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PRESENTATION

Operator

Please be advised that this conference call is being recorded. Good morning, and welcome to the Manulife Financial First Quarter 2022 Financial Results Conference Call. Your host for today will be Mr. Hung Ko. Please go ahead, Mr. Ko.

Hung Ko - Manulife Financial Corporation - VP, Group Investor Relations

Thank you. Welcome to Manulife's earnings conference call to discuss our first quarter 2022 financial and operating results. Our quarterly earnings material, including the webcast slides for today's call are available on the Investor Relations section of our website at manulife.com.

Turning to Slide 4. We will begin today's presentation with an overview of our first quarter highlights and an update on our strategic priorities by Roy Gori, our President and Chief Executive Officer. Following Roy's remarks, Phil Witherington, our Chief Financial Officer, will discuss the company's financial and operating results and provide an update on the key implications of IFRS 17 on Manulife's financial results and key performance indicators.

After the prepared remarks, we will move to the live question-and-answer portion of the call. We ask each participant to adhere to a limit of 2 questions, including follow-ups. If you have additional questions, please re-queue and we will do our best to respond to everyone.

Before we start, please refer to Slide 2 for a caution on forward-looking statements and Slide 39 for a note on the non-GAAP and other financial measures used in this presentation. Note that certain material factors or assumptions are applied in making the forward-looking statements, and actual results may differ materially from what is stated.

With that, I'd like to turn the call over to Roy Gori, our President and Chief Executive Officer. Roy.

Roy Gori - *Manulife Financial Corporation - President & Chief Executive Officer*

Thanks, Hung. Thank you, everyone, for joining us today. Yesterday, we announced our first quarter 2022 financial results. Our diversified footprint, operational resilience and proven digital capabilities enabled us to deliver solid results in the first quarter despite a challenging operating environment caused by the resurgence of COVID-19 and global market volatility.

You'll see on Slide 6, we delivered solid core earnings of \$1.6 billion, a modest 4 percent decrease from the prior year quarter as we continued to benefit from the diversity of our businesses. And we also reported net income of \$3 billion, an increase of \$2.2 billion over the prior year quarter, reflecting strong investment-related experience and a gain from the closing of the U.S. variable annuity reinsurance transaction.

We achieved new business value of \$513 million. The resurgence of COVID-19 and tighter containment measures impacted many of our markets in Asia and lowered NBV. This was partially offset by double-digit growth in both Canada and the U.S., exemplifying the benefit of our business diversification. While the rapid and unprecedented resurgence of COVID-19 disrupted new business activities in multiple markets in Asia, our diversified, digitally enabled, and well-established distribution channels delivered double-digit growth in APE sales and NBV relative to the average levels during the first wave of the pandemic in the first and second quarters of 2020.

And Global WAM had another quarter of strong net inflows, generating \$6.9 billion with positive contributions across all geographies and business lines. Finally, we reported embedded value of \$64.8 billion or \$33.35 per share as of December 31, 2021, an increase of \$3.7 billion or 7.3 percent from the prior year. We believe that embedded value is an important valuation metric. Additional information on our embedded value can be found in the appendix and our 2021 Embedded Value Report.

Turning to Slide 7. We are laser-focused on delivering on our strategic priorities. Our highest potential businesses accounted for 63 percent of total company core earnings in the first quarter of 2022. In Asia, we successfully commenced offering insurance solutions to VietinBank's 14 million customers as part of our exclusive 16-year bancassurance partnership in Vietnam. And in our Global WAM business, we announced the launch of the Real Asset Investment Strategy in Canada, which provides investors access to a mix of global private and public real asset investments, combining the benefits of broad private asset exposures with the liquidity benefits of allocating to public markets.

We continue to execute on our ambition to be the most digital customer-centric global company in our industry. In Asia, more than 10 percent of APE sales resulted from leads generated using advanced analytics to identify additional needs from existing customers. We launched an enhanced Manulife Vitality mobile app experience in Canada for our Individual Insurance business, giving the app a new look and feel with easier navigation to further drive member engagement. In the U.S., we enhanced our eApp by implementing automated background checks, which reduced onboarding cycles from 3 weeks to 5 days, and reduced costs and call center volumes.

In our Global WAM retirement business, we enabled registration directly through the mobile app in Canada, resulting in approximately 50,000 Canadian customers using our mobile application by the end of the quarter. We've made tremendous progress on our digital journey, as evidenced by the 20-point improvement in our Net Promoter Score from plus 1 in 2017 to plus 21 in 2021.

In recent months, our service levels were impacted by temporary workforce capacity constraints and at the end of the first quarter, the rolling four quarter average NPS was tracking below our 2022 target of plus 31. We're taking actions to boost the average NPS in 2022. We are committed to continuing to execute on our strategy to attract, engage and retain customers by delivering an outstanding experience for every interaction. We remain on track to achieve our 2025 supplemental goal of plus 37. In line with our semi-annual reporting of NPS, we will provide a more fulsome update with our second quarter 2022 results.

Turning to Slide 8. We continued to drive progress on our expense efficiency, portfolio optimization, and high-performing team priorities during the quarter. We achieved an expense efficiency ratio of 50 percent despite a modest decrease in core earnings as we continued to proactively manage costs amid the challenging environment. Of note, we closed the variable annuity reinsurance transaction in the U.S. with a deal multiple of 11.8 times and released \$2.4 billion of capital. And we've commenced share buybacks to deliver shareholder value and neutralize the impact of the transaction on core EPS.

Turning to Slide 9. During the first quarter, we witnessed a rapid and unprecedented resurgence of COVID-19 in Asia. The spike in daily new confirmed cases significantly exceeded prior waves for many of our markets. This resulted in tighter containment measures, notably in Hong Kong, Mainland China and Vietnam. These containment measures have challenged the broader economy and the insurance industry as a whole. We are encouraged to see recent signs of stronger customer demand returning as case counts are declining. For example, in Hong Kong, we saw confirmed cases decrease from the peak of 77,000 daily to 300 daily as of May 1, and containment measures have begun to relax in late April.

Turning to Slide 10. Despite the ongoing prevalence of COVID-19, we have demonstrated a strong track record in managing the challenges over the past 2 years. A clear example is our Hong Kong business, where we've gained market share and increased our ranking by 1 spot to number 5 on insurance and retained our number 1 market position in MPF in 2021. We have delivered 19 consecutive quarters of year-over-year growth in core earnings.

We've also scaled and digitized our distribution force, growing agency headcount by 7 percent and increasing our ePOS active agent adoption to over 80 percent. Our NBV margin improved 3 percentage points this quarter compared to the prior year as we focused on increasing health and protection mix, and scaling our MOVE platform to help more customers become healthier.

Since the outbreak of COVID-19 in 2020, we've delivered resilient results due to the investments that we've made into our talent, digital and distribution channels. As markets across Asia navigate the challenges of the pandemic, we continue to be well positioned to serve our customers' needs. The strong demand that we've witnessed in North America and ongoing attractive megatrends in Asia give us optimism about the opportunity as those markets recover from the pandemic.

Turning to Slide 11. We delivered solid results in the first quarter of 2022, and I'm very proud of the performance of our business during the quarter, despite a challenging operating environment caused by the resurgence of COVID-19 and global market volatility. We closed the transaction to reinsure over 75 percent of our U.S. variable annuity business with a deal multiple of 11.8 times and released \$2.4 billion of capital.

We remain committed to generating shareholder value as we commenced share buybacks to neutralize the impact of the transaction on core EPS. Our solid foundation, global presence, diverse business and continued strong execution uniquely positions us to succeed and deliver on our growth targets.

Thank you. And I'll hand over to Phil Witherington, who will review the highlights of our financial results and provide an update on IFRS 17. Phil.

Phil Witherington - *Manulife Financial Corporation - Chief Financial Officer*

Thanks, Roy. We're off to a solid start for the year despite a challenging operating environment. I'll now highlight the key drivers of our first quarter results.

