Torchmark Corporation

1st QUARTER 2013 CONFERENCE CALL

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Mike Majors

Thank you. Good morning everyone. Joining me today are Gary Coleman and Larry Hutchison, our Co-Chief Executive Officers, Frank Svoboda, our Chief Financial Officer, and Brian Mitchell, our General Counsel.

Some of our comments or answers to your questions may contain forward-looking statements that are provided for general guidance purposes only. Accordingly, please refer to our 2012 10-K and any subsequent forms 10-Q on file with the SEC.

I will now turn the call over to Gary Coleman.

Gary Coleman

Thank you Mike, and good morning everyone.

Net operating income for the First quarter was $132 million or $1.39 per share – a per share increase of 9% from a year ago. Net income for the quarter was $120 million or $1 .27 per share – also a 9% increase on a per share basis.

With fixed maturities at amortized cost, our return on equity for the first quarter was 15.6% and our book value per share was $35.98 – a 10% increase from a year ago. On a GAAP reported basis, with fixed maturities at market value, book value per share grew 20% to $45.88.

Life Insurance

In our life insurance operations, premium revenue grew 4% to $471 million and life underwriting margins increased 6% to $133 million. The growth in underwriting margin exceeded the premium growth due to lower amortization on our deferred acquisition costs.

The lower amortization rate is a result of improvements in persistency attributable to our ongoing conservation program, and is incorporated in our guidance for the full year.

Net life sales decreased 4% to $85 million.

On the health side, premium revenue, excluding Part D, increased 23% to $222 million and health underwriting margin grew 25% to $50 million. Improvement in the health underwriting margin was due primarily to the addition of Family Heritage.

Health sales increased 57% to $25 million.

I will now turn the call over to Larry Hutchison for his comments on the insurance operations.

Larry Hutchison

Thank you Gary

First, let's discuss American Income

At American Income, life premiums were up 9 percent to 174 million dollars and life underwriting margin was also up 7 percent to $56 million. Net life sales decreased 3 percent for the quarter to $38 million. The producing agent count at the end of the first quarter was 5,612, up 10 percent from a year ago and up 8 percent during the quarter.

While net sales decreased for the first quarter, we are very pleased overall with the progress that continues to be made at American Income. Trends have been very positive since the beginning of March and we expect sales growth for the full year 2013 to range from 10 to 14 percent.

Now, Direct Response

In our direct response operation at Globe Life, life premiums were up 4 percent to $168 million and life underwriting margin increased 1 percent to $39 million. Net life sales were down 5 percent to $37 million. However, the new business written in the first quarter of 2013 had a profit margin approximately 1-2 percent higher than the year-ago quarter.

Response rates continued to be lower than normal in the first quarter. We believe this is possibly due to the state of the economy, as the expiration of the payroll tax credit had a significant impact on the pocketbook of the families in our target market. However, as we indicated on our fourth quarter call, it's not unusual to have fluctuations like this from time to time in Direct Response.

Based on positive test results, we are confident that our 2013 initiatives will help increase response rates in 2013, and we still expect mid-single digit sales growth in 2013. These initiatives include rate adjustments and higher face amount offerings on adult products.

Now, Liberty National

At Liberty National, life premiums declined 2 percent to $70 million while life underwriting margin was up 10 percent to $19 million. Net life sales fell 4 percent to $7 million while net health sales declined 13 percent to $3 million. The producing agent count at LNL ended the quarter at 1,375 – up 8 percent from a year ago, but down 3 percent during the quarter.

While the agent count was down sequentially in the first quarter, we continue to be pleased with the progress being made in turning around Liberty National. As we've said many times, this is a slow process and agency growth tends to occur in a stair-step pattern. We continue to work to change the culture of this agency.

The implementation of the laptop presentation is occurring a little more slowly than expected but steady progress is being made.

With respect to geographic expansion, we will be opening four new offices over the next ninety days and we are optimistic that agent growth will continue going forward. Sales growth is expected to range from 4 to 8 percent for the full year 2013.

<u>Now, Family Heritage</u>

Health premiums were $46 million and health net sales were $11 million. As we've previously indicated, we intend to grow this agency through geographic expansion and implementation of our internet recruiting program. For 2013, we expect premium income to range from $188 million to $196 million with margins as a percentage of health premium of about 19 to 20 percent. We expect sales of approximately $48 million to $50 million in 2013.

<u>Medicare Part D</u>

Premium revenue from Medicare Part D grew 4 percent to $77 million, while the underwriting margin increased 2 percent to $8 million. Part D sales for the quarter fell 65 percent to $9 million due to the decrease in low-income subsidized enrollees for 2013.

As we've mentioned before, we won't receive as many new auto-enrollees under the low-income subsidy program in 2013 as we did in 2012, so we won't have the type of sales and premium growth we had in 2012. We expect a decrease of approximately 5 to 7 percent in our Part D premiums for 2013 due primarily to price competition in the employer group market that we've discussed previously.

I will now turn the call back over to Gary.

<u>Gary Coleman</u>

To complete the insurance operations, administrative expenses were $43.9 million for the quarter, 8% more than the year ago quarter. The increase is in line with our expectations and primarily due to the addition of Family Heritage. As a percentage of premium, administrative expenses in 2013 should be around the same level as 2012.

