. Operator?

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) So our first question comes from the line of Erik Bass of Autonomous.

Erik James Bass - Autonomous Research US LP - Senior Analyst of US Life Insurance

Can you provide some more color on what drove the elevated LTC Med subclaims this quarter? And what the leading indicators you're seeing that give you confidence that health and LTC claims are going to return to a more normal level next quarter?

Paul Harrington McDonough - CNO Financial Group, Inc. - CFO & Executive VP

Sure. Erik, it's Paul. So the driver was simply an increase in new claimants in the quarter. And the leading indicators that we're referring to are number 1, just the fact that we're sitting here on August 1. And so we've seen July plans first month of the quarter, and those have trended favorably in both long-term care and MedSup.

And then with respect to long-term care, we have a leading indicator that's fairly reliable in the form of calls that come into our customer service call center from policyholders or from family members of policyholders inquiring about how to make a claim as they contemplate making a claim at some point in the future. And those calls are trending favorably as well.

Erik James Bass - Autonomous Research US LP - Senior Analyst of US Life Insurance

Got it. That's helpful. I mean, I guess, what caused the surprise this quarter then? Because I would have thought you would see similar leading indicators that would have flagged kind of an increase in potential activity.

Paul Harrington McDonough - CNO Financial Group, Inc. - CFO & Executive VP

Yes. I think it's a question, Erik, as to when we have the leading indicator and the reliance that we put on it. So we're sharing current information, and we're always incorporating into the financials that we're filing each quarter, the most recent information and our best estimate. I guess I'd emphasize one other thing, Erik, and that is the long-term care, obviously, and really all of our products are a long duration in nature. And I think it's a little bit dangerous to read too much into a single quarter.

I will say that long-term care has performed extremely well over the last few years. I would emphasize that even in the second quarter where claims were a bit elevated relative to our expectations. They were still below pre-COVID levels and our view of the economics of this business over the long term haven't changed. We continue to feel really good about the business.

Erik James Bass - Autonomous Research US LP - Senior Analyst of US Life Insurance

It makes sense. And if I could just sneak in one more. I just want to follow up on your comments on the Bermuda captive, should we take that 3Q close is still realistic and still the goal? And is there any change in your view on freeing up the \$150 million to \$200 million of capital in that inception?

Gary Chandru Bhojwani - CNO Financial Group, Inc. - CEO & Director

Erik, this is Gary. I'll take that one. Just a couple of comments I'd like to make about Bermuda. There's no question in our mind. Number 1, there's no question in our mind that participating in Bermuda and being a member of that community would be good for CNO. We believe in the value of it, which is why we continue to work on it. So we absolutely see that there's value for CNO and our shareholders.

Second, we're eager to join the Bermuda community. We think we would be good citizens. And we think we have value to add in being part of that community.

And third, being good citizens and being valuable in that community also means that we respect the deliberations and the process that the Bermuda Monetary Authority is going through. We full well expect a successful conclusion. We certainly hope for that, and we believe we've met all the requirements, but we want to be respectful of their process, their deliberations, their analysis and which is why you're seeing us refrain from making specific comments.

We think that's the best course of action at the time. We want to make sure we give the Bermuda Monetary Authority every opportunity to do their job and continue to interact with us in good faith, which they have. We've enjoyed the interactions and we continue to feel very good about them. But we're going to refrain from any more specific commentary until they complete their deliberations.

Operator

Our next question comes from the line of John Barnidge of Piper Sandler.

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

My question is around expenses. Were there any onetime expenses in the first half of the year related to Bermuda that persists in the balance of '23? Or maybe asked differently, they will no longer be present that we should be thinking about run rate?

Paul Harrington McDonough - *CNO Financial Group, Inc. - CFO & Executive VP*

John, it's Paul. Certainly, we've had some expenses relating to the work we're doing to form the Bermuda company and that would not persist in terms of start-up expenses. Having said that, there are run rate expenses associated with operating in Bermuda that will be incremental to the run rate prior to Bermuda. And that's incorporated in our expense ratio guidance for the full year.

This isn't directly response to your question, but in the same sort of context, I would say that in the first half, there were somewhat elevated litigation expenses, particularly related to the ongoing breach with litigation, which we expect will diminish in the second half.

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

Great. And then my next question will be on product. Any new product introduction we should be thinking about for the pipeline for that, the commentary on like 60% under that simplified life. Can you maybe talk about, is that going to have increased conversion from velocity of processing versus paper and non-accelerated underwriting and under penetrated market.

Gary Chandru Bhojwani - *CNO Financial Group, Inc. - CEO & Director*

John, this is Gary. Thanks for the question. We believe, and I think this is a commercial wisdom in the industry that quicker decisioning usually results in better sales because you have a reduced likelihood of buyers or mores or something like that. And it also serves to help you a little bit from a competitive perspective. So we look forward to continuing to deploy these types of processes and technologies to continue to make the decision faster.

And then, of course, there's efficiencies on our end, right? The more we can do this in an automated way and the less we can handle paper, the better our expense ratios are going to be. So there's a win-win all the way around if we can continue to bring more and more of our business under this type of automation decision process. So that's definitely the goal.

It takes time. We've got systems that have been around for a long, long time. So it takes time to do this, but we remain focused on that. So that's kind of on the process, if you will. I don't know if I can call that a new product, but that's certainly a new process and we'll continue to do that.

In terms of product, you saw the results on our Medicare Supplement. We're very pleased with how that continues to play. We think there's continued opportunity there for us to continue to grow that. We've got some new products we've launched in worksite. So we'll continue to do that.

I think if we can do 1 or 2 new products a year, I would be thrilled with that. We have to navigate that as we move forward. But I've been pretty pleased with the work that our folks have done and we'll continue to do that so you should look -- you should expect to see us continuing to do that.

And I point to some of the sales and recruitment success we've had directly emanating from that. More agents just want to join us when they know we remain committed to building more products and improving our processes and more consumers get interested. So we'll continue to do that, absolutely.

Operator

Our next question comes from the line of Ryan Krueger of Stifel.

Ryan Krueger

On long-term care, was there any commonality in the higher new claims incidents in the quarter, whether it be by issue year or any commonality or did you just see a broad-based increase in incidents this quarter?

Paul Harrington McDonough - CNO Financial Group, Inc. - CFO & Executive VP

Ryan, it's Paul. So nothing specific that was called out as we went through the analysis internally. So I think it's fair to say it was more broadly based.

Gary Chandru Bhojwani - CNO Financial Group, Inc. - CEO & Director

Ryan, if I could just interject. I just want to, I guess, draw more attention to a comment Paul made earlier about the importance of looking at this type of claims data on a much broader perspective. Honestly, we just don't get that worked up on a quarter-to-quarter movement. It just doesn't tell us that much. It takes much more time, and we're not seeing anything here that gives us that kind of concern.

I just want to emphasize the long-term nature of claims that I understand that when we release quarterly results, people want to try and extrapolate that or at least understand if there's something to be extrapolated. We just don't see it. We don't see it.

Ryan Krueger

Understood. And then a separate question on fee income and fee revenue. Can you just give us a little more perspective on the seasonality there and kind of what we should expect from I think, 2Q and 3Q are typically lower than the first quarter and the fourth quarter, but does any help you could provide there?

Paul Harrington McDonough - CNO Financial Group, Inc. - CFO & Executive VP

Brian, it's Paul again. That's exactly right. The bigger quarters are the first and the fourth quarters. And that's because this is primarily driven by the sale of MedAdvantage product. So that's really the first point.

The second point is that we've had some mix shift away from MedAdvantage back to that MedSup in the wake of introducing the new MedSup product in the second half of last year. So in the quarter, that was another contributor.

Operator

Our next question comes from the line of Wilma Burdis of Raymond James.

