



Manulife Financial Corporation (MFC)

Updated November 14th, 2018 by Josh Arnold

Key Metrics

Current Price:	\$17	5 Year CAGR Estimate:	14.9%	Volatility Percentile:	62.1%
Fair Value Price:	\$23	5 Year Growth Estimate:	4.0%	Momentum Percentile:	13.4%
% Fair Value:	73%	5 Year Valuation Multiple Estimate:	6.4%	Growth Percentile:	20.3%
Dividend Yield:	4.5%	5 Year Price Target	\$28	Valuation Percentile:	90.4%
Dividend Risk Score:	D	Retirement Suitability Score:	C	Total Return Percentile:	86.7%

Overview & Current Events

Manulife Financial Corporation is a multinational insurance and financial services company headquartered in Toronto, Ontario, Canada. The company operates as Manulife in Canada and Asia, while its United States business is primarily operated through the John Hancock Financial subsidiary. Manulife reports financial results in Canadian dollars. With that said, the company is cross-listed on both the Toronto Stock Exchange and the New York Stock Exchange, where it trades under the ticker 'MFC' with a market capitalization of US\$34 billion. Although the company's reporting currency is Canadian dollars, this report will refer to the NYSE-listed shares and convert all financial results to U.S. dollars.

Manulife reported Q3 earnings on 11/07/18 and results beat consensus, leading us to boost our earnings-per-share estimate for this year. Earnings-per-share rose 42% against the year-ago quarter as the company saw strong growth across most of its segments. Core return on equity came in at 14.8% against 10.6% in the year-ago period, an enormous improvement in profitability that drove earnings higher. Total assets under management and administration rose 2% year-over-year while net flows for the wealth management business rose fractionally. Insurance annualized premium equivalent sales increased 8% as the core insurance business led the way during a very strong quarter. In addition, the company's efficiency ratio fell from 57.1% in last year's Q3 to just 49.5% this quarter, helping to drive margins higher. The cost savings are part of Manulife's plan to achieve a 50% long-run efficiency ratio and drive \$1 billion in cost savings and avoidance by 2022. Judging by Q3's results, it is certainly well on its way. After the strong Q3 report, we boosted our earnings-per-share estimate for this year from \$1.90 to \$2.00, reflecting strong revenue and margin performance.

In addition, the company approved a 14% increase in the dividend and a 40 million share buyback program that will be used opportunistically. We have reduced our share count estimate for 2023 accordingly.

Growth on a Per-Share Basis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
EPS	\$0.26	\$0.78	-\$0.27	\$0.02	\$0.88	\$1.26	\$1.28	\$1.28	\$1.49	\$1.73	\$2.00	\$2.43
DPS¹	\$0.94	\$0.68	\$0.50	\$0.52	\$0.52	\$0.49	\$0.51	\$0.52	\$0.56	\$0.63	\$0.76	\$0.92
Shares	1,610	1,758	1,778	1,801	1,828	1,848	1,864	1,977	1,975	1,978	1,990	2,070

Manulife Financial Corporation's growth history is spotty at best. We believe that Manulife is capable of delivering long-term earnings-per-share growth of around 4% per year. We see low single digit revenue growth and margin expansion as producing higher earnings, as they did in Q3.

Valuation Analysis

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	Now	2023
Avg. P/E	---	22.9	---	---	13.7	13.0	15.1	13.4	9.6	11.1	8.4	11.5
Avg. Yld.	2.9%	3.8%	3.1%	3.4%	4.3%	3.0%	2.5%	3.0%	3.9%	3.3%	4.5%	3.3%

¹ Note: While Manulife did indeed cut its dividend in the 2007-2009 financial crisis, the 2013 decline in per-share dividends was due entirely to foreign exchange fluctuations (the company declares its dividends in Canadian dollars, while NYSE:MFC shareholders are paid in U.S. dollars at the prevailing exchange rate).

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Manulife Financial Corporation's valuation history has been nearly as volatile as its earnings. Based on comparable valuations in the insurance sector, we believe that a fair valuation multiple for Manulife is a price-to-earnings ratio of around 11.5. Manulife is trading at a price-to-earnings ratio of 8.4 today. If the company's price-to-earnings ratio can expand to 11.5 over 5 years, this will boost the company's annualized returns by 6.4% per year during this time period.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2023
Int. Cov.	1.5	0.9	-1.2	1.1	2.3	4.6	4.8	3.4	4.3	3.2	3.5	3.5
Debt/A	87.1%	86.0%	94.2%	94.6%	94.8%	94.3%	94.1%	94.0%	94.1%	94.2%	94.0%	94.0%
Std. Dev.	44.4%	87.8%	40.0%	32.2%	29.8%	20.4%	17.3%	22.8%	29.9%	15.1%	20.0%	20.0%
Payout	362%	87%	N/A	N/A	59%	39%	40%	41%	38%	36%	38%	38%

Manulife's interest coverage deteriorated noticeably during the 2007-2009 financial crisis. At the same time, the proportion of its balance sheet that was comprised of debt surged to ~94%, and the company's leverage has not declined from that level in the decade since. With that said, we believe that today's Manulife is very different from where it was ten years ago. We also note that the likelihood of another Great Recession-level financial crisis in the near-term is rather low. We forecast the payout ratio to remain in line with where it is today at 38% in the coming years.

