# FIRST LIFE INSURANCE COMPANY 1997

## Chairman's Statement

First Life Insurance Company Ltd. is pleased to report continued and improved profitability in 1997, greater shareholder strength and increased operating efficiencies.

During the year under review, the Government of Jamaica was forced to intervene and commit in excess of $12 billion to support the major life insurance companies which faced insolvency. The performance of First Life in such a business environment was commendable and indicative of both the sound judgement of your Board of Directors and the capital strength of the company.

Group revenues for 1997 increased by 10.0% to $1,065.8 million (1996: $968.6 million). While the improvement in revenues was modest given the annual inflation rate of 9.2%, this was acceptable when viewed in the context of negative growth of 2.4% in the economy for the same period, substantially lower investment rates in 1997 compared to 1996 and a deliberate reduction in individual life sales by First Life.

Net profits for the year rose 21.7% to $161.8 million (1996: $132.9 million) yielding earnings per share of $0.54 (1996: $0.44). In recording this improved result, the three main profit centres of the Company, health insurance, life insurance and pension management, as well as the major subsidiaries Jamaica Property Co. Ltd. and Pan Caribbean Merchant Bank Ltd., all posted improved contributions. Consequently, the profit to revenue ratio increased to 15.2% from 13.7% in 1996.

This improved profitability in the company and its subsidiaries was in part due to a 3.7% reduction in management expenses, the result of a determined and prolonged effort to reduce overhead expenses and achieve acceptable levels of productivity within the Group. It is worthy of note that over the past three years First Life's management expenses have grown at an average annual rate of 9.3% compared to an average annual inflation rate of 16.9%. Lower individual life sales and a restructured agents' commission schedule dramatically reduced the Company's commission expenses and also contributed to the improved return on revenue.

First Life's balance sheet strengthened in 1997. Surplus investment assets in excess of policyholder liabilities grew by $64.7 million to $1,530 million (1996: $1,465.3 million). The quality of our investment assets also continued to improve with risk-free Government of Jamaica securities growing by over $290 million to account for 51% of the investment assets backing our policyholder liabilities (1996: 27%).

The Company's net worth improved by $81.7 million to $1,598.0 million (1996: $1,516.3 million). Net worth per share stood at $5.33 at the end of 1997.

**Employee Benefits**

Nineteen Hundred and Ninety Seven was another successful year for the Employee Benefits Division with all products showing growth in revenue and profit contributions.

In pursuing our commitment to making health insurance one of First Life's engines for future growth, we continued to focus on providing customers with superior quality service that is appropriately priced. The market reaction has been rewarding. Earned premiums from health insurance totalled $407.0 million (1996: $313.3 million), an increase of 29.9%. At the end of 1997 First Life held a 45% share of the health insurance market up from 34% in 1996.

Much of 1998 will be devoted to upgrading the computer system serving the company's group life and health operations. This will further improve our service quality by providing greater flexibility in product offerings and increased efficiency in processing of client information.

During the period under review, pension funds under management grew by 33.6% to $611.6 million (1996: $457.8 million). Growth was however, affected by an unusually high rate of refunds consequent on staff redundancies as our client companies intensified their restructuring efforts. Pension legislation which should have addressed this "leakage" caused by refunds, did not materialise in 1997.

The four pension fund pools administered by First Life, recorded an average yield of 20.0%, considerably better than inflation at 9.2%. This was achieved in spite of zero growth in the capital value of our real estate.

In 1997, despite the availability of very good equity buys on the stock market, real interest rates were very attractive and as many of the main players in the stock market were cash deficient, we judged it best to increase our share of investments in the money market, especially with Government instruments.
As a result, First Life's pension funds' portfolio at year end comprised 56.2% Government securities up from 39.8% in 1996.

Contracts have been signed for a new computerized pension administration system which is expected to considerably improve the management of company and employee information and report response times. We expect the programme to be completed by mid-1998.

Creditor Life premiums showed modest growth of 6.8% to record premiums of $34.5 million (1996: $32.3 million). Given the negative growth of the economy this is hardly a surprising result.

**Individual Life**

Shareholders will recall that in 1996 we reported efforts to contain the cost of writing new individual life business. These included the closure or merger of several branches, severe administrative and marketing cuts, a restructured commission scale and reduced agent count. The natural result of these changes were experienced in 1997.

New business annualized premium income in 1997 was dramatically reduced to $10.3 million (1996: $29.3 million). At the same time, because of the reduced front-end costs, the contribution of this division to First Life's profitability improved considerably to $4.8 million (1996: $8.4 million loss).

It is worthy of note that the entire industry wrote 22% less business in 1997 compared to 1996 with only two of the eight companies challenging this trend.

Notwithstanding our strategic decision not to grow this aspect of our business, First Life remains absolutely committed to its present and future policyholders. Indeed, the strength of our capital and the extent of our surplus assets should inspire policyholder confidence in the company's continuing stability.

**Investments**

Despite the magnitude of the financial crisis which faced our economy and the Government in 1997, some gains continued to be made towards macro-economic stability. Most importantly, inflation fell below double digits for the first time in six years to record 9.2%, considerably better than the 15.8% and 25.6% of the previous two years.

In accordance with the policy of adjusting yields on Government securities in relation to inflation, average Treasury Bill yields fell from 39% in 1996 to 22% in 1997. Nonetheless, this left considerable real rates of return on Government instruments. The fact that these securities continued to offer a better return to risk than equities or real estate was reflected in First Life's investment portfolio. The yield on average assets for 1997 was 22.3% or 12.5% points above inflation. Net investment income however fell to $99.1 million (1996: $122.2 million) in tandem with lower yields, even as investment assets grew by $205.3 million to $2,530.4 million (1996: $2,325.1 million).

During the year, the equity portfolio was realigned to include additional Blue-Chip stocks and a select few "recovery" equities whilst disposing of those with little near future upside potential. The 7.25% return on the equity portfolio did not match the performance of the stock market index of 18% and was due to the losses on disposal of some stocks. However, we feel confident that the portfolio is now positioned to out-perform the index in 1998.

**Property**

Except for the real estate investment of the pension funds, all the property holdings of First Life are concentrated in our subsidiary Jamaica Property Company Ltd. (JPCo.). This property portfolio largely comprises the surplus assets of First Life, that is, they are not required to back any policyholder liabilities. At December 1997, the properties were valued at over $1,600.0 million.

Given the weak performance of the economy, the continued down-sizing of businesses and additional commercial office space coming on the market in 1997, JPCo. performed creditably in posting flat revenues of $ 190.2 million (1996: $188.7 million).

At the close of the year JPCo.'s vacancy factor stood at 11.0% (1996: 12.3%). This improvement is attributable to the financial strength of our main tenants allowing them to withstand the harsh economic environment, to determined marketing efforts and continued strong demand for space in the company's shopping plazas. It is hoped that a number of initiatives taken in 1997 will bear fruit in 1998 and continue to improve the company's occupancy levels.

In 1997 further preparatory work was carried out for JPCo. to enter low-income housing development. During 1998 a building system considered flexible, modern and efficient, will be tested on a 144-unit project and if successful, a larger 450-unit project will be started.

**Banking and Investment Management**

The past year was one of consolidation for Pan Caribbean Merchant Bank (PCMB). Revenue of $59.6 million was flat (1996: $59.5 million) as was pre-tax profit of $7.7 million. PCMB's performance was respectably measured against the background of the massive bank failures and losses in 1997.

Consistent with our policy to limit the Bank's credit-related exposure in a deteriorating economy, 61% of revenues came from fee business as opposed to 36% in 1996. Bank assets and assets under management grew from $1.9 billion to $2.5 billion.

Pan Caribbean received a satisfactory rating for the second consecutive year since the introduction of written inspection reports from the Bank of Jamaica. In December 1997, Parliament approved an amendment to the Financial Institutions Act reducing from 180 days to 90 days, the maximum period a loan could be overdue before interest reversals and loss provisions are required. As PCMB had always employed a 90-day internal standard, the bank's results were unaffected by this amendment.

The Future

It seems clear that despite Government's projections for economic growth, it is likely that in 1998 the country will again experience economic contraction. In order to protect the gains made against inflation over the last two years and to finance the massive debt service occasioned by the FINSAC bail-outs of $73 billion, interest rates are set to remain fairly high in 1998 and Government's budget will inevitably reflect significant cost cuts and increased taxes. Economic growth is therefore hardly possible and indeed, further business failures are most likely before any upturn takes place.

In such an environment of inordinate business risk, the objectives of First Life and its subsidiaries for the near future are clear. First, we must continue to focus on preserving and improving the quality of our assets, particularly in the Bank and in the insurance and pension operations. Further, we intend to carefully explore new opportunities for profitable growth and importantly, we must ensure the proper and timely implementation of our investment in technology during 1998 as our future competitiveness depends on this.

In December 1997, Mr. James Morrison who served as Finance Director to First Life, resigned. I would like to record my sincere appreciation for the contribution he has made to the Company over the past five years. He continues to serve First Life as a member of the Board of Directors.

I would like to thank the Board of Directors for their continued wise counsel during 1997 and the management and staff for their unflinching commitment to First Life and its subsidiaries. Most of all I wish to express our appreciation to our thousands of customers for their continued loyalty and support.

Richard O. Byles, M.Sc.
Chairman