Wilma Carter Jackson Burdis - *Raymond James & Associates, Inc., Research Division - Research Analyst*

I guess first question, how do you think about pricing for Medicare supplement heading into 2024? And if Medicare Advantage writers end up increasing their pricing for 2024, would that benefit your revenue given you sell third-party products there?

Gary Chandru Bhojwani - *CNO Financial Group, Inc. - CEO & Director*

Yes. I was just -- I'll answer it at a high level and then Paul can fill in the mine.

Because we participate on a fee basis, if the pricing goes up, we would have a benefit. I think that part is clear. In terms of what the likelihood of that is, I don't know for you I'm not sure if that's where your question was going or...

Paul Harrington McDonough - *CNO Financial Group, Inc. - CFO & Executive VP*

Gary, maybe I could provide some perspective that I think would be responsive warm up. So in terms of how we think about pricing, MedSup in '24, I think that was the question. We'll do what we always do, which is to look at the claims experience and that informs the rate increases that we filed around this time of year, every year.

One of the nice things about this product is we have this annual opportunity. This year, there's an additional dynamic I think, that's fair to reference and that's the approval of Legembi for Medicare claims, the Alzheimer's treatment. It's guesswork at this point to know how that will impact claims. But I think directionally, it will and so will incorporate some assumption about that in our rate filing for '24.

Wilma Carter Jackson Burdis - *Raymond James & Associates, Inc., Research Division - Research Analyst*

And maybe just give a little bit of color on -- it seems like you don't want to comment too much on Bermuda right now, given you're in active discussions, but assuming you free up the \$150 million to \$200 million of capital, could you talk about some of the uses there?

Paul Harrington McDonough - *CNO Financial Group, Inc. - CFO & Executive VP*

Sure. So we'll deploy excess capital the way that we always have, which is to try to put it to its highest and best use. Historically, on the margin that has resulted in share repurchase so I suspect at least some portion of that gets deployed in that way.

Operator

Our next question comes from the line of Scott Heleniak of RBC Capital.

Scott Gregory Heleniak - *RBC Capital Markets, Research Division - Assistant VP*

I just had a quick question on the guidance. It sounds like it mostly reflects lower VII assumptions. But is there anything more we should be thinking about expected run rates of the different segments, life, annuity health in the back half of the year? I know you mentioned that Health claim should settle down versus the first half of the year. But is there anything else that we should be considering or looking at in the different segment units versus first half?

Paul Harrington McDonough - CNO Financial Group, Inc. - CFO & Executive VP

Sure. Scott, it's Paul. So let me provide -- let me try to provide some perspective on the second half forecast, which, together with the first half actual result in our updated EPS guidance.

So for sure, the biggest sort of dynamic is income from alts, which were quite low in the first half, and we're assuming we'll refer to more of a long-term run rate expectation in the second half, which we think is a reasonable expectation for a couple of reasons.

Number 1, we report all on a 1-quarter lag, as you know. And if you consider that equities have generally performed well recently, credit spreads have tightened. Volatility has been down, all of which would typically bode well for our alternative portfolio.

In addition, some of the recent underperformance relates to some idiosyncratic results in our portfolio, mostly driven by investments that performed exceptionally well in 2021 and 2022 and gave some of that back in recent quarters.

We have taken some actions to reduce further exposure in those areas. So we think we're positioned well to perform well in the second half. So that's the first thing.

The second thing is health claims, as you mentioned and that we've talked about. The third is in our Life margin. The first quarter is typically seasonally lower. So the second half should look better than the first half. In that context, and also our advertising expense is typically higher in the first half than in the second half, and you should expect that to continue this year.

Fourth, I would reference the fact that our net investment income allocated to products has trended favorably and you should expect that to continue as the yield on the allocated portfolio continues to improve based on continued higher new money rates and that will benefit margin across all of our products.