Starting on Slide 13. We generated solid core earnings of \$1.6 billion in the first quarter of 2022, a modest 4 percent decrease from the prior year quarter. This year-over-year change was driven by a number of factors: lower new business gains in Asia, an unfavourable impact of markets on seed money investments, and lower in-force earnings in U.S. annuities due to the variable annuity reinsurance transaction that closed on February 1. These items were partially offset by experience gains, in-force business growth in Canada and Asia, higher fixed income yields and a lower cost of debt in Corporate and Other, and higher new business gains in Canada and the U.S.

Of note, the unfavourable impact of markets on seed money investments was \$63 million and consisted of approximately \$37 million from equity funds and approximately \$29 million from fixed income funds. The overall amount was larger than our disclosed sensitivity would imply, mainly reflecting the impact of material interest rate moves not contemplated in our sensitivity.

Net income attributed to shareholders of \$3 billion was up \$2.2 billion from the prior year quarter, reflecting gains from the direct impact of markets again related to the U.S. variable annuity reinsurance transaction and larger gains from investment-related experience. Of note, we recognized a gain of \$658 million from investment-related experience, \$100 million of which was included in core earnings as 'core investment gains', with the remaining \$558 million reported outside of core earnings.

We recognized other gains of \$763 million, largely driven by a one-time after-tax gain of \$842 million from the U.S. VA reinsurance transaction. The cumulative net gain from this transaction is \$802 million after including a one-time after-tax loss of \$40 million recognized in the fourth quarter of 2021.

The gain of \$207 million from the direct impact of interest rates was due to the flattening of the yield curves and gains from widening corporate spreads, partially offset by realized losses on sales of AFS bonds. The impact of equity markets in the quarter was a loss of \$110 million.

Slide 14 shows the recent history of our investment-related experience. Over the past 3 years, including through the pandemic and related market volatility, we have continued to generate strong investment-related experience. While experience can vary period to period, since 2019, our investment-related experience gains have well exceeded \$100 million on average each quarter.

The average quarterly gain of \$212 million since the start of the pandemic in early 2020 is also comparable to the average of \$192 million we reported during 2019. Overall gains from fixed income reinvestment have been strong and steady, and credit experience has been a reliable contributor. ALDA has also been a contributor over this period, although the experience varied significantly quarter-to-quarter due to its mark-to-market nature. Through the cycle, our ALDA portfolio has performed well and exceeded our long-term return assumption, as I noted in our fourth quarter 2021 results.

Slide 15 shows our Source of Earnings analysis for the first quarter of 2022 compared to the prior year quarter. Expected profit on in-force increased 3 percent. Excluding the impact of the U.S. VA reinsurance transaction, the increase was a strong 7 percent from the prior year.

New business gains decreased by 31 percent from the prior year period, primarily driven by lower critical illness sales in Mainland China, lower sales in Hong Kong and several markets in Asia Other due to the strong COVID-19 wave as well as lower COLI product sales in Japan.

Policyholder experience was a net favourable \$50 million on a pre-tax basis, reflecting the diversified nature of our business. Favourable experience in U.S. long-term care more than offset losses in U.S. Life, and Canada recorded a net favourable experience while Asia was largely neutral.

Slide 16 shows the recent history of our policyholder experience. As we mentioned previously, the pandemic and related macroeconomic environment impacted our policyholder experience differently across product lines and geographies. The diversity of our businesses and our use of reinsurance provided an offset, and on a cumulative basis since the start of the pandemic in early 2020, the net impact was close to neutral, in fact, slightly positive.

Slide 17 shows our earnings by segment and return on equity. We delivered core earnings growth of 4 percent in our Global WAM business, reflecting growth in net fee income. Core earnings in Asia decreased by 5 percent, driven by lower new business volumes in Hong Kong and several markets in Asia Other, reflecting the adverse impact of COVID-19 containment measures, lower sales in Japan, and unfavourable product mix in Mainland China. Core earnings in Canada increased by 19 percent, reflecting higher in-force earnings, more favourable policyholder experience and new business gains in the Individual Insurance business.

Core earnings in the U.S. decreased by 3 percent, largely due to the VA reinsurance transaction. Excluding the impact of the transaction on in-force earnings, core earnings would have increased 4 percent as compared to the prior year quarter. The core loss in Corporate and Other increased by \$91 million, primarily driven by the unfavourable impact of markets on seed money investments. And we delivered a core ROE of 11.8 percent.

Turning to Slide 18, which shows our APE sales and new business value generation. In the first quarter, we generated APE sales of \$1.6 billion, down 9 percent from the prior year as growth in North America was more than offset by a decline in Asia. In Asia, APE sales decreased 17 percent due to adverse impacts from COVID-19 in Hong Kong and several markets in Asia Other as well as lower COLI product sales in Japan.

We delivered new business value of \$513 million, down 14 percent from the prior year quarter. In Asia, new business value decreased due to the factors I noted earlier and unfavourable product mix in Mainland China. This was offset by double-digit NBV growth in North America as we continued to see strong customer demand in our Canada and U.S. insurance businesses.

Turning to Slide 19. Our Global WAM business continued to benefit from our geographic and line-of-business diversification as evidenced by strong net inflows of \$6.9 billion and gross flows of \$38.5 billion in the first quarter. In Retail, net inflows were \$4 billion compared with net inflows of \$6.5 billion in the prior year quarter. The decrease was driven by lower gross flows, mainly in fixed income products and higher mutual fund redemptions in Canada.

Institutional Asset Management net inflows were \$0.9 billion compared with net outflows of \$7.2 billion in the prior year quarter. The increase was driven by the non-recurrence of a \$9.4 billion redemption by a large institutional client in the first quarter of 2021.

In Retirement, net inflows were \$2 billion compared with the \$2.1 billion in the prior year quarter. Overall, Global WAM's average AUMA increased by 8 percent compared with the prior year quarter, driven by market performance over the past 12 months and continued net inflows. Net fee income yield decreased by 0.5 basis point to 42.9 basis points, primarily driven by a modest decline in fee spreads. And our core EBITDA margin increased 20 basis points, driven by growth in net fee income, reflecting higher average AUMA.

Turning to Slide 20. We continued to maintain a strong balance sheet and capital position. We have \$25 billion of capital above the Supervisory Target and our LICAT ratio of 140 percent is strong. The 2 percentage point decrease compared with the fourth quarter was mainly due to the impact of higher interest rates, partially offset by capital released from the U.S. VA reinsurance transaction.

Our financial leverage ratio increased by 0.6 percentage points from the prior quarter, driven by a net issuance of securities, the impacts of higher interest rates on AFS bonds, a stronger Canadian dollar, and share buybacks, partially offset by growth in retained earnings.

We commenced share buybacks and purchased approximately 3/4 of 1 percent of our common shares in the first 2 months following the U.S. VA reinsurance transaction, demonstrating our commitment to deliver shareholder value and neutralize the impact of the transaction on core EPS.

Slide 21 shows the summary of our financial performance for the quarter. The mixed performance of our profitability and growth metrics reflects the impact of a challenging operating environment with our global strength and diversity being a notable mitigant. Our balance sheet remains strong and provides us with financial flexibility to deliver on our strategic and capital deployment priorities.

Slide 22 outlines our medium-term financial targets and recent performance. While some of these metrics are tracking below our targets this quarter, we're pleased with the performance and resilience of our business, given the temporary disruption caused by the resurgence of COVID-19 and global market volatility. We remain confident in our ability to continue to deliver on our targets over the medium-term.

Turning to Slide 23. I'm pleased to give an update on the key implications of IFRS 17 on Manulife's financial results and key performance indicators. Before I start, I want to remind you that the new accounting standard does not impact the fundamental economics of our business or our financial strength, claims paying ability or dividend capacity, though it will impact where, when, and how specific items are recognized in the financial statements.

There are a few key items that I want to walk through with you. First, a contractual service margin or CSM for short, will be established on our in-force business at transition, representing unearned profits, and will be treated as available capital under LICAT. Overall, we expect a decrease in equity of approximately 20 percent, mainly driven by the establishment of CSM at transition.

Second, as we write profitable new insurance business, our CSM balance will grow. Since CSM will amortize into earnings in the future, a growing CSM will be an important component of future earnings growth.

Third, recognition of new business gains and certain investment-related activities will be deferred under IFRS 17, and therefore, we expect a reduction in core earnings of approximately 10 percent upon adoption.

Fourth, we expect IFRS 17 to improve the stability of our earnings relative to IFRS 4.

Fifth, our capital position will remain strong in an IFRS 17 environment. And we also expect our LICAT ratio to be more stable than is currently the case under CALM and IFRS 4.

Finally, as a result of the adoption of the new standard, some of our medium-term financial and operating targets will be increased, and we're confirming the remaining targets are unchanged by IFRS 17.

Slide 24 highlights the expected changes to our medium-term financial and operating targets, where some will be increased upon transition to IFRS 17. Our core ROE target will be increased to 15 percent plus from the current 13 percent plus, driven by expected changes in core earnings and equity. And we do not expect material changes to our remittances or changes to our dividend per share or its trajectory. As a result, the target dividend payout ratio range will be updated to 35 to 45 percent from the current 30 to 40 percent.

We are confirming our remaining medium-term financial and operating targets under IFRS 17, however, given the CSM represents unearned profit and available capital under LICAT, we intend to adjust our definition of financial leverage ratio to include the CSM in the denominator. And given the CSM is an intrinsic part of the value of the business and an objective metric that illustrates the growth and future earnings generation capability of our insurance businesses, on transition we will be adding 2 new medium-term financial targets relating to the CSM, new business CSM growth of 15 percent per year and CSM balance growth of 8 to 10 percent per year.

After this call, we will release a presentation and video, which will provide additional information on the impacts of IFRS 17 adoption on our financial reporting and targets. These materials will be available on our Investor Relations website. This concludes our prepared remarks. Operator, we will now open the call to questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions). And the first question is from Meny Grauman from Scotiabank. Please go ahead.

Meny Grauman - *Scotiabank Global Banking and Markets, Research Division - MD of Financial Services Equity Research & Analyst*

Hi, good morning. You referenced unfavourable product mix in China. I'm just wondering if you could give us a little bit more detail on that. Is that COVID-related or is that something else?

Anil Wadhvani - *Manulife Financial Corporation - President & CEO, Manulife Asia*

Thanks, Meny. This is Anil Wadhvani. So if you recall, we had mentioned at our previous earnings call that we are seeing regulatory changes at an industry level that are impacting the critical illness proposition. And as a consequence of that, we saw a very different product mix year-on-year. We had a resounding first quarter 2021 in China, and on account of some of the adjustments that we have been making in response to the regulatory changes, the product mix was significantly different in quarter one of 2022.

So that effectively kind of drove the difference. I do want to kind of qualify that some of these changes, while it does kind of create a challenge for us in the short-term, from a medium to long-term perspective, that is good for the sustainable growth of our insurance business in China.

Meny Grauman - *Scotiabank Global Banking and Markets, Research Division - MD of Financial Services Equity Research & Analyst*

Thanks for that. And then just more broadly on COVID, I think, Roy, you talked in your presentation about some of the case counts coming down, especially in Hong Kong. Do you have a sense of when - I mean this is a million-dollar question of when these very restrictive measures will ease up? Is there any sense you have in terms of timing there? When we'll actually see a more open sales environment in Hong Kong especially, but more broadly as well?

Roy Gori - *Manulife Financial Corporation - President & Chief Executive Officer*

Yes. Thanks, Meny. Let me start, and I'll hand back to Anil to provide a little bit more color and flavour. The thing that I would say is that in Q1 of this year, we saw a really unprecedented resurgence of COVID in Hong Kong, but in also other markets in Asia. And it really was dramatically different to anything we saw in prior waves. And the example that I gave earlier was that of Hong Kong, where we saw a COVID case count high of 77,000 on a given day in the quarter versus the previous high of about 150 cases per day. Now the encouraging sign is that we're seeing COVID case counts reduce significantly, which is what we saw in North America, quite frankly, and in other parts of the world.

In May, for example, in Hong Kong, the case count came down to about 300, and that is certainly a big positive. So in general, we see that the situation we saw in Q1 was more temporary in nature. The case counts are certainly improving, and the containment measures are being lifted. So it's temporary in nature. We are encouraged by the movement and the momentum since the end of the first quarter, but it's not necessarily true that we'll see an immediate bounce back in one quarter.

But again, if I think about the medium-term outlook for Asia, we are just as excited today as we were, you know, last year and in prior years. The Asia opportunity is undeniable. It's incredibly significant. And quite frankly, we demonstrated the strength of our franchise through 2020 and '21, where we saw a really significant growth momentum and where we, quite frankly, gained market share versus many of our peers. But Anil, you may want to provide a little bit more flavour on what you're seeing on the ground.

Anil Wadhvani - *Manulife Financial Corporation - President & CEO, Manulife Asia*

Thanks, Roy. So Roy mentioned a couple of times that Hong Kong, obviously, was a key recipient of the unprecedented surge that we saw. And we also kind of saw some of the lingering impact of COVID in many of our Southeast Asian markets. Having said that, if you look at our earnings profile, Hong Kong did deliver a positive earnings growth despite the unprecedented challenges. So did Japan. We also saw positive earnings growth in Singapore, Philippines and Indonesia. The market that was really challenged was China for reasons that I've mentioned earlier.

And if I look at the outlook, Meny, what we are seeing is that the vaccination rates are improving. And that is kind of leading to a greater confidence on relaxation measures as well as a positive impact on customer sentiment. Having said this, I also want to point out to the fact that we have again seen some severe lockdowns in Shanghai on account of the surge that we've witnessed recently.

So -- the point being that we will, in the short-term, have to navigate these challenges, which, as Roy alluded to, are temporary in nature. But again, medium-term, the secular trends in Asia are quite undeniable, and we are very uniquely positioned on account of market-leading positions in many of our geographies to be able to address this opportunity.

Meny Grauman - *Scotiabank Global Banking and Markets, Research Division - MD of Financial Services Equity Research & Analyst*

Thank you. I'll re-queue.

Operator

Thank you. The next question is from Doug Young from Desjardins Capital Markets. Please go ahead.

Doug Young - *Desjardins Securities, Research Division - Diversified Financials and Insurance Analyst*

Good morning. Just on IFRS 17, are we to assume that you're planning on putting the interest rate volatility through the AOCI? And if that's the case, is there any logistical issues we should be considering with the choice of that option?

Phil Witherington - *Manulife Financial Corporation - Chief Financial Officer*

Thanks, Doug, for the IFRS 17 question. This is Phil. We have decided to elect the OCI option in the standard. And let me provide a little bit of context for that. One of the key changes that comes with IFRS 17 is that the direct linkage that exists between the expected return on assets and the liability discount rate, that goes away with IFRS 17, and that provides the potential for additional short-term variability arising from the impact of interest rates on both assets and liabilities.

What the OCI option allows for, and this is an option that the standard provides for, is that movements arising from interest rates, both assets and liabilities are offset within OCI. And therefore, it provides us offsetting effect of short-term variability that does arise from those movements in rates. And it provides, therefore, for more stable net income.

Now we are a global company, and we do expect a number of our global peers to take the same approach in electing the OCI option. And from a - one of the things you referenced in your question is the logistical aspects. I don't see any particular challenges from a logistical perspective, given that there will be very transparent disclosure of the movements in assets and liabilities within OCI. And so, I feel that this is certainly no less transparent, possibly even more transparent than adopting a fair value through P&L approach.

Doug Young - *Desjardins Securities, Research Division - Diversified Financials and Insurance Analyst*

Just a follow-up. I guess where I was going, I think if assets are under AOCI, and you can correct me because I'm probably or may be wrong, but you only recognize a return by selling an asset. Do I have that right? And is that the mechanics we have to think about instead of generating returns on an ongoing basis, you have to actually recognize that? Is there any issue with that?

Phil Witherington - *Manulife Financial Corporation - Chief Financial Officer*

Thanks for the follow-up, Doug. Let me clarify that. What we're talking about with the AOCI option is where we record the impact of movements in interest rates. So with this selection, our fixed income asset portfolio will be classified as fair value through OCI, which means movements in fair value of those assets will be recorded in OCI, but what stays in the both core earnings and therefore, net income is the effective yield on those assets.

And of course, we do buy to hold for the long-term, so I think that's a sensible approach for our business. And to the extent that there are realizations of gains or losses over time, they would form a component of net income as they would for a smaller AFS portfolio in the current environment.

Doug Young - *Desjardins Securities, Research Division - Diversified Financials and Insurance Analyst*

Okay. That I'll probably have to follow-up on a few things there, but the - okay, the second question and I guess, for you as well, Phil, can you update us on what you consider to be excess capital? And by that, meaning what you would be willing to use for a transaction or what you think is available to be used for stock buybacks?

Phil Witherington - *Manulife Financial Corporation - Chief Financial Officer*

Yes. Thanks for the question on capital, Doug. When I think about capital, I think there's always an element of judgment in determining what is excess and what is not. The benchmark that we use is we look at our internal operating range, which is derived from a series of stress scenarios. And above that operating range, we determine is capital that is available for use, depending upon judgments that management will make over a period of time, taking into account factors such as the external environment. And I don't, in any way, apologize for the fact that we do take the approach of managing the balance sheet conservatively.

And when I look at the amount of capital that we have in excess of the upper end of our operating range, we said about a year ago that we hold \$10 billion above the upper end of that range, and it's still above \$10 billion today. So there is financial flexibility for us to deploy capital. We have been deploying capital in the quarter as a result partly as of the completion of the U.S. variable annuity transaction.

And as I said in my remarks during the quarter, we repurchased approximately 3/4 of 1 percent of our issued shares, which is a deployment of capital in the order of \$280 million from memory. But I think that represents a really strong start to the NCIB. And of course, to remind you as well, we increased the dividend by 18 percent in the fourth quarter.

Roy Gori - *Manulife Financial Corporation - President & Chief Executive Officer*

I just want to add to Phil's comments. Sorry, Doug, I was just going to add that focusing on our financial strength, financial flexibility and our capital strength has been a really significant priority for us over the last 4, 5 years. We articulated at our Investor Day in 2018, portfolio optimization being a significant strategic priority for our franchise. We set a goal of bringing up \$5 billion worth of capital over 5 years. We achieved that goal 3 years ahead of schedule. In fact, we've actually exceeded \$6 billion. At the same time, our leverage has come down from circa 30 percent at that time to about 25, 26 percent.

So being in a strong financial position, obviously was a very important part of navigating the pandemic. When we entered the pandemic there was a lot of uncertainty and having that financial strength or the source of value, and we feel really good about the fact that we have \$10 billion in excess of our upper operating range which provides us the flexibility to do buybacks or inorganic transactions, but also gives us the comfort in navigating challenging environments. Thought that context might be helpful as well.

Phil Witherington - *Manulife Financial Corporation - Chief Financial Officer*

And Doug, this is Phil again. I should be careful at my age about recalling numbers from memory, I said \$280 million of capital through the NCIB in the quarter. It was \$380 million of capital deployed.

Doug Young - *Desjardins Securities, Research Division - Diversified Financials and Insurance Analyst*

Okay. Thank you.

Operator

Thank you. The next question is from Tom MacKinnon from BMO Capital Markets. Please go ahead.

Tom MacKinnon - *BMO Capital Markets Equity Research - MD & Analyst*

Yes, good morning and thanks for taking my question. Just with respect to the impact of new business, particularly in Asia, if I look at sales, they were actually up quarter-over-quarter nicely, but impact of new business was down. And if I look at - the impact of new business was like down 30

percent quarter-over-quarter and if I look year-over-year, the sales in Asia may have been down -- insurance sales may have been down 18 percent, but the impact of new business was down 50 percent.

So, you know, obviously, this kind of shows up in the NBV margin, but maybe you can tell us as to is what we saw in the first quarter just strictly an anomaly? Is it a change in mix? Is it - how should we be looking at this going forward just in light of continued lockdowns? And is the mix of business that you're selling now kind of indicative of the mix of business you're going to continue to sell? And then I have a follow-up. Thanks.

Anil Wadhvani - *Manulife Financial Corporation - President & CEO, Manulife Asia*

Thanks, Tom. So there were 3 factors that impacted new business gain, as you rightly pointed out. So one, as we mentioned earlier, the COVID impact in Hong Kong was quite significant, and that had an impact on volumes as well as new business gain in Hong Kong. I do want to underscore the point that on account of the strong in-force management, Hong Kong was able to deliver a 1 percent earnings growth despite some unprecedented challenges.

The second factor was Japan. So Japan, as we have relayed on previous earnings calls as well, we have been focusing on a much more diversified set of product mix as oppose to focusing primarily on COLI. And that, in combination with the focus we have employed on in-force as well as expense efficiency actually has resulted in Japan growing its core earnings throughout 2021, but also in the first quarter of '22.

And last, but certainly not the least, which is what I alluded to earlier, was China. And China had a couple of factors there, Tom. One, China had a resounding quarter one in 2021 on account of some of the regulatory changes that had impacted the product mix at an industry level. We have seen a very different product mix in quarter one of 2022. So that obviously had a knock-on impact on volumes, but certainly had a knock-on impact on new business gain as well.

The second is that quarter one has an element of seasonality, where China has an oversized contribution on account of the door opening in quarter one. So that as we kind of get into quarter two and beyond, will start to normalize where the contribution of China is going to be much lower in terms of sales as compared to what we witnessed in quarter one. So those were the factors that, in effect, kind of led to the decline of new business gain versus the decline in sales.

Roy Gori - *Manulife Financial Corporation - President & Chief Executive Officer*

Tom, I just want to reinforce one point that Anil made earlier, and that is that Q1 of '21 was a very strong quarter for us for Asia, in particular. New business value in that quarter was up 39 percent on the prior year, and earnings were up 21 percent. So the benchmark of last year is a very high benchmark. Now that's not to discount the challenges, but it is a high benchmark from a comparative perspective.

The other thing that I'd sort of leave in your mind is that our international business currently gets reported under the U.S. segment. Asia figures significantly in the international segment. And in Q1 of this year, new business value growth of international was 25 percent, which we see as, again, another encouraging sign as to the outlook for the coming quarters.

Tom MacKinnon - *BMO Capital Markets Equity Research - MD & Analyst*

Okay. So I guess it kind of sounds as if China becomes a little less contributor to this and Hong Kong comes more, then we would probably see the new business gains as a percentage of insurance sales go up in the future? Would - is that a safe way of trying to characterize it?

Anil Wadhvani - *Manulife Financial Corporation - President & CEO, Manulife Asia*

That's correct, Tom. And you would see that even in some of the past years with China. I do want to qualify that kind of combined with some of the product mix shifts that have happened. So you need to take both those factors into account.

Tom MacKinnon - *BMO Capital Markets Equity Research - MD & Analyst*

Okay, thanks. And then the second question is just with respect to long-term care experience, I think it continues to be favourable. I think when it was favourable through COVID, I got the impression that you weren't necessarily changing your reserving outlook. In fact, I think you were adding some of that excess into reserves, thinking things were going to mean revert. Any update on the thinking there?

Steve Finch - *Manulife Financial Corporation - Chief Actuary*

Thanks, Tom, it's Steve here. And yes, as Phil pointed out in his remarks, we've continued to see very good diversification between mortality and longevity, particularly in the U.S. So what we've seen and we saw this quarter were continued offsets. So we saw gains in long-term care, primarily from elevated mortality that were only partially offset by elevated mortality in the U.S. Life business.

In terms of the reserving that you were referring to, when the pandemic started, we saw a hesitancy for care. So people - the incidence rates dropped as well as some people that were receiving care stopped receiving care. And we set up reserves for that situation because we believe and continue to believe that people need the care and they will seek care when it's viewed as safe to do so. We continue to hold a sizable IBNR reserve for that event at approximately USD 130 million. So the thinking hasn't changed there. We do expect that people will seek the care, but we're well provided for that.

Tom MacKinnon - *BMO Capital Markets Equity Research - MD & Analyst*

And just on that, can you comment on any kind of inflation impact as it relates to long-term care? The nature of your product, how that might - I mean everybody is getting good rate increases with respect to long-term care, but some of the thinking there. Thanks.

Steve Finch - *Manulife Financial Corporation - Chief Actuary*

Yes. Sure, Tom. And I'd start by saying, overall, in terms of inflation, Manulife is well positioned in the event that there continues to be higher inflation. We've got some pluses and some minuses. On the liability side, you mention long-term care where there is, you know, cost of care increases that will come through in terms of higher claims costs. But there are mitigants that we see in that line of business. For instance, during the pandemic, we've seen - and actually leading up to the pandemic as well, there's been a trend towards home care away from particularly nursing home care, and home care is materially less expensive than nursing home care. So we've seen some offsetting trends in the business that we will continue to watch out for. As you note, the successful rerate program, if there were higher inflation, the premium increases that we would seek would take that into account as well, so there's mitigants.

And the last thing I'd point out is on the asset side. In the period - in the situation of higher inflation, our ALDA portfolio, a significant part of the portfolio, close to 75 percent is in real assets. And we would expect higher nominal yields in an inflationary environment over the medium-term. So conclude with, we're well positioned as a company overall in an inflationary environment.

Tom MacKinnon - *BMO Capital Markets Equity Research - MD & Analyst*

Okay, thanks for that.

Operator

Thank you. The next question is from David Motemaden from Evercore ISI. Please go ahead.

David Motemaden - *Evercore ISI Institutional Equities, Research Division - MD & Fundamental Research Analyst*

Hi, thanks. Good morning. Just a follow-up question on Hong Kong. Roy, I think you made some comments on promising signs of consumer demand returning. And I know that they just relaxed some restrictions last week. But outside of case counts going down, do you have any - could you elaborate on some of the metrics that you have that give some evidence that consumer demand is returning?

Roy Gori - *Manulife Financial Corporation - President & Chief Executive Officer*

Yes. Thanks, David. Again, I'll start and I'll hand to Anil, who will have a much better feel for what's happening on the ground. But at the highest level, actually, one of the biggest trends that we're seeing globally is that the pandemic is really forcing consumers and the general population to appreciate the importance of insurance. So we're seeing folks really look at how well covered they are and whether they actually need to increase their coverage or not. And quite frankly, that was certainly a driving force in why we saw our new business value in Canada increase by 30 percent in the quarter and for the U.S. by 56 percent. So as a global phenomenon, I think we're just seeing the pandemic just highlight the importance of the products that we offer and this is really driving a stimulation from a needs perspective.

Obviously, the temporary headwind is just the COVID case counts and the containment measures. And it's not just that the case counts are high. Obviously, when the situation is challenging on the ground, it translates into the customer sentiment and whether people are actually thinking about going out and buying products or not, but there is a correlation. And again, we see that as more temporary in nature. But demand is really very strong across the board where we see people -- where the general population moved back to more normalized methods of actually managing the crisis. It's true not just in North America, it's definitely true in Asia as well, and again, in Hong Kong, we're seeing that, but Anil, you might be able to provide a bit more of a flavour there.

Anil Wadhvani - *Manulife Financial Corporation - President & CEO, Manulife Asia*

Thanks, Roy, and thanks, David. So in Hong Kong, what we are witnessing is obviously, the relaxation measures on account of the higher vaccination rates that you alluded to, is giving more opportunities for our distributor partners to connect with customers. And as you can imagine, once these relaxation measures come into force, there's obviously a knock-on impact on the customer sentiment as well. So that should all go well. Now you're right that this is more a recent phenomena. It only happened on April 21st. So we are obviously kind of watching that closely. But a combination of factors and just kind of witnessing the activity on the ground gives us to believe that there will be more opportunities for customer and distributor interaction. I also want to point out a couple of other factors. We had a very strong quarter and Paul could probably add some comments on MPF as well.

We saw record flows on our retirement business as well as continue to kind of consolidate our market position on the MPF side. We continue to grow our agent headcount, as you would have noticed. Our agent head count in Hong Kong was up 7 percent. And again, we have a quality franchise on the ground and have been investing in improving our digital capabilities, expanding our distribution, obviously investing in our talent. And that has resulted into the resiliency that Hong Kong has delivered with 19 consecutive quarters, including quarter one '22 of year-on-year earnings growth. So we feel pretty optimistic as we kind of go along. And as I said, the relaxation measures is a positive indication in that direction. Paul, any comments that you would like to add?

Paul Lorentz - *Manulife Financial Corporation - President & CEO, Manulife Investment Management*

No, I think you covered it, Anil. We've just seen continued growth in the Hong Kong retirement business and particularly in a year with difficult markets, it's really the best quarter ever in terms of flows. So I think it just speaks to consumer sentiment and the importance of what we're offering.

Anil Wadhvani - *Manulife Financial Corporation - President & CEO, Manulife Asia*

Yes. I just wanted to add one more point, David, is that we are also kind of seeing some great demand on our critical illness and medical products. And that should not surprise us given what we have witnessed on account of COVID, that has simply gone and cemented the need for health and protection in the minds of our clients.

David Motemaden - *Evercore ISI Institutional Equities, Research Division - MD & Fundamental Research Analyst*

Got it. And as a follow-up there -- and thanks for that color, it was really helpful - just in terms of the impact of new business in Asia, sort of the cadence of that as we head forward. Just anything just sort of how you guys are thinking about it that you can help us as we think about the earnings power of the company or the segment in Asia, specifically going forward.

Anil Wadhvani - *Manulife Financial Corporation - President & CEO, Manulife Asia*

Yes. Again, as I said, David, earlier that the fundamentals of our business haven't changed. I think what has really been the constraining factor is that once the containment measures come into force, firstly, obviously, it has an impact on customer sentiment, as you would imagine, but also it does kind of restrict the movement both of our customers and distributor partners. So that's really been the constraining factor. The fundamentals of our business and the way we are positioned, the quality of our franchise on the ground has only got better. And that's been illustrated as I said, by the market share gains that we've now got for consecutive years in Hong Kong as well as more broadly across Asia.

So that is really the limiting factor for us that we will have to navigate in the short term. And it's really hard for us to predict that, as you can imagine, but as I said, we feel, given our track record of execution and the quality franchise that we have, that we are in a very good position to be able to address the customer demand.

Phil Witherington - *Manulife Financial Corporation - Chief Financial Officer*

And this is Phil, David, if I could just add one thing. I'd just add one thing to that, David. We haven't in the past provided guidance, medium-term guidance, specifically on new business. And with the transition to IFRS 17, one of the things you may have noticed is that we've added guidance with respect to generation of new business CSM that we expect to grow over the medium-term at 15 percent. So we hope that, that's something that you and the rest of the analyst community will find helpful in terms of providing guidance on where we expect new business to be in the future.

