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PRESENTATION

Operator

Greetings, and welcome to the Industrial Alliance Second Quarter Earnings Results conference call. (Operator Instructions) As a reminder, this conference is being recorded on Thursday, July 30, 2020.

I would now like to turn the conference over to Marie-Annick Bonneau, Head of Investor Relations. Please go ahead.

Marie-Annick Bonneau - *iA Financial Corporation Inc. - Head of IR*

Good afternoon, and welcome to our second quarter conference call. All our Q2 documents, including press release, slides for this conference call, MD&A and supplementary information package are posted in the Investor Relations section of our website at ia.ca. This conference call is open to the financial community, the media and the public. I remind you that the question period is reserved for financial analysts. A recording of this call will be available for 1 week starting this evening. The archived webcast will be available for 90 days, and a transcript will be available on our website in the next week.

I draw your attention to the forward-looking statements at the end of the slide package. A detailed discussion of the company's risk is provided in our 2019 MD&A available on SEDAR and on our website with an update in our Q1 2020 MD&A.

I will now turn the call over to Denis Ricard, President and CEO.



Denis Ricard - iA Financial Corporation Inc. - CEO, President & Director

Good afternoon, everyone, and thank you for joining us on this call today. I will first introduce everyone attending the call on behalf of IA. First is Jacques Potvin, Chief Actuary and CFO; Mike Stickney, Chief Growth Officer; Alain Bergeron, Chief Investment Officer; Renée Laflamme, in charge of Individual Insurance and Annuities; Sean O'Brien, responsible of our Mutual Fund business and Wealth Management Distribution Affiliates. And we have 2 new seasoned executive with us, François Blais, in charge of our Dealer Services, Special Market Solutions and iA Auto and Home. François has been in the business for over 16 years. And finally, Éric Jobin, responsible for our Group Businesses. And Éric has been in the business for 29 years.

This morning, we released our results for the second quarter of 2020, which was also the first full quarter since the COVID-19 pandemic began. From the very beginning of this pandemic, our priority has been the health and safety of our employees and advisers as well as continuing to serve our clients well. The deployment of our business continuity plan has enabled our employees and advisers to pursue their activities supported by safe and secure processes. They are, thus, able to provide clients with the service level similar to the level prior to the pandemic.

In addition, during these difficult times, companies like ours have an important social role to play, and we have continued to provide relief for our customers and to support our communities in various manners. From the first weeks of the pandemic in March, we implemented a variety of relief measures for our clients, including deferral of payment on premiums, loans and leases. In addition, during the lockdown, we granted rebates on premiums for an approximate amount of \$20 million. Overall, more than 235,000 clients have taken advantage of our relief measures.

Now moving to the results. I'm quite pleased with the results that were reported this morning. Indeed, these results, which would have been good in normal times, are excellent in the current context. They are a clear demonstration of the strength and the resiliency of our business model.

As shown on Slide 3, our reported EPS for the quarter was \$1.71 and core EPS was \$1.57. When compared to the second quarter of 2019, a quarter in which we achieved very good results, reported EPS is up 1% year-over-year. In the current context, we have every reason to be satisfied.

As for capital, we concluded the quarter with a solvency ratio of 124%, well above our target range, and with a leverage ratio of 25.6%. Factors supporting our strong results include favorable policyholder experience and macroeconomic variations. It is also important to underline the quality of our investment portfolio and strategies.

While market volatility continued to be high during the quarter, our hedging program performed well with no major loss. Also, in most lines of business, our sales were quite solid, with results superior to Q2 2019. This shows the adaptability of our distribution networks as well as the high performance of the technological tools that would provide to support our sales force while working at a distance.

I now want to comment on the acquisition of IAS, which was concluded at the end of May. IAS is a strategic addition to iA Financial Group. For more than 20 years, iA have been active in the Canadian dealer services business, and we are now the leader in this market. In January 2018, with the acquisition of DAC, we decided to enter the American vehicle warranty market. Our solid results with this division over the past 2 years demonstrate our capacity to grow rapidly in this market.

But to achieve our ambition and meet our growth objectives, we needed to be a bigger player to have a more meaningful footprint. With the acquisition of IAS, one of the largest independent solution provider in the U.S. vehicle warranty market, we now have a leading presence, which will serve our long-term growth strategy.

In the shorter term, in the context of the current pandemic, we had to review our projections and our integration plan. Although they operate in the same market, IAS revenue stream is complementary, and that's exactly the same as DAC. For example, as IAS is more present in the new car dealerships, its sales were more impacted by the pandemic than DAC.

With that in mind, we decided to accelerate the integration. The pandemic also created opportunities in the sense that the widespread telework made us realize that there are more potential efficiency synergies on the corporate side than initially envisioned. So far, the integration is progressing well, and we are still confident that this acquisition will enable us to rapidly create value for our shareholders.

In the short term, contribution to earnings will be lower than initially planned. Nevertheless, excluding acquisition and integration costs, IAS should be accretive starting in 2020. More importantly, in the longer term, with this acquisition, we are now better positioned to pursue our growth in this fragmented market and to seize opportunities that are likely to occur in the aftermath of the current crisis.

I will conclude my remarks by mentioning that although our second quarter results are strong, the pandemic is not over and a lot of uncertainty remains. In the coming months, our priority will continue to be the health and safety of our clients, employees and distributors, support for our communities and preserving iA financial strength. We will continue to manage the company in a sound and prudent manner with emphasis on the best interest of our clients and shareholders.