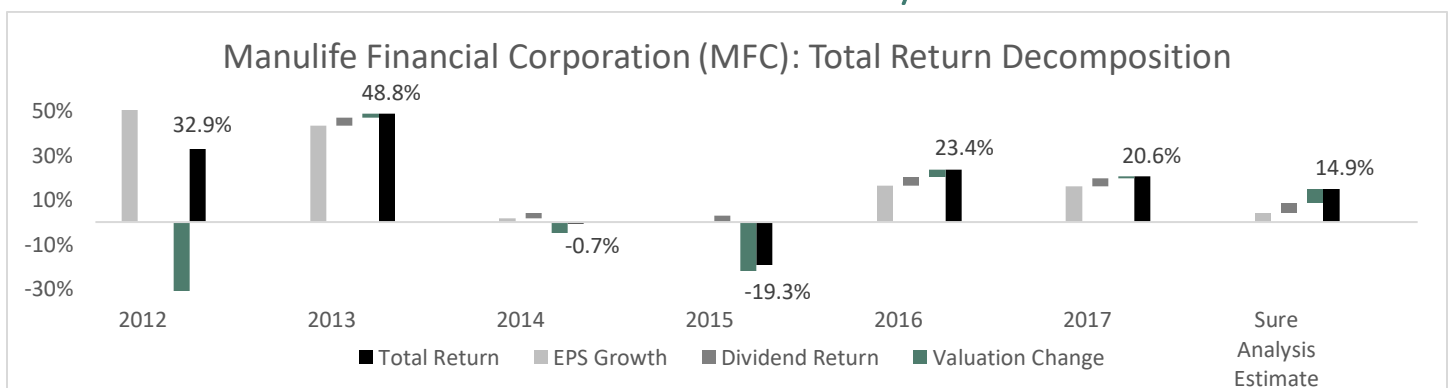
Qualitatively, Manulife's competitive advantage is its dominance of the Canadian insurance industry as well as its global reach. Together, this allows the company to harvest the profits from its domestic segment and reinvest them internationally to drive long-term growth.

Final Thoughts & Recommendation

Manulife Financial Corporation's growth history is volatile, and we do not expect the company to grow any faster than a long-term annualized rate of 4% per year. With that said, the company still has an appealing total return profile. Manulife appears priced to deliver returns of 14.9% per year despite a slow growth rate. Valuation expansion and dividend payments will deliver the majority of Manulife's returns moving forward. This demonstrates the power of investing in undervalued businesses that are committed to returning capital to shareholders.

With that said, Manulife is far from the most compelling opportunity within the Canadian financial services industry. That title likely belongs to one of the 'big 5' banks – the Royal Bank of Canada (RY), the Toronto-Dominion Bank (TD), the Bank of Nova Scotia (BNS), the Bank of Montreal (BMO), or the Canadian Imperial Bank of Commerce (CM). For investors looking for exposure to the Canadian financial services industry, those 5 banks are likely the best bet. For those already overweight in the Canadian banks, Manulife may be worth consideration at its current price, as we rate it a buy.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Revenue	31080	35309	36472	51561	29118	18101	49265	26976	40276	45002
SG&A Exp.	7328	6745	7503	4107	4416	4485	4322	4874	5282	5581
Net Profit	487	1234	-1612	220	1707	3028	3190	1740	2258	1596
Net Margin	1.6%	3.5%	-4.4%	0.4%	5.9%	16.7%	6.5%	6.5%	5.6%	3.5%
Free Cash Flow	7461	10584	11207	10991	10798	9229	9788	8128	12850	13728
Income Tax	75	-1384	-775	-98	-492	564	608	257	148	184

Balance Sheet Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Total Assets (\$B)	171.27	195.36	424.70	452.52	487.52	482.38	499.12	506.50	534.53	580.15
Cash & Equivalents	N/A	N/A	11847	12551	13456	12801	18158	12888	11237	12696
Acc. Receivable	N/A	N/A	671	11273	19792	17071	16593	26161	26551	25055
Goodwill & Int.	8152	8662	5906	5331	5140	4976	4704	6762	7496	7825
Total Liab. (\$B)	149.20	167.92	400.03	428.15	462.23	455.12	469.89	476.28	502.77	546.62
Long-Term Debt	4517	4365	5840	7031	8650	8280	7724	6880	9550	10475
Total Equity	21505	26008	22839	22187	22477	24385	26505	27854	28558	29946
D/E Ratio	0.21	0.16	0.24	0.29	0.35	0.31	0.27	0.23	0.31	0.32

Profitability & Per Share Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Return on Assets	0.3%	0.7%	-0.5%	0.1%	0.4%	0.6%	0.7%	0.3%	0.4%	0.3%
Return on Equity	2.2%	5.2%	-6.6%	1.0%	7.6%	12.9%	12.5%	6.4%	8.0%	5.5%
ROIC	1.8%	4.2%	-5.2%	0.7%	5.2%	8.7%	8.8%	4.7%	5.8%	3.7%
Shares Out.	1,610	1,758	1,778	1,801	1,828	1,848	1,864	1,977	1,975	1,978
Revenue/Share	20.56	21.65	20.66	28.82	15.42	9.72	26.19	13.64	20.37	22.66
FCF/Share	4.93	6.49	6.35	6.14	5.72	4.96	5.20	4.11	6.50	6.91

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.

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