David Motemaden - *Evercore ISI Institutional Equities, Research Division - MD & Fundamental Research Analyst*

Yes. No, that is helpful sort of like a value of in-force or it's how I've been thinking about the CSM. And then maybe if I can just sneak one more in for Phil. I know you guys - when interest rates were going down, you put some capital into Hong Kong or to help support the Hong Kong business. Obviously, rates have moved up pretty significantly. Any plans to remit that out, the capital that you put in?

Phil Witherington - *Manulife Financial Corporation - Chief Financial Officer*

Thanks, David, for the question. We are expecting remittances from Hong Kong in this calendar year. And you may recall, I think I provided an update last quarter and said remittances in 2021 from Asia were in the order of \$900 million. A good chunk of that was capital from Hong Kong as well. So when I look at the outlook for remittances for the remainder of this year, I do see it as being a strong remittance year. And I think that does reflect the favourable interest rate environment.

David Motemaden - *Evercore ISI Institutional Equities, Research Division - MD & Fundamental Research Analyst*

Thank you.

Operator

Thank you. The next question is from Paul Holden from CIBC. Please go ahead.

Paul Holden - *CIBC Capital Markets, Research Division - Executive Director of Institutional Equity Research*

Thank you. Good morning. So first off, thanks for the additional disclosure on IFRS 17, helpful, and I'd say well putting those numbers out at this point in time. My question is, to what extent will the level of interest rates influence that book value, estimated book value impact of 20 percent? So you sort of ran through some of the mechanics of how it works, but I guess on a net basis, I'm just trying to understand what kind of influence we might see from moves in bond yields between now and the implementation of IFRS 17?

Phil Witherington - *Manulife Financial Corporation - Chief Financial Officer*

Thanks, Paul, for the question. This is Phil. I'll make a start, and Steve Finch may want to add as well, given the nature of the question. But one thing we expect as we transition to an IFRS 17 environment is that our net income as well as our capital position, our LICAT ratio will be more stable. We're seeing from all of the work we've done so far, less sensitivity to changes in interest rates on a net income basis and LICAT capital ratio basis than we see in the current environment. So we do certainly consider that element as well as many other elements of IFRS 17 as a significant positive. And it's not only the impact of interest rates that is creating a stabilizing force under IFRS 17 as well. Other factors such as the new business accounting, the investment accounting, whereby we don't capitalize future investment returns upfront. I think that there are also factors that provides for a greater stability of both core earnings and net income into the future. Steve, I didn't know whether you wanted to comment further, particularly on interest rates.

Steve Finch - *Manulife Financial Corporation - Chief Actuary*

Yes. Thanks, Phil. Phil was commenting on what we see as a positive in terms of reduced sensitivity on our LICAT ratio from interest rates under IFRS 17 as well as our book value, but also to your question, we will establish an opening balance sheet at the start of 2022. So we're already past that point, obviously, so we know what interest rates are. So we're factoring that in when we're talking about the impact to book value or equity that Phil covered. Thank you.

Paul Holden - *CIBC Capital Markets, Research Division - Executive Director of Institutional Equity Research*

So, sorry, I want to follow up on that one, so I understand. So what you've done is you mark-to-market the book value impact for current rates. So I'm hoping to get any kind of characterization around how sensitive that estimate is to potential changes in rates between now and then because when the bond market is moving a lot, just day to day, but, you know - and you don't have to quantify it for us because it's probably too early to do that, but any kind of sense of magnitude, I think, would be welcome.

Steve Finch - *Manulife Financial Corporation - Chief Actuary*

Sure. I'll start. And so if you look at - I'll start with our LICAT ratio. If you look at the LICAT ratio that we disclosed the sensitivity under the current regime, we have, as we said at the end of Q1, a 50 basis point increase in interest rates would result in a LICAT ratio declining by 3 points. We expect that to reduce materially under IFRS 17. So that's the point about reduced sensitivity of the IFRS 17 regime with respect to interest rates.

Paul Holden - CIBC Capital Markets, Research Division - Executive Director of Institutional Equity Research

Okay, and is there any reach where I can use on that sensitivity to how book value is impacted?

Steve Finch - Manulife Financial Corporation - Chief Actuary

I would - directionally the same. Phil, I don't know if you have additional comments there.

Phil Witherington - Manulife Financial Corporation - Chief Financial Officer

I think the only thing I would emphasize is that through the information we released yesterday and talked about today, clearly, we show an expected impact on transition of - at 20 percent, which will help inform, I think, some of the book value calculations. But a couple of other things to add. When we look at future sensitivity to interest rates, Steve gave the LICAT example. We would expect that to be much closer to neutral in the IFRS 17 environment. So I think that's one factor.

But as well, I think the CSM is very important. The CSM represents future earnings that will emerge into income. And that really is in economic terms an asset, that because it's being smoothed into earnings is accounted for as a liability, and therefore, consistent with the consultation that OSFI launched in - on the LICAT 2023 guideline, in June 2021 - one element that, that consultation included was a clear statement that the contractual service margin would be an add-back to available capital. And therefore, we think it's a very important measure, not only of future earnings but also of financial strength. And I think that's relevant to book value considerations as well.

Steve Finch - Manulife Financial Corporation - Chief Actuary

And just one additional point. Just in case I wasn't clear earlier, we are effectively past the transition date because the transition is for 2022 at the start of the year. So we passed the date of the opening balance sheet. So that's why we're saying the interest rates as of the opening balance sheet date are already known because they're in the past.

Paul Holden - CIBC Capital Markets, Research Division - Executive Director of Institutional Equity Research

Okay. Second question is related to, excuse me, related to investment-related experience, obviously a big positive in Q1. As I look forward, you know, again, asset values are repricing pretty quickly here and most of them down. Just kind of wondering if you can help us walk through the potential puts and takes sort of maybe what happened, what drove the gains in Q1, what you've seen post-quarter and how that might influence investment experience going forward.

Scott Hartz - Manulife Financial Corporation - Chief Investment Officer

Sure. Hey, Paul, it's Scott. Thank you for the question. And yes, thanks for noticing the gains we saw on the ALDA portfolio in the first quarter, \$283 million. And it was pretty broad-based, I would say, the biggest drivers were our private equity and real estate, but really 5 of the 6, ALDA categories had returns above their long-term expectations. Obviously, we've seen public markets drop a bit in the first quarter and more so far in the second quarter. And that ultimately, if it continues, will weigh on private equity, which is the most correlated to that. But if you look at the first quarter, public markets in the U.S. were down about 5 percent and the read we're getting on private equity is it has been up like 2 to 3 percent. So while there is some correlation, they certainly don't move in lockstep, but if public markets drop enough, it will definitely impact private equity valuations.

For our portfolio, just remind you that we tend to get the data about a quarter in arrears for most of the private equity portfolio, and for the first quarter, it's even worse than that. We don't get the year-end statements for a lot of the funds to get in, so we're, in many cases, lag 2 quarters. So the fourth quarter was a very good quarter for private equity. So that's going to provide a bit of a tailwind for the rest of the year, which will mitigate a little bit the headwind we will likely see if public equity markets, you know, continue to go down or stay down as much as they have been in the

second quarter. But beyond that, private equity represents about 25 percent of our ALDA portfolio. The other 75 percent as referenced earlier by Steve, is in real assets. It's in real estate, timber, agriculture, oil and gas. And what's driving down the public equity markets is concerns about higher inflation, higher interest rates and higher inflation will definitely be a positive for 3/4 of the portfolio. So we're feeling pretty good about expectations for returns on the overall ALDA portfolio for the balance of the year.

Paul Holden - *CIBC Capital Markets, Research Division - Executive Director of Institutional Equity Research*

That's great. Thank you. Helpful.

Operator

Thank you. The next question is from Gabriel Dechaine from National Bank Financial. Please go ahead.

Gabriel Dechaine - *National Bank Financial, Research Division - Analyst*

Good morning. You might want to consider limiting questions here because we're going over an hour on each of these calls for 2 years now. So anyway, question - I'll just ask you the buyback question. Market is very volatile and just wondering what - your April filings didn't indicate that you bought back any stock or very little that is. Just wondering what your view on buybacks are in the current environment.

Phil Witherington - *Manulife Financial Corporation - Chief Financial Officer*

Hey, Gabriel, it's Phil. So when we completed the - in fact, when we announced the U.S. VA transaction, we made our intention very clear there that we would repurchase 3 percent of our issued stock in order to neutralize the impact of the transaction. That remains our objective. We have clearly got off to a great start with the three-quarters of 1 percent that's been purchased in the first couple of months of the program. I can't really provide guidance on how buybacks will continue into the future, but there's clearly more for us to do in order to get to that 3 percent, and we remain committed to doing at least that by the end of the year, such that as we get into 2023, the impact of the lost earnings from the transaction - lost earnings from the block arising from the transaction will have a neutral impact on 2023 EPS and beyond.

Gabriel Dechaine - *National Bank Financial, Research Division - Analyst*

Perfect, thanks.

Operator

Thank you. The next question is from Darko Mihelic from RBC Capital Markets. Please go ahead.

Darko Mihelic - *RBC Capital Markets, Research Division - MD & Equity Analyst*

Hi, thank you. Good morning. I will try and make it brief as well. First question relates to inflation, but on a different level. We are seeing some Canadian banks suggest that they're going to pay their employees more. You know, a lot of your business is in Canada and U.S. with a lot of inflation, so Phil, how does this impact your expense efficiency? And then secondarily, how have you thought about your expense program under IFRS 17?

Phil Witherington - *Manulife Financial Corporation - Chief Financial Officer*

Great questions. Thank you, Darko, and thanks in particular for asking about expenses. Expenses does remain one of our highest strategic priorities. It's 1 of the 5 that we've laid out.

(Technical Difficulties]

Hung Ko - *Manulife Financial Corporation - VP, Group Investor Relations*

Apologies, I think we have lost connection with Phil. I think we will come back to that question, Darko. Apologies, maybe if there's another one that we can ask and have another speaker respond to that first.

Darko Mihelic - *RBC Capital Markets, Research Division - MD & Equity Analyst*

Sure. I have a question for Anil as well in Asia. And I specifically wanted to get back to the question that Tom had asked about VNB margin. One of your main competitors in Asia suggested that outside of China and Hong Kong, that their VNB is actually higher than pre-pandemic levels. I didn't sense that, that was the case for you guys. You guys only really highlighted in Hong Kong. So can you talk to maybe some of the other places, Indonesia, Malaysia, Vietnam, you name it, are you, in fact, losing share out there? And why would you not be in a position to have higher VNB versus pre-pandemic levels?

Anil Wadhvani - *Manulife Financial Corporation - President & CEO, Manulife Asia*

Thanks for the question. So our business, in fact, through the pandemic has been quite resilient. And I did mention erstwhile that in many of our key geographies, we've actually kind of gained market share despite the onset of pandemic. And that's something on account of a few factors. We've expanded our distribution, our digital capabilities (inaudible) that have followed through with a strong execution culture, so we have kind of seen market share gains in (inaudible). In quarter one 2022, we obviously had an unprecedented impact of the resurgence. And I would reckon if you look at our results in Hong Kong or otherwise, you know, the results continue to be quite resilient. The lingering impact that we saw in Southeast Asia, to my mind, we've already kind of seen that subside.

And with the vaccination rates going up, as well as the containment measures kind of coming down, we believe that we are very well positioned to be able to kind of address that. You mentioned Vietnam. I do want to kind of emphasize that in quarter one, we were able to retain our market-leading position in Vietnam. We have almost 60,000 agents, 3 bank partners. So we are very well positioned to be able to kind of address these opportunities. You will probably see some quarter-on-quarter variation on account of volume and product mix. But again, given the quality of our franchise and our market-leading position, we feel very confident to be able to address the Asia opportunity.

Darko Mihelic - *RBC Capital Markets, Research Division - MD & Equity Analyst*

Great. Thank you. And Anil, maybe just sticking with you, I'm not sure if Phil is back. When you guys mention IFRS 17, and you say core earnings are expected to decline by 10 percent. My suspicion is on a segmented basis that Asia would drop more. Can you give us any insight?

Anil Wadhvani - *Manulife Financial Corporation - President & CEO, Manulife Asia*

Yes. I think Phil probably would be the best to kind of respond to that. But the only thing I would kind of leave with you is that the fundamentals of our business and the way we would conduct our business doesn't change because of an accounting methodology change. So we believe that, yes, while the new business gains will now be recognized as part of the CSM, the drivers as well as the growth opportunity in Asia as well as a strategy kind of remains kind of pretty intact. But I'll kind of turn it to maybe Steve or maybe to Phil if they have any additional commentary on IFRS 17.

Hung Ko - *Manulife Financial Corporation - VP, Group Investor Relations*

Thank you, and I think we have Phil back on, so I will pass it to Phil.

Phil Witherington - *Manulife Financial Corporation - Chief Financial Officer*

I'm back on. I apologize for the slight technical difficulty we had there, but we're back, and I'll finish off on the new business question. And as you know, Darko, Asia is one of our key growth opportunities and therefore, is a key driver of the new business value that's generated in the group. And for that reason, of course, when we transition to IFRS 17, we would expect a notable impact of the reclassification of new business or the deferral of new business gains as CSM to be visible and the transition impact for our Asia segment. We're not providing segmental level guidance at this point, that clearly to come in as we approach in the months approaching transition.

However, what I do want to add is that an important strategic target that we laid out at Investor Day is that we see that our Asia business will represent 50 percent of our core earnings, and that's our Asia segment and our Global WAM Asia business, 50 percent of our core earnings by 2025. IFRS 17 doesn't change our strategic target there, so I think that helps put into context the extent of the impact that the IFRS 17 transition might have.

Now getting back to your question before I lost connectivity, your question on expenses. I think everything that we've seen in the higher inflationary environment does validate the course of action we had taken. To date, the focus on expense efficiency, including automation and digitization is paying off. In the first quarter, despite a period of higher inflation, we have reported flat core expenses and flat total expenses as well, so I think that validates the approach. It is paying off. As I look forward, I think there are clearly inflationary headwinds, and so I would expect expenses to be higher than neutral and higher than we've seen in the past couple of years. But I also think our expense base will be more resilient than would otherwise be the case, and I suppose the peer group as a consequence of the actions that we've already taken. When I think about the future of the expense program, there'll be an even bigger focus on digitization and automation, which, in many ways, provides some level of greater resilience to inflation.

Darko Mihelic - *RBC Capital Markets, Research Division - MD & Equity Analyst*

Thanks very much.

Operator

Thank you. The next question is from Mario Mendonca from TD Securities. Please go ahead.

Mario Mendonca - *TD Securities Equity Research - MD & Research Analyst*

Good morning. I have a couple of questions, so I'd be happy with brief responses if it's appropriate. Expenses obviously, are going to be higher and expenses are a very important assumption in all reserves, not just long-term care, but every reserve. So as we approach the end of the year, and perhaps this is for Steve, when you get to Q3, I would imagine that one of the big, big assumption reviews you're going to need to do is on expenses. As you sit there today, could this be a large expense - a large charge in Q3 to strengthen expense assumptions?

Steve Finch - *Manulife Financial Corporation - Chief Actuary*

Thanks, Mario. With respect to the basis change, we did do a fulsome review of expenses last year and updated those assumptions that -- you know, what I could tell you about how I think about expenses and the reserves is it's a long-term assumption. So, we're seeing some higher inflation now. Phil covered, what we're seeing with respect to, you know, our expense program, our very strong continued focus there. So I think it's - what I

would tell you is it's premature for me to conclude on very long-term trends here. It's something that we'll continue to watch really closely. I talked earlier about some of the offsets that we might see on the asset side, but, you know, overall, I think with respect to the impact of inflation overall, Manulife is well positioned.

Mario Mendonca - *TD Securities Equity Research - MD & Research Analyst*

Now every company, of course, uses long-term averages. What - over what period do you look at inflation assumptions? Is it like a 5-year, 10-year? Do you look at the last 5 years, the last 10 years? How do you do that?

Steve Finch - *Manulife Financial Corporation - Chief Actuary*

So when we're looking at things like interest rates, long-term interest rate assumptions and long-term inflationary trends, we look over a longer period than that, but we do place additional weight on more recent periods. And we also factor in what the outlook is. You know, I think it's a volatile environment, and I would - with the actions that the Fed is taking and so on, I don't think we would conclude yet that inflation is higher for a long period of time. In fact, some are calling for inflation to have peaked and coming back down. So we do take the long-term view.

Mario Mendonca - *TD Securities Equity Research - MD & Research Analyst*

Okay. Phil, you said that given the way you're going to account the election you made on liabilities and assets going through OCI, that is the fixed income assets, and you said the effective yield would, of course, still be reported in earnings. That makes sense. But the value of owning these assets is more than just the effective yield. There's also the expected capital gains on those assets. So number one, am I right in saying that net income like core earnings will include some estimate of the expected mark of the expected appreciation of the assets? And number two, if I've got that right, what sort of expected return will you use for the purposes of core earnings?

Phil Witherington - *Manulife Financial Corporation - Chief Financial Officer*

Great, Mario. Thank you for the question. So the first answer is no. We're not taking into account any expected capital gains on our fixed income portfolio in our expected definition of core earnings. It is an effective yield approach. We invest in bonds with the expectation we typically hold them to maturity. There is inherently some trading and to the extent there is some turnover of the portfolio, that will show through as realized gains and losses in net income over time. However, the - there is another element, which is the rest of the portfolio, the non-fixed income portfolio, largely ALDA, that will be accounted for on a fair value through P&L approach under IFRS 17 and our core earnings definition will include the expected long-term rate of return. And to your question, how do we determine that? We're making no changes to our expected long-term rate of return for our non-fixed income assets. It will be the same assumptions that we currently apply under CALM.

One other point that I should also highlight on the topic of the fixed income portfolio that will be fair value through - sorry, fair value through OCI effective interest yield through core earnings. We will also record within core earnings the expected credit loss on those assets, which is an approach that is consistent with other global financial institutions that already adopted IFRS 9.

Mario Mendonca - *TD Securities Equity Research - MD & Research Analyst*

Yes, that's all very clear, and I understand that. Now real quickly on long-term care. Mortality is good. You're holding \$130 million of IBNR, that's good as well. What - are there any underlying negative trends right now in long-term care, specifically around severity that are being somewhat masked by the positive we're seeing on mortality?

Steve Finch - *Manulife Financial Corporation - Chief Actuary*

Thanks, Mario. I talked a little bit earlier about some of the trends that we're seeing and continue to see through the pandemic, which is hesitancy for care in all settings, which we expect will revert. We have also seen more recently that while there is sort of inflation in unit costs, the actual amount of service being provided is less than pre-pandemic. So that could be due to staffing shortages, et cetera. And I mentioned earlier also the trend that's continuing to more home care, which would be a positive. So there is - there are a number of things that we're seeing in the portfolio, but it's too early to say which of these, if any, are longer-term trends. You know, remind you that we've consistently updated the assumptions and when we updated the assumptions in 2019, we saw experience that was consistent with those assumptions. So we are, you know, we'll be continuing to track this closely. Certainly expect that the diversification on mortality versus longevity in our portfolio more broadly will continue.

Mario Mendonca - *TD Securities Equity Research - MD & Research Analyst*

Okay. And then just finally, under the sort of caption of where there's smoke, there's fire. Let me ask this. On one of the calls, one of the U.S. insurance calls, several folks were asking questions about a long-term care transaction. Now clearly, they weren't asking about Manulife, they're asking that of the other U.S. insurance company. And it got just a ton of attention that it looks like long-term care might be moving into that transactable bucket. And it was all done in the context of higher interest rates. Is that plausible now? Or is that still a pipe dream that there could be something happening in long-term care for any of these companies, not just Manulife, but any U.S. company.

Naveed Irshad - *Manulife Financial Corporation - Global Head of Inforce Management*

Hey Mario, it's Naveed here. I would say that all things being considered, certainly higher interest rates will create some tailwind on this. But what we're seeing is that bid-ask spreads continue to be quite wide on LTC blocks. And we are connected to the market on a regular basis to understand the potential opportunities, and we look quite granularly at different blocks and sub-blocks to assess transactability. I think the key thing here is as the experience accumulates, counterparties will gain confidence in the assumptions, which in turn informs the valuation of the blocks. That's what we saw in the VA side. We saw that as the experience emerged, the bid-ask spreads narrowed. We see signs of that on long-term care, but I think there's still quite a ways to go for those bid-ask spreads to come in to a point where a transaction would make sense for our shareholders.

Mario Mendonca - *TD Securities Equity Research - MD & Research Analyst*

Thank you for your candor. I'm all set.

Operator

Thank you. And the last question is from Lemar Persaud from Cormark Securities. Please go ahead.

Lemar Persaud - *Cormark Securities - Equity Research Analyst*

Thanks for taking my question. I'll be really quick. I just want to come back to a comment that Phil offered in response to one of the earlier questions and looking at the target for new business CSM growth. So just understanding that your IFRS 17 target for new business CSM growth at 15 percent, it's a medium-term target. Just wondering, would some of the softness in Asia suggest that, that 50 percent target is not likely to be achieved in 2023, just given, you know, the reliance on Asia for new business gains?

Phil Witherington - *Manulife Financial Corporation - Chief Financial Officer*

Lemar, this is Phil, and thanks for picking up on that new element of our guidance. I think to Anil's and Roy's earlier comments, many of the headwinds we're currently seeing in Asia do relate to the impact of the resurgence of COVID and the pandemic. And the experience we've had in North America is that the bounce back, it can be very quick once the waves of the pandemic pass. And I think as we've seen with the fifth wave of the pandemic,

I think Hong Kong is a good example. It's very intense, but it's also reasonably short and getting back to 300 cases per day in Hong Kong means that I think that is a good reason to be optimistic.

Anil talked about the drivers of demand re-emerging, but we're also seeing that in other geographies as well. And I think the fact that Mainland Chinese customer business is also being seen through our Macau business as well, I think that provides a good illustration that the demand is certainly there. It's a case of really accessing it as and when the borders fully re-open between Mainland China and Hong Kong. I would also highlight that 15 percent growth in CSM, new business CSM, is not just Asia. We expect the U.S. and Canada to be important contributors to that. And as Roy mentioned earlier, within our U.S. segment is our international business. And that's something that we have identified as a high opportunity growth business and something that will be accretive to our targets.

Roy Gori - *Manulife Financial Corporation - President & Chief Executive Officer*

Lemar, I would just add in closing that one of the positive developments with IFRS 17 that we're quite excited about is the focus on CSM and CSM growth. We think that this will be a critical way to assess insurance companies going forward, and that's why we've introduced the 2 new medium-term targets: the CSM balance growth of 8 to 10 percent and the new business CSM growth of 15 percent, as you articulated. We think that, that focus for a company like ours that is fast-growing and has demonstrated the diversity to grow through challenging times that, that will shine, I think, quite a positive light on the growth outlook and the opportunity. And we feel, again, that the temporary challenges that we're seeing, particularly in Asia, that they will be just temporary and that we'll get back on track in due course.

Lemar Persaud - *Cormark Securities - Equity Research Analyst*

Great, thanks for that.

Operator

Thank you. There are no further questions registered at this time. I'd like to turn the meeting back over to Mr. Ko.

Hung Ko - *Manulife Financial Corporation - VP, Group Investor Relations*

Thank you, operator. We will be available after the call if there are any follow-up questions. Have a good day, everybody.

Operator

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

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