And then finally, on expenses, you should expect those to continue to trend lower. And that's based on some timing related to run rate expenses. I mentioned the elevated litigation expense mostly related to Beach Road in the first half that we expect to be lower in the second half. And then just in general, continued expense discipline. So it's really the combination of all of those things that inform our outlook for the second half and the full year.

Scott Gregory Heleniak - RBC Capital Markets, Research Division - Assistant VP

Okay. That's really helpful detail. So on the VI, it sounds like based on your commentary, you're feeling a lot better and what you're going to see at least Q3 versus Q2 on the reported number at all. I don't expect the number, but it's -- you are expecting sequential improvement, I would assume?

Eric Ronald Johnson - CNO Financial Group, Inc. - CIO

Yes. This is Eric Johnson. Let me jump in here. And certainly, in the second quarter, it was up from the first quarter, still not where I want it to be over the longer haul. Yes, there's going to be variation from quarter-to-quarter what was -- what trended positively in the quarter with real estate and infrastructure, hedge funds and PE private credit, which, as Paul said, has always been a very strong performer for us.

We had a bit of a tougher quarter surprisingly because that's an area that we've done historically done extremely well in. In some respects, our old portfolio has aspects of a -- it's a little bit nontraditional. It has aspects of a carry book, which means it our allocations that throw off very healthy cash dividends. And yet in a sense, are -- have been effect of the last several quarters by the slope of the yield curve and by the Fed action has caused the underlying asset revaluation.

Now that's in late innings which supports Paul's earlier comments about probably having a better second half of the year there. But throwing off the portfolio throwing off cash dividends pretty much on time and on schedule and actually the higher end of our expectations. So yes, I think we're in the kind of the later innings of the last of what's been not the easiest several quarters for all, but feel good about what's ahead.

And last comment, we've -- our total general account book yield is up 12, 13 basis points year-to-date. And one of my favorite CEOs as we saying about basis points and billions. And I think that that will serve us very well, as Paul said, looking forward. So I hope that has been helpful.

Scott Gregory Heleniak - *RBC Capital Markets, Research Division - Assistant VP*

Yes. Okay. Got it. Yes, last one, just switching a little bit. Just wondering if you could talk about some of the mortality trends you're seeing in the life book versus this quarter versus some of the recent quarterly run rates? And how is that comparing to pre-COVID mortality trends that you were seeing on the life side? Can you -- you can share more stuff?

Paul Harrington McDonough - *CNO Financial Group, Inc. - CFO & Executive VP*

Sure. The mortality assumption in our life products is that it's a little bit worse than pre-COVID and the context for that is the assumption that COVID has translated to an endemic state, which still creates some amount of excess mortality. So that's the basic assumption that hasn't changed since we most recently revisited it back in the fourth quarter of last year. Our experience in the second quarter was a little bit better than that, not materially, but to the plus side of our long-term expectations.

Operator

Our next question comes from the line of Suneet Kamath of Jefferies.

Suneet Laxman L. Kamath - *Jefferies LLC, Research Division - Equity Analyst*

I wanted to start with the health margin. I hear you on the long-term care, and we have to look at this over a long period of time. But just on the MedSup piece, it does look like that margin was -- has been low now for lower than kind of where it's been for 2 quarters in a row. And we did note that some of the health insurance companies have talked about elevated utilization amongst older age individuals.

So I just wanted to unpack that a little bit, seeing if you guys are being impacted by what some of the HMO companies are talking about and what gets that kind of back on track.

Paul Harrington McDonough - *CNO Financial Group, Inc. - CFO & Executive VP*

Sure. So yes, so we had some somewhat elevated claims activity in MedSup in the quarter, likely driven by some of the stuff that other companies have talked about. But I would -- and based on July experience, we see that moderating.

The other point I would make is that our MedSup book has been declining in size as a result of the decline in MedSup sales over the last few years. And that's begun to turn around with the new product we introduced late last year, but nevertheless, for the last couple of years, including through the second quarter, that explains more than half of the decline in margin quarter-over-quarter.

Suneet Laxman L. Kamath - *Jefferies LLC, Research Division - Equity Analyst*

Okay. Got it. And then I guess on the expense ratio. I think it's been running close to 20% in the first half. And so if you're sticking with your kind of '19 to 19.4%, that would mean something closer to 18, I guess, for the second half. And is that the right way to think about it? And then are there

sort of discrete things that you're doing to bring the expense ratio down. I get that some of the Beechwood stuff will fall off, but it seems like it's got to be a little bit better than full year guidance just to kind of get you to where you want to land.

Paul Harrington McDonough - CNO Financial Group, Inc. - CFO & Executive VP

Yes. So all of those observations are absolutely correct. We nevertheless feel good about the forecast for the reasons that I've talked about. The expenses are trending favorably. They were lower this quarter than they were a year ago. And there's some timing first half versus second half just on run rate expenses. And then the other things that I mentioned, we expect will drive us to an expense ratio for the full year in the range in our outlook.

Suneet Laxman L. Kamath - Jefferies LLC, Research Division - Equity Analyst

Got it. And if I could just sneak one more in. Just on the investment losses, I think they've been traveling around \$20 million for the past 2 quarters. Just wondering what's going on there. Is that something where you're selling out losses to go up in quality? Or what's just -- if you could unpack that a little bit, that would be helpful.

Paul Harrington McDonough - CNO Financial Group, Inc. - CFO & Executive VP

Yes, I can make just a couple of comments. And then Eric, I'd turn it over to you. So the biggest driver of the realized loss in the quarter was we sold some First Republic bonds. But Eric, if you want to provide some more color beyond that?

Eric Ronald Johnson - CNO Financial Group, Inc. - CIO

Yes. Taking the first half of the year as a whole, the -- there's about 3 factors that work. One would be, as Paul mentioned, about -- probably about 30%, 35% would relate to the First Republic that's in the review mirror. Another 30%, 35% would relate to some up in yield and up in quality opportunities that we had, particularly during the first quarter, where we were able to rotate up in quality and up in book yield at the same time, where the kind of the payback period on the loss would be 2, 3, 4 years of future investment.

So pretty quick return on the loss out of corporates into agencies was very easily done during the early part of the year. And then the residual, like 20%, 30% would relate basically just to kind of the ongoing kind of portfolio pruning that you're doing all the time to pick away at migrating credits that feels good about, as you did say you about them. So one part opportunistic, one part of problem and one part just normal maintenance would be a way of thinking about it.

Operator

Our final question comes from the line of Tom Gallagher of Evercore.

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

Paul, I hear what you said about looking at July data being favorable for long-term care claims. But even with the 2Q being elevated, I think you said it's still below pre-pandemic levels. And so I guess my question is, isn't it reasonable to assume you're more likely to revert to this level or higher, if I think about steady state over the next several quarters? Or do you think there's some reason why you'll have a permanent benefit on the loss ratio with this product?

Paul Harrington McDonough - CNO Financial Group, Inc. - CFO & Executive VP

Tom, it's Paul. So I think reasonable people could certainly disagree on this. We're all sort of just making guesses. But our view is that the claims will settle in over the long term. It's something better than pre-COVID just because I think some behaviors have actually changed in terms of how people interact with the health care system.

So that's a long-term view. We'll see if it proves correct or not. And then in the near term, just the near-term indicators would suggest that the third quarter will look a lot better than the second quarter.

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

Got you. And from the standpoint of the changes you made with the new LDTI accounting, does that contemplate a longer-term improvement in long-term care claim trends as well? Or do you -- is the current reserving using similar assumptions as pre-pandemic levels?

Paul Harrington McDonough - CNO Financial Group, Inc. - CFO & Executive VP

So we revisit our assumptions in the normal course in the fourth quarter [underage] GAAP under -- and under LDTI, and we didn't make any significant change in assumptions in the most recent fourth quarter.

I'm looking at Karen DeToro on the screen here. Karen, you agree with that? Yes. Does that make sense, Tom? Does that answer your question? Maybe I'm not understanding your question.

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

No. That does. No, yes. So long term, you haven't really changed the long-term assumptions. So to the extent that if there were to be favorability that should be, we'll call it, an earnings benefit on a go-forward basis. Is that fair, Paul?

Paul Harrington McDonough - CNO Financial Group, Inc. - CFO & Executive VP

Well, we didn't significantly change the assumptions in the fourth quarter of this year as compared to the fourth quarter of last year. I think our assumptions are a little bit different now than they were before March of 2020.

Karen Jeannine DeToro - CNO Financial Group, Inc. - Chief Actuary

Right. I just add that [the normal] process of reviewing those assumptions in the fourth quarter this year, we don't have any evidence to date that at this point, would cause us to believe that a change is warranted, but we'll do that as part of our normal annual review.

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

Right. Okay. And one final one, if I could. Just at a curiosity, the -- now when I look at your guidance, it implies \$0.80 to \$0.90 per quarter of earnings for the back half of the year. Was that in line with what it was before this quarter and when you put out the guidance initially, was there always an expectation of much stronger earnings in the second half of the year to that magnitude? Or has that changed? Are you assuming some mean reversion benefit now that you weren't assuming before?

Paul Harrington McDonough - CNO Financial Group, Inc. - CFO & Executive VP

Yes. Tom, that's a good question. Actually, our plan for the second half has not changed materially. Some puts and takes across different things, but in total, essentially the same from an earnings per share perspective. So really, all of the drivers to the change are what we experienced in the first half, largely the alts in the first and the second quarter and then long-term care primarily and a little bit of MedSup in the second quarter.

Operator

As there are no additional questions right at this time I'd like to turn the conference call back over to Adam Auvil for closing remarks.

Adam Auvil - CNO Financial Group, Inc. - VP of Corporate Development

Thank you, Operator, and thank you all for participating in today's call. Please reach out to Investor Relations team if you have any further questions. Have a great rest of your day.

Operator

Ladies and gentlemen, this concludes today's CNO Financial Group Second Quarter 2023 Earnings Call. Thank you for joining. You may now disconnect your lines.

DISCLAIMER

Refinitiv reserves the right to make changes to documents, content, or other information on this web site without obligation to notify any person of such changes.

In the conference calls upon which Event Transcripts are based, companies may make projections or other forward-looking statements regarding a variety of items. Such forward-looking statements are based upon current expectations and involve risks and uncertainties. Actual results may differ materially from those stated in any forward-looking statement based on a number of important factors and risks, which are more specifically identified in the companies' most recent SEC filings. Although the companies may indicate and believe that the assumptions underlying the forward-looking statements are reasonable, any of the assumptions could prove inaccurate or incorrect and, therefore, there can be no assurance that the results contemplated in the forward-looking statements will be realized.

THE INFORMATION CONTAINED IN EVENT TRANSCRIPTS IS A TEXTUAL REPRESENTATION OF THE APPLICABLE COMPANY'S CONFERENCE CALL AND WHILE EFFORTS ARE MADE TO PROVIDE AN ACCURATE TRANSCRIPTION, THERE MAY BE MATERIAL ERRORS, OMISSIONS, OR INACCURACIES IN THE REPORTING OF THE SUBSTANCE OF THE CONFERENCE CALLS. IN NO WAY DOES REFINITIV OR THE APPLICABLE COMPANY ASSUME ANY RESPONSIBILITY FOR ANY INVESTMENT OR OTHER DECISIONS MADE BASED UPON THE INFORMATION PROVIDED ON THIS WEB SITE OR IN ANY EVENT TRANSCRIPT. USERS ARE ADVISED TO REVIEW THE APPLICABLE COMPANY'S CONFERENCE CALL ITSELF AND THE APPLICABLE COMPANY'S SEC FILINGS BEFORE MAKING ANY INVESTMENT OR OTHER DECISIONS.

©2023, Refinitiv. All Rights Reserved.