I will now let Mike comment on business growth. Following Mike's remarks, Jacques will give us an update on the earnings and capital.

On that note, I'll pass it over to Mike.

Michael Stickney - iA Financial Corporation Inc. - Executive VP & Chief Growth Officer

Thank you, Denis, and good afternoon, everyone. I will start my remarks with a few comments on the IAS acquisition. As mentioned by Denis, we were happy to conclude this acquisition in May. The integration process started very quickly following the closing of the acquisition, and some synergies are already materializing. For example, the proportion of IAS' business insured by DAC is increasing more quickly than expected. Integration will continue over the next quarters. One of our priorities will be to maximize both revenues and efficiency synergies, mainly with DAC and IAS, but also with iA's corporate services.

Now looking at the second quarter sales results, please refer to Slide 5, which shows solid results from many of our business units. In Individual Insurance, our distribution networks are fully operational at a distance. From the beginning of the pandemic, we were confident that our technological tools would facilitate our advisers' transition to remote distribution. This is now confirmed by our strong sales results during the second quarter. Indeed, Individual Insurance sales in Q2 totaled nearly \$53 million, which constitutes a 10% year-over-year increase. With the addition in June of a PAR policy to widen our product offering, sales should remain strong in the coming quarters.

For Individual Wealth Management, starting with guaranteed products, sales continue to be excellent, totaling nearly \$175 million.

Seg fund sales were also impressive with gross sales of almost \$600 million, up 10% year-over-year. Noteworthy in May, for the first time ever, the company ranked first in the industry in gross seg fund sales. We also remain #1 in the Canadian industry with net sales totaling \$417 million for the quarter.

In perspective, for both Individual Insurance and individual seg funds, we are of the view that our high-performance digital platform has been a key factor in supporting our advisers in selling at a distance.

Now moving to mutual funds. Gross sales were up 4% year-over-year at more than \$504 million. Net sales recorded inflows of nearly \$50 million and were, therefore, positive for the first time since Q1 of 2018. This performance was supported by strong growth from our affiliate networks.

Now looking at Group businesses. In the Employee Plans division, clients adapted quickly to the new reality, and sales totaled nearly \$23 million, significantly up from \$4 million in the same quarter last year.

In the Dealer Services division, total sales of \$189.5 million were down 30% from 2019 as they were slowed by the temporary closure of car dealerships due to the pandemic.

As for our sales in the Special Market Solutions division, they totaled \$44.9 million, down from \$61.1 million a year earlier. This decrease is largely explained by the drop in travel insurance sales.

Lastly, in Group Savings and Retirement, sales were up slightly from last year. In our U.S. operations, sales momentum remains strong in Individual Insurance as they increased by 33% year-over-year. In Dealer Services in the U.S., sales decreased by 7%, which is primarily due to the pandemic. Furthermore, IAS sales in the first half of the year have been tracking reasonably close to U.S. retail car sales, which have slowed down because of the pandemic.

Finally, in our P&C affiliate, iA Auto and Home, direct written premium continued their steady growth and increased by 11% year-over-year. Overall, these sales results pushed premium deposits to nearly \$2.7 billion in the second quarter, which represents an increase of 5% year-over-year.

Assets under management and administration decreased by 2% year-over-year, primarily due to the decline in equity markets at the end of March and to the sale of iA Investment Council at the beginning of June.

Now moving to Slide 6, you will find a revised assessment of our sales expectation for the remainder of 2020. You will notice that the outlook is generally better than our initial assessment in May. Indeed, for many business units, sales are expected to be normal or close to normal. This assessment is based on the current state of the pandemic and may vary depending on how the situation evolves.

For businesses more directly impacted by the pandemic, like Dealer Services and Special Market Solutions, we expect sales to return to the levels seen in early 2020 as we emerge from the pandemic.

To conclude, I want to underline that our strong sales in Q2, especially in the individual sectors, are the outcome of our successful distribution strategy. This shows that our distribution networks are valuable assets and that, with the support of high-performance IT tools, they are key to our success in this new reality.

I will now turn it over to Jacques to comment on Q2 earnings.

Jacques Potvin - iA Financial Corporation Inc. - Executive VP, CFO & Chief Actuary

Thank you, Mike, and good afternoon, everyone. We are very happy with our profitability and capital strength in the second quarter.

Starting on Slide 7, reported EPS was \$1.71, which is higher than a year ago when earnings were especially strong. On a core basis, excluding mainly macroeconomic gains, EPS was also solid at \$1.57. Year-to-date, core EPS is up 3% year-over-year.

Now looking to items of note on Slide 8. Policyholder experience was quite favorable in almost all our business units. It was particularly positive at iA Auto and Home and in our group businesses. Macroeconomic variations also had a positive net impact of \$0.10 EPS on the results despite a \$0.07 EPS loss from our hedging program.

There were still high market volatilities during the second quarter, and our hedging program performed well in protecting our balance sheet. The hedging loss that was incurred is consistent with the volatility risk indicator that we provided in May.

Strain produced a \$0.05 EPS loss, which can be explained by the combination of the first quarter drop in interest rates and of a less favorable sales mix. Income on capital also generated a \$0.05 EPS loss, mainly due to a provision for default for a corporate bond in the aerospace sector.

On the tax side, the 2019 true-up was the main factor supporting the gain of \$0.04 EPS.

Finally, the gain from the sale of iA Investment Council was mostly offset by acquisition and integration costs for recent acquisition with a resulting \$0.02 noncore EPS gain.

Now looking at policyholder experience on Slide 9. Each business unit had experienced close to or better than expectations. Starting with Individual Insurance, overall experience was as expected. Adverse mortality and morbidity experience was offset by favorable lapse experience and lower

expenses. Individual Wealth Management reported a result close to expectations as lower income from our distribution affiliates was partly offset by favorable longevity in single premium annuities.

Our Group Insurance sector recorded a gain of \$0.05 EPS. This gain mainly comes from the Dealer Service division where experience was favorable as a result of lower P&C claims. Experience was in line with expectations in Employee Plans, while it was slightly favorable in Special Market Solutions.

Group Savings and Retirement reported a gain of \$0.03 EPS from several positive sources such as favorable launch activity, lower expenses and higher income on assets under administration. U.S. operations reported experience slightly above expectations. More specifically, in the Individual Insurance division, experience was generally as expected as favorable lapse experience was offset by negative mortality. As for the Dealer Services division, lower expenses resulted in a small gain.

Finally, experience at iA Auto and Home was once again much better than expected with a gain of \$0.07 EPS, due mainly to lower claims. It is noteworthy that positive experience generated by lower claims due to the pandemic was completely offset by significant premium refunds paid to clients. Therefore, we consider the net experience gain at iA Auto and Home to be unrelated to the pandemic.

Please refer to Slide 11 for our capital position. Following the acquisition of IAS, our solvency ratio continues to stand strong and well above our target range of 110% to 116%. As of June 30, 2020, our solvency ratio was 124%. In addition to macroeconomic variations and the sale of iA Investment Counsel, organic capital generation of about \$70 million explains the increase in our solvency ratio during Q2.

With this robust solvency ratio of 124%, combined with a leverage ratio of 25.6% and with our high-quality investment portfolio, the company continues to be in a strong financial position.

During the second quarter, the impact of the pandemic was generally less severe than our initial assessment. As for the rest of the year, it will, of course, depend on how the situation evolves. Based on the current state of the pandemic, Slide 13 presents how we now expect COVID-19 to impact earnings for the remainder of 2020.

During the first half of the year, due to the lower interest rate, strain had a negative impact on our earnings. Following management actions, namely repricing of certain products, strain should improve in the coming quarters. As for experience, pandemic impacts are lower than initially anticipated. More importantly, we expect COVID-19-related loss to be non-recurrent once the pandemic is over.

Overall, we now believe that our 2020 results could be better than we anticipated when we disclosed our first quarter results. This assessment obviously depends on how things will evolve and on whether or not there will be a second wave.

I will conclude by saying that the Q2 results clearly show that iA is strong and resilient and that our earning power remains significant even in a difficult environment.

Operator, we will now take questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from Steve Theriault with Eight Capital.



Steve Theriault - *Eight Capital, Research Division - Principal & Head of Research*

If I could start with a question on IAS. I hear you saying today that we'll see positive accretion in '20 and '21. But looking out a little bit further, you're suggesting that the outlook is unchanged. And when I look back into my notes, I see about \$0.40 of accretion in 2022 and greater than \$0.50 in 2023. Can we still assume that's reasonable guidance as we look out a couple of years?

Denis Ricard - *iA Financial Corporation Inc. - CEO, President & Director*

Sorry. It's Denis here. Listen, with the COVID right now, the time that we're looking at is not as far as that. So we concentrated, let's say, on this year and next year to see to what extent our projections or the revised projections were in line in the original ones, and that's why we came up with this kind of revision this time.

Now we haven't gone, let's say, further than that. I mean, we don't see actually at this point why we would not post-COVID be able to generate that kind of accretiveness. So -- I mean, I would say, the reasons why we were having those results in 2022 and on, they are still there, for example, this is a market where it's quite fragmented. We know that we're going to, at some point, consolidate the market. So we believe that it's still possible to get there.

Steve Theriault - *Eight Capital, Research Division - Principal & Head of Research*

And you talked about accelerating the integration. Are as a result, are integration costs going to be any higher either as a result of that acceleration or just due to the pandemic generally?

Jacques Potvin - *iA Financial Corporation Inc. - Executive VP, CFO & Chief Actuary*

Jacques speaking. They could be slightly higher because we've decided to integrate, I would say, on the corporate side more system. But at the end of the day, the benefit will be higher as well.

Steve Theriault - *Eight Capital, Research Division - Principal & Head of Research*

Okay. And then the other thing for me was just on the impaired investments. And probably for you again, Jacques. How much of the rise in the gross impaired investments was due to the aerospace bond you made mention of in your release? And I guess, broadly, can you provide any kind of outlook around credit impairments looking out over the near term?

Denis Ricard - *iA Financial Corporation Inc. - CEO, President & Director*

Yes. I think I'm going to ask Alain to answer that one.

Alain Bergeron - *iA Financial Corporation Inc. - Executive VP & CIO*

Sure. In terms of the first question, which was about how much was related to the aerospace sector, it's actually -- it's all related to that.

In terms of future potential impairment, I mean, what you have now is our best estimate of what we see. But of course, we recognize that the economy is in a fluid situation. We have \$14 billion of corporate bond portfolio. On the other hand, it's important to recognize that this is a fairly high-quality portfolio in terms of its corporate assets. So I think this is our best guess at this stage.

Operator

Our next question comes from Meny Grauman with Scotiabank.

Meny Grauman - Scotiabank Global Banking and Markets, Research Division - MD of Financial Services Equity Research & Analyst

First question just on the organic capital generation, \$70 million, so effectively double what we saw in Q1. I'm wondering how sustainable that is. I know you talked -- you mentioned that it's sensitive to the second wave. But assuming that we don't get that, is that sort of a sustainable quarterly rate, in your view?

Jacques Potvin - iA Financial Corporation Inc. - Executive VP, CFO & Chief Actuary

Jacques speaking. I would say so far, so good when I look forward. Of course, with COVID, we never know what may happen with the second wave. But when I look at the different lines of business, all the experience, there has been some pluses, some minuses. But overall, it's better than what we anticipated at the beginning. And I would say the market is adjusting. And if I take, for example, let's say, in Group Insurance for LTD, we were expecting much worse experience than that. And we know that now even if people are working from home, we know that different professionals are able to return, people are able to work, which is great.

So I'm expecting actually that it will continue according to what we showed on the slide. So this is our best view as of today.

Meny Grauman - Scotiabank Global Banking and Markets, Research Division - MD of Financial Services Equity Research & Analyst

And then just going back to IAS. I would have thought -- my understanding was that auto sales on both sides of the border are recovering faster than what anyone expected. So in terms of your commentary, I'm just wondering what you're seeing that is different from what we knew in Q1. I'm wondering, is it related to the uptick in COVID in the U.S.? Are you seeing an impact of that in particular?

Denis Ricard - iA Financial Corporation Inc. - CEO, President & Director

Well, obviously, we follow very carefully the car sales on both side of the border. And I'm sure, Mike, that you have a lot of information on that question.

Michael Stickney - iA Financial Corporation Inc. - Executive VP & Chief Growth Officer

Sure. It's -- yes. And things are a little different between the 2 countries. I'll talk about the U.S., obviously, because IAS is kind of central. There's been a nice recovery from April and May. I mean there was -- sales were off quite a bit, 40%, 50%, 60% through April and May. And so they're coming back. But for the year, kind of taking a longer-term view here, and expect that overall retail car sales will be up 10% to 15% for the year. And our -- when I look at our revenues on that business, we're sort of lining up very well with those kind of numbers. So that's our expectation for the year. And obviously, that creates some headwinds on profits for the year, too.

Meny Grauman - Scotiabank Global Banking and Markets, Research Division - MD of Financial Services Equity Research & Analyst

And do you expect -- given the business mix difference between DAC and IAS, do you expect DAC to actually perform better than IAS through this pandemic?

Michael Stickney - iA Financial Corporation Inc. - Executive VP & Chief Growth Officer

That's what we're seeing through the first half. DAC has a higher percentage of used car sales. And they've been less affected if we follow data in any kind of detail. Used car sales have been holding up better. So we've got that trend working for us as well.

Operator

Our next question comes from Gabriel Dechaine with National Bank Financial.

Gabriel Dechaine - National Bank Financial, Inc., Research Division - Analyst

Just to follow up on this IAS stuff. I think 2021, excluding integration costs, was looking like \$0.27 of accretion. You're saying it's lower now? Can you quantify how much lower?

Jacques Potvin - iA Financial Corporation Inc. - Executive VP, CFO & Chief Actuary

Gabriel, Jacques speaking. I will say something. It would be probably between \$0.05 and \$0.10 lower than that \$0.27. That will be our guess today.

Gabriel Dechaine - National Bank Financial, Inc., Research Division - Analyst

Okay. And it sounds like the lower sales volumes are the primary driver, and I get that. Is there any -- are there any implications of this accretion change on the goodwill? We've seen goodwill write-downs in the past, also reflective of sales volume trend and just wondering how that looks for you guys.

Jacques Potvin - iA Financial Corporation Inc. - Executive VP, CFO & Chief Actuary

Okay. Jacques speaking, again. About goodwill, we had to do an impairment test at the initial purchase price allocation, and there's none to be added at all. No impairment sign here at all. And for the foreseeable future, there's none that we see as well because of what Denis mentioned in his allocation that, we will push harder for synergies to compensate for that short term, I would say, short-term lower profit.

And we mentioned it at the acquisition. It's a growth story, and Denis mentioned it earlier in an answer as well. We have the financial strength to go through that crisis. And there is a lot of moment -- in that fragmented market and we really believe that we will thrive post COVID in that market.

Denis Ricard - iA Financial Corporation Inc. - CEO, President & Director

In a nutshell, it's Denis, with the proper initiatives that we are contemplating right now. We believe that over a very short period of time, the economic value that we measured on that business will be maintained.

Gabriel Dechaine - National Bank Financial, Inc., Research Division - Analyst

All right. Moving on to the, I guess, actuarial side of things. On Slide 13, you talked about all the elements of the business that are going better or worse than you expected at the start of the year. And then in the noncore category, you talked about a potential URR charge at the end of the year, not surprising given the moving rates. But just trying to quantify about the 10 or 15 or 20 basis point change that you have in mind now.

And then not related to rates, but mortality, I believe 2 quarters in a row now that we have negative mortality experience in Individual Insurance. Maybe there are different factors behind each outcome. But is that a potential source of an actuarial review or focus?

Jacques Potvin - *iA Financial Corporation Inc. - Executive VP, CFO & Chief Actuary*

Okay. Jacques, again. You will guess, the appointed actuary. About URR, I would say that this quarter, there continued to be discussion at the Canadian Institute of Actuaries. And I would get more information later this year, but it seems that it's a higher possibility, probability that there will be something coming in 2021. And we have the tradition to do something ahead of time, so I will certainly do something at year-end when I will get more comfort that it's coming. And above that, I have no issue whatsoever because Alain's team has been great at doing management action. And I have plenty of management action to be able to compensate for that.

As for mortality, when I look at the mortality right now, for sure, it's really too early to tell because we would complete our experience study. And because of COVID, I will try to complete my experience study sooner than Q4. Actually, I have a great idea in Q3 how it's going there.

But when I look at the experience of Q2, most of the experience -- negative experience in mortality is due to COVID. So almost all of it is coming from COVID. So -- and in the U.S., we know that it's coming from COVID as well. So -- and it's important to mention that in the review of assumption, we need to factor that -- there what's permanent, not what's temporary. So we're working on that. And I will be able to give you more flavor in Q3.

Gabriel Dechaine - *National Bank Financial, Inc., Research Division - Analyst*

Okay. And my last one, Denis and Jacques, you both sound more upbeat about the earnings outlook this year, and you've itemized all the items there. Does that commentary apply to internal capital generation as well? Because Q1, we had \$35 million, this quarter \$70 million, which is more on track with what you targeted in normal times. Or are we looking at this quarter as more representative?

Jacques Potvin - *iA Financial Corporation Inc. - Executive VP, CFO & Chief Actuary*

For sure. And if you recall well Q1, the hedging program we had, we suffered a very big loss, and it ate the profit that we usually get. So you're totally right, Gabriel. We're in the ballpark right now in Q2.

Operator

Our next question comes from Doug Young with Desjardins Capital Markets.

Doug Young - *Desjardins Securities Inc., Research Division - Diversified Financials and Insurance Analyst*

Just wanted to see, going back to the credit impact of \$0.04, I don't know if this is for Alain or for Jacques, was that related to an increase in the asset default provision? Or was that an impairment? Or -- can you describe that? Because I did see your asset default provision did increase almost \$43 million sequentially. And I'm just wondering, of that \$43 million, how much related to bond downgrades? And was that \$0.04 embedded in that?

Jacques Potvin - *iA Financial Corporation Inc. - Executive VP, CFO & Chief Actuary*

Doug, Jacques speaking. I don't know the \$43 million you're referring to, but it's an impairment provision we took for a specific private placement, private debt that we have in a company that is working. Actually, the business model of that company is renting airplanes to airlines. So that's what we did.

Doug Young - *Desjardins Securities Inc., Research Division - Diversified Financials and Insurance Analyst*

So that's an impairment provision. That's not necessarily related to a downgrade of a fixed income investment.

Jacques Potvin - *iA Financial Corporation Inc. - Executive VP, CFO & Chief Actuary*

Exactly. Yes, exactly.

Doug Young - *Desjardins Securities Inc., Research Division - Diversified Financials and Insurance Analyst*

And then if you look, in the Rolling 9, it's on page 17 at the very bottom, you talked about the provisions for potential losses and fixed income security is contained in the actuarial policy liabilities. And if you look sequentially, it increased \$43 million. And so what my question is, I get the \$0.04, and that's related to impairment. Was there other impacts on your results that you didn't break out necessarily that were a result of negative credit migration, so bond downgrades?

Jacques Potvin - *iA Financial Corporation Inc. - Executive VP, CFO & Chief Actuary*

Okay. Okay. Now I know the number you're speaking about. So when we have a default, the default will affect the loss. There will be a loss in our gain and loss analysis. So you will see it. As for downgrade, those ones -- they will be dealt with my business change at the end of the year. And the way we're working, we've done that for many years. We have management actions that are positive items, that are pluses and there are movement of interest rate, could be movement of IRR -- of URR. Now IRR no longer matter because we have derisked that one, but that could be downgrade as well.

And the important thing every quarter, when I table my reserve, when I calculate my reserve, I make sure that I'm positive on that account which I am at the end of Q2, I was also at the end of Q1. So that's the way it affects our results.

Denis Ricard - *iA Financial Corporation Inc. - CEO, President & Director*

So in a nutshell, provided that you have enough management action, downgrades don't affect our results.

Jacques Potvin - *iA Financial Corporation Inc. - Executive VP, CFO & Chief Actuary*

For the quarter, no.

Doug Young - *Desjardins Securities Inc., Research Division - Diversified Financials and Insurance Analyst*

So it doesn't affect -- so this is part of your year-end? And so when you look at the downgrades that have occurred so far and then you look at all the moving pieces, you're not necessarily concerned that there's going to be a bigger credit hit as a result of those downgrades? Is that a fair way to kind of think of it?

Jacques Potvin - *iA Financial Corporation Inc. - Executive VP, CFO & Chief Actuary*

Actually, the one that we know today, I have enough management action to cover them. And I have even enough management action to cover downgrades coming down the road in Q3 and Q4. But when I say that, just -- we need to be cautious here. If a second wave hit at one point in time, I cannot guess, I don't know what would be. But like Alain mentioned earlier, we have a defensive portfolio, and we're quite pleased with the quality of our portfolio. So when I look at that, I will say I'm very fine with my reserve.

Doug Young - *Desjardins Securities Inc., Research Division - Diversified Financials and Insurance Analyst*

Okay. And then tying that back to Slide 13, and I read that the noncore and I read the reserve section of that, the IRR, URR and you really haven't identified anything of materiality that really would have a huge impact on your year-end reserves.

So based on what you see today, like is it fair to just assume when I read that, that you don't anticipate that there's going to be any huge impact or big impact, negative or positive, from your year-end actuarial reserve, with the caveat being that we're in a fluid situation and there has been -- you're still looking at the mortality side. But is that a fair thing to think about where you stand today? As you look forward, you don't anticipate any big year-end impact?

Jacques Potvin - *iA Financial Corporation Inc. - Executive VP, CFO & Chief Actuary*

It's a fair statement, knowing that it's fluid.

Doug Young - *Desjardins Securities Inc., Research Division - Diversified Financials and Insurance Analyst*

Okay. And then just lastly, expected profit was down. You kind of identified the IAS acquisition as being one impact, and then the market movements has been the other impact. And you described what the IAS impact was. But if you were to back out those 2 items, would expected profit have been up year-over-year?

Jacques Potvin - *iA Financial Corporation Inc. - Executive VP, CFO & Chief Actuary*

Yes. Actually, yes. If we look at that, the expected profit overall, the 2 items you just mentioned, because 10% on the growth of EPS and there are other factors as well. And one factor was mentioned when we tabled our guidance in February. It's related to the fact that we mentioned that we are investing in technology. And I would say that the good sales results we had in Q2 are already due to, I would say, investment in those good technology to support the distribution.

There were some expenses as well. We mentioned cybersecurity as one place we are spending more to protect the company as well as IFRS 17 that was another project on which we are spending more this year. It will be the same next year compared to the previous year.

Another element also explaining the expected -- lower growth on expected profit on in-force is PPI. If you recall well, in Q3 last year, there was goodwill write-down. It was related to the fact that we were expecting less revenue. And this one was a 1% impact on the growth of expected profit on in-force.

Operator

Our next question comes from Scott Chan with Canaccord Genuity.

Scott Chan - *Canaccord Genuity Corp., Research Division - Director of Research of Financials & Financial Services Analyst*

Just on your investment portfolio, and I guess management's decision to exit residential mortgages and focus on the multi-residential and non-residential markets. What were the factors coming up that decision? Is it more risk, more yield? Or is there anything else there?

Denis Ricard - *iA Financial Corporation Inc. - CEO, President & Director*

Yes. The line was not very clear. So hopefully, I got your question right. I think this question is about the -- your question is about the residential mortgage exit that we made?

Scott Chan - *Canaccord Genuity Corp., Research Division - Director of Research of Financials & Financial Services Analyst*

That's right.

Denis Ricard - *iA Financial Corporation Inc. - CEO, President & Director*

Okay. Good. Listen, this business -- I mean, we've been in the business of residential mortgage for a long, long time. Because at first it fit some of the needs we had in our balance sheet to back some of the liabilities that we had. And over the years, basically, we came up with the conclusion that there were other assets that would be better to match those liabilities. So that business in itself was kind of orphan. There was no strategic link to any other businesses in our portfolio. We needed to invest in technology to bring that up to a higher level, and it's a business, as you know, that we are competing against like the banks and credit unions.

So it was pretty easy for us to -- when we looked at our strategic initiative, that they did not fit where we wanted to go. So it has nothing to do with, let's say, capital or things like that. It's more like it's no strategic fit. And it was not very big, so it doesn't have that much impact overall.

Scott Chan - *Canaccord Genuity Corp., Research Division - Director of Research of Financials & Financial Services Analyst*

Is it 7% of your portfolio? Is that what I guess from last quarter? Or am I looking at that wrong?

Denis Ricard - *iA Financial Corporation Inc. - CEO, President & Director*

I just don't understand your question. Sorry, I don't hear you.

Scott Chan - *Canaccord Genuity Corp., Research Division - Director of Research of Financials & Financial Services Analyst*

You said the exposure is not that big. Is it -- was it 7% of your portfolio?

Denis Ricard - *iA Financial Corporation Inc. - CEO, President & Director*

Well, in fact, it was a bit a mix of a lot of the businesses -- some of the businesses that we have. I mean we were directly getting the profit out of that business -- other businesses. We were only the administrators. So from my recollection, it's -- I think it's a bit more than \$1 billion of business that was really on our book that we had profit from, let's say, net interest margin. The rest was just a business that we administered for a third-party. So nothing really big.

Scott Chan - *Canaccord Genuity Corp., Research Division - Director of Research of Financials & Financial Services Analyst*

Okay. I got it. And just on the mutual fund side, nice quarter. And you talked about the affiliates benefiting. Is there an update on kind of that target to convert AUA to AUM? Because I'm assuming that was the biggest benefit that helped this quarter and maybe the industry a little bit as well.

Denis Ricard - *iA Financial Corporation Inc. - CEO, President & Director*

Yes. Maybe, Sean, you want to comment on the success we have with affiliates?



Sean O'Brien - *iA Financial Corporation Inc. - EVP of Wealth Management*

Yes. It's just, thanks, Denis. Yes. So the affiliate channel has really proven to be kind of a positive buffer, I think, during tough times. There's support really, I think, that came through with the positive net sales in the past quarter. And the outlook is it'll probably continue to be positive going forward. So it's a good trend from the affiliate group.

Operator

Our next question comes from Paul Holden with CIBC World Markets.

Paul Holden - *CIBC Capital Markets, Research Division - Executive Director of Institutional Equity Research*

So 2 questions to start related to capital. I want to get a picture on to what extent organic capital generation might change with the IAS transaction. I understand profitability might be lower than you originally assumed. But obviously, there's still going to spin-off of capital. So I want to get a little bit of a better picture there.

And then two, now that you've already kind of rebuilt a bit more of a capital buffer, how are you thinking about that with respect to capital intentions in the, let's call it, over the next 12 months?

Jacques Potvin - *iA Financial Corporation Inc. - Executive VP, CFO & Chief Actuary*

Okay. Jacques speaking. I will answer to the first part, and Denis will answer the second question, Paul. So you're totally right that, with IAS, we expect more profit. And that profit will flow directly as organic capital, so will help to build capital even more faster than before. So you're totally right on that.

Denis Ricard - *iA Financial Corporation Inc. - CEO, President & Director*

Regarding capital, Paul, interesting question. Obviously, with IAS, the IAS acquisition, and you heard a lot about integration. Our focus right now is really on the integration, not only the business people in the U.S., but also the Canadian people here that have support functions and where we see some good synergies between Canada and U.S. So our focus is there right now.

You should not expect, let's say, significant acquisitions in the short term. It's not -- I mean, when I look at where the capital will go over the next 12 to 24 months, certainly, building up capital is certainly the priority right now, even though we are very comfortable with where we are. There is not much, I think, we want to do in the short term in terms of deploying it for acquisition. And once that we get comfortable enough with the integration, how it goes and the results that we get out of it, then obviously, the second phase will start and we'll be a bit more active on the acquisition side.

Paul Holden - *CIBC Capital Markets, Research Division - Executive Director of Institutional Equity Research*

Okay. Final question from me is with respect to the Individual Insurance sales in Canada. I think a surprisingly good quarter, at least from my perspective. I'm surprised to see a positive number there. Maybe flesh out a little bit more what you would attribute that to? Is that strong digital channels or were the traditional channels? Did those hold up better than expected?

And second part of the question, you introduced a PAR product that came late in the quarter. Maybe kind of a perspective on how much that might be able to influence sales growth in coming quarters?

Denis Ricard - *iA Financial Corporation Inc. - CEO, President & Director*

That's for you, Renée.

Renée Laflamme - *iA Financial Corporation Inc. - Executive VP of Individual Insurance, Savings & Retirement*

Yes. Thank you very much. Yes, we're very pleased with the results as well. Of course, we had a good month of June. We had a good quarter. I would say 2 things. We had a few larger cases than usual, and we also strongly believe that our technology has made the difference. We were up and running for selling at distance very quickly in all our distribution channel. So that's good.

You will recall as well that we have launched in February a Universal Life YRT product, which has had great success. As you mentioned, we launched our PAR product in mid-June. So we don't see the effects of the PAR product right now in our Q2 results. However, I can say that we're pleased with the reaction of the marketplace. There's been a good adoption by all distribution network. It's a little bit too early to comment on trend and volume expectations, but we're happy with the launch of the PAR.

Denis Ricard - *iA Financial Corporation Inc. - CEO, President & Director*

Maybe yes, I just want to add something. I mean, iA has always been recognized as a provider or an insurer of covering the family market, the mass market, although we are still present, we are present in higher amounts as well. But I mean, for the most part, we are very present on the family market and the mass market or the mid-market, whatever you want to call it.

And so in a situation as we are right now, combined with the technology that Renée was mentioning, obviously, it created kind of an advantage for our business model. When we see that our business model is resilient, it's a combination of the fact that we are presenting all distribution, we have the right technology and also we target the right market.

Operator

Our next question comes from Tom MacKinnon with BMO Capital Markets.

Tom MacKinnon - *BMO Capital Markets Equity Research - MD & Analyst*

First question just with respect to the -- I think you mentioned you got lower revenue from PPI in terms of lower commissions. And then I think you also said you had lower distribution income from affiliates as well in the Individual Wealth section. Now that doesn't seem to be consistent with the company that as well in the press release notes better-than-expected sales in Individual Insurance and some pretty good growth in terms of even gross sales, if you look in the Individual Wealth.

So can you explain why you had pretty good sales if you're not collecting -- you're not getting very much -- you're getting lower-than-expected revenue from these distribution arrangements that you have? And I have a follow-up.

Jacques Potvin - *iA Financial Corporation Inc. - Executive VP, CFO & Chief Actuary*

Okay. On that one, Tom, Jacques speaking, I would say that when we make those comments in regard of the revenue of those distributors, not the revenue of the manufacturer. And we always compare our sales with an amount considering growth. If we take, for example, the affiliate, when we table the guidance, for sure, we wanted to grow that business. And with the COVID-19, it's tough to recruit new people that is part of our strategy.



As for PPI, I would say the results, they are lower than what we expected at the beginning of the year, but it's related to commission. And the fact, if you recall well in Q1, sales were quite down. And PPI, part of their business are in big cases. And it was impossible to close those big cases because the paramedical firm was closed and we were not able to get the underwriting information also.

Tom MacKinnon - *BMO Capital Markets Equity Research - MD & Analyst*

Okay. So it sounds like your sales were good, but other companies didn't have as good as sales. So that's why it hurts -- that's why your revenue was lower than anticipated from these affiliated companies. Is that the correct way of looking at it?

Jacques Potvin - *iA Financial Corporation Inc. - Executive VP, CFO & Chief Actuary*

Yes.

