

## Recommendation

Buy

## Target Price

\$46.00

## Risk

Low

## Average Daily Volume

150 day: 2,726,000

## Quick Facts

**Recent Price** C\$41.60  
**52 Week Range** \$36.37-\$44.23  
**Shares O/S** 1,502 million  
**Market Cap.** \$63 billion  
**Symbol** MFC:TSX  
**Year End** December 31

	<u>EPS</u>	<u>Multiple</u>
<b>2006a</b>	\$2.51	16.6x
<b>2007e</b>	\$2.80	14.9x
<b>2008e</b>	\$3.08	13.5x
<b>Book Value</b>	\$15.48	2.7x

	<u>Rate</u>	<u>Yield</u>
<b>Dividend</b>	\$0.96	2.3%

## MANULIFE FINANCIAL CORP.



Data Source: BigCharts.com

*Manulife Financial Corporation is a financial services company. Manulife Financial offers clients a diverse range of financial protection products and wealth management services.*

### CONCLUSION: BUY – 12 MONTH TARGET INCREASED TO \$46.00

Overall a good quarter, albeit, about \$0.01 below our estimate and consensus. MFC reported EPS (fd) in Q3/07 of \$0.70 per share up 13% Y/Y. On a constant currency basis EPS increased by 18%. The earnings were driven by positive equity markets and real estate appraisal gains offset in part by the negative impact of lower long term interest rates on the US Protection group and a write-down of BCE bonds. Reported ