FINAL TRANSCRIPT

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MFC - Q3 2008 Manulife Financial Corporation Earnings Conference Call

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PRESENTATION

Operator

Good afternoon. Welcome to the Manulife Financial Q3 2008 financial results conference call for November 6, 2008. Your host will be Amir Gorgi. Mr. Gorgi, please go ahead.

Amir Gorgi - *Manulife Financial - AVP, Investor Relations*

Thank you. Good afternoon. I would like to welcome everyone to Manulife Financial 2008 -- sorry, earnings conference call to discuss our third quarter, 2008, financial and operating results. If anyone has not yet received our earnings announcement,

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statistical package and slides for this conference on webcast, they are available in the investor relations section of our website, at www.manulife.com. As in prior quarters, our executives will be making some introductory comments. We will then follow with a question and answer session.

On behalf of the speakers that follow, I wish to caution investors that the speaker's remarks may contain forward-looking statements within the meaning of the Safe Harbor provisions of the Canadian and US security laws. Certain material factors or assumptions are applied in making forward looking statements and actual results may differ materially from those expressed or implied in these statements. For additional information about the material factors or assumptions applied in making these statements and about the material factors that may cause actual results to differ materially from expectations, please consult the slide presentation for this conference call available on our website, as well as the securities filings referred to in the slide entitled, Caution Regarding Forward-looking Statements.

When we reach the question and answer portion of our conference call we ask each participant to adhere to a limit of one or two questions. If you have additional questions please requeue as we will do our best to respond to all questions. Now, I would like to turn the call over to Dominic D'Alessandro, our President and Chief Executive Officer. Dom?

Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

Thank you, Amir, and good afternoon, ladies and gentlemen. Thank you for joining us on this call. Earlier today we reported third quarter share holder's earnings of $510 million, down from the $1.7 billion reported in the third quarter of last year. This resulted in fully diluted earnings per share of $0.33 and return on equity of 8.2%. The decrease in earnings is attributable to the sharp decline in global equity markets and to a lesser extent to credit related charges. Continued economic turmoil in the quarter resulted in the bankruptcy of the fourth largest US investment bank, Lehman Brothers and prompted the US government to rescue the world's largest insurer, AIG. Despite this economic backdrop, all of our business franchises remain strong.

Excluding currency movement and a large group insurance sale last year our insurance sales were up 16% in the quarter, while wealth management sales were down by 6%. New business embedded value generated in the quarter was strong and amounted to $540 million, up 5% compared to the same period last year. Before Peter begins his review of our financial results, I would like to comment on how the conditions in the global markets have affected our Company. Equity markets declined sharply in the third quarter down 19% in Canada, 9% in the United States and 15 to 20% in Asia. Notwithstanding these declines, our capital position at September 30 was very satisfactory with an MCCSR of 193%. Unfortunately the decline in equity markets continued into October as indices fell further by about 15% in Canada and the United States and by more than 20% in Asia. This put enormous pressure on our capital ratios. In view of all the interest in the subject, I would like to take a few minutes to explain.

The regulatory capital required to support guarantees arising from our variable annuities business is calculated using stochastic modeling techniques, and. has to be sufficient absorb any adverse scenario to a very high confidence level, usually expressed as CTE-95. CTE-95 is almost always described as the average of the worst 5% of the thousands of scenarios generated by the model. What is perhaps less well known is that CTE-95 is equivalent to an immediate market decline of about 35% being 30% in the United States, 40% in Canada and 60% in Japan. Very importantly, with no growth for 10 years. Now given that to the end of October, markets had already declined on a year-to-date basis by more than 30% in North America and by almost 50% in Asia to provide for further declines of the magnitude required by CTE-95 it seemed to be unreasonably punitive. So, we reviewed the matter with OSFI and they agreed that under the circumstances CTE-95 should appropriately be modified. The fact that any obligations due under our variable annuity guarantees only become payable over periods beginning seven years from now and extending for 30 years was also an important factor in their decision.

In October the capital requirements for segregated fund guarantees was modified by OSFI to require CTE-98 for payments due within one year grading down to CTE-90 for amounts due beyond five years. CTE-90, while providing us with some welcome capital relief, remains a very robust standard. It is equivalent to an immediate market fall of about 20%, and again, no growth for 10 years. So subsequent to the quarter, as a prudent step to further solidify our capital base we executed a binding credit

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agreement with the six largest Canadian banks to provide a five year term loan of $3 billion. The proceeds of this financing will be used as necessary to provide additional regulatory capital to our operating subsidiaries.

Our pro forma MCCSR after reflecting this new financing, the latest capital requirements for segregated funds and the market declines since September 30th is estimated at a very robust 225% which is well above our target range of 180 to 200%. As these ratios indicate, barring a very sizeable collapse in markets, we expect to remain well capitalized at year end. I believe we are well positioned to consider any opportunities that arise because of the extremely turbulent financial markets. And, with that, I would like to ask Peter to take us through the numbers with more detail with the usual question and answer session to follow. Peter.

Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

Thank you, Dominic.

On slide seven, shareholders' earnings for the third quarter indicated at $510 million or $0.33 per share as just noted. The sharp declines in global equity markets in the third quarter of '08 negatively impacted reported earnings by $574 million or $0.38 per share. Excluding the impact of equity markets, our results this quarter would have been a more normal $1.084 billion. Credit losses primarily driven by the financial sector exposures including Lehman Brothers and AIG amounted to $253 million at $0.17 per share. These items were partially offset by investment related gains arising from supporting our long-term insurance obligations with more non-fixed income assets, adding longer duration fixed income assets and by the favorable impact of widening spreads and steepening interest rates. As would be expected, our wealth management segments were more adversely affected by market conditions than were our insurance segments.

On slide eight, turning to a source of earnings, equity market volatility and financial sector credit related charges partially offset by investment related gains resulted in an experience loss of $168 million in the quarter. Net changes in actuarial assumptions decreased reported earnings in the quarter by $28 million. In light of the increased equity market volatility, the Company increased the provision for adverse deviation on segregated fund guaranteed reserves to the highest levels permitted by professional actuarial standards, resulting in a post tax strengthening of policy liabilities of $641 million. As well, the provision for adverse deviation for interest rate risk was reduced by $578 million post tax, as this provision had risen to excessive levels. Other smaller basis changes in the quarter netted to a $36 million post tax reduction in policy liabilities. Earnings on surplus were $111 million in the quarter lower than in previous quarters, due to lower gains realized on available-for-sale assets and reflecting credit charges on surplus funds. Income taxes for the quarter, while unusual in certain business segments, were at normal levels across the Company overall.

On slide nine we outline in more detail the impact of the equity markets on our results. As Dominic just noted, global equity markets experienced sharp declines in the third quarter. The actuarial practices require us to calculate our reserves as if these market declines are permanent. Of the $574 million charge, $307 million related to normal reserves strengthening for segregated fund guarantees and $154 million related to the strengthening of policy holder liabilities that are supported by equities. Although these guaranteed benefits cannot be monetized currently and the bulk of these payments are only expected to occur over seven to 30 years or longer, the valuation of these guarantees is quite sensitive to short term changes in market levels. Accordingly, I would like to take a moment to review some key details of our segregated fund guarantees.

On slide 10, we provide a brief overview of the nature of the segregated fund guarantees. These products are effectively designed to provide consumers with the equivalent of a private pension plan tailored to the individual needs. We sell variations of these products across the US, Canada and Japan. It is important to note that the underlying benefits are generally payable seven to 30 years in the future, have no liquidation risks as guarantees cannot be accelerated or monetized by our policyholders. Despite the recent sharp declines in global equity markets, we still expect the fees collected on these contracts to exceed the benefits payable over their lifetime.