Now, I want to spend a few minutes discussing our investment operations.

First, excess investment income:

Excess investment income (which we define as net investment income less required interest on policy liabilities and debt) was $56 million, a decline of $8 million or 13%; 6% on a per share basis from the first quarter of 2012. Sequentially, excess investment income was essentially level with the fourth quarter.

Due to lower new money rates and the possible calls of hybrid securities, we expect excess investment income in 2013 to decrease approximately 7% to 8%. However, reflecting the impact of share repurchases, we expect 2013 excess investment income per share to be down around 2% compared to 2012.

Now, regarding the investment portfolio:

Invested assets are $12.7 billion, including $12.1 billion of fixed maturities at amortized cost.

Of the fixed maturities, $11.5 billion are investment grade with an average rating of A-, and below investment grade bonds are $573 million, compared to $585 million at the end of last quarter and $723 million a year ago.

The percentage of below investment grade bonds to fixed maturities is 4.7% compared to 6.5% a year ago. With a portfolio leverage of around 3½ X, the percentage of below investment grade (BIG) bonds to equity, excluding net unrealized gains on fixed maturities is 17%, which is less than most of our peers.

Overall, the total portfolio is rated A-, the same as a year ago.

In addition, we have net unrealized gains in the fixed maturity portfolio of $1.5 billion compared to $873 million a year ago.

Regarding investment yield:

In the first quarter, we invested $387 million in investment grade fixed maturities, primarily in the industrial and utility sectors.

We invested at an average yield of 4.31%, an average rating of BBB+ and an average life of 27 years. Over the last 5 quarters, the yield on new investments has averaged 4.3%.

For the entire portfolio, the first quarter yield was 6%, down 47 basis points for the 6.47% yield in the first quarter of 2012. Of this decline in yield, 14 basis points was due to the addition of Family Heritage and 8 basis points is due to the $300 million of bank hybrids called in the third quarter of 2012.

On the last call we indicated that we held approximately $225 million of bank hybrids that we expected to be called in 2013. In the first quarter, $66 million were called leaving $159 million of those securities in the portfolio as of March 31. As of today, we have not received a notice of intent to call on any of these securities.

However, if all $159 million of these securities are called and assuming a 4.25% reinvestment rate, the lost annual income related to these calls would be approximately $3 million after tax.

On past analyst calls we have discussed the current low interest rate environment and the impact of a "lower for longer" rate scenario. As discussed our concern regarding an extended period of low interest rates continues to be the impact on earnings, not the GAAP or statutory balance sheets.

As long as we are in this low interest rate environment, the portfolio yield will continue to decline and thus pressure excess investment income. However, the decline will be slowed by the fact that on average, only 2-3% of fixed maturities will run off each year over the next five years, and that assumes the calls of the bank hybrids that we previously discussed.

Assuming a new money rate of 4.25% for the next five years, we estimate that the portfolio yield at the end of 2017 would be around 5.55%. Assuming a 4% new money rate, the portfolio yield at the end of 2017 would be around 5 basis points lower or 5.5% At these rates we would earn a small spread on the net policy liabilities, while earning the full 550 – 555 basis points on our equity less the interest required to service our debt.

In either scenario we will still generate substantial excess investment income.

Now, I will turn the call over to Frank to discuss share repurchases and capital.

Frank Svoboda

Thanks, Gary**.**

I want to spend a few minutes discussing our share repurchases and capital position.

First, regarding share repurchases and parent company assets:

In the first quarter, we spent $90 million to buy 1.6 million Torchmark shares. So far in April, we have used another 20 million dollars to buy another 345 thousand shares. So, for the full year through today, we have spent 110 million dollars of parent company cash to acquire 1.9 million shares.

The available liquid assets at the parent consist of assets on hand plus the expected free cash flow from operations. As we've said before, free cash flow results primarily from the dividends received by the parent from its subsidiaries less the interest paid on debt and the dividends paid to Torchmark shareholders.

The Parent started the first quarter with liquid assets of $147 million, including $94 million that has been invested to redeem our senior notes that mature on August 1, 2013. This leaves approximately $53 million of liquid assets available for other corporate purposes. Assuming shareholder dividends remain at the 17 cent per share level approved by the Board in its February meeting, we expect free cash flow for all of 2013 to be around $360 million dollars. Along with the $53 million of liquid assets available as of the beginning of the year, the Parent will have around $413 million of available liquid assets for the full year.

As of today, after deducting the $110 million of year to date share repurchases, the Parent will have around $303 million available between now and the end of the year.

As noted before, we will use our cash as efficiently as possible. If market conditions are favorable, we expect that share repurchases will continue to be a primary use of the remainder of the funds. We also expect to retain approximately $50 million of liquid assets at the parent company.

Now, Regarding RBC at our Insurance Subsidiaries:

We plan to maintain our capital at the level necessary to retain our current ratings. For the last three years, that level has been around an NAIC RBC ratio of 325%. This ratio is lower than some peer companies, but is sufficient for our companies in light of our consistent statutory earnings, the relatively lower risk of our policy liabilities and our ratings.

At December 31, 2012, consolidated RBC was 347%, and adjusted capital was approximately $95 million in excess of that required for the targeted 325% consolidated ratio.

