

# FINAL TRANSCRIPT

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## **MFC - Q4 2008 Manulife Financial Corporation Earnings Conference Call**

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## PRESENTATION

**Operator**

Please be advised that this conference call is being recorded. Good afternoon and welcome to the Manulife Financial Q4 2008 financial results conference call for February 12, 2009. Your host for today will be Amir Gorgi.

Mr. Gorgi, please go ahead.

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**Amir Gorgi** - *Manulife Financial Corporation - VP IR*

Thank you and good afternoon. I would like to welcome everyone to Manulife Financial's earnings conference call to discuss our fourth-quarter 2008 financial and operating results.

If anyone has not yet received our earnings announcement, and statistical package, and slides for this conference call and webcast, these are available in the Investor Relations section of our website at [Manulife.com](http://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 speakers' remarks may contain forward-looking statements within the meaning of the Safe Harbor provisions of Canadian and US securities laws. Certain material factors or assumptions are applied in making forward-looking statements and actual results may differ materially from those expressed or implied. 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 would ask each participant to adhere to a limit of one or two questions. If you have additional questions, please requeue, and we will do our best to respond to all questions.

With that, I would like to turn the call over to Dominic D'Alessandro, our President and Chief Executive Officer. Dominic?

**Dominic D'Alessandro** - *Manulife Financial Corporation - President and CEO*

Thank you, Amir, and good afternoon, ladies and gentlemen. Thank you for joining us on this call.

Earlier today we reported a significant loss for the fourth quarter of CAD1.870 billion. Net income for the year was CAD517 million, down very sharply from the CAD4.3 billion reported last year. Fully diluted earnings per share were CAD0.32, and return on equity was a mere 2%.

This poor performance is largely attributable to the very sharp decline in global equity markets and to a much lesser extent, falling interest rates and rising credit-related charges. Peter will take you through the numbers in some detail in a few moments, and so I won't dwell on them here.

2008 was certainly the most difficult year of my professional career. I think that is true for all of us in the financial services sector and probably true for those in many other businesses as well.

The extraordinarily difficult market conditions affected us in many different ways, including lower investment gains, lower fees on assets under management, and higher equity impairment charges. The most telling indicator of their adverse impact is the very large increase in reserves that we had to establish for guarantees related to our variable and segregated fund offerings. At the end of 2008, reserves for segregated funds and variable annuities stood at almost CAD5.8 billion, compared to some CAD500 million at the end of 2007.

As we have explained in the past, the bulk of our obligations under these agreements are payable over a 30-year period beginning in seven years or so from now. We are hopeful that, in time, equity markets will recover and thereby allow us to recapture these reserves through our income statement. Of course, should equity markets not improve, further additions to the balance sheet

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reserves may become necessary. The details of our sensitivity to market movements are discussed in Mr. Rubenovitch's presentation.

When I announced that I would retire as CEO of our fine Company a year ago, I never imagined it would be under circumstances that are as difficult as they have turned out to be. We have tried to respond in an appropriate fashion and we were successful in strengthening our capital base by the addition of CAD2 billion in term loans and CAD2.3 billion in common equity. The capital ratios of our main operating subsidiaries are well above internal targets and are amongst the highest we have ever enjoyed.

Because the very poor financial markets so adversely affected our reported results, they tend to overwhelm everything else. It would be easy to conclude that the year was one that we would all sooner forget. The reality is that there were many achievements in 2008 that we are very proud of. These should be kept in mind as we review our financial results.

Some of the highlights for the year are -- our sales of life insurance were at record levels in each of our insurance businesses in the United States, in Canada, and in Asia and Japan.

Despite the unprecedented market volatility, wealth sales were in line with the strong levels of a year ago. A number of important changes were made, and more are planned, to reduce the risk attached to our savings products.

We wrote a lot of profitable new business in 2008. Our premiums and deposits totaled CAD70 billion, and we reported record new business embedded value of CAD2.3 billion, up 10% from a year ago.

We continued to expand our distribution capabilities through the addition of distributors such as Edward Jones in the United States, adding new channels such as our managing general agents in Japan, expanding to new cities in China where we added seven licenses during the year, and acquiring Berkshire Securities here in Canada.

Also our costs remain under excellent control.

Finally, I would ask you to pay close attention to Peter's discussion of asset quality which, given the times, is more comprehensive than usual. It shows that we are well positioned to deal with the challenges which may lie ahead.

With that, I would like to ask Peter to take us through the numbers in more detail. Peter?

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**Peter Rubenovitch** - *Manulife Financial Corporation - SEVP and CFO*

Thank you, Dominic.

The reported loss for the fourth quarter of 2008 amounted to CAD1.870 billion or CAD1.24 per fully diluted share. You will note that this loss differed by CAD370 million from the estimate of CAD1.5 billion that we indicated on December 2.

In addition to the fourth-quarter drop in equity markets, there was also a sharp drop during the quarter in the swap interest rates which are used to value our segregated fund guarantee liabilities. This was a primary reason for the difference in our reported result. Other items that changed from the December estimate were largely offsetting, and the net of these accounted for the balance of the reported earnings difference.

If we turn to slide eight, the loss in the fourth quarter was largely driven by increased accruals for the impact of drops in equity markets and interest rates on guarantee reserves, equity values and fees, partially offset by changes in actuarial methods and assumptions. These items, which I'll discuss in more detail in the following slides, totaled over CAD2.7 billion in the quarter.

Shareholders' net income for the full year 2008 was CAD517 million, down from CAD 4.3 billion reported in 2007.

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Full year earnings for 2008 were negatively impacted by over CAD3.7 billion of accruals due to the unprecedented decline in worldwide equity markets and by almost CAD500 million in provisions and reserve increases for credit defaults and downgrades, primarily in respect of exposures to the financial sector that we largely reported on in the third quarter.

As detailed on slide nine, the fourth quarter's results were affected by several large non-cash items, which are summarized in the table on a post-tax basis.

The sharp declines in global equity markets in the quarter resulted in charges exceeding CAD2.9 billion, largely in relation to segregated fund guarantees.

Accruals for credit impairments and credit downgrades in the quarter totaled CAD128 million.

Changes in actuarial methods and assumptions, resulted in net gains of CAD521 million in the quarter. These net gains reflect updates to our seg fund guarantee assumptions. Excluding the seg fund changes, overall changes in actuarial methods and assumptions resulted in a net charge of CAD288 million in the period.

Finally there were two notable tax-related items in the quarter which had been previously discussed as contingencies in prior quarters. We increased tax provisions for investments in leveraged leases and reflected the impact of expected changes in Canadian tax law in relation to fair value accounting for insurance companies.

In fact, it is interesting to note the cash provided by operating activities in the fourth quarter was CAD2.6 billion, up from CAD2.3 billion a year ago, reflecting the non-cash nature of these items.

Turning now to slide 10, we outline in more detail the impact of equity markets on our results. As noted, North American markets were down 22% or 23% in the quarter, while Asian markets were down some 20% or 21%.

Our actuarial practices require us to calculate our reserves based on quarter-end equity values, and accrue accordingly.

Of the CAD2.9 billion equity-related charge, CAD1.8 billion related to normal movement in reserves for segregated fund guarantees.

As well, the sharp drop in swap interest rates over the quarter reduced the discount rates used in the measurement of our segregated fund guaranteed obligations and resulted in an additional charge of CAD602 million this quarter.

Although these guaranteed benefits cannot be monetized currently and the bulk of these payments are not payable for many years, the valuation of these guarantees is quite sensitive to short-term changes in market levels which are reflected as charges in the current quarter's income statement.

The remaining items include CAD196 million related to declines in equity values in our liability segments; CAD100 million in reduced capitalized future fee income on equity-linked and variable universal life products; CAD59 million of lower fee income; and CAD158 million of impairments accrued on equity positions in the Corporate and Other segment.

If we turn now to slide 11, pre-tax credit impairments in the fourth quarter were CAD110 million, compared to the negligible amounts of the fourth quarter of the prior year.

For the full year 2008 pre-tax credit impairments totaled CAD517 million, primarily due to charges on financial sector exposures in the third quarter. This compares to the exceptional credit experience of '07, which we had previously indicated was considered to be unsustainable.

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As discussed in prior quarters, our actuarial practices require us to strengthen our reserves upon credit downgrades; and therefore we also took a pre-tax charge of CAD88 million in the current quarter for the reserve impact of credit downgrades.

On a post-tax basis, credit impairments and credit downgrades in the quarter totaled CAD128 million.

In light of the macroeconomic environment we continue to be pleased with the credit performance of our portfolio.

As indicated on slide 12, the fourth-quarter review of the actuarial methods and assumptions underlying policy liabilities produced a net reduction in the policy liabilities of CAD506 million, resulting in a post-tax increase in earnings of CAD321 million.

Changes related to non economic assumptions including releases due to updates to mortality and expense assumptions. These were partially offset by an increase in reserves for lapses and other policyholder behavior assumptions.

Refinements to reinvestment return and scenario testing assumptions resulted in increases in policy liabilities. Other changes to valuation models and assumptions resulted in modest reserve releases.

Overall, changes to seg fund guarantee reserves within the basis changes were a post-tax release of CAD609 million, offset by a net increase of CAD288 million post-tax related to other product lines.

On slide 13 we summarize the level of provisions for adverse deviation, or PfADs, over the last three years. The Company continues to have significant and growing provisions for adverse deviation in our policy liabilities.

At year-end, general account PfADs and non-capitalized margins on our seg funds were 14.8% of total policy-related liabilities, including seg funds.

Significant increases in PfADs were due to the impact of the adverse '08 equity markets on the potential future costs of segregated fund guarantees and also were a result of currency movements, increases on noncredit investment PfADs to offset the impact of higher market spreads on expected returns, and due to increased usage of non-fixed income assets.

Overall, the higher PfAD levels, while largely driven by market events, do show that our prudent approach to valuation is being maintained.

If we look at our source of earnings on slide 14, the impact of the investment markets on our fourth-quarter results is clearly shown in the summary. Most materially, the sharp decline in equity markets and credit-related charges produced CAD3.7 billion of pretax experience-related losses. Excluding market-related items, experience was a moderate gain, consistent with historic trends.

Equity markets also impacted the earnings on surplus, where lower realized gains and impairment charges on equities designated as available-for-sale led to a pretax loss of CAD101 million. Other sources of earnings categories were less impacted, showing that our core earnings remain strong.

Expected profit on in-force was essentially unchanged from last year, with favorable currency movements partially offsetting lower market driven fee income.

The lower year over year new business strain reflects the more favorable sales mix and pricing actions taken in 2008.

Changes in actuarial assumptions, net of prior amounts and modest management actions, increased pre-tax earnings in the period by CAD480 million.

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Income taxes for the quarter, while unusual in certain business segments, were at normal levels on an overall basis, reflecting a recovery in light of this quarter's losses.

On slide 15 there is a summary of the details of our reserves and capital in relation to segregated fund guarantees.

Due to the sharp global equity market declines in the fourth quarter, the reported amount at risk, which represents the excess of guaranteed values over fund values, has increased to CAD27 billion, up from CAD13 billion last quarter.

Despite this increase, as indicated, we still expect to make a net present value profit on this portfolio, albeit a modest one.

As a result of declines in equity markets and swap interest rates, we strengthened our balance sheet reserves by CAD3.5 billion in the quarter, such that they now stand at CAD5.8 billion at year-end. All of this reserve is a PfAD, as the expected present value portfolio result is that we will earn a profit on this business.

In addition to the balance sheet reserves, required MCCR regulatory capital totaled almost CAD2.5 billion at year-end and, using a benchmark capital ratio of 200%. This implies that total balance sheet reserves plus benchmark capital amounted to CAD10.7 billion at year-end, an increase of CAD8.6 billion from a year ago.

The CAD10.7 billion of reserves and capital that presently supports our segregated fund liabilities is over CAD10 billion above the expected cost of these obligations and totals fully 40% of the amount presently at risk but contingently payable over many years.

As previously noted, the framework that is used to generate the scenarios that must be covered by reserves and capital do not assume any immediate bounceback in equity markets or mean reversion of markets from recent declines. Therefore we calculate reserves and capital starting with the current adverse equity market levels and then consider scenarios that reflect further significant declines in equity values, followed by a period of a decade or longer without any growth in equity values. In other words, a tail event, followed by another tail event.

This is the conservative framework under which our variable annuity obligations are calculated, even though these guarantees are, as a portfolio, only due in many years and not subject to the risk of acceleration or liquidation. This is a highly prudent basis for considering these risks.

Turning to slide 16, there were several developments in the quarter that impacted our regulatory capital and reserve levels. Early in the quarter, OSFI announced refinements to the MCCR guidelines pertaining to the calculation of required capital on segregated fund guarantees. Under the revised capital rules, different confidence levels are used such that less capital is held in respect of longer term segregated fund guarantee payment obligations, with increasing required capital levels as payment dates become more proximate.

Given our portfolio profile, this will require that we provide for these obligations through a combination of reserves and capital, generally at the CTE90 level, which is approximately equivalent to a 96% confidence level.

A CTE90 scenario starts with current market levels and then assumes on average an immediate 20% decline in equity markets and no growth for about a decade. This is still a very conservative framework. Most importantly, it continues to have significant impact on our earnings and capital as equity markets remain volatile.

During the fourth quarter we also received regulatory approval on favorable changes to our internal segregated fund guarantee model assumptions related to discount rates and policyholder behavior assumptions.

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To date, we have used the swap curve to value our segregated fund guarantee reserves. We are presently in the process of updating our reserve models to reflect the expected yields on the assets being invested to support our segregated fund obligations.

We expect that in the first quarter these changes will be fully reflected in the calculation of these seg fund guarantee reserves, and while we do not expect immediate reserve reductions, it is important to note that the reported fourth quarter CTE of 65 as a level is likely to result in a higher than CTE70 reserve level on the amended basis.

During the quarter, as summarized on slide 17, we successfully added CAD4.3 billion to our capital accounts, financed by CAD2 billion of term financing and the issue of CAD2.3 billion of new common equity.

The five-year term loan was provided by leading Canadian banks, is repayable without penalty at the Company's option at any time, and is priced on a floating-rate basis at three-month BAs plus 380 basis points.

The common share issue included over CAD1.1 billion sold by way of private placement to eight existing institutional investors and almost CAD1.2 billion sold to a syndicate of underwriters in a bought deal public offering.

It is interesting to note that even after the equity raised and the Q4 results, our book value per share is up by 6% over a year ago.

On slide 18, you will note that our capital positions at year-end were very strong, well above internal and regulatory targets.

Because of the capital raising at regulatory capital requirement changes, MLI's fourth-quarter MCCR ratio increased to 233%, up from 193%, despite the impact of sharp declines in the global equity markets on our accounts. The higher ratio is consistent with management's current objective of targeting a capital ratio that is above 200%, the upper end of our historic MCCR target range, for as long as equity markets remain so turbulent and volatile.

JHLICO's RBC ratio has not yet been finalized, but at present we estimate the year-end ratio position will be around the 400% level, also a very strong capital ratio position.

Slide 19 provides an updated estimate of capital and earnings sensitivities going forward. As noted, MLI's reported MCCR ratio was 233% at year-end. A 10% equity market correction from year-end levels is estimated to result in a decline of approximately 20 points in our MCCR ratio.

From a consolidated earnings perspective, we estimate that a one-time equity correction of 10%, followed by normal market growth, would reduce reported earnings by about CAD1.6 billion.

Turning to slide 20, premiums and deposits amounted to CAD70 billion for '08, in line with the CAD69.4 billion reported last year. Increased premiums arising from higher sales of fixed wealth products, insurance business growth, and a stronger US dollar were offset by the decline in variable wealth product deposits.

Full-year sales for '08 were also strong. Record sales levels were achieved in each of our life insurance businesses and despite the unprecedented market volatility, wealth sales were in line with the strong levels of 2007.

During 2008, new business embedded value totaled a record CAD2.3 billion, an increase of 10% over 2007, with both insurance and wealth management segments contributing to this growth.

Our insurance businesses had a record year, contributing close to CAD900 million of new business embedded value, up 10% from a year ago, with strong growth in Canada, the US, and Japan.

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Record levels of new business embedded value were also generated by our wealth management businesses in the year, totaling CAD1.4 billion, an increase of 10% over '07 levels, with particularly strong growth this year in Canadian Wealth.

Consistent with sales, new business embedded value in the fourth quarter was up from the third quarter, but down from the fourth quarter of last year. This was, nonetheless, one of our best quarters on record.

Consistent with prior years, we are also updating our in-force embedded value disclosure, which we determine and report at year-end. Overall, in-force embedded value grew by a very strong CAD13.4 billion during '08.

While the poor equity markets drove a substantial CAD4.6 billion reduction in embedded value from experience, this was more than offset by the beneficial impact of currency due to depreciation of the Canadian dollar and the impact of lower discount rates used for embedded value calculations.

Discount rates are directly based on current risk-free market rates plus a risk premium. As risk-free rates dropped substantially in '08, this resulted in lower embedded value discount rates. The net result is that, on a per-share basis, the embedded value has grown from CAD21.85 per share to CAD28.68 per share. This embedded value reflects only the value of in-force business, determined based on valuations and assumptions applied to our in-force book.

This calculation does not reflect the value of new business which we expect to write in the future, which is typically added to embedded value to determine enterprise value. This is, I believe, the first time that our share price is trading below in-force embedded value per share.

Turning to slide 23, total funds under management as of year-end '08 were CAD405 billion, CAD8 billion higher than a year ago. The impact of capital markets is quite evident in these results, as strong positive net policyholder cash flows of CAD18 billion and favorable currency movements of CAD64 billion were reduced by over CAD77 billion of net negative investment income due to some CAD90 billion of market value declines.

The volatile markets adversely affected the fourth quarter's results for all divisions.

Wealth management segments in each of our divisions had significant charges related to seg fund guarantees as well as reduced fees due to low levels of assets under management.

Insurance segments also had lower earnings as a result of lower capitalized future fee income on equity-linked and variable universal life products as well as unfavorable investment experience. This was partially offset by strong in-force business growth in our core segments.

The Corporate and Other segment reported losses primarily due to charges for potential losses on our available-for-sale equity portfolio and additional tax-related provisions on levered lease investments. This was partially offset by the positive impact in earnings from changes in actuarial methods and assumptions compared to 2007. These items overshadowed the underlying consistent results of our operations.

On slide 25, we summarize the earnings differential between '08 and '07 for both the fourth quarter and the full year, excluding investment and market related gains and losses. Reviewing our operations excluding these impacts is helpful for achieving a more fulsome understanding of our non-investment related performance.

As indicated, this quarter all operating divisions had earnings after adjustments for the unusual market impacts that are generally comparable or better than the results on a similar basis in the prior year.

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US Insurance and Asia and Japan revealed significant growth due to strong in-force business growth in U.S. Life and Japan, as well as more favorable claims experience in U.S. Long Term Care. In Canada, strong in-force business growth in Individual Insurance and Manulife Bank were offset by lower asset-based driven fee income in Individual Wealth.

The shortfall in U.S. Wealth management is directly attributable to lower fee income on lower asset base due to year-over-year equity market declines.

Turning to sales on slide 26, U.S. Insurance group finished the year with a strong result despite the soft fourth quarter sales volumes across the industry. John Hancock Life ranked number #1 in U.S. individual insurance sales for the fifth consecutive quarter and ended '08 with record sales volumes for the year. During the quarter, the business announced the launch of new variable universal life product that offers superior cash value and retirement income potential to pre-retirees.

Long Term Care reported a 48% increase in Group sales in the quarter, driven by increased sales from existing groups including plan upgrades and re-enrollment programs. This increase was offset by Retail sales which declined as a result of changes in consumer behavior in light of economic uncertainty and our recent price increases in this product line.

On slide 27, net flows for the U.S. Variable Products Group were a positive CAD8.1 billion in '08, in line with '07 levels. Consistent with overall industry trends, all segments experienced decreased fourth quarter sales volumes due to volatile economic markets and heightened economic uncertainty.

Despite the volatility, Mutual Funds sales for '08 were up 12% over '07, while Group Pensions continue to report strong transfer volumes.

We continue our comprehensive review of our variable annuity offerings and in January, initiated product changes that reduce the risk profile of this line. Additional product changes are being developed. As well, new VA business written in the U.S. is now being hedged as written; and we are planning to extend our hedging programs to our key businesses in other geographies.

Given newly announced VA product changes and continued volatility in equity markets, softer sales are anticipated next quarter.

On slide 28, Canadian Individual Insurance reported its second best sales quarter ever, just CAD1 million short of the previous quarterly record. Full year sales set a record and exceeded last year's levels by 12%. While universal life continued to be the largest selling product, all product lines reported strong growth. Affinity sales were also higher.

Sales growth in the Group businesses slowed somewhat as companies deferred decisions on their pension and benefit plans while they assess the impact of the slowing economy on their businesses.

Group Savings had its best sales quarter of '08 driven by sales in the small case market. Group Benefits sales in the quarter were in line with the third quarter result and, excluding an unusually large case sale in '07, were up 4% for the year.

Despite the softer sales volumes in the fourth quarter, both Group Benefits and Group Pension businesses are presently seeing increased quotation activity.

Turning to slide 29, Canadian Individual Wealth Management reported net flows of CAD4.7 billion, up CAD2.5 billion from the prior year. Manulife Bank had another record lending quarter with new loan volumes exceeding last year's levels by 45%. New loan volumes of CAD4.8 billion for the year were driven by the continued success of ManulifeOne. The credit quality of the Bank's portfolio continues to be excellent.

Segregated fund sales of CAD1.4 billion were up 10% from the fourth quarter of last year.

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Sales of Fixed Products were exceptionally strong, with fourth quarter sales up 68% from a year ago. This increase was partially offset by a modest decrease in mutual fund sales volumes.

On slide 30, Insurance sales in Asia and Japan for the fourth quarter and full year exceeded prior year comparables by 38% and 40% respectively. Japan insurance sales for both the fourth quarter and full year were more than double those of the prior year, driven by new products and a new distribution channel, the MGA channel. Products launched in the year included increasing term and corporate owned medical and life insurance.

In Other Asia, sales were up 13% from the prior year, with fourth quarter sales in line with last year. Sales growth for the full year was driven by strong bancassurance and agency sales in Singapore and a growing distribution base in China.

On a full-year basis, Hong Kong insurance sales were 5% higher than the prior year, driven by product enhancements, but down 14% versus 4Q07.

Turning to Wealth Management, in Asia and Japan net flows were down from '07 levels due to the volatile markets. Despite lower sales in the fourth quarter, Japan full year net flows are up 14%.

I would now like to take a moment to review our investment portfolio, which continues to perform very strongly. Gross unrealized losses on our fixed income securities totaled CAD9 billion or 8% of our total fixed income portfolio as of year end. This was largely due to credit spread widening.

Fixed income security trading below 80% of cost for more than six months totaled less than 1% of total fixed income assets.

Our holdings of UK hybrid securities amount to about CAD750 million on a cost basis. Commercial mortgages and arrears totaled less than CAD35 million.

Slide 33 summarizes our limited exposure to today's more topical investment items. Our exposure to problematic investments is relatively modest.

We have CAD 2billion in asset-backed securities, none of which are backed by sub-prime and 92% of which are rated AA or higher.

Our sub-prime RMBS holdings were down to an amortized cost of CAD747 million at year end, as we continue to enjoy average paydowns of approximately CAD10 million to CAD12 million per month on this portfolio. We have limited exposure to hybrid securities issued by UK and European financial institutions, with the cost representing 0.5% of our total investment portfolio.

On slide 34 you can see that average credit quality continues to be strong. Only 5% of our bond portfolio is below investment grade and less than 2% is rated single B or lower. The modest credit migration observed since year end '07 reflects downgrades, but also selective investments as we capitalize on widening credit spreads.

As seen on slide 35, when compared to the S&P Universe our bond portfolio downgrades as a percentage of total issuers held has consistently outperformed the benchmark universe's downgrade ratio.

Slide 36 summarizes the unrealized losses on our fixed income securities.

Due to general spread widening, gross unrealized losses in this portfolio have increased from CAD6 billion last quarter to CAD9 billion, a relatively modest 8% of the total fixed income portfolio of CAD113 billion. Net unrealized losses were CAD5.2 billion or less than 5% of fixed income securities.

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As previously indicated, we have the ability to hold these securities until maturity, and have provided for expected levels of defaults in our actuarial reserves. As a result, we presently anticipate no significant earnings impact in respect of these gross unrealized losses, provided the expected underlying cash flows from these assets remains undiminished.

Fixed income securities trading down 20% or more for at least six months totaled less than CAD1 billion, a relatively modest level given the size of our portfolio.

Slide 37 summarizes unrealized losses on equities that are designated as available-for-sale securities. Due to declining equity markets, gross unrealized losses on this portfolio have increased from CAD489 million to some CAD828 million, which represents 23% of the original value of this portfolio. This is not unfavorable given the magnitude of recent declines in equity markets.

AFS equity securities trading down 20% or more for at least six months totaled less than CAD50 million, again a quite modest sum.

On slide 38, I'd like to take a moment to review our real estate related investments. Our mortgage portfolio has a carrying value of CAD31 billion and represents 16.5% of our total invested assets. Of these loans, over 25% are insured by CMHC, a Canadian federal government agency.

We have been extremely conservative with the underwriting of the remainder of the portfolio, specifically the commercial loan book. We curtailed loan originations and renewals when credit risk, covenants and spreads did not achieve our desired economics; and we did not participate in loose underwriting practices in recent years. This has resulted in a conservatively appraised portfolio which has an in-force loan-to-value ratio of approximately 60% and a debt service coverage ratio in excess of 1.6 times.

We continue to be diversified by property type, with lighter exposures to ailing economic regions and minimal loan values currently in arrears.

Our commercial and mortgage-backed security portfolio of CAD6 billion is about 3% of total invested assets. Our portfolio is of very high quality, over 90% rated AAA and of seasoned vintage, with most exposures originated in '05 or prior. The vast majority of recent originations continue to be rated AAA.

Most importantly, despite the securitized nature of the CMBS portfolio, we underwrite our CMBS portfolio on a mortgage by mortgage basis, not simply relying on bundled ratings or aggregate loan-to-value metrics. This approach gives us a high degree of comfort with the quality of our holdings.

Finally on slide 40, highlights of our equity real estate portfolio, which totals some CAD7 billion and represents 3.9% of our total invested assets. This is an extremely high-quality unleveraged portfolio that consists of commercial real estate concentrated only in cities with highly diverse economies. Our commercial real estate has a 93% occupancy rate and an average lease term of 5.6 years.

While we have experienced a modest drop in industrial property occupancy in select cities, this is in respect of a very small portion of our portfolio and has had a minor effect on our Net Operating Income. As well, only 10% of our tenant leases are scheduled for renewal in '09.

In the event of a commercial real estate recession, we anticipate that our cash flows on this portfolio should continue largely undiminished. And we look forward to the opportunity to buy additional real estate at reduced prices.

So in conclusion, sharp declines in equity markets and interest rates have reduced this quarter's reported earnings substantially, particularly in relation to our reserves for segregated fund guarantees. But, our business units continue to perform well exclusive of these market related events.

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Our sales performance remains strong, and we continue to grow our new business embedded value. Our investment portfolio asset quality remains sound and our key capital ratios exceeded target levels. Thank you very much.

**Dominic D'Alessandro** - *Manulife Financial Corporation - President and CEO*

Thank you, Peter. Operator, we are ready for the question-and-answer portion of our call.

## QUESTIONS AND ANSWERS

### Operator

(Operator Instructions) Tom MacKinnon, Scotia Capital.

**Tom MacKinnon** - *Scotia Capital - Analyst*

Yes, thanks very much; good afternoon. I have just got a question about the change in this discount rate methodology you are using for seg fund reserves. I understand it, like you are holding CAD5.8 billion in seg fund reserves at December 31. And if you actually implemented this new methodology, the CTE would be 70 instead of 65. Is that the correct way of looking at that, or above 70 instead of 65?

**Peter Rubenovitch** - *Manulife Financial Corporation - SEVP and CFO*

Well, we haven't done it, but our estimate is that it would be somewhere above 70.

**Tom MacKinnon** - *Scotia Capital - Analyst*

Okay, and can you explain a little bit about the change in methodology? It sounds like you're not going to use -- is this swap stuff just too volatile, not applicable anymore?

**Dominic D'Alessandro** - *Manulife Financial Corporation - President and CEO*

We will let Simon explain the technical nature of this change.

**Simon Curtis** - *Manulife Financial Corporation - EVP and Chief Actuary*

Yes, Tom, it's Simon Curtis. Historically we use swap curves to discount our segregated fund guarantee cash flows, because the reserves historically were not particularly big. Now that the reserves have grown materially in the fourth quarter, we are basically implementing a full CALM methodology and then deploying the proceeds of asset raising into the reserves to back these guarantees.

As we do that in the first quarter, we believe the yields that we will be using in the valuation will be higher than swap yields then. So we just primarily, when we look at that, we think that what today discounts at a swap curve and it comes out of the CTE(65) that same reserve would be over CTE(70) using sort of a CALM-type methodology.

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**Tom MacKinnon** - Scotia Capital - Analyst

So if nothing had actually changed in the whole world -- or changed in the world between December 31 and March 31, you would hold the same amount of dollar amount of reserves and they would be above CTE(70) and not CTE(65)?

**Dominic D'Alessandro** - Manulife Financial Corporation - President and CEO

Most probably, yes.

**Tom MacKinnon** - Scotia Capital - Analyst

Now, the sensitivities that you show on slide 19, it's interesting to note that I guess with everybody, all the contracts and the money, the EPS sensitivity changes from what you've previously disclosed; but the MCCSR sensitivity doesn't really change.

I am wondering first of all, are these things all sort of based on like a CTE(70) as well? And then why would the one change and then the other one not change?

**Simon Curtis** - Manulife Financial Corporation - EVP and Chief Actuary

Tom, it's Simon again. Hopefully this isn't too technical an answer, but basically as these contracts get more in the money, we are seeing that the distribution of how our requirement changes between reserves and the required capital component is shifting.

We are getting marginally larger reserve hits and therefore bigger earnings impact as you're seeing. But we're not seeing the required capital -- more of that increase is taking place in the reserve and less in the required capital. And that sort of moderates what we see in terms of the sensitivity of the MCCSR ratio.

**Tom MacKinnon** - Scotia Capital - Analyst

Okay. So it's sort of the statistical nature of developing the reserves, is it?

**Simon Curtis** - Manulife Financial Corporation - EVP and Chief Actuary

Exactly. If you remember, the capital requirement here is the difference between one calculation of the requirement, that is CTE(90), another calculation at a lower confidence level for the reserves.

We are seeing that basically now more of that increase shows up in the reserve and less in that incremental required capital piece. And that tends to dampen the growth or the impact on the capital ratio.

**Tom MacKinnon** - Scotia Capital - Analyst

These are done holding -- on the balance sheet holding CTE(70)? Is that what these would be done at, these sensitivities?

**Simon Curtis** - Manulife Financial Corporation - EVP and Chief Actuary

This was really done using -- this latest sensitivity was estimated using our year-end reserve, which as we said would probably be about CTE(70) (multiple speakers) discount rate.

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**Tom MacKinnon** - Scotia Capital - Analyst

Okay. Is that generally what you'd normally want to hold? I know it's somewhere between 60 and 80. Just why did you hold 80 the last quarter, and why 70 now?

**Peter Rubenovitch** - Manulife Financial Corporation - SEVP and CFO

Last quarter we saw that markets were becoming quite volatile, so we elected to be a little more conservative. I think that would be the key determinant there.

**Tom MacKinnon** - Scotia Capital - Analyst

Then finally this shareholder portion you talk about, these UK hybrids, is that -- that would be excluding the par stuff, is that right?

**Peter Rubenovitch** - Manulife Financial Corporation - SEVP and CFO

Yes, that's correct.

**Tom MacKinnon** - Scotia Capital - Analyst

Okay, thanks.

**Operator**

Jim Bantis, Credit Suisse.

**Jim Bantis** - Credit Suisse - Analyst

Good afternoon, two questions. Just a question with respect to capital plan. I know that the Company took great efforts to take the capital ratio up to 233% at year-end. But obviously since then we've seen the S&P decline by 10% and we have seen the asset impairment cycle gain momentum. And now we are hearing comments from the rating agencies with respect to a potential downgrade.

So I just want to ask about the capital plan going forward in lieu of this worsening backdrop. In the context of where would be an acceptable MCCR ratio; would you go below 200%? And put that in the context of the rating agencies as well, please.

**Dominic D'Alessandro** - Manulife Financial Corporation - President and CEO

Well, I think that given the uncertain environment that we are in, we would like to keep obviously our capital ratio higher rather than lower. We think the level at which it is at does allow us some absorption capacity for adversity.

We will be looking at maintaining as I say a very strong capital ratio. There's a number of initiatives that's we can undertake, include raising additional capital in the form of other than common equity or some debt instruments, and actions of that kind.

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**Jim Bantis** - *Credit Suisse - Analyst*

Dominic, to what extent do you worry about losing your AAA rating with one of the agencies or the commentary that's coming from Moody's at this point as well?

**Dominic D'Alessandro** - *Manulife Financial Corporation - President and CEO*

Well, I don't know if there is -- I think us and one other AAA-rated company in our space in the world. You know, you are aware of the environment just as we are.

I think that rating agencies are taking a close look given the environment. If we did lose ratings a notch, I think that would still leave us at the top of the rating pile with respect to all of our competitors. It in fact would keep us ahead of most of them.

Of course it's not something we would like to do and that we want to see. You know, we lost our AAAs -- it's ironic that in my very first month with the Company we lost our AAA rating back in 1994. We worked very hard for 10 years and finally recovered it. And now in my last month with the organization, the specter of a downgrade looms.

So we would like to keep our AAA and we will do whatever we can to keep it, but we have to be realistic that the environment is very poor and rating agencies do what they feel they need to do.

**Jim Bantis** - *Credit Suisse - Analyst*

Thanks very much, Dominic. A quick question for Don, please, with respect to the investment portfolio. Looking at the private placements, CAD23 billion. A very large number with not a lot of disclosure. I'm wondering if you can break that up for us.

**Don Guloien** - *Manulife Financial Corporation - SEVP and Chief Investment Officer*

Yes, we have on the call here Scott Hartz and Warren Thomson -- Warren who is taking over my job as Chief Investment Officer, and Scott Hartz who is managing the entire general account of Manulife. So if you guys, Scott, do you want to take that one?

**Scott Hartz** - *Manulife Financial Corporation - EVP US Investments*

Sure, you know, our private placement portfolio would look similar to that of most of our peers. It's largely investment-grade, largely in the triple-B and triple-A areas, largely not related to financials so has not had some of the stress that the public markets have seen.

We tend to be more heavily weighted in utilities, which has been a bit safer haven these days, and also in some sort of government-backed. Which you wouldn't expect in a private book, but we would do a number of deals with government leases, which create for a very strong portfolio.