Tom MacKinnon - *BMO Capital Markets Equity Research - MD & Analyst*

Okay. Second is really on IAS. And Renée, you may have mentioned this, but you look at U.S. dealers, sales were down 7%. If I look in Canadian, in which you've gotten Dealer Services, yet you have lower claims associated with the COVID environment. Yet you're saying now that second half of 2020 and into 2021, you're going to have lower-than-expected earnings accretion as a result of IAS.

With Dealer Services sales really not that off -- really not off that much, a pretty good used car market and claims lower, what is it that you're seeing that's driving down your expectations with this? I believe you had mentioned probably about maybe 2 months ago that you expected 2021 to be generally in line with your original guidance. So maybe what has changed just in the last couple of months with respect to your thoughts on IAS?

Denis Ricard - *iA Financial Corporation Inc. - CEO, President & Director*

Yes. Well, a lot has changed, especially in the U.S. And I think I will let somebody who lives in the U.S. comment on that one because there's a lot that has changed since the last time we made some kind of guidance on that business.

Michael Stickney - *iA Financial Corporation Inc. - Executive VP & Chief Growth Officer*

Okay. Yes. Thanks, Denis. Yes, the benefit hindsight, we're probably a little too optimistic around the end of May about the auto environment in the U.S. The trend in the U.S. on COVID was fairly positive up to and near the end of May. And obviously, things have deteriorated a lot as things opened up, especially in the Southern states, which we have a fair amount of business there.

And then secondly, going on to your sort of question about comparing, we've gotten pretty good profit with weaker sales in Canada. In the U.S., it works differently. A lot of the business is reinsured to the dealers. The dealers have their own reinsurance company. So we have a higher percentage of essentially what is fee income. And it's just very dependent on car sales and the fee income. So we don't get the recovery on, say, lower warranty claims, that sort of thing that we're seeing in Canada.

Tom MacKinnon - *BMO Capital Markets Equity Research - MD & Analyst*

Okay. And then finally, just with respect to the URR, I think, Jacques, you said there's been some sort of discussions with the Canadian Institute of Actuaries, and that seems like a possibility of maybe something coming down the pipe in 2021. Your comments about perhaps moving at the end of 2020, is that just -- I know you've moved ahead of the industry in the past. Is that just what you -- you would do that just because you have the capability and you want to try to stay ahead of the curve with respect to that? and how much do you think that potential URR move to be, 10, 15 points that you're going to be making?



Jacques Potvin - *iA Financial Corporation Inc. - Executive VP, CFO & Chief Actuary*

Yes. Actually, it's our tradition to have a strong balance sheet and be well positioned with a conservative reserve. So I will, I really did continue that tradition.

In regards of the metric, it's tough today to say, but I will expect something between 10 and 20 bps. And I have, like I said earlier, I have the management action to be able to cover it.

Tom MacKinnon - *BMO Capital Markets Equity Research - MD & Analyst*

Okay. So that's the move that you're thinking that you might make, 10 to 20 bps by the end of 2020. (inaudible) from CIA, correct?

Jacques Potvin - *iA Financial Corporation Inc. - Executive VP, CFO & Chief Actuary*

Yes. Actually, I will have more information in Q4 than right now. So what I mentioned earlier is that when I listen to the different discussion about that, I think the probability is higher than when I spoke at the conference call in Q1. So I think the possibility is higher, probability is higher today than it was before. And I think that the metric around those numbers, and I have the management action to be able to cover it. So that's really where I'm sitting right now. But I will decide that in Q4.

Tom MacKinnon - *BMO Capital Markets Equity Research - MD & Analyst*

And that's more of your decision. As it stands right now, you see the CIA perhaps doing something coming more in 2021?

Jacques Potvin - *iA Financial Corporation Inc. - Executive VP, CFO & Chief Actuary*

Yes. Actually, Tom, on that one, last time the CIA moved, it was supposed to be the last move because of IFRS 17 that was coming down the pipe, okay? So that was what behind the fact that we thought that we will be down with the change in URR. But the fact that IFRS 17 has been delayed by another year, it just opened a window and the CIA is thinking about that today. The fact that we have another year to do with the current accounting regime. So that's why and interest rates are low. So that's the situation we're in.

Tom MacKinnon - *BMO Capital Markets Equity Research - MD & Analyst*

Yes. As I understood, they weren't going to do some -- IFRS 17 was 2022, and they weren't going to do anything until then. It's been pushed out to 2023. So as you mentioned, there's perhaps a window to do one intermittent move before moving to IFRS 17. Do you think I have that right?

Jacques Potvin - *iA Financial Corporation Inc. - Executive VP, CFO & Chief Actuary*

Exactly. Yes.

Operator

Mr. Ricard, there are no further questions at this time. Please continue with your presentation or closing remarks.



Denis Ricard - *iA Financial Corporation Inc. - CEO, President & Director*

Thanks a lot. I would be brief here. Listen, COVID has hit, people were scared and people were very prudent in terms of their business. I think, right now, we realize that we are very strong, capital is strong, generation of capital. That's the first thing. Second is the resilience of our business growth model, driven by technology and distribution. And finally, we're committed to growth long term, and IAS really fit that purpose. So we are very, very optimistic that the IAS will be a platform for us to grow.

So with that said, thanks a lot. Have a great day.

Operator

That does conclude the conference call for today. We thank you for your participation and ask that you please disconnect your line. Have a great day, everyone.

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