Now, before I turn the call back to Larry, I would like to briefly make just a couple of comments relating to the addition of Family Heritage.

On our last call, we indicated our expectation for Family Heritage to contribute between 16 and 20 cents per share to our 2013 net operating earnings after-tax incremental financing costs. At this time we believe Family Heritages contribution to our operating earnings per share should be close to the midpoint of that range.

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

<u>Larry Hutchison</u>

Before I give guidance I want to make sure I corrected stated Health premiums and Health net sales for Family Heritage. The health premiums were $46 million and heath net sales were $11 million.

Guidance

In 2013, we expect our net operating income will be within a range of $5.50 per share to $5.75. This guidance incorporates the underwriting improvements Gary discussed earlier.

Those are our comments. We will now open it up for questions.

Question and Answer

Jimmy Bhullar *- JPMorgan Chase & Co. - Analyst*

Hi, good morning. I had a couple of questions. First on American Income; if I look at life insurance sales, they've actually gotten weaker the last few quarters, even though the agent count has actually been growing. So wanted to just get an idea on what's been driving that, and what drove the decline this quarter. And Direct Response -- I think you mentioned you expect mid to single-digit sales growth for this year. If we look at the last several quarters, sales even there have, over the last five quarters, gotten progressively worse. And the economy is still the way it was two or three months ago, so it doesn't seem like -- it seems like it's trended in the wrong direction. But what gives you the comfort that sales for this year will be within what your range is?

Larry Hutchison *- Torchmark Corporation - Co-CEO*

Jimmy, as you know, at American Income sales are directly related to the number of agents in the field. And if you look at the agent count at American Income at the end of the fourth quarter, it was 5,176. At the end of the first quarter, the agent count was up to 5,612. But the increase did not occur until the latter part of the quarter. What is driving the surge towards the end of the quarter is that we changed our mid-level manager compensation in the fourth quarter of 2012. And we did that to reward increased agent retention rather than simply agent recruitment. This change resulted in both the focus and the compensation for our field managers. And while we've seen an improvement in agent retention in March, it's taken several months for that change to be embraced by the field. I guess in the short run the compensation change probably hurt our recruiting efforts in the fourth and the first quarter. Where over a longer period of time, we believe the compensation change will result in an increased agent count.

With respect to Globe Life, our confidence that we'll have single-digit growth this year is based on our initiatives for 2013. Those will include rate adjustments and higher face amount offering on adult products. Our testing results for the race and face amounts have been positive. And that's what we believe will drive the growth for Globe Life and Accident Insurance Company.

Jimmy Bhullar

Okay. And then if I could just ask one more. On Liberty National, the agent count has actually been recovering a little bit in the decline this quarter. Anything specific that drove that?

Larry Hutchison

I think what drove it this quarter is that at the end of the fourth quarter, beginning of the first quarter, middle management's focus was on year-end open enrollments in our worksite division. That takes their focus off recruiting in the fourth quarter, and created a slight decline in the agent count.

Jimmy Bhullar

And you still expect it to grow over the next few quarters.

Larry Hutchison

Yes. Our guidance for agent growth for the year is that we believe at the end of 2013 at Liberty National the agent count should be between 1,750 and 1,850 agents.

Jimmy Bhullar

Okay, thank you.

Sarah DeWitt *- Barclays Capital - Analyst*

Hi, good morning. I'm just following up on Liberty National. Could you just elaborate on what gives you the confidence that you can hit your updated full-year sales target there? And then longer term when do you think you get back to double-digit sales growth in that channel?

Larry Hutchison *- Torchmark Corporation - Co-CEO*

I think double-digit sales growth at Liberty National will come fairly slowly. I think it would be another 16, 18, 20 months before we have that kind of sales growth. Two changes have occurred at Liberty National in this quarter. The first is a systems change. We just changed the work week. Business is now turned in Monday for the previous week rather than on Friday afternoon. This encourages our agents to sell products over the weekend. We find at American Income that about 40% of our new business is written on the weekend. Although we don't anticipate a 40% increase in sales at Liberty, we do think this will have a positive response. And, secondly, we are looking at some geographic expansion. We are planning in the next 90 days to open four new offices in areas outside our traditional markets, Sarah. Virginia, Louisiana, Texas, Oklahoma are likely to be expansion sites for these offices.

Gary Coleman - *Torchmark Corporation - Co-CEO*

Sarah, I might add that we've given guidance of 4% to 8% growth for the year in sales at Liberty. And we had a 4% decline in the first quarter. We will see double-digit growth in the second half of the year, but that is based on low comparisons from the prior year. I agree with Larry. For us to have sustained 10% growth, it's going to take a longer period of time. But a key to that was just what Larry mentioned. The opening of new offices in more urban areas where there is a higher population, where there is more opportunity to recruit agents, as well as have customers.

Sarah DeWitt

Okay, great. Thanks. And then just on American Income and direct sales, how should we be thinking about the trajectory of those sales as we go through the rest of the year? Particularly given your comments about some of the changes of manager compensation at American Income?

Larry Hutchison

I think the trajectory of the sales at American Income would be high single digit in the second quarter. And you'd probably see double-digit sales growth in the third and possibly into the fourth quarter. But for the year, again, our guidance is we're going to see sales of 10% to 14%. And we'll see agent growth continuing throughout 2013.

Gary Coleman

On the Direct Response, in the second quarter we're looking for low single-digit inquiries, with double-digit increases in the second half year.

Sarah DeWitt

Great, thanks for the answers.

Steven Schwartz- *Raymond James & Associates - Analyst*

Hey, good morning everybody. The question I want to ask is, on the Direct Response initiatives that you are taking, you mentioned premium rates. Larry, my assumption here would be that you're looking to lower them?

Larry Hutchison - *Torchmark Corporation - Co-CEO*

Yes.

S**teven Schwartz**

Okay

Larry Hutchison

What we do with testing is we try different premium rates. And based on our experience we know that if we lower certain rates we'll have higher response rates. And so would write a more profitable block of business.

Steven Schwartz

Okay. Does that -- well, that's an interesting thing. So, we assume that -- obviously with lower rates you would think that the margin would be lower than what you wrote in the first quarter. But then you just said more profitable business. So that a little bit confusing.

Gary Coleman – Torchmark Corporation-Co-CEO

Well the lower rates, we get a better response rate and so we issue more policies, though. So, although the premium rate for policies is down, the issuance of the greater number of policies gives us more revenue to spread our acquisition costs over.

Steven Schwartz

Okay. So lower loss ratio but better expense ratio. And then on the higher face values, is that - are you raising the minimum or are you just adding on top of that?

Larry Hutchison

We are adding on top of that. If you're talking about a larger face amount it is offered to the customer.

Steven Schwartz

And where are you now, that ceiling, and where are you going?

Larry Hutchison

We are planning to roll this out at the end of May. If I understand your question, you're asking where are we going? This will be rolled out at the end of May, the first part of June. Is that your question, Steve?

Steven Schwartz

No, I meant, like the face value today is X, and you're going to Y, of the maximum face side.

Gary Coleman *- Torchmark Corporation - Co-CEO*

On the high side for us today, it's about $50,000. So here we think we can move up toward $100,000.

Steven Schwartz

Okay, very interesting. Thank you.

Erik Bass *- Citigroup - Analyst*

Hi, good morning, just a couple things; on Liberty just one thing. If you could give maybe a little bit more color on the reception of the changes that you've made over the past year to make the business more akin to American Income. And how you have seen maybe the productivity changing since making those changes.

Larry Hutchison *- Torchmark Corporation - Co-CEO*

Well the change of Liberty to make it more like American Income is a variable cost model. Starting in 2012, all the agents we hired are independent contractors. As we promote agents through the system, this would become middle management, they become branch managers. They're paid strictly on commission. And so it's quite a different system, Erik, in that they are really entrepreneurs and they're running their business. There are other system changes. Certainly the recruiting systems have changed. They're like American Income. Another big change has been the introduction of the laptop. We are installing the entire process in the Liberty National agencies. It will take all of 2013 to install that laptop system. The laptop is not just the technology of you're selling with the laptop. It changes your recruiting systems, your lead systems, it changes your training systems. So it is quite a system change that you're introducing into that agency. But at the end of the process we think it's a much stronger process. You have better data to manage with, and you have stronger sales presentations by the agents. And because they are better trained, it helps productivity because you will have a higher face per sale at the end of the process.

Erik Bass

Okay. And then one other general question. You've mentioned the impact of the economy, and the payroll tax credit specifically, related to Direct Response. But given your target customer base across channels, do you think there is any impact from the economy more broadly on sales trends through your agent-sold business, as well?

Larry Hutchison

I think it is less of a factor on the agent-sold business because the agent is sitting across the kitchen table explaining that need. But Direct Response, there's less contact. You are reaching simply through the mail. And we don't think in the long term it will have a negative effect upon those sales, but it may be more contacts are needed to complete the sale in the Direct Response system.

Erik Bass

Okay. So you're not seeing the pressure on the wallet of the individuals leading to a tougher sales environment for the agents. It is still need driven.

Larry Hutchison

It's need driven. As we look at our laptop data, I'm not seeing a difference in closing rates that comes through that laptop data.

Erik Bass

Okay, thank you. That is helpful.

Jeff Schuman *- Keefe, Bruyette & Woods - Analyst*

Thanks, good morning. I was hoping you could talk a little bit more about conservation. You started these initiatives a few years ago. It's clear that you are realizing some results. I was wondering if you can give us a sense of -- have you fully, at this point, achieved what you thought you would achieve? Or is there still maybe more upside there? And then I'm also wondering whether the economy negatively is impacting conservation, just as it is in sales in some channels. And whether, if that eases at some point, whether that could provide some upside.

Gary Coleman *- Torchmark Corporation - Co-CEO*

First of all, Jeff, this year we will, out of about $250 million of lapsed premium, we will conserve around $36 million of that premium. And I think last year it was around $30 million. And the year before that, when we first got started, it was less than $15 million. I don't think we've reached the max. As a matter of fact, in looking forward, we see it increasing. I don't know if it'll increases a great deal more. At the $36 million this year, we are conserving 14% of the lapses. And we may see that percentage go up but not a great deal. As far as from the economy side, I would think an improving economy would help in the program. But we really don't have any feel right now of what the impact of the economy is.

Jeff Schuman

Okay. And then on the risk-based capital, you're somewhat above your 325% target. As you pull ordinary dividends, will that tend to draw you down towards the 325%? Or is there maybe at some point some potential to contemplate a small extraordinary dividend?

Frank Svoboda *- Torchmark Corporation - CFO*

Gary, do you want me to take that?

Gary Coleman

Yes, go ahead.

Frank Svoboda

Yes, Jeff, as we do take out some of the dividends over the course of the year, that will tend to bring it down some. Our initial projections show the decrease in that excess, or shows a little bit of a decrease in that excess. At this point in time, we are not - we have no immediate plans to distribute any of that. As we take a look at the funding needs for the various growth initiatives that we have down at the subsidiary levels, we probably should have a little bit better idea on that later on here in the year.

Jeff Schuman

Okay that's it for me. Thank you.

Randy Binner *- FBR Capital Markets - Analyst*

Great thank you, I just wanted to follow up again on sales; just a couple more details. First, on American Income, I just want to make sure I understand this correctly, with the middle management disruption, or distraction that happened with the compensation shift in the fourth quarter. Is that a situation where you change the way they were paid, and that caused them to not focus as much on recruiting? Or it caused them to leave, and now that you've solidified that base of middle managers, they can focus on recruiting again? Or is it just they are now more focused on recruiting because that's how they're getting paid?

Larry Hutchison - *Torchmark Corporation - Co-CEO*

Well the change in compensation is to reward the middle manager for the length of service of the agents. So the compensation changes, part of that compensation is based on the retention of the new agents. We're trying to extend the agent life from three or four months to four, five, and six months. I think that changes the focus of the middle manager a little bit because you're not so concerned about an agent in the first three months. You are concerned about an agent in that first six, seven, or eight months. So that is the intent. But any time you change compensation at an agency, and change focus of the agency, it generally has a negative short-term impact on recruiting.

Randy Binner

Okay. So it wasn't that you lost these individuals. It's just that they weren't as focused on near-term recruiting, and that hit sales because there weren't as many?

Larry Hutchison

Randy, the real issue we're trying to address is, we're not concerned with losing middle management so much as losing entry-level agents. And thus we changed compensations, we changed our systems, we’re trying to encourage better training and better retention of the agents.

Gary Coleman - *Torchmark Corporation - Co-CEO*

Yes, in addition to that, another change to go along with that is that we were probably promoting agents too early in the past. And so now we've lengthened the time from which an agent, a new agent, can get promoted to entry-level management. That will make them a better manager and that will help in their training and recruiting of the new agents. And the bonus we have will help with the retention of the new agents. Again, the key to this is not only recruiting agents, but getting them to stay longer.

Larry Hutchison

Right and Randy, specifically what we did is, in the past, we were taking agents and putting them into entry level management sometimes as early as 15 to 30 days. In the fourth quarter we corrected that and now they're not promoted until a 90-day period. That allows a new agent to focus entirely on sales field experience in their first 90 days. And we're seeing a positive result of that. In March, we saw a greater number of managers that were successfully recruiting and supervising new agents when we compare that to March of 2012.

Randy Binner

Okay. So the March trend that is better is the recruiting effort, not necessarily the sales effort yet.

Larry Hutchison

Well if you have more agents you have greater sales so that goes hand-in-hand. What we are really seeing in March is better retention of the new agents. And we're seeing a greater recruiting effort into middle management.

Gary Coleman

And it didn't translate in production. I think Larry mentioned earlier, the agent growth came late in the quarter. 70% of the agent growth in the first quarter really came in the last two to three weeks of the quarter. So we should see the impact starting next quarter.

Randy Binner

You said 70% of it was in the last two or three weeks?

Gary Coleman

Yes

Randy Binner

Seven-zero - okay. Wow. Okay and then just one more on Globe. Can you just remind us of the test results you run in Globe? How broad are those? And how good a predictor have those been in the past of how those are going to perform?

Larry Hutchison

They're very good predictors. At any point in time, Chuck Hudson and his group are testing five, six, seven different tests. And based on those test results, they have a high confidence level that when they roll out that full program, that the full program will have the same results as the test results. What's been a little different is some of these response rates have been lower into fourth quarter and the first quarter. We think those response rates will return to normal and be reflective of the test results that we are seeing.

Randy Binner

Okay, one more, if I can? The short-term debt is going up on the balance sheet. This is unrelated to sales. But are you all using a little bit more commercial paper? Is that what we're seeing with short-term debt?

Frank Svoboda *- Torchmark Corporation - CFO*

Yes, during the first quarter we did have an increase in the commercial paper, which is not atypical for the first quarter of the year, as we are awaiting for the dividends to be able to come in from the insurance subsidiaries. So, we do need an increase in the short term. At the current time, it is back down to $233 million as of today. So it's just a little bit of a timing thing there at the end of the quarter as far as the actual balance is concerned.

Randy Binner

Perfect, thank you.

Bob Glasspiegel *- Langen McAlenney-Janney - Analyst*

Good morning McKinney. I wanted to talk about Family Heritage. It looks like you lowered your premium assumption for the year but raised your margin. What are the dynamics that are going? These weren't big changes and it looks like if you multiply it out it's $0.5 million more of underwriting income, if you take the midpoint of the ranges. But what's driving the premiums down a little bit and the margin up?

Larry Hutchison *- Torchmark Corporation - Co-CEO*

I think what drove the sales down a little bit -- let's talk about sales activity first. Sales activity in the first quarter was less than projected because we had a decline in recruiting activity early in the quarter. If you look at the agent numbers actually, we ended the quarter with slightly higher agent numbers. We didn't see that in January, into early February.

Gary Coleman *- Torchmark Corporation - Co-CEO*

Yes, Bob, I think, really, as far as the premiums, the bigger thing is that I think our projection was a little higher in the fourth quarter than it should have been. We just have better numbers to work with. Frank, why don't you talk about the changes in the margins or the percentages.

Frank Svoboda *- Torchmark Corporation - CFO*

Yes. And part of that, Gary, it goes hand-in-hand, part of the decrease in the premiums is an improvement, if you will, in the modeling, given that the newness of the block of business and the acquisition; still looking at getting the modeling of that business out. So it resulted a little bit in a lower premium. At the end of the day, we have a little bit of a lower obligation margin on it, as well. So the margin we expect to still be slight improvement in that, even though the net underwriting income is approximately the same as what we had originally projected. So you're seeing that margin move from a little under 19% to somewhere in between 19% to 20%.

Bob Glasspiegel

Okay

Frank Svoboda

It's fairly stable going forward.

Bob Glasspiegel

Okay, I guess I understand that. It looks like the underlying margin in health widened 100 bps year over year -- this is about a trend that's been in place -- despite the fact you had more 20% margin in the mix of the Family Heritage. Which, while it's more than we thought it was going to be, it's less than your total. So it looks like there's something positive going on, on the rest of the book on the margin front. Anything worth noting or just a blip in the quarter?

Gary Coleman

I think one thing worth noting is in the Liberty National health side, if you compare first quarter this year to last year, the claims were down significantly. First quarter 2012, the ratio was 58.4%. That was the high for the year. We ended the year at policy obligations of 57%. But, still, the first quarter this year is low at 55.5%. Part of that is maybe seasonal. But the major part of that is that we've got a large cancer block that we are having improving claims experience. So, for the year, it looks like that ratio should hold somewhere between 55% and 57%, which is lower than last year. Which means that for Liberty we could pick up 1 percentage point in the margin for this year for Liberty health. On the American Income health, we had lower claims there. But that's something that is mainly because we had a high first quarter last year.

Bob Glasspiegel

Right

Gary Coleman

It is really the Liberty National health where we saw the biggest improvement in the margin.

Bob Glasspiegel

Okay. So I guess what you are saying is, the health margin in Q1, ex Family Heritage, was a little bit better than normalized, because of LNL, but still better than you thought it was going to be, too.

Gary Coleman

Right.

Bob Glasspiegel

Somewhere in between where you thought and this quarter is the right underlying margin?

Gary Coleman

Yes.

Bob Glasspiegel

I got it, and last question. A lot of noise and cross currents going on, on Medicare Advantage. And we're sitting around waiting for Med-Supp market to improve as this gets depopulated. But, I guess we keep moving the ball down the field. Is there anything really important we need to know thinking about --?

Larry Hutchison

Brian, why don't you try and answer Bob's question.

Brian Mitchell *- Torchmark Corporation - General Counsel*

Yes, sir. We are looking at numerous proposals that come out, it seems like, almost weekly from Washington, from both sides of the aisle as to how to change, restructure Medicare. There are so many proposals that have come about that it's really been difficult to project what is likely, what they are likely to settle on. One week it seems like the two sides are merging together, and then the next they will be farther apart. It is something that we are tracking, along with the funding constraints for Medicare Advantage. I think there has been some noise and news on that in the last week or so, as well. So, it's something we look at regularly. But at this point it's just not pinned down on what is going to happen.

Bob Glasspiegel

Okay. So we're at least a year away from an improving -- a dramatically improving Med Supp environment?

Larry Hutchison *- Torchmark Corporation - Co-CEO*

Well Bob,

Bob Glasspiegel

Or could it be closer than that?

Larry Hutchison

No, I think we think it would be a year away because the disenrollments would probably start next October.

Bob Glasspiegel

Right

Larry Hutchison

So between now and next October we don't see much movement. In the fourth quarter we should have a clearer picture-- As to what is going to happen with Medicare Advantage disenrollments.

Bob Glasspiegel

Okay. I want my candy now but I guess I can wait a little bit. (laughter) Thanks a lot.

Larry Hutchison

Sure

Mark Hughes *- SunTrust Robinson Humphrey - Analyst*

Thank you, good morning.

Gary Coleman and Larry Hutchison – Torchmark Corporation - Co- CEO'S

Good morning.

Mark Hughes

On the Med Supp sales, on that same topic, you had good momentum in the fourth quarter. Not quite as much momentum here in Q1. I don't know if you touched on this earlier in the call, but any meaningful changes there?

Larry Hutchison *- Torchmark Corporation - Co-CEO*

Mark, I think what drives the Med Supp sales in the first quarter, and somewhat in the fourth quarter, are the group sales. If you look at individual sales in the first quarter, I think those had strong growth. It was the group sales that were off. I think in prior calls someone described it as lumpy events that we tend to either get groups or we don't get groups. So it comes in in bunches, or it comes in in lumps. I think for the year we are projecting a 10% increase in Med Supp sales. But we'll have a better idea of that actually in the fourth quarter, because that's when most of those group sales come through for Med Supp.

Mark Hughes

Got you, and then you had provided an estimate for the year-end headcount at Liberty National. Can you provide the same sort of forecast for American Income?

Larry Hutchison

Sure. We expect the agent count at year end for American Income to be between 5,900 agents to 6,000 agents.

Mark Hughes

Thank you.

Paul Sarran *- Evercore Partners - Analyst*

Hi, good morning,

Larry Hutchison – Torchmark Corporation - Co-CEO

Good morning Paul.

Paul Sarran

I think you mentioned at Direct Response the margin on new sales this quarter was 1% to 2% better than the margin on sales in the quarter a year ago. How does that compare to margin on the overall in-force?

Larry Hutchison

I don't think I have that number in front of me. It was higher than the overall in-force but I can't tell you how much.

Paul Sarran

Okay, and then just a quick question on buybacks. How does the stock price or the valuation of your stock influence your thinking in terms of use of cash for buybacks or timing?

Frank Svoboda - ***Torchmark Corporation - CFO***

Yes Paul. Go ahead Gary.

Gary Coleman - *Torchmark Corporation - Co-CEO*

I was going to say, Paul, first of all, on an overall basis, we are constantly looking at what the shares are trading for versus what we think the value of the stock is. And, although our PE has improved, especially over the 2008-2009 period, we still think it is a good buy. Now, as far as on a quarterly basis, as far as our share repurchases, I know years ago we used to concentrate more on the first part of the year. Our thoughts over the last couple of years, is really to spread it out over the year. We spent $90 million the first quarter this year versus $90 million last year. One example I'll give you is in the second quarter of 2012, we doubled up and spent $180 million. That's because there was a softness in the market price during the quarter. Our present plans are, with concern to where the stock price is today, we will spread the rest of our share repurchases fairly evenly over the year. However, we have the ability to react quickly. And if the share price does fall at any point in time, we can step in and buy more.

Paul Sarran

All right, thanks.

Eric Berg - *RBC Capital Markets - Analyst*

Thank you very much. I just had one question regarding your health business. I hear, or I have heard that the health business margins were modestly better than you expected in the quarter. But premiums are not growing and it seems that the in-force is not growing, at least that's what appears to be the case. Would you agree with that characterization or disagree? And, more importantly, what is the future of your health business? Do you see it as a growing business over time? That is my one question. Thank you.

Larry Hutchison - *Torchmark Corporation - Co-CEO*

Let's address the last part of the question first in terms of our future in health business. It depends on the segment. If you're talking about Part D, I think we see that as an opportunistic market. We currently pricing for 2014. And it's hard to predict, or we don't plan on growth in Part D, necessarily. Our non-Medicare business, we certainly see growth there with the addition of Family Heritage. As we grow that agency, that business will grow. Additionally, as Liberty National grows in the worksite, we'll see a growth in those health sales. For Medicare supplement, as we talked earlier on the call, it's difficult to see what the future of Medicare supplement is. It's tied somewhat to Medicare Advantage disenrollments. When we have a clear picture of the actual disenrollments, it will be easier for us to predict how much our Medicare supplement business will grow in the individual market. Certainly a great deal of our growth for Medicare supplements come through our group business. And we continue to try and grow our group Medicare supplement business.

Gary Coleman - *Torchmark Corporation - Co-CEO*

Eric, I also will add that one thing that has contributed to the decline in premiums over the last four or five years, is that we had a very large hospital block in Liberty National that we stopped selling business. That business has been running off and it's just about gone. So that drag won't be there going forward.

Eric Berg

Great then, thank you.

John Nadel - *Sterne, Agee & Leach, Inc. - Analyst*

Hi, good morning. I just wanted to revisit the discussion on the bank hybrids. It went pretty quick on what was called, what hasn't been called, how much is left. And I just also wanted to see if you could just tie that into what is assumed in your guidance range.

Gary Coleman ***- Torchmark Corporation - Co-CEO***

Okay, John. Coming into the quarter we had $225 million of bank hybrids that were likely to be called. We have some more, but they are either not callable or they're make whole calls, which we are not considered about.

John Nadel

Got it.

Gary Coleman

There is $225 million that we are concerned about being called. During the quarter, $66 million of those bonds were called.

John Nadel

Okay

Gary Coleman

And that leaves us $159 million of exposure. And as I mentioned earlier, we haven't received any notice that these bonds are going to be called as of the current day. We are a little surprised that they haven't been, but we will wait and see. For guidance purposes, we are running different scenarios. And within the range we have considered all of them being called to none of them being called. But, as I mentioned, I think, if all of them got called, the after-tax impact on an annual basis would be $3 million. So built into the guidance is somewhere between $0 and $3 million.

John Nadel

Perfect. Everything else has been asked and answered. Thank you.

Seth Weiss ***- BofA Merrill Lynch - Analyst***

Hi, thanks a lot. Just one quick question on Liberty and the margins there. In terms of the new office expansion, is this going to have any impact to margins that we should watch out for in the second quarter or is it all passed along to the branch offices?

Larry Hutchison ***- Torchmark Corporation - Co-CEO***

No. This is a variable cost model, so sales in those branches, the branch manager is responsible for the office, any leads. Any office expenses are borne by the agency not the Company.

Seth Weiss

Okay, great. Thanks. And just in terms of the 4% to 8% of sales expansion, how much do you attribute to this new expansion versus more organic growth?

Larry Hutchison

More of the growth will be organic growth because it takes a few months for a new office to recruit and build of its sales force. But it's really long-term growth we're talking, is the need to expand geographically outside our traditional markets.

Seth Weiss

Okay, great. Thanks a lot.

Chris Giovanni ***- Goldman Sachs - Analyst***

Thanks, most addressed. The comments you made in terms of the potential to accelerate deployment if there is a softness in the price, would that be the same kind of mechanism that we saw last year, and then I guess some in 1Q, in terms of the commercial paper borrowing and then getting the dividends up maybe in the subsequent quarters? Or do you have enough capital at the subs to do that on the quarterly basis?

Gary Coleman ***- Torchmark Corporation - Co-CEO***

Well the thing is the dividends that are coming up through the companies are based on last year's earnings. We know we are going to get those dividends. We also know the timing. If we want to accelerate repurchases, you're right; we would probably use commercial paper. But that would be very short term because that paper would only be outstanding until we got the dividend money up to pay that off. And that is what we did last year, is we borrowed a little extra in the second quarter to expand our share repurchases. And then the latter part of the year we didn't buy as much and we used the funds to pay back the short-term debt.

Chris Giovanni

Yes, okay. And then the Family Heritage acquisition, from an M&A standpoint can you comment at all in terms of appetite, and if there's anything else out there? Or are you just focused really on this acquisition now?

Gary Coleman

Well, we would like to find another Family Heritage, maybe a little bit bigger. Our approach has not changed. We have always been looking for a company that has controlled distribution that is selling in the middle income market. Although Family Heritage sells health, we prefer life, but, still, we are very happy with Family Heritage. We will continue to look. But as we said before, there is just not many of these type companies out there. Family Heritage was a little bit of a surprise to us, and we're glad we were able to get it. We are looking, it's an ongoing process, but it's just tough because there's just not that many type of companies out there on the market.

Frank Svoboda *- Torchmark Corporation - CFO*

Yes, Chris, one thing I would just add to that is that it really is key for us to be looking for somebody with that captive distribution. And a lot of the opportunities that come across to us do not have that type of distribution. They will have an independent distribution associated with them, and not something that we're trying to expand into.

Chris Giovanni

Okay. And then last question, just in terms of the supplement last quarter within Family Heritage, you guys had a different agent count. You had 1,160 versus the restated number for year end this year of 702. Can you just talk a little bit about what the difference is and why the restatement of agent count?

Larry Hutchison *- Torchmark Corporation - Co-CEO*

I think -- this is Larry -- it was restated as we got better information from the Company as to what are active agents -- and we've tried to have a uniform definition among the Torchmark companies how we define an active agent -- there was really no change. We haven't had departures from the agency. What’s really changed is the definition of an active agent.

Chris Giovanni

Okay. So that 40% difference is just agents that are actively selling the Family Heritage product.

Larry Hutchison

We've changed the definition. So it's an agent that actually has sold in the last 60 days, that's consistent among the companies.

Chris Giovanni

Okay, alright, thank you very much.

Vincente Lui *- Morningstar - Analyst*

Hi, good morning, just a quick follow-up on Direct Response. If you look at the statistics, you basically achieved 40% of sales, for the mail and insert media piece, and then about 60% after six months. And it seems like pretty stable over time. Just curious to hear your thoughts in terms of the impact of the Direct Response initiatives you mentioned on the pace of sales generation. Any change to the statistics going forward, as you can see?

Gary Coleman *- Torchmark Corporation - Co-CEO*

If you're asking about our new initiatives and the pace at which it will increase production, as far as the rate adjustments and the higher face amounts, we’re really-- it won't be rolled out until mid to late second quarter. So it will be the second half of the year before we see an impact on the sales.

Vincente Lui

Okay. But does the pace really matter from an accounting standpoint? Or just some interesting statistics you keep track of?

Gary Coleman

I'm not sure I understand the question.

Vincente Lui

So, the distribution here is about 40% in four months, 50% in five months, and then 60% after six months, right? And then I would assume the 40% in the second half of the year as the effectiveness of the insert basically loses effectiveness over time. When you have this new initiatives, you probably changed that distribution somewhat. But from a sales and from a sales recognition standpoint, if you look at the whole year it doesn't really change a thing, does it?

Gary Coleman

As far as adding the new initiatives, I don't think it would change. I think you're talking about the percentages of the lag time in which we receive new business.

Vincente Lui

Right

Gary Coleman

Yes, I don't think this will change those lag times. These products aren't so different. It's just that, what I'm saying, it's going to provide additional production, because we're providing products either rates we haven't had before or face amounts. So it's incremental production. But as far as a lag, I think it will probably be about the same.

Vincente Lui

Okay, great. That's helpful. Thank you very much.

Operator

And it appears there are no further questions at this time. I would like to turn the conference back over to our speakers for any additional or closing remarks.

Mike Majors *- Torchmark Corporation - VP of IR*

Ok, thank you for joining us this morning. Those are our comments. And we will talk to you again next quarter.