**Jim Bantis** - *Credit Suisse - Analyst*

So along those lines, is there any level of the delinquencies that you can provide us to give us additional comfort?

**Scott Hartz** - *Manulife Financial Corporation - EVP US Investments*

Well, anything that would be delinquent we would have impaired, so there's very little in that bucket. I think there's less than 1% of the book is currently not paying.

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**Jim Bantis** - *Credit Suisse - Analyst*

Got it, okay. Thanks very much.

**Operator**

Nigel Dally, Morgan Stanley.

**Nigel Dally** - *Morgan Stanley - Analyst*

Thanks and good afternoon. First can you provide us with an update on your acquisition appetite? Clearly the world has deteriorated. Does that make you want to sail closer to shore, or are you seeing opportunities to take advantage of some of the turmoil?

Then I just had another question on your seg fund balance sheet reserves. Can you provide us some details on how sensitive your reserves are to different CTE levels? For example you have reduced your CPE level from 80 as of September down to 65. What would have the impact been if you had kept the CTE level unchanged at 80?

**Dominic D'Alessandro** - *Manulife Financial Corporation - President and CEO*

Okay, the acquisition scenario or appetite for acquisitions, you know I would agree with you that there's a lot of assets for sale because of the market conditions. On the other hand, as I mentioned, we want to remain well capitalized to provide for continuing adversity, should it happen.

So we are going to be very judicious. If we were to undertake an acquisition it would be done in a way that didn't compromise the comfort or the cushion that we have in our capital levels.

With respect to the CTE65 and 80, I see Simon is jotting down some notes. I think the important thing to bear in mind is, because when we through these numbers around, is exactly what our model says the CTE65 is.

Both CTE65 and CTE80 are very negative scenarios for -- essentially they assume very little improvement, in fact some decline from current market levels and no improvement for the duration of the modeled period. The extent of the carrying cost, if you can call it that, varies between 65 and 80. It will obviously be more expensive at 80 than it is at 65. But they are both quite conservative scenarios.

**Nigel Dally** - *Morgan Stanley - Analyst*

What would our CTE80 have been?

**Simon Curtis** - *Manulife Financial Corporation - EVP and Chief Actuary*

Well the range is quite big now that the guarantees are well in the money. So if we see CTE65 that result that we reported was about CAD5.8 billion. At CTE60 it would be probably be in the range of CAD4.5 billion. CTE80 would probably be more in the range of CAD8 billion. So there's quite a big range now given that these are well in the money.

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**Dominic D'Alessandro** - *Manulife Financial Corporation - President and CEO*

I think I would add that one of the things to bear in mind is that we've got a reserve of CAD5.6 billion on our balance sheet. For a shortfall in our guarantees, as I think the chart showed, which was about CAD26 billion; and so that CAD26 billion as best we can calculate is payable beginning quite a few years from now and over a long period of time.

And it's a judgment issue. I mean we do it by calculation and so on. But is it reasonable to hold CAD5.6 billion of reserves for an obligation which today is CAD25 billion? An obligation which isn't payable in cash for a long, long time?

We think -- I personally think -- that it's quite a conservative posture. As I like to say, if we were a pension plan and had that type of deficit, we would be recording much lesser charges than we have recorded, maybe a tenth of what we have had to book.

So, you know, I am not meaning to dance around this. This is a serious exposure that we have; but I think it needs to be understood fulsomely, and that it is an exposure that isn't settleable in cash anytime soon. And as I said, markets may go down.

But we are hopeful that over the intervening period to the time that we commence paying some of these obligations that there will be an improvement in equity markets.

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**Simon Curtis** - *Manulife Financial Corporation - EVP and Chief Actuary*

I would just add one comment, that when you look at the disclosure we did in that table in the set, you can see that the expected cost is still slightly negative. Which really means that entire CAD5.8 billion reserve is still a margin for at-risk deviation. So going forward if markets -- just from today, not looking backwards at all -- but over the next seven to 30 years revert and grow at an average 2% a quarter, none of that reserve will really be needed to pay off the benefits.

So obviously it's a material exposure. There's a material reserve that needs to get set up. But there is still potentially a significant release of that reserve in the future.

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**Nigel Dally** - *Morgan Stanley - Analyst*

That's very helpful, thank you.

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**Operator**

Jukka Lipponen, KBW.

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**Jukka Lipponen** - *KBW - Analyst*

Good afternoon. What were your losses in the commercial real estate and mortgage loan portfolios at their peak in the late '80s or early '90s?

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**Peter Rubenovitch** - *Manulife Financial Corporation - SEVP and CFO*

I'm not sure we have that sitting at our fingertips.

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**Dominic D'Alessandro** - *Manulife Financial Corporation - President and CEO*

Could we get back to you on that one?

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**Don Guloien** - *Manulife Financial Corporation - SEVP and Chief Investment Officer*

I will attempt to answer that one, Jukka. It's Don Guloien on the speaker. We don't know what the losses are back then; however that experience is embedded in the minds of all our mortgage underwriting people, which is one of the reasons why we started to become so very cautious in the selection and equity real estate and in our mortgage underwriting in more recent times.

When I say recent, I am talking about starting five years ago we started to get very conservative. And that's why we enjoy such high ratios in the quality of the portfolio in terms of low loan-to-value ratio and high debt service coverage ratio.

We also stress-test them for a variety of scenarios including higher interest rates, which isn't an immediate concern, but also obviously lower vacancy rates. Our equity real estate portfolio was 92%, 93% occupied. Very high-quality tenants. No exposure to New York. Our bias is for highly diversified economies. You know, New York is a great place to operate, but obviously suffering a great deal of stress right now. And virtually no leverage anywhere in our equity real estate portfolio, which makes it kind of unique.

There is I think one building that has a tiny mortgage on it that we assumed, but if you allow for that, virtually no leverage on the portfolio.

So the experience of that period is indelibly printed on the minds of all our people that have anything to do with real estate.

**Jukka Lipponen** - *KBW - Analyst*

My second question is regarding the Reinsurance division. Can you give us a little more color why the markets in the quarter had an impact there?

**Peter Rubenovitch** - *Manulife Financial Corporation - SEVP and CFO*

They have a seg fund portfolio, so it's identical to everywhere else. That particular line didn't do well.

**Jukka Lipponen** - *KBW - Analyst*

Thank you.

**Operator**

Colin Devine, Citigroup.

**Colin Devine** - *Citigroup - Analyst*

Good afternoon, gentlemen. A couple questions. First just to frame up this variable annuity risk, I was wondering if you could give us a split of the type of exposure you have. Specifically, is it withdrawal benefit products, income benefit products, or accumulation? Since how they may perform can be fairly different.

Then for Don on the commercial mortgage book, certainly the loan-to-value ratios and the debt service coverage are little bit below some of your peers here in the States, but they are close. I just -- it would be very helpful if you could give us some sense of when you've been originating mortgages? How many of those are recent? Some sort of aging of the book if you might.

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**Dominic D'Alessandro** - Manulife Financial Corporation - President and CEO

Okay, so Hugh McHaffie is here, who heads up our variable annuity business (technical difficulty) States and Hugh can answer the question about --

**Hugh McHaffie** - Manulife Financial Corporation - EVP US Wealth Management

Colin, I can give you a split here on the IB versus WB. As you recall, we had sold IB in the late '90s and 2010 and primarily most of that was reinsured. So the net amount of risk is relatively small at about [CAD]345 million at the end of the fourth quarter.

Then since 2003/04, we have been selling primarily a GWB benefit, and that is where the more significant exposure is. The net amount of risk at the end of the fourth quarter was a little over 10 billion in the United States. So primarily most of the risk that we have would be in the WB benefit.

**Colin Devine** - Citigroup - Analyst

Okay, just I want to make sure we are all on the same page here with terms. If what is -- if we look at what the account value is of your WBs today, versus what the guaranteed amount is, how much is the difference? Is that what you are saying is 10 billion?

**Hugh McHaffie** - Manulife Financial Corporation - EVP US Wealth Management

Yes, the account value would be around 35 billion on the WBs with -- excuse me. The income benefit would be around 35 billion with account value around 25 billion, so than a net exposure of 10 billion.

**Colin Devine** - Citigroup - Analyst

On the IBs or the WBs?

**Hugh McHaffie** - Manulife Financial Corporation - EVP US Wealth Management

On the WBs.

**Colin Devine** - Citigroup - Analyst

So they are 10 billion in the money at the end of the year?

**Hugh McHaffie** - Manulife Financial Corporation - EVP US Wealth Management

That's correct.

**Colin Devine** - Citigroup - Analyst

Okay. Then when you are saying that people can't start withdrawing these for six to seven years, are you saying specifically on your contracts an individual is not able to draw them? Or that you are assuming they don't? Because certainly at least two-thirds of the people buying these are over age 60 and generally that's when the WBs kick in.

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**Hugh McHaffie** - *Manulife Financial Corporation - EVP US Wealth Management*

Colin, I guess the numbers that we gave you on the seven through 30 years is first of all worldwide modeling, and that is what we look at -- that the net money out on these benefits. So you have to look at the net money.

Clearly people in the United States can take money immediately. You are correct about two-thirds of the in-force GWB business would be, say, above age 60.

And just for a note, we are experiencing about 8% withdrawal rate on those contracts. But that then means that 92% are not taking money, and we factor that into the net cash flow over a seven- to 30-year period. That is what you are -- when we say seven to 30.

**Colin Devine** - *Citigroup - Analyst*

Now, when you strengthened reserves, there was some wording in there about utilization assumption changes. If you could just expand on that.

**Dominic D'Alessandro** - *Manulife Financial Corporation - President and CEO*

Simon, utilization assumption changes in our model, strengthened reserves?

**Simon Curtis** - *Manulife Financial Corporation - EVP and Chief Actuary*

Yes, we reviewed all our assumptions in the fourth quarter, as we do each year. On the variable annuities loss, I think the updated withdrawal assumption is about 4.6% out of the 5% utilization. So when people lapse.

And the lapse rates, the minimum lapse rates we use are about 3%.

**Colin Devine** - *Citigroup - Analyst*

Okay. Then Don; and then I have one quick follow-up for Dominic.

**Don Guloien** - *Manulife Financial Corporation - SEVP and Chief Investment Officer*

Yes, your question on the mortgages, okay, it's a very good story. I want to get all elements of it out here. There is an increasing amount of concern about what's going on the commercial mortgage market in the United States; and in our opinion that concern is warranted.

If you saw the activity of the conduits and the securitized vehicles, the underwriting standards in latter years certainly exposed investors to an ever-increasing amount of risk. And we would concur with the view that there is going to be increased stress in that market.

That view has been evidenced by the originations in CMBSs by Manulife, the participation in them, where basically 80% of our entire volume of CMBSs were written in 2004 and prior. So we choked off pretty completely the participation in the later vintages because we saw deterioration in the underwriting standards.

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In fact the 20% that is in the years 2005, '06, '07, and '08 are almost exclusively at the AA and many of them at the AAA level. Extremely high quality. I think virtually all of them are at AAA actually; but certainly all above AA, other than negligible amounts. So --

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**Colin Devine** - Citigroup - Analyst

What about your whole loans?

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**Simon Curtis** - Manulife Financial Corporation - EVP and Chief Actuary

Yes, I'm going to get there, Colin. So that is an area that is going to undergo quite a bit of stress. But we feel that we will be very, very well protected for that stress.

In terms of the whole loan origination, that has been more steady. And because we're doing the underwriting, we do our own appraisals, and our appraisals come in consistently more conservative than those that are available by the external appraisers. Again, this is reflecting what has been going on with the conduits, where you get a flexible appraisal and a higher loan-to-value ratio effectively from that.

We were happy to see those loans go to other people. So our loans have been very conservatively underwritten.

I would also point out that of our entire mortgage book roughly 60% of it is in Canada, 40% of it is in the United States. And within the 60% Canada piece, roughly half -- and I am using very rough numbers -- are insured by the Canadian federal government through the CMHC.

On the piece that is in the United States, which you might think is the most exposed, again these loans are regularly -- on a quarterly basis we do collateral reviews with update, up-to-date assessments of the property. And those are reflected in our loan-to-value ratios and our estimates of debt service coverage capability.

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**Colin Devine** - Citigroup - Analyst

Has your restructuring activity accelerated much?

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**Don Guloien** - Manulife Financial Corporation - SEVP and Chief Investment Officer

No, not on our portfolio, although we were a little ahead of the curve. We did help out people who originally -- desirous of increasing their appetite by selling off loans the past few years. And we were worried about what was going on in the Midwest, and we have sold loans at actually quite good prices prior to the issues emerging.

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**Colin Devine** - Citigroup - Analyst

Okay. Then for Dominic, you mentioned in your opening remarks this being your final month. Should I take that to assume then you are stepping down at the end of February, or were you talking more generally?

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**Dominic D'Alessandro** - Manulife Financial Corporation - President and CEO

No, Colin, I hate to disappoint you.

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**Colin Devine** - *Citigroup - Analyst*

No, actually it would disappoint me if you were leaving early.

**Dominic D'Alessandro** - *Manulife Financial Corporation - President and CEO*

No, I plan to -- things are unfolding here as -- other than for the market, but apart from that, Don is taking charge, but I am here till the Annual Meeting.

**Colin Devine** - *Citigroup - Analyst*

So you will be around for another conference call?

**Dominic D'Alessandro** - *Manulife Financial Corporation - President and CEO*

I think Don will probably want me to take that call.

**Colin Devine** - *Citigroup - Analyst*

I'm glad to hear you wouldn't miss it for the world, Dominic. Thanks.

**Don Guloien** - *Manulife Financial Corporation - SEVP and Chief Investment Officer*

Colin, he will only be around the corner when I need him for advice; and he's promised me that 24/7 he will be available for that advice.

**Colin Devine** - *Citigroup - Analyst*

But you are not going to give him access to the corporate jet, I hope.

**Dominic D'Alessandro** - *Manulife Financial Corporation - President and CEO*

No, that's one of the things I left out. If we ever got one, I should have negotiated that Don would let me ride it. We don't have one. It doesn't look like we're going to get one tomorrow.

**Don Guloien** - *Manulife Financial Corporation - SEVP and Chief Investment Officer*

And we are not looking for one, Colin.

**Dominic D'Alessandro** - *Manulife Financial Corporation - President and CEO*

Though they might be cheap now.

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**Operator**

Michael Goldberg, Desjardins Securities.

**Michael Goldberg** - Desjardins Securities - Analyst

Thanks, two quick ones. First of all, what is the impact of the OSFI change on the MCCSR calculation?

**Peter Rubenovitch** - Manulife Financial Corporation - SEVP and CFO

Michael, I think you asked that in our last go-round in this item, and we really don't look at it this way because we have other things that we have been updating. We really had a simple methodology when that reserve was small, so it was favorable to us. But we really -- we don't have a detailed breakout of the impact of (multiple speakers).

**Dominic D'Alessandro** - Manulife Financial Corporation - President and CEO

But at the time the change was made, I seem to remember that was worth about 20 points to us. Is that not right?

**Simon Curtis** - Manulife Financial Corporation - EVP and Chief Actuary

I don't have that. It's Simon. I don't have the numbers in front of me. I believe that's right.

Obviously the impact as the reserve is bigger would be more material now. So we obviously benefited quite materially from that, but I do believe that's right.

**Peter Rubenovitch** - Manulife Financial Corporation - SEVP and CFO

Give you an idea.

**Michael Goldberg** - Desjardins Securities - Analyst

Okay. And in slide 9, your change in actuarial methods and assumptions was CAD321 million. But you said something about if you excluded something related to seg funds, it would be a CAD288 million charge. I am confused.

What is it that would be related to seg funds? And why would it be a release under these circumstances?

**Peter Rubenovitch** - Manulife Financial Corporation - SEVP and CFO

Maybe Simon will go through that, but the point I was making is that all other businesses, it would have been a charge. The seg funds piece, the updates were favorable to incomes on the seg fund change. But Simon, I don't know if you want to add anything to that.

**Simon Curtis** - Manulife Financial Corporation - EVP and Chief Actuary

Yes, sure, Peter. It's Simon Curtis again. Yes, the CAD321 million number was the net impact of the change in methods and assumptions.

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I think what Peter was giving you in that comment was just an additional comment that if you wanted -- because we thought people might be -- it would be a question that would come up. Was that to get to that CAD321 million, if you just isolated the segregated fund guarantee businesses, there was a post-tax release of CAD609 million; and there was a net increase on all the other lines of CAD288 million.

That has nothing to do with the market performance. That was really just the result of the assumption reviews on the policyholder behavior, making sure we refined our cash flow calculations to be as accurate as possible given that these guarantees are more material. Plus some of the change in the CTE level would also have flown through that number.

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**Dominic D'Alessandro** - *Manulife Financial Corporation - President and CEO*

Not for Michael but for the other people on the call, I believe when Peter was speaking to that slide he said 521 instead of 321.

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**Peter Rubenovitch** - *Manulife Financial Corporation - SEVP and CFO*

Yes, I misspoke. I apologize.

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**Dominic D'Alessandro** - *Manulife Financial Corporation - President and CEO*

Everybody caught it, I think, but just to be sure.

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**Peter Rubenovitch** - *Manulife Financial Corporation - SEVP and CFO*

I missed it. I'm sorry.

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**Michael Goldberg** - *Desjardins Securities - Analyst*

Okay, so just so I'm clear on this, were you saying that that includes the change in the CTE level from 80 to 65?

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**Simon Curtis** - *Manulife Financial Corporation - EVP and Chief Actuary*

No, when we took that charge at the third quarter, I think we mentioned that we set up CAD1 billion of additional segregated fund guarantee reserves to build us up to the CTE level. When we booked the -- that was booked as a separate additional accrual.

When we did the year-end accounts, half of that accrual was released; and that's the part that went through the basis changes.

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**Michael Goldberg** - *Desjardins Securities - Analyst*

Okay, thank you.

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**Operator**

Doug Young, TD Newcrest.

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**Doug Young** - TD Newcrest - Analyst

Yes, just the first question on the dividend. Obviously your MCCSR is 233. If you look at the sensitivity where the market is today you are closer to 210, 213. You are spending CAD1.7 billion annually for the dividend.

How do you balance off, if the markets continue to deteriorate, whether you go and raise equity capital or debt capital, or you take a look at the dividend and paring back the dividend?

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**Dominic D'Alessandro** - Manulife Financial Corporation - President and CEO

Well, I think that's a good question. The dividend we are comfortable with at the level that it's at, given the conditions that now exist. If the markets as you point out decline precipitously, we would have to re-examine the sustainability of the dividend, absent any other actions we may take.

As I said earlier, we are going to be initiating some actions to try to generate some capital over the next little while. There are some capital instruments that are available in the marketplace to us. And so it's something that we are very aware of and are watching very closely.

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**Doug Young** - TD Newcrest - Analyst

So essentially you would be looking to do these initiatives before you would take another look at the dividend? Is that it essentially?

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**Dominic D'Alessandro** - Manulife Financial Corporation - President and CEO

I think that's right, and again it's difficult to be definitive because if tomorrow markets go down 25%, we have got to respond in some way. If on the other hand markets stabilize or stay within a few percentage points of where we are now, that's a different conclusion.

So it's very sensitive. That's why we gave you the numbers. We have got huge, huge exposure given the way these amounts have to be determined; and we've got more sensitivity than we would like.

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**Doug Young** - TD Newcrest - Analyst

Can you share with us what those opportunities or initiatives are from a capital perspective that you are looking at?

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**Dominic D'Alessandro** - Manulife Financial Corporation - President and CEO

Well, we are thinking -- I don't know whether -- is this --? People are shaking their heads at me here. But anyway you will hear about them in due course.

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**Doug Young** - TD Newcrest - Analyst

Okay, second just on the US variable annuity business, we have heard other companies in the US quantify the changes that they have been making in terms of increasing pricing or changes of investment parameters. Can you talk about what changes Manulife has made to the US product?

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**Dominic D'Alessandro** - *Manulife Financial Corporation - President and CEO*

I think Hugh or John?

**Hugh McHaffie** - *Manulife Financial Corporation - EVP US Wealth Management*

It's Hugh McHaffie. You know, the specific changes that we made, we announced last December, encompassed a slight fee increase by 10 basis points. But more importantly we reconfigured the equity risk, equity component that was available in our asset allocation portfolios. That, given the current volatility, is a significant piece as to reduce the exposure to equity. So that was completed.

In addition we changed up some of our income deferral bonuses, taking away one of the features. That was the significant change we made.

Then finally we had modified our ratchet or step-up. You know, I think this is the first round of changes for us. We are -- this is the season for changes in the US for the variable annuities, and we are seeing most companies have either changed or filed new changes; and we will see where things go.

The equity volatility continues to be high. I would suspect that you would see us continue to look at some additional de-risking in the near future if volatility stays where it is at.

**Doug Young** - *TD Newcrest - Analyst*

What is the max exposure that can go into equities now? Is this on just new or is this on in-force as well?

**Hugh McHaffie** - *Manulife Financial Corporation - EVP US Wealth Management*

The max exposure is about 72%, 73% now in our variable annuity business, and that is effective both for new business and our in-force business.

**Doug Young** - *TD Newcrest - Analyst*

Okay. Just one last if I may on the URR, Simon. We saw industrial lines make a change. Can you talk a bit about where Manulife stands on the URR?

**Simon Curtis** - *Manulife Financial Corporation - EVP and Chief Actuary*

Sure, yes. Our exposure when we do this scenario testing is to decline in interest rates. So we look at this scenario with declining interest rates as our basis. On that basis following the CIA's approach, we assume long-term ultimate reinvestment rates for all our non-fixed interest. It's 4% in Canada and 4.1% in the US. Those are for long bonds. Then at the short end of the curve it's about 2.5%.

**Doug Young** - *TD Newcrest - Analyst*

So those are your URR assumptions, those 4% in Canada and 4.1% in --?

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**Simon Curtis** - *Manulife Financial Corporation - EVP and Chief Actuary*

That's right, for long bonds. Then those URR assertions for any shorter-term reinvestments that we do in our investment strategies are closer to 2.5%.

**Doug Young** - *TD Newcrest - Analyst*

Okay. You've made no changes to your URR assumption at the end of 2008. But I guess essentially if rates stay where they are, we may have to see some changes at the end of 2009. Is that a fair way to characterize it?

**Simon Curtis** - *Manulife Financial Corporation - EVP and Chief Actuary*

Well, our URRs are lower than the ones that -- sort of the maximum ones that you can use under the CIA's prescription. But so we would not anticipate having to change anything during 2009.

But we would have to look at it again in next year's basis changes, depending on how the interest rates perform this year.

**Doug Young** - *TD Newcrest - Analyst*

Okay, thank you.

**Operator**

Mario Mendonca, Genuity Capital Markets.

**Mario Mendonca** - *Genuity Capital Markets - Analyst*

Good afternoon and thank you for taking the call a little bit longer today. On the private placements, Don, that's probably the most frequently asked question on Manulife, aside from equity markets lately. Just as a general comment, we need a lot more information there, because it's a big number.

Maybe the question I have is -- the Company has gross unrealized losses about CAD9 billion I think in total. That's for the HFT and the available-for-sale. How much of that relates to the CAD25 billion private placement portfolio?

**Scott Hartz** - *Manulife Financial Corporation - EVP US Investments*

Mario, it's Scott Hartz. We don't have those numbers in front of us. I would say generally speaking the private placement portfolio is little bit lower average quality than the public bond portfolio.

Where we have done below investment grade in the past has been large -- to a greater extent in the private portfolio, where you can get secured and you can get covenants and so forth. So -- and the way we price that is to use public market pricing plus a spread for the illiquidity.

So as public spreads have widened out significantly, you would see the gross unrealized loss go up on that book. So I would expect on a pro rata basis that it might be just a tad higher, because it's a little bit lower quality.

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**Mario Mendonca** - *Genuity Capital Markets - Analyst*

Tad higher than the public?

**Scott Hartz** - *Manulife Financial Corporation - EVP US Investments*

That would be my expectation, yes.

**Mario Mendonca** - *Genuity Capital Markets - Analyst*

Have there been any impairment charges on those securities?

**Scott Hartz** - *Manulife Financial Corporation - EVP US Investments*

You know, you saw our impairment charges for the quarter. I think Peter talked about them. They were fairly modest for the year. They were large due to the public financials. I think in the fourth quarter a portion of them was due to privates; but a small, a smallish portion, certainly well less than half.

**Don Guloien** - *Manulife Financial Corporation - SEVP and Chief Investment Officer*

It is a portfolio in pretty good shape, though, Mario, and I think your suggestion is a constructive one. We would be happy to provide more transparency to that portfolio. I think it would be actually reassuring to investors and thank you for that.

**Mario Mendonca** - *Genuity Capital Markets - Analyst*

Yes, it's coming up pretty frequently. Another quick question and maybe you have answered this already. The CAD912 million that you refer to in the notes on page 38 of the supplement, that 900 and -- it's with respect to footnote 3. It makes it sound like the increase to reserves would've been CAD912 million greater pretax had you not changed valuation assumptions and methodologies.

Is that the same as the CAD609 million after-tax that you refer to in discussing page 9 of the presentation?

**Simon Curtis** - *Manulife Financial Corporation - EVP and Chief Actuary*

Mario, it's Simon here, Simon Curtis. Yes, that's right. That CAD912 million is the pretax number. And then the number that we were discussing today, the CAD609 million, is the same number on a post-tax basis.

**Mario Mendonca** - *Genuity Capital Markets - Analyst*

I understand it. Then finally I think I've misinterpreted rating agencies before, so I want to take a little chance, risk here, and ask you to help me interpret it. Moody's today has said that they are assessing -- in looking at Manulife's ratings, they're making an assessment as to management's plans to reduce the Company's risk profile via the additional equity offerings and/or expansion of the equity risk hedging program.

It may not be entirely appropriate to ask you about your conversations with rating agencies, but what I'm trying to understand is -- is there a discussion with the rating agencies now about Manulife raising common equity to maintain its rating, or extending the hedging program to in-force books spokes business?

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**Peter Rubenovitch** - *Manulife Financial Corporation - SEVP and CFO*

No, we have had no discussions of any of that sort. They have been privy to the same sort of update as we are sharing with you in terms of our performance. I think they have fairly standard language when they talk about the things they consider to be key parameters, and that's what they would reflect in their disclosure. So you shouldn't read more into it than that.

**Mario Mendonca** - *Genuity Capital Markets - Analyst*

So Peter, you can say to me now that they are not asking you to raise additional common equity?

**Peter Rubenovitch** - *Manulife Financial Corporation - SEVP and CFO*

No. No rating agency has asked us to raise equity. In fact we have very high ratings and they have to rate what we offer them. You know, we are very open with them and discuss our general concept about capital structure and business plans; but nobody has asked us to do anything to maintain or do anything with ratings. That's not a type of discussion we have had.

**Mario Mendonca** - *Genuity Capital Markets - Analyst*

Thank you.

**Operator**

Eric Berg, Barclays Capital.

**Eric Berg** - *Barclays Capital - Analyst*

Thanks very much and good afternoon to everyone. Thanks for allowing the call to continue here. My first question is a broad one, Dominic. It's to you.

That is, for people who want to sort of get away from all this actuarial talk, it's been very freighted this conversation in CTE this and CTE that, very, very heavy actuarial. People like myself who would like to understand why it is that there has been such an enormous earnings hit again at Manulife because of the stock market, that we are not seeing to anywhere nearly the same degree in the United States at your competitors, is this simply a matter of the fact that they hedged and you didn't? Or is there more to this story?

**Dominic D'Alessandro** - *Manulife Financial Corporation - President and CEO*

Well, I don't know the details of the charges that they are reporting. I suspect some of it is because they've hedged. I don't know that they are holding reserves at quite the same level as we are. I don't know what the -- I don't study their accounts.

So we are giving you our facts. Our facts are that our contracts are underwater by about CAD26 billion. We have set up, because of the mechanisms that we use, the formulas, our models, we set up CAD5.7 billion. I don't know what the equivalent numbers are at our competitors.

You know, I think, Eric, that would be very useful information if we could get that. I don't know how they reserve under that regime.

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I hear stories about that they hedge part of their portfolios but not all of them; but they park some of the exposure in entities that are not constrained or not subjected to regulatory capital requirements. You know, I just don't know. I don't know how to respond to your question.

We have a lot more equity risk. There's no question about it. We've known we have had this equity risk. It was almost intentional that we chose to take equity risk in years gone by thinking that we were a logical repository given the nature of our liabilities and the obligations we were taking on. We had to invest them in a portfolio of assets, and equities have performed very, very well.

And we had a different accounting regime when we had that approach. We lived with it for a good long time and our exposures grew as they did. We were late in activating our hedging program. We had it ready to go; we hired all the people, set up all the systems. But it took us a while -- longer than we should have -- to get it going.

And the markets got away from us. No one expected them as I said at the last call to collapse quite as significantly as they have. Again, you've got to put on your hat as a business person and say to yourself this is the exposure that they have. This is -- there's no mystery here. There's no opaqueness. There's no level three assets. There's no complex instruments. This is a very, very simple exposure.

We have equities that are not worth what we paid for them. Do you believe that over time markets will recover and that shortfall will be made up? We do our accounts on the basis that the market will never recover; and therefore we need to set up an amount today which with just normal interest rates at 6% will grow over the period of time that the cash flows are going to be disbursed sufficient to satisfy those cash flows.

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**Eric Berg** - *Barclays Capital - Analyst*

Very helpful. My second and final question is as follows. I think that Simon said in response to Nigel's question earlier that if the CTE had not been lowered to 65 from 80 that there would have been about a CAD3 billion additional reserve increase after-tax.

Is that -- that's not my question, but if you could confirm that, Simon?

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**Simon Curtis** - *Manulife Financial Corporation - EVP and Chief Actuary*

That number was not that large. I think the reserve would have been CAD8 billion versus the CAD5.8 billion that we are holding.

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**Eric Berg** - *Barclays Capital - Analyst*

Okay. So CAD2.2 billion.

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**Dominic D'Alessandro** - *Manulife Financial Corporation - President and CEO*

And that's pretax, Eric.

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**Eric Berg** - *Barclays Capital - Analyst*

Okay, that's helpful, CAD2.2 billion pretax in addition.

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My question is this, and Dominic, I know you've touched on this, but I'm hoping you can build on your previous answer. If this were a commercial bank facing increasing strain and we saw reserve strength going down, we would say the bank is underreserving.

Again, help us understand what is the logic, the rationale for bringing that down in a deteriorating -- in an environment that you yourself say is not stable but is getting worse?

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**Dominic D'Alessandro** - *Manulife Financial Corporation - President and CEO*

Well, I think again you have to get into some of -- and believe me I have spent more time on this than I ever thought I would want or need to.

But all of it is a function of your model that you use in order to project out what probability and determine these CTE levels. As we run as I understand it 5,000 or more scenarios at CTE zero, which is what we expect, we gave you that information in the package.

We expect that if markets would just perform from now on until -- just perform in accordance with past experience, that we wouldn't have to pay any obligations; and we would still make money on the entire portfolio. The markets don't have to boomerang back. They just have to perform over a period of time consistent with historical norms.

So as you have heard, depending on what -- because these amounts are payable over such a long period of time, depending upon what assumptions you make, particularly around discount rates, it has an impact on that reserve that's thrown up at the reporting period.

We intend to, as Simon says, use a different discount rate to reflect the nature of the assets that we're going to be investing that reserve in. And that will throw up a CTE level that's quite a bit higher than what we are reporting. As Simon said, 70. It might be higher than 70. We haven't done that number yet.

So a lot of this is -- a lot of these calculations are supported by quite precise models, but in point of fact it doesn't (technical difficulty) that they are at the end of the day just an estimate.

You have to stand back and say to yourself -- and fortunately this is an easy one, relatively easy one to do. Do you say, I've got this obligation; it's spread out over all these number of years; how much do I need today to take care of it?

We've said, our figure has said that is CAD5.7 billion. And our model says using the assumptions we've made that that's a CTE(65). As I just explained, somebody else might use a different model and come up with a number of, I don't know, CAD4 billion. And that might be in their model because of their assumption the CTE is 65 too. Or it could be a CTE of 80. It all depends on the assumptions that the model makes.

Now we've tried to -- I would love to tell you that I have a textbook here that gives me everybody's model and I know that my model is exactly like everybody else's. But I'm told that you get four actuaries in a room and ask them to go run four models on this, they're not going to come up with the same answer. They are all going to have their own particular judgments as to each of the factors that -- this is a very long answer about a very technical.

I tried to reduce it to in its simplest form, you have an obligation of -- you have a potential hole of CAD26 billion. You have a hole of CAD26 billion. What is the appropriate amount to take through earnings today?

We've taken through CAD5.7 billion. In addition we have another CAD4.4 billion in our 200% MCCSR.

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So you've got for the CAD26 billion of obligation payable over, as I say, seven to 30 years or more; you've got CAD11 billion that's been sequestered today.

Is that too much? I think it's very, very, very conservative. You might think it's too little. But I don't know there's an absolutely correct answer. There isn't a laboratory some place where you can go and assay this thing and say -- is it 24-carat gold or 18-carat?

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**Eric Berg** - *Barclays Capital - Analyst*

Thank you.

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**Dominic D'Alessandro** - *Manulife Financial Corporation - President and CEO*

I think, operator, that concludes our call. Ladies and gentlemen, thank you very much. Again I want to repeat that we are going through some extraordinarily difficult times. We have not seen markets behave like this in 100 years.

Notwithstanding the difficult times that we've gone through, I think our Company is holding its own. Our businesses are doing really well. Operationally we are more efficient and more effective. Our distribution is growing, and our product offerings around the world are gaining favor.

We service well over 20 million customers around the world. All of those good things that happen, as I said earlier, are overshadowed by the fact that these markets have fallen very, very precipitously. Should they continue to fall, we've given you the facts to allow you to make a determination as to what the impacts would be on our capital and on our net income.

Clearly given the situation (technical difficulty) our focus is going to be pretty -- to stay close and manage our business and make sure that we can make it through whatever rough patches remain to be visited upon us. In the end, your judgment has to be whether this is a franchise that distinguishes itself in many other ways.

I remind you that while we may have a lot of equity risk, I believe that our assets have held up much better. We have much less credit risk than others and other kinds of risk. You know, all the people who supposedly were hedged on this exposure, I don't notice that they are reporting much better earnings than I am.

So, I would be very interested if one of you could do an analysis and say Manulife has got this hole, and this is how much they provided; and so-and-so has got that hole and here is how they've done with it; and so on and so forth. It would be very, very interesting.

I think that those facts would show that we are providing for this situation in our usual conservative manner. And I hope that at some point we will be able to report to you that the tide has turned and we are regaining or we are stopping the bleeding at least, and the strength of the franchise and of our businesses will become apparent to you once again.

Look at our performance in the revenue line. I'm very, very pleased with the way we are controlling our expenses in this Company. And I'm very, very pleased with how we are growing the organization. So those are a bit of an editorial. Thank you very much and we will talk to you next quarter.

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**Operator**

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

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