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Turning to slide 11, we provide details on our reserves and capital in relation to segregated fund guarantees. Consistent with our SIP disclosure, the second column represents the fund value net of amounts reinsured while the third column represents the excess of guaranteed values over funds values -- or amount at risk. The fourth column in this table entitled Expected Level represents the present value of benefits less the present value of offsetting fees based on averaging projecting benefits and revenues across all scenarios we run to determine reserves and capital at CTE-0 for the expected level. The negative figure in this column indicates that as of the end of the third quarter, we estimate that we expect to make a net present value profit of $1.5 billion based on the average expected result. Many of you may recall slightly different number when we did the interim brief on the matter, and the difference relates to the total contract, the (inaudible) of the contract versus the guaranteed component. And, the number would be unchanged today as far as we could tell. The fifth column entitled Reserve Level represents the amount we hold in our actuary reserves at quarter end reflecting the worst 20% of all scenarios or CTE-80. This is approximately equivalent to a 92% confidence level. In the final column entitled Capital Level effectively represents the sum of our reserves and required capital reflecting the worst 5% of all scenarios or CTE-95, which is approximately equivalent to 98% confident level. The frame work we used to generate the scenarios that must be covered by reserves or capital assume no mean reversion of markets to rebound from recent declines. Therefore, under the existing framework we are required to maintain reserves and capital based on the assumption that the very adverse equity market moves to date are permanent and the CTE-95 level result is equivalent to assuming a further decline in equity values of some 35% which will occur and not be followed by any growth in equity values for a decade or longer. In other words a tail event followed by another tail event. This is a very onerous framework given that our variable annuity obligations are contingent on future market performance, most are long-term with payments only due in many, many years and these are not subject to acceleration or liquidation risks.

For those of you who listened to our call on October 14, you will note that the final reserve in capital numbers reported in the third quarter are revised from the estimates that we had disclosed on October 14. The total OSFI requirements to be covered by reserves and capital decreased from $5.7 billion to $5.1 billion, the portion booked as balance sheet reserves increased from $1.4 billion to $2.3 billion. The primary reason for this was an increase in the amount of adjustments to bring the reserves to the maximum CTE-80 level. The adjustment to bring the reserves to the CTE-80 level continues to be largely offset from earnings-- an earnings perspective by a reduction in excess interest rate risk reserves. I like to point out that we continue hold interest rate risk reserves that are more conservative than the worst of the prescribed scenarios in actuarial standards, and that our segregated fund guarantee reserves as of September 30th are at the highest levels permitted by actuarial standards.

We turn now to slide 12, our capital positions at the end of the third quarter remained within our internal target ranges and were significantly above regulatory levels. MLI's reported MCCSR ratio declined from 200% to 193% in the third quarter reflecting the sharp decline in global equity markets partially offset by internal redeployment of excess capital resources. While JHLICO's RBC ratio is formally calculated and reported annually, the estimated position at the end of the third quarter is 340%. The reduction from year end '07 driven by related party capital movements and investment results.

Turning now to slide 13, as Dominic noted earlier, there have been several recent developments that will impact the regulatory capital levels going forward. OSFI recently announced improvements to the MCCSR guidelines pertaining to calculation required capital and segregated fund guarantees. The previous capital rules are based on a single confidence level regardless of the date in which an insurer was expected to make payments. As such, these rules did not provide any distinction between the level of capital required for distant payment obligations and those that were near term payment obligations. Under the revised capital rules, different confident levels are used to ensure that an appropriate level of capital is held in respect of shorter and longer term payment obligations increasing required capital as payments dates become more proximate. Given our portfolio profile, this will require that we provide for the majority of our reserves in capital at the more moderate CTE-90 framework which is approximately equivalent to 96% confidence level result.

As mentioned earlier, the CTE-90 scenario depicts on average an immediate 20% decline in markets and no growth for over a decade. This is quite conservative. It is still a very onerous framework will result in significant volatility in our capital ratios should equity markets continue to gyrate. In addition to the OSFI changes we have reviewed and are updating our internal model assumptions to better reflect the actual experience. In particular policy holder behavior is more favorable than the current model assumptions, and as a result we will be updating our assumptions accordingly. Finally, as recently announced, we

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successfully executed a binding credit agreement for additional financing totaling $3 billion that is being provided by Canada's six largest banks. This loan facility has the five year term and is priced at a floating rate of Canadian Banker's Acceptance plus 380 points. Yesterday, this was the borrowing rate of about 6.4%. This facility is prepayable without penalty in whole or part at anytime of our choice.

Given our modest historic levels of leverage, the financing to MFC will be available to be deployed, as required, downstream as qualifying capital in the MFC's regulated insurance subsidiaries.

Given these recent developments, slide 14 provides an update on our estimated MLI MCCSR position and sensitivities going forward. As Dominic observed, factoring in the OSFI changes, updated model assumptions and use of $2 billion of our new term funding facility as regulatory capital even after reflecting October's continued sharp decline in global equity markets we estimate that our MCCSR ratio as of October 31 of 2008 would be at approximately 225%. A further 10% market correction from the October month end levels would result in a decline of approximately 20 points in our MCCSR ratio. It would take a market correction of 25% from the October 31st levels to reach the lower end of our targeted MCCSR range of 180 to 200%.

Based on these sensitivities, we expect all our insurance subsidiaries to close the year end at or above our internal target capital levels. Going forward, because the reserve methodology requires us to fully capitalize the impact of current period market performance as if it is a permanent long-term impact and because under the conservative basis on which the reserves are calculated much of our segregated funds guarantees are now considered to be "in the money", we'll see considerable volatility in net income both positive and negative from equity market performance. While the impacts may be material, I would emphasize they will not represent crystallized amounts as the guarantees for which reserves are being accrued are generally payable many years into the future. Therefore, variable annuity related charges to earnings such as we are likely to book in the fourth quarter should markets fail to recover from the October month end levels we will reverse and generate positive income when the markets do eventually recover from the current low levels. Given the volatility that our stochastic based reserve methodology for variable annuity exposures is likely to produce, while equity markets remain unusually volatile it may be useful to consider operating results both on a "as reported" and on an "operating earnings" basis which is adjusted for these non-cash variable annuity related accruals.

Turning to slide 15, pre-tax credit impairments in the third quarter were $323 million, well above the levels reported over recent years. In light of the macro-economic environment we continue to be very pleased with our credit position.

On slide 16, we provide further details of the $253 million of credit related charges incurred in the quarter. Exposures to Lehman, AIG and Washington Mutual resulted in $192 million post tax charges indicated. All other credit's impacted earnings by $17 million. In addition, credit downgrades reduced this quarter's earnings by $44 million. As discussed in prior quarters our actuarial practices require us to strengthen our reserves upon credit downgrades, and therefore we took a charge in the current quarter for the reserve impact of such credit downgrades.

Turning now to slide 17, I would like to take a moment to provide an update on investment portfolio which continues to be well diversified and a very high quality. As discussed in prior quarters, our exposure to problematic investments is quite modest, and we continue to enjoy positive cash flows on these holdings. Specifically our subprime RMBS exposures are down to $473 million at quarter end. We continue to enjoy average monthly prepayments of approximately $10 to $12 million on this portfolio. We have also successfully avoided the wide range of other complex instruments that are performing so poorly. And, we have never written credit default swap protection and we do not add credit risk in our securities lending practices.

On slide 18, we provide an update to the slide we presented at a recent Investor Day summarizing our limited exposure to other more topical investments. Our commercial mortgage backed security portfolio of $5.7 billion is of exceptionally high quality, with over 89% rated AAA today, and of great vintage, with over 86% originated in 2005 or prior. Despite the securitized nature of the CMBS portfolio, we assessed each underlying holding not simply relying on the bundled rating or loan to value indicated for the portfolio. Given heightened market uncertainty we have reduced our securities lending activities considerably, with the

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total amount outstanding as of October 31st at $1.2 billion all of which is backed by the highest quality liquid collateral. We also disclose our modest disclosures to US Airlines and North American auto industries.

As shown on slide 19, our credit quality portfolio continues to be of high-quality. Only 5.2% of our bond portfolio is below investment grade and of that, less than 2% is rated B or below. Slight credit migration from our '07 year end position reflects some downgrades but also selective investments as we are seeing credit spreads widen and. believe we are once again being paid adequately for taking on credit risk.

Finally as slide 20 illustrates, our bond portfolio has consistently performed better than the general market. Compared to the S&P universe, our portfolio downgrades as a percentage of total issues has outperformed the referenced benchmark.

Moving on to slide 21 operating results, premiums and deposits of $16.4 billion were in line with the prior year despite the challenging environment . Premiums in the third quarter were up 20% over the same period in '07, driven by strong insurance sales and recurring premiums. As expected, deposits were lower due to volatile and unsettled market conditions.

Turning to slide 22 during the third quarter, new business embedded value totaled $540 million, an increase of 5% over the third quarter of last year on an equivalent basis. Strong levels of new business embedded value were generated by insurance businesses, particularly in Canada Individual Life, US Long-Term Care and Japan. Excluding a large group insurance sale in the prior year, total insurance sales were up 16% on a constant currency basis. Overall, insurance sales in the quarter produced new business embedded value of $212 million, an increase of 10% over '07. Wealth management sales were down 6% reflecting very unsettled markets but generated new business embedded value of $328 million in the quarter, compared to $322 million in the same period last year.

On slide 23, total funds under management on September 30, '08 were $385 billion. $14 billion lower than the prior year. The impact of capital markets is quite evident in these results. Strong positive net policyholder cash flows of $17 billion and favorable currency boom is $19 billion were overshadowed by over $42 million of negative investment income due to some $52 billion of market value declines.

On slide 24, US insurance earnings were US$298 million in the third quarter, up 49% from the US $200 million a year ago. The increase in earnings was driven by strong enforced business growth, favorable claims experience and investment related gains. This was partially offset by higher strain on new sales levels compared to a year ago and an increase in Variable Life reserves in the lower equity markets.

Turning now to slide 25, John Hancock Life Insurance again ranked number one in US individual sales-- this is for the fourth consecutive quarter. Sales in the third quarter increased 7% over prior year levels, primarily driven by higher universal life and term sales. Long-term care sales momentum continued, with third quarter sales up 9% over a year ago. Group sales were strong in the quarter, both due to the addition of new groups and new enrollment programs for existing groups. Our new leading edge product continues to contribute an increasing portion of retail sales representing more than 20% of the quarter's volume.

On slide 26, US wealth management earnings of US $22 million in the Variable Products group for the third quarter was down significantly from a year ago as a result of the impact of lower equity markets being reflected in higher segregated fund guarantee reserves and lower asset-driven fee income. We are undertaking a comprehensive review of our variable annuity offerings and expect to make significant changes to reduce risk and improve the profitability of this line.

On slide 27, net inflows for the Variable Products group were US $1.4 billion, down from a year ago. Variable Annuity sales were down 30%, which we believe is consistent with what the industry will be reporting this quarter. Despite the decline, sales through our new distribution relationship, Edward Jones, increased 15% over the prior quarter. The pension sales for the quarter were up 16% over the same quarter of the prior year, driven by strong transfer volumes. Mutual fund sales were up 13% versus a year ago. This was more than offset by increased withdrawals in light of market uncertainty.

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Turning to US Fixed Products group on slide 28, the third quarter earnings were negative due to this segment's share of credit and equity related investment losses. On the sales front, Fixed Products recorded very strong sales up 80% over the prior year, as equity market volatility and an upward sloping yield curve drove increases in both Fixed Deferred and Payout Annuity sales.

On slide 29 Canada Group and Individual Insurance reported increased earnings over the prior year, while Individual Wealth Management posted a significant decline due to a rise in reserves for segregated fund guarantees. Group earnings were up due to improved claims experience and individual insurance enjoyed favorable investment related results.

Turning to the Canadian Insurance sales on slide 30, all major product lines and in particular Universal Life and Term, contributed to a strong result in our Individual Insurance segment in Canada. Sales grew 8% in Individual Life and 6% in Affinity. Excluding the jumbo case sale in the third quarter of '07, Group Benefit sales were up 32% this quarter, driven by sales of our trustee and signature product suites. Group Pension sales declined by 7% over the same quarter of the prior year largely due to equity market volatility.

On slide 31 Canadian Individual Wealth Management posted net flows of $1.2 billion for the quarter, more than doubling the prior year's level. Segregated fund sales, driven by IncomePlus exceeded the prior year by 32%.

Manulife Bank reported record loan volumes in the third quarter, exceeding $1.3 billion. Overall, new home volumes were up 39% in third quarter of '07, due to continued success of ManulifeOne. The credit quality of the Manubank portfolio continues to be exceptionally strong with impaired loans only representing a nominal two basis points for 0.02% of total bank lending assets, significantly below industry averages. Market volatility helped boost fixed product GIC and annuity sales, where deposits of $177 million exceeded the prior year's level by 62%.

Turning now to slide 32, Asia and Japan earnings were US $208 million versus US$216 million a year ago. This quarter's results benefited from strong in-force business growth and insurance sales, particularly in Japan offset by lower fee income and higher segregated fund guarantee cost due to equity market declines.

On slide 33, you will see that insurance sales in Asia and Japan increased by 39% over the third quarter of '07. Japan sales were more than doubled that of the prior year, up 160% as the business benefited from new product introductions and continued transaction in the newly established MGA channel. In Other Asia, insurance sales rose by 3%. Singapore achieved strong sales through both its bancassurance and agency channels and sales in China were consistent with the branch expansion program. Hong Kong individual insurance sales were up 10%, driven by success of the recently launched products and increased agent focus on the insurance products versus wealth products.

We turn to slide 34, wealth management net flows in Asia and Japan were US $762 million, down from prior quarters as a result of the turbulent markets.

On slide 35, earnings from the Reinsurance Division was US $47 million, up from US $42 million a year ago. The increase was primarily driven by improvements in P&C claims experience and favorable investment related gains. Partially offsetting these favorable items were charges related to segregated fund guarantees and higher Life Reinsurance claims.

The Corporate and Other segment reported a third quarter loss of $192 million, versus earnings of $21 million in the prior year. This variance was primarily caused by lower realized gains on available-for-sale assets, credit and equity impairments on assets in the surplus segment, costs related to our Variable Annuity hedging program and non-recurrence of a '07 claims gain relating to our run-off John Hancock Accident and Health business.

This quarter's financial results have been adversely affected by the volatility of equity markets. However, our global franchises remain strong and we are well positioned to increase market share. Our balance sheet is strong and asset quality is excellent. With the refinements the segregated fund capital requirements and our new bank financing, our estimated capital levels as of

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October 31st are at a very solid 225% MCCSR capital level, despite the significant year to date market declines. As new opportunities emerge, we are well positioned to consider them with both prudence and diligence.

Thank you. Let me turn the call back over for

Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

Thank you Peter, you can catch your breath now. Operator, we are ready for the question and answer portion of our conference call.

QUESTIONS AND ANSWERS

Operator

(OPERATOR INSTRUCTIONS) The first question is from Colin Devine from Citigroup. Please go ahead.

Colin Devine - *Citigroup - Analyst*

Good morning. And first I would like to say, John, I appreciated your remarks at the beginning as to how Manulife came to be in the financial situation it is today. The part that I guess troubles me the most about this, though, and what you didn't address is where were the Company's risk management systems when this was happening? Peter has laid out many times over the years his comfort with taking the 10% to 15% market decline on the VA product and that you felt that was prudent, and that's why you didn't hedge. But once the market started to fall below that, you've clearly modeled many times what the impact would have been on your MCCSR. I do not believe that was any surprise to Manulife, what happened. Why was not -- why was some sort of proactive action not being taken in October while all of this was going on, because what would you have done if OSFI effectively hadn't moved the goalpost for you? Because it seems [essentially] you might have had to raise $5 billion of equity.

Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

Well, I guess let me answer those questions one at a time. If we hadn't been able to move the goalpost, as you say, or as I would say, have a more realistic reflection of what a prudent level of reserving for this risk is, we might have had to raise capital in another form, And we probably would have done that. Why didn't we hedge earlier, I think was your first question?

Colin Devine - *Citigroup - Analyst*

No, that's not the question. It's why didn't you start react or starting to hedge once you went through your tolerance level at the 15%? That is, in our view, where the breakdown here has occurred.

Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

Well, I mean, you are entitled to your view, Colin, that it was a breakdown. I guess that we didn't expect the volatility in the markets that actually transpired. We didn't expect the markets to be as unsettled as they turned out. We didn't expect all of these financial institutions to fail. In one week, we had massive reorganization of the financial sector. Maybe you guys saw it at Citibank, but we didn't see it. And to jump into the market when volatility was at its peak would have been prohibitively expensive to our shareholders.

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We think that the risk that's embedded in this product is one that Manulife and all insurance companies, frankly, are ideally suited to absorb, within limits, within limits. You know, we are happy with our position. Our modeling suggests to us that even with these low levels of market indices that this business will generate very nice profit for us, as one of the slides that we had in the book there showed. I think you would have to agree that reserving on the basis that, where the markets have just gone down 40%, and they are going to down another 40%, and, and most important, stay there for 10 years is the level of reserving that most people, most reasonable people, would think is excessive. If any other institution in any other business had to reserve on those eventualities, there would be nobody doing business, Colin. You would need a staggering amount of capital, and at the end of the day all you would be doing is increasing the price of the service provided to customers to levels that no one could afford.

Colin Devine - *Citigroup - Analyst*

Dominic, we didn't disagree that OSFI made the right decision, and that the capital limit requirements were completely unrealistic. It's what was the Company doing from October 1st to the end of the month that let it get caught like this, okay? (multiple speakers) But the second thing -- Dominic, I'm not done yet. Dominic, hold on, please, sir. If you are so happy with this product and if you are so happy the profitability is there, okay, then how come, as Peter noted, you are doing a complete redesign of the product? That suggests to us quite the opposite, sir.

Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

Well, I think you are right. We clearly did not appreciate that markets would fall quite as sharply as they did and expose us to the level of potential risk that they have. Like everybody else, we follow the marketplace, and we notice that our competitors have also been affected. And as is normal in competitive markets, when the competitors experience what they do, they adjust their behavior accordingly. So we're going to look at our product to make it more profitable. We're going to perhaps adjust our pricing, perhaps adjust the features, perhaps do both.

Colin Devine - *Citigroup - Analyst*

And you still feel you are adequately reserved?

Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

Well, you know, you have got to look at the amount of the reserves that we have in relation to the pattern of outflows. I think when we -- I'm pretty sure when we got together in -- whenever we had the last conference call, did we not have --

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Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

October 14th, yes.

Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

October 14th, we had displayed for you the cash flow patterns on this book of business. You know, the first cash out on this business starts seven years from now, and then it continues for 30 years. Even in the worst scenario, the scenario CTE-95, where the markets go down 40% and stay there for 10 years, in the worst period our maximum outflows are $800 million pretax. Against the pretax revenue base of Manulife, with -- given all our other businesses, I suggest to you that that is affordable.

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Colin Devine - *Citigroup - Analyst*

Thanks. I don't disagree, but then it begs to differ, because why is the product going through a major product redesign? But we'll let you get on to the next question.

Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

Okay. Thanks, Colin. You have given us a good grilling.

Operator

The next question is from Michael Goldberg of Desjardins Securities. Please go ahead.

Michael Goldberg - *Desjardins Securities - Analyst*

Thanks. I've got a couple of questions for now, not as hard-nosed as that, but --

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Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

Thank you, Michael. We appreciate all the kindness we can get.

Michael Goldberg - *Desjardins Securities - Analyst*

Can we view the $318 million gain that you talked about as an offset to the $578 million after-tax impact of the weak equities? In addition, how much is that $318 million after tax? I presume it is a pretax number.

Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

It is a post-tax number, Michael. I would think of it against the credit. The way I would describe it is the equity-related move is going to cycle through quarter to quarter and be quite erratic. You should think of that as an accrual that you have your own views on over time.. But we own our investment results and our credit results, and I think operationally both of those were a little volatile this quarter. We did quite well on our investment assumptions and results, and we did not as well with the financials having credit impairment.

Michael Goldberg - *Desjardins Securities - Analyst*

So it's a post-tax number?

Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

That's correct.

Michael Goldberg - *Desjardins Securities - Analyst*

Okay. And does the gain on the increased nonfixed income investments backing liabilities in effect arise from revaluation as those assets are shifted from backing surplus? If so, how much more is backing surplus with a potential gain?

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Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

You're quite close. Essentially, we look at the cash flows in the liability segment, and we have for a period of time had a program to support our liabilities with more total return or non-fixed income assets, some of which right now are still in surplus. Others will be originating over time. So this is a little lumpy because of the nature of when we are able to do things. But it's a program we have had in place for a period of more than a year, and will continue until we hit our objectives, for probably another couple years. We're going to have to source these assets at our target rates of return.

Michael Goldberg - *Desjardins Securities - Analyst*

If you moved it all now --

Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

(multiple speakers) today as opposed to not that long ago, where we basically had to sit on our hands and we couldn't get assets with the attributes we were looking for.

Michael Goldberg - *Desjardins Securities - Analyst*

So is it that you don't have the assets now, or they're sitting -- going -- they're up against surplus?

Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

Yes, there is some in surplus, but we are not at the level we want to be in the total Company.

Michael Goldberg - *Desjardins Securities - Analyst*

Okay. Great. I'll requeue.

Operator

The next question is from Eric Berg of Barclays. Please go ahead.

Eric Berg - *Barclays Capital - Analyst*

Thanks very much and good afternoon. Dominic, in the earlier exchange, you indicated that several things happened in the world that you didn't anticipate. Let's just agree, lots of us didn't anticipate it. A tremendous amount of wealth was lost. That is proof positive that most people who were right in your camp didn't anticipate it. But it is a fact some things happened that you didn't anticipate, and we almost had a very bad situation here.

So my question is, getting away from the past and now trying to look forward, what are you doing in running this Company right now, since we know things can happen that you didn't anticipate? Apart from changing your variable annuity, which could take months, what are you doing right now to prevent yourself from being in another similar situation? Are you, for example, hedging more?

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Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

Well, Peter wants to go first here.

Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

Let me just start off with some operational things. We are now hedging all the new business originated in the US so that we don't add to our existing position. There are some elements of our offering which we can tune fairly quickly. We would expect as early as January to have probably some amendment. So we are taking action on those fronts. As well, we have made sure that our capital is quite robust in case markets remain volatile. But it's a case of trying to have appropriate action as opposed to excessive. Raising a ton of equity is very, very costly if markets bounce back, and we want to have reasonable responses to development. But there is no question this needs attention.

Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

And I think in fairness, too, Eric, we discontinued our buyback program to conserve capital. I guess that we probably had and have faith in our Company and in our ability to raise capital, given our ratings and our standing in the industry, given the strength of our franchises, our different businesses around the world. That gave us the confidence that we would be able to withstand the market movements that we have experienced. As to -- an additional step we did was to get the bank financing to put our MCCSR up to probably historically high levels. We could withstand, I don't know, a drop of 25%, 30% in the equity markets from today before we pierced our MCCSR target range of 180 to 200.

Now, you know, we run this Company for our shareholders and for our policyholders. What's a prudent level of capital to keep? You tell me. If we'd have had twice the capital at the beginning of this, people would have been criticizing that we're underemploying and inefficient in managing their money. So I think we have had a tail event here. We've had the worst meltdown in I don't know how many decades -- certainly in my lifetime. And I think one ought to be a little bit reasonable about why didn't you have the capital to anticipate the tail, and which, by the way, we did have the capital to anticipate the tail. It's the second tail that was a bit problematic. So I think that, all in all, we have come out of this a heck of a lot better than just about anybody on our industry, frankly. And if you -- when you look at some of the questions about aggregate risk and so on, just look at our books. We knew that we have -- I mean, we have shown you this. You can read it in our Annual Report. Manulife has very relatively minor amounts of any other kind of risk. We don't have a lot of credit risk on our books. We don't have a lot of interest rate risk on our books. We choose to take our risk -- we chose to take our risk, if I could put it that way, in equity markets. We feel confident as to their behavior over the long term. I am very pleased that we are where we are today, given what has transpired in the markets. I think a lot of our competitors would like to be in an equivalent position to us.

Eric Berg - *Barclays Capital - Analyst*

My second question, and then I'll requeue, is a conceptual one. Peter, and maybe this should be better addressed to -- well, obviously to Peter or to Simon, if he is in the group today. But you indicated in your prepared remarks, Peter, that the earnings -- something about the earnings could be quite volatile going forward. I need some help in understanding why that is. By my question, I mean this. Whether the stock market goes up or down, 5% , 10%, whatever the changes are and whatever the direction, you are using the same methodology. You are calculating the required reserves and capital under the regulatory rules. Why are we in a period where the earnings will necessarily be volatile going

---

Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

Because you'll have -- I'll try to answer that in layman's terms. You would have moneys moving out of your capital account -- either out or into your capital account, which would go through your income account.

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Eric Berg - *Barclays Capital - Analyst*

But wouldn't that be the case regardless of where the stock market was?

Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

No. I think, Eric, the simple way to answer it is that the reserve and capital required for segregated fund guarantees is very volatile. And so, depending on whether you maintain the same CTE level or not within some band, it is going to move around quite a bit as markets are volatile. My view is that's not really the same thing as what we normally consider operating income. And so I am explaining in advance that we had volatility this quarter. We're likely to have it next quarter.

As long as markets are turbulent, our income statement is going to reflect the changes in the reserves related to segregated fund guarantees, which are calculated on a stochastic basis, and it is quite sensitive. Given that they are very long duration obligations, the mark we're taking, that reserve charge or release -- it could be a big release if markets rally -- is likely to be volatile. It is more so the case now that the product is more in the money because markets have moved down, but the whole thing is really somewhat accounting presentation, because in the end you want to decide how much is our ultimate obligation, and is it much more accurate this quarter than last. And I would submit to you, there is an element of update, but there is also an exaggerated impact in how we book those reserves.

Eric Berg - *Barclays Capital - Analyst*

I will requeue. I have follow-up questions. Thank you.

Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

Well, Simon is here. Is there anything you wanted to add, Simon, to what was said here about why there would be volatility on a reporting period to reporting period in the earnings statement?

Simon Curtis - *Manulife Financial - EVP & Chief Actuary*

Well, I would just reiterate what Peter said, that the accounting and capital model that we have to follow for Canadian GAAP and MCCSR is based on using the end-of-period market values. So even though we are very conservatively accrued for reserves and for capital, as the markets move, we have to reflect that market movement and the capitalized impact of that market movement each period. So I think --

Eric Berg - *Barclays Capital - Analyst*

But Simon, wouldn't that impact, wouldn't your accounting be agnostic to the height of the market? My question is, whether these contracts are in the money or out of the money, a percentage point change in the market from whatever the starting point I would think would have the same effect, or no?

Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

No. I think once they're in the money, it is more volatile. And secondly, because full credence is given to the starting value, what happens every time that starting value changes, it impacts your result. I think you understand the general trend, Eric.

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Eric Berg - *Barclays Capital - Analyst*

Yes. Thank you.

Operator

The next question is from Andre Hardy from RBC Capital Markets. Please go ahead.

Andre Hardy - *RBC Capital - Analyst*

Thank you. Back on the topic of earnings, Peter, even though you consider those as unusual, do you care to give us a sensitivity, like you gave us a sensitivity on capital?

Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

I am not in a position to update, because it depends on a range of things, and in particular where we stay in the CTE corridor. But it is not as clear now as it might have been previously.

Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

As we were at the CTE-80, and it all depends what CTE level we choose to go to at the next reporting period.

Andre Hardy - *RBC Capital - Analyst*

You just chose to go from 69 to 80. What was that based on, and can we read anything into that?

Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

We decided that the markets were quite volatile. So at this time we strengthened the reserve. But we haven't committed to do that indefinitely, so we revisit that decision as things develop.

Andre Hardy - *RBC Capital - Analyst*

And I guess another way to ask the question, there will be -- there was a change in how OSFI asks you to provide for capital and reserves.

Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

I guess to be clear, we went to OSFI with our situation here, showing what we think is a punitive computation. So I've explained about four times here that we have had a tail event and now we must not only provide for that tail event, but assume that another one is going to happen. What is really onerous in the scenario that we've got to reserve -- maintain capital for is that you have to assume that after that second tail event there is no improvement for more than a decade.

Now, that's like nuclear winter. If you actually had that type of scenario transpire, I think the Japanese index would be 2000 and stay there for 10 years. I don't know, the Canadian index would be like 4000 or 5000 and stay there for 10 year. So we went to our regulator and explained that we thought this was excessive under the circumstances, given that a tail event had already occurred. They deliberated, as their objective in life is to make sure that our policyholders are looked after. They came up with

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what I think is a reasonable and, I understand, not inconsistent standard with other jurisdictions, which is to require a CTE level of 90 for payments due beyond five years.

Andre Hardy - *RBC Capital - Analyst*

I guess the question I was trying to ask is, this quarter, obviously, equity markets are down, but are we going to see a reserve gain related to the OSFI changes?

Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

No. I am sorry. I said no, and Simon is fidgeting. Did I say the wrong thing?

Simon Curtis - *Manulife Financial - EVP & Chief Actuary*

No, you said the right thing. I want to clarify one thing. The discussions at OSFI were really around the additional capital that we needed to hold on top of our reserves. Nothing in our discussions with OSFI impacts the GAAP reserves. Our GAAP reserves follow the same practice as they did previously. And in fact, we actually strengthened our reserves this quarter relative to where they were historically in the range. So our reserves on the balance sheet are very strong, at the highest level we can hold, and the discussion with OSFI was just really around the additional capital for a subsequent market decline.

Andre Hardy - *RBC Capital - Analyst*

Okay, so just the capital over the CTE-80?

Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

Yes, that's right.

Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

That's exactly right.

Andre Hardy - *RBC Capital - Analyst*

Last one, and it's a quick one. On page 9, Peter, you go through the different earnings impacts. The 154 related to equity support and general account liabilities, those equities are still on the books?

Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

Well, they are probably worth less would be my first comment, but generally speaking, yes.

Andre Hardy - *RBC Capital - Analyst*

Said differently, those losses haven't been crystallized, have they?

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Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

[Not on the liabilities].

Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

No, no.

Operator

The next question is from Doug Young of TD Newcrest. Please go ahead.

Doug Young - *TD Newcrest - Analyst*

Just regarding the $318 million gain that flowed into earnings, curious as to the amount that came from terming out the asset liability mismatch on the North American insurance business; if there was such an event, what the earnings impact would be; and if there was that event, the amount of reserve that would have been released in the capital, released associated with that.

Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

The term-out component was fairly minor versus the interest rate mismatch we had. So the basic mismatch is still there. What we really did is in recent quarters, we hadn't been dealing with the duration on long-term care. In other words, we hadn't been buying the long bonds that we normally would have bought as they weren't attractive. In this quarter, we caught up for a number of quarters of new business term-out. That would be the impact related to extending duration. So the core mismatch that we've talked about over a period of years now at this juncture is basically substantially unchanged.

Doug Young - *TD Newcrest - Analyst*

And so what was the earnings impact from that, Peter? Was it material? Was it 10%, 15% of the $318 million?

Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

Just poking around here -- so I think it would noteworthy, but not the biggest item by far. I think it would be -- does anybody have a number here?

Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

No.

Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

I don't think we have a breakout. We will poke around. We'll see if we can -- I will comment if I can get it in a few minutes.

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Simon Curtis - *Manulife Financial - EVP & Chief Actuary*

It's Simon here. We don't have it in front of us, but we will find it. It is not a material amount of the $318 million. And just to answer one further part of your question, there is no knock-on effect on the required capital. That's only an earnings item.

Doug Young - *TD Newcrest - Analyst*

Okay. And a second question is just regarding the $3 billion of capital that you're borrowing from the banks. I guess you have the ability to pay it back without penalty. And how quickly do you plan to pay it back, would be the first part. The second, obviously this increases your debt to cap. I'm just wondering what the conversations that you may or may not have had with the rating agencies, what impact that could have on your ratings.

Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

Doug, we expect all our ratings to be maintained. So that's the second question. One or more of the agencies may comment that more leverage is less attractive than less leverage. But that is our expectation. In terms of paying it back, if long-term sources of funds were extremely attractive, we are free to do it, refinance it at any time. So it will be dependent on market conditions and developments, but we are unconstrained in that area.

Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

But I guess I would like to just add that all things being equal, we would like to get the banks repaid sooner rather than later.

Doug Young - *TD Newcrest - Analyst*

Dominic, are you free to use that capital for acquisitions?

Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

The purpose of the capital is we designated it, or at least -- I don't know whether legally we're bound to use it in a -- we are going to use it to downstream to our operating companies to bolster their capital position. Capital is fungible once it is in the organization. It is certainly not our intention to use the $3 billion to go out and make an acquisition.

Simon Curtis - *Manulife Financial - EVP & Chief Actuary*

But I think, more importantly, it does not encumber our ability to do acquisitions in any way, shape or form.

Operator

The next question is from Jukka Lipponen from KBW. Please go ahead.

Jukka Lipponen - *KBW - Analyst*

Good afternoon. One thing -- in terms of the potential issuance of equity, if you were to make a larger acquisition, I would assume that you are not ruling out issuing equity in that scenario.

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Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

No, we are not.

Jukka Lipponen - *KBW - Analyst*

Second question, you showed the regulatory target for the RBC ratio as 200%. Can you clarify what you are meaning by that?

Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

What is that in respect of?

Jukka Lipponen - *KBW - Analyst*

On slide 12, you showed for John Hancock, [there is alliance] on the regulatory target for RBC [ratio as 200].

Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

That is the regulatory framework, at which point you would probably have discussions with your regulator. But our internal target is higher than that and we are above our target.

Jukka Lipponen - *KBW - Analyst*

I think the regulatory target is 100, or the official --

Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

Okay. I don't know. Maybe the 200 is the band in which one could operate. We intend to be above that.

Jukka Lipponen - *KBW - Analyst*

Okay. Thank you.

Operator

The next question is from John Reucassel from BMO Capital Markets. Please go ahead.

John Reucassel - *BMO Capital Markets - Analyst*

Thank you. Just hoping to get a little detail on the bank funding. So this is going to be borrowed at the holdco. Is it going to qualify as Tier 2 at MLI? Is that what it is going to do?

Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

No, [it's ported] at the holdco, and we can downstream it in whatever form we like. It would probably equity, equity or contributed surplus.

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John Reucassel - *BMO Capital Markets - Analyst*

And OSFI -- so it is five-year paper, but OSFI gives you permanent Tier 1--?

Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

Yes, we are underleveraged, John. So we have that capacity. And OSFI is fully aware of it. If we had been more leveraged, then that wouldn't have been as acceptable.

John Reucassel - *BMO Capital Markets - Analyst*

Okay. And is there any security on the debt?

Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

No.

John Reucassel - *BMO Capital Markets - Analyst*

So straight unsecured loan to a financial service holding company?

Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

That's correct.

John Reucassel - *BMO Capital Markets - Analyst*

Wow, okay. And you did mention --

Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

Wow, terrific, you mean, John?

John Reucassel - *BMO Capital Markets - Analyst*

Yes. I am surprised the banks do that, but good for you.

Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

It is a reflection on the credit quality of the borrower.

John Reucassel - *BMO Capital Markets - Analyst*

You mentioned you're doing hedging now, Peter. I am just trying to -- you know, I guess I look at the US companies, and some of these US companies have elaborate hedging programs, and it doesn't seem to really help them.

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Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

I am glad you mentioned that.

John Reucassel - *BMO Capital Markets - Analyst*

And then hedging is not capital relief at OSFI. So --

Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

I am glad you mentioned that, too, John.

John Reucassel - *BMO Capital Markets - Analyst*

Well, I guess the real question here is why not just -- isn't it just best to, if you want to settle this issue, reinsure it or issue equity?

Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

No. I think if we reinsured it, we'd have issues with counterparty risk and price. And so we need a strategy that includes a range of things, and I think hedging does fit in. What we're looking at is exchange-traded contracts, because we don't want to exchange the long-term economic risk for short-term counterparty risk. We do have a program in place. It hedges a substantial portion, but not 100% of the product. There are some components that you can't track and trade on an exchange-traded instrument. We are expanding that to include new business to try and slow the growth while we refine the product. But we are as sensitive as anybody and then some about the shortfalls of hedging. And that's why we are only looking to use it appropriately.

John Reucassel - *BMO Capital Markets - Analyst*

Okay. So just one last question. On the equity issue, Dominic, I understand your reluctance, and I am sure shareholders, but the market, right or wrong, may be pricing some of this in. It would maybe give you a little more flexibility on doing acquisitions. It would certainly strengthen up your balance sheet. So why not do it? Is that just a naive assumption on my part, or is it just too expensive, or--?

Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

No, I mean, it is a very good question. You keep talking about strengthening our balance sheet. I think we have one of the strongest balance sheets in the financial services industry, not just in insurance, but in financial services, period. Our ratings reflect that fact. I guess that we were very mindful of the experience of others who raised equity during this turbulent period, and it didn't workout particularly well for them. We see equity as a more expensive form of capital than what we were able to raise.

Of course, if we didn't have any options, we would have raised the equity. But I don't know why as a shareholder, given that the Company is extraordinarily well capitalized by any measure, whether you measure leverage in the crude way or you measure liquidity exposures or the fact that I've got permanent funding, I've got no borrowing, really, to speak of, I've got a lot of cash, I mean, this is a very, very robust balance sheet. The "exposure," if I can put it in quotation marks, arises because of an extraordinarily onerous capital requirement. I don't think -- did any of you know what CTE-95 was or what the scenario was that you are talking about, a decline of 40%, staying there for 10 years? Don't you think that is onerous?

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John Reucassel - *BMO Capital Markets - Analyst*

Dom, I agree it is onerous. I just -- I guess what I am looking at here is a once-in-a-lifetime opportunity to maybe grab some real estate out there.

Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

Well, we're not going to miss that opportunity. Our practice has been to fund very big transactions when we did them, or when they were imminent, not raise the money first and then find that you are scrambling to invest it and settling for less than optimum situations. I mean, judge us by our record. When we did the John Hancock transaction, no one -- we didn't have the capital sitting on our balance sheet with that deal. We think that the respect in which our firm is held and the following that we enjoy, we think that if a proper deal showed up, we could finance it then and there.

John Reucassel - *BMO Capital Markets - Analyst*

Okay. And just a last question. The bank funding, you could draw on that today and none of it has been deployed? Is that correct?

Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

We signed the agreements last -- yesterday, I think.

Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

[It will take us] a few days, and then we will begin drawing -- we will draw in a short timeframe.

John Reucassel - *BMO Capital Markets - Analyst*

Okay. Thank you.

Operator

The next question is from Darko Mihelic from CIBC World Markets. Please go ahead.

Darko Mihelic - *CIBC World Markets - Analyst*

Hi. Thank you. I am just trying to conceptualize -- much like you are helping us out with the concept of CTE-95, I am try trying to conceptualize what happens if these markets continue to be volatile for another year and we have passage of time. How long does it take to roll into the bucket of CTE-90? You mentioned that most of your book is seven-years-plus out. Isn't there like a bucket that moves into the five-year timeframe?

Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

Exactly. I think that every year that goes by, your cash flow pattern becomes more front-ended, and you then start needing to reserve at not CTE-90, but CTE-95 and then eventually CTE-98. But I think our first outflows are seven years from now.

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Simon Curtis - *Manulife Financial - EVP & Chief Actuary*

Yes, our first net outflows would be around seven years from now. If you are looking back at the October 14th presentation, we were showing that we really don't have any material outflows until 10 years from now. Really, there are negative flows or slight -- or small positive flows in the (multiple speakers)

Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

It is quite a period of time.

Darko Mihelic - *CIBC World Markets - Analyst*

Okay. I think that -- am I right, when I'm looking at your capital in your [sipack] on page 41, am I right in assuming that you may have moved capital from the US subsidiary into the Canadian subsidiary? Would that be a correct characterization?

Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

That's part of it. We have moved capital from a number of places. That's correct.

Darko Mihelic - *CIBC World Markets - Analyst*

Is it a material amount?

Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

No. The biggest amounts were from other spots. We tend to store excess capital in places that are tax advantaged, but some did come from the US. But that is normal. The US is a big business for us. It normally does remit capital back to the parent. The timing, we adjusted it one quarter from what might be basic. But yes, there's normally movements from the US.

Darko Mihelic - *CIBC World Markets - Analyst*

And just one last question, if I may. This whole experience, has it changed what you might look at in terms of acquisitions? I think we are all very familiar with what Manulife may have had on its wish list maybe a year ago. Given what has happened, has that changed now in terms of your appetite for what particularly you might be interested in actually acquiring?

Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

I don't think so. I think our wish list remains undisturbed as a result of what's transpired now. Again, you look across the spectrum of the industry, and different companies have different problems that have different sources. Some have VA issues and some have the credit issues. And we are still keen on sticking to businesses that we understand and products that we've got experience with and that we have had success with in the past. So you can draw your own inventory of companies who meet that criteria.

Darko Mihelic - *CIBC World Markets - Analyst*

Thank you. Fair enough. Thank you.

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Operator

The next question is from Mario Mendonca from Genuity Capital Markets. Please go ahead.

Mario Mendonca - *Genuity Capital Markets - Analyst*

A question about -- I think it is page 14 of your presentation. You indicate that the October 31, '08, MCCSR is about 230. I think you used 230 and you used 225 on a few occasions, but I suppose you're talking about the same number. Is that right?

Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

Yes, it is actually 225. There was one gremlin that crept into our slide, so I apologize.

Mario Mendonca - *Genuity Capital Markets - Analyst*

Okay. So it is really 225. Okay. I understand.

Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

That is based on that $2 billion that I indicated we are planning to downstream.

Mario Mendonca - *Genuity Capital Markets - Analyst*

Right. And presumably the other $1 billion stays at the holdco or goes somewhere else if it's needed.

Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

That's correct.

Mario Mendonca - *Genuity Capital Markets - Analyst*

Now, the 225, you can be at 205 with a 10% drop in markets from October 31st levels. In the S&P, that would only be like an 875 S&P, and we are at like 910 right now. So, 35 to 40 points on the S&P, all it takes is a US bank to report a miss in earnings and we will be down 35 points on the S&P tomorrow.

Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

And we will be at an MCCSR within our range.

Mario Mendonca - *Genuity Capital Markets - Analyst*

Right. No, I totally appreciate that. You'll be at an MCCSR of about 200. The point I'm making is in S&P's negative outlook that they've put on the Company, they are saying the MCCSR has to stay above 200 and the debt to capital can't go over 25, and the debt to capital pro forma is 25.

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Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

Mario, first of all, you are referring to Moody's. S&P did not see anything unattractive about us. The Moody's comment, and if you've looked at their rating actions recently, they are looking at equity-related risk as being more volatile, as we are. And they're commenting, although they have confirmed our ratings, that we have equity-related risk. We have described that in lurid detail for you.

And I guess our view is we have quite a bit of capital to deal with the volatility we're facing, and we have other choices, other flexible choices either on our balance sheet or in the capital markets, if the move was bigger, than what we can currently absorb. But that would be a pretty big move over what has already happened. I take it that 5% and 10% happens in a day, but another 30%, 40% is a quite dramatic move.

Mario Mendonca - *Genuity Capital Markets - Analyst*

The question I'm asking, though, is it's 35 or 40 points to get to a point where Moody's would want to downgrade the operating company --

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Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

No, I don't think that's clear. First of all, they have us on outlook which is a medium-term wait and see, just so you're clear.

Mario Mendonca - *Genuity Capital Markets - Analyst*

No, but it says it right there. I am reading it. It says, if the MCCSR were to drop below 200%, it would be downgraded from a AAA.

Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

Mario, they have us at a AAA. It's Moody's. They have us at a Aa1, Mario.

Simon Curtis - *Manulife Financial - EVP & Chief Actuary*

I also believe that is listed as one of a number of considerations that they would look to. They have both negative considerations and positive considerations. Some of the positive considerations we are actually doing as we speak.

Mario Mendonca - *Genuity Capital Markets - Analyst*

I will get to the question. The question is, would you be content to allow the operating company rating to drop, or would you want to raise capital before?

Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

I guess that we'll cross that bridge when we come to it.

Mario Mendonca - *Genuity Capital Markets - Analyst*

You don't have a preference you can share with us?

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Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

Well, a lot of companies operate with lesser ratings at the holding company level than we do. We would have to do a trade-off between the advantages and disadvantages. We are very proud of our rating and would be loath to sacrifice it. On the other hand, how much capital do any of you think, if you were operating a business, should I anticipate? How much should I load up with? What scenario should I plan on? I mean, it is a little difficult to conclude that somehow there is a magic level here. We are better capitalized than anybody that's reported. We're better capitalized than anybody that's reported, and that is as at October 30th, after the markets fell -- I don't know, in October what did they fall?

Simon Curtis - *Manulife Financial - EVP & Chief Actuary*

Lots.

Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

Lots. So, Mario, how much capital do you want us to maintain?

Mario Mendonca - *Genuity Capital Markets - Analyst*

No, I am not asking for any capital at all. It's Moody's that's [suggesting it].

Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

I think the rating agencies, Mario, the important point is, they're actually quite happy. The fact that one of them -- we're rated by five -- made some comments that weren't completely neutral about our progress through this turbulent time is a testament to our situation. The other four are completely satisfied that we are responding appropriately. Moody's is as well, but they are saying it's an area they want to monitor. It is of higher interest.

Mario Mendonca - *Genuity Capital Markets - Analyst*

Can I just ask one other thing, then, sort of related? The reserve versus the capital, increase in the required capital, there was a change from the October 14th presentation -- more of a reserve charge, less of an increase in the required capital. I think Amir was good enough to explain, essentially, Simon, you were working with imperfect information when you were originally making your estimates. The question I have is, if in fact the Company chooses to take -- to meet the appropriate -- the support for the segregated fund guarantees through reserve increases rather than an increase in required capital, are you indifferent to which one to use, whether it's earnings or whether it's -- do you prefer to just take the charge through earnings or do you prefer to go through required capital? Are you kind of indifferent in that respect?

Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

Yes, I think there is a choice to be made. To the extent you take it through reserves, it reduces the amount of capital by a bigger among than the reserve, but it goes through income. So you need to look at it depending on the situation and do what is appropriate. This quarter we elected to strengthen the reserve because there has been a material change in volatility, and we thought it was the right thing to do, and we have taken the charge. We will have to debate that next quarter depending how the market moves and the situation we find ourselves in.

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Mario Mendonca - *Genuity Capital Markets - Analyst*

When you take it through earnings, to the extent that you can release other reserves this quarter, for example, and just write risk reserves or maybe the investment gains, are you concerned at all that by taking it through the earnings side you are consuming future profits of the Company?

Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

I wouldn't presume an actuarial loss [set], just to be really clear. And I think the other thing that is very important is if people understand the nature of the risk and the charge, then I think -- you know, we are providing very fulsome disclosure. We will have to make the choice as to whether we want a reserve or a capital amount. But I think our investors will understand.

Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

And Mario, just I think, as Simon -- or as it was described earlier, the reserve for the seg fund guarantees we consider to be a pad.

Mario Mendonca - *Genuity Capital Markets - Analyst*

Right, I understand that. So you are saying it is from one pad to another, but total pads are the same?

Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

Simon wants to say something here.

Simon Curtis - *Manulife Financial - EVP & Chief Actuary*

Yes, I was just going to add one comment, that as you know, this time of year is when we do our review of all our methods and assumptions. As we had been working through this in the latter part of the summer and early fall, we had been looking at our levels of pads, and our interest rate risk pads had built up to be levels beyond our historic practices and beyond levels that external reviewers were getting comfortable with. So we had that amount that we knew we were either going to have to redeploy or come into income. And it just -- it seemed prudent at September 30th, given what we were seeing in the markets, to put that into the risk reserves for segregated fund guarantees. I would emphasize that there has been no weakening in our overall pad practices to fund that reserve strengthening.

Mario Mendonca - *Genuity Capital Markets - Analyst*

That's critical. Thank you.

Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

Mario, I just want to update and make sure everybody understood, though, based on your first question, Moody's has in fact affirmed our Aa1 rating. They have a negative outlook, and it relates to obviously what is going on in the industry. S&P has also reaffirmed our AAA rating. So that is just over the wire now -- important that both be kept in context.

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Mario Mendonca - *Genuity Capital Markets - Analyst*

Yes. And it's Moody's that's saying they wouldn't want the ratio to fall below 200%.

Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

Among the whole host of considerations that they would consider, it includes that.

Okay, Operator, we are well past our time. We've got time for two more questions, maybe

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Operator

The next question is from Tom MacKinnon from Scotia Capital. Please go ahead.

Tom MacKinnon - *Scotia Capital - Analyst*

Thanks very much. Good afternoon. I noticed the -- maybe this question for Simon. I noticed that moving to the CTE-80 was a lot more costly than what you had laid out in the October 14th presentation. And then consequently, the interest rates, it might have been a [C3] pad change, was a lot higher than you initially led us believe as well. I am just trying to gauge as to how much more room is there in this interest rate pad going forward to perhaps help in the fourth quarter? And then is there any other benefit from generally a longer-term -- or a rise in long-term interest rates that might be able to help you out in that regard as well?

Simon Curtis - *Manulife Financial - EVP & Chief Actuary*

I'd say, Tom, that the release of the C3 interest rate pad that we made in the third quarter was really all that we're contemplating at the moment. We are not contemplating adjusting that any further at the moment.

Tom MacKinnon - *Scotia Capital - Analyst*

And then with respect to any kind of rising longer-term interest rates, is there any possibility there as well?

Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

Yes, that would be very helpful.

Simon Curtis - *Manulife Financial - EVP & Chief Actuary*

Yes, I mean, obviously --

Tom MacKinnon - *Scotia Capital - Analyst*

And you're undergoing review with respect to that, and that was not related at all in terms of this pad, C3 pad that you let go of?

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Simon Curtis - *Manulife Financial - EVP & Chief Actuary*

No, it wasn't, Tom. There was no incorporation of higher -- assumption of higher interest rates in the future in that number. Obviously, given that we have a long-duration insurance book, any increase in interest rates over time is going to be beneficial, though.

Tom MacKinnon - *Scotia Capital - Analyst*

Okay. Have you done what that 225 MCCSR would be if you had all $3 billion downstream?

Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

It would probably be 10 points higher.

Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

Yes, approximately.

Simon Curtis - *Manulife Financial - EVP & Chief Actuary*

10 to 12 points higher, yes.

Tom MacKinnon - *Scotia Capital - Analyst*

Okay, thanks.

Operator

The final question is from Jim Bantis from Credit Suisse. Please go ahead.

Jim Bantis - *Credit Suisse - Analyst*

Thanks for taking my call. Just two quick questions in the context of trying to understand how much more capital is available to you before going to common equity with respect to reinsurance of individual insurance blocks. Has any of that been done this quarter?

Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

No. We have quite a number of things on the balance sheet, including reducing risk, looking at reinsurance, et cetera, that could provide flexibility. But at this juncture we've done none of those.

Jim Bantis - *Credit Suisse - Analyst*

Peter, those would still be relatively meaningful, too?

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Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

Yes.

Jim Bantis - *Credit Suisse - Analyst*

Okay. And then the last question is, I think on one of those lines, Peter, you had suggested that you were updating internal model assumptions with respect to policy behavior on seg fund products. Has that already been completed, or is that another quiver in the -- available to you?

Simon Curtis - *Manulife Financial - EVP & Chief Actuary*

It's Simon here. When we were giving the update on where we are at the end of October, that is factoring in what -- the assumption updates we think we would be making to withdrawal rates on the segregated fund (multiple speakers).

Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

It was not reflected in the Q3 results.

Jim Bantis - *Credit Suisse - Analyst*

But at the October 31st -- got it.

Peter Rubenovitch - *Manulife Financial - SEVP & Chief Financial Officer*

It's in the October estimate, yes.

Jim Bantis - *Credit Suisse - Analyst*

Okay, great. Thanks very much.

Dominic D'Alessandro - *Manulife Financial - President & Chief Executive Officer*

Thank you, everybody, for joining us on this call. I must say you are a tough audience to impress. We have been through an extraordinary period that I think, our Company, we are very proud of how it's withstood the turbulence in the marketplace, and in fact point out that we've got an ample level of capital, in fact more today than we have had in quite a while, notwithstanding everything that has happened. And I would repeat again that we remain -- we have all of our flexibility available to us to remain a leading insurance company in our industry and to take advantages of the -- that will for sure emerge because of the turbulence that has been experienced by everybody.

So thank you very much, and we will look forward to talking to you next quarter, if not sooner.

Operator

Thank you. The conference has now ended. Please disconnect your lines at this time, and thank you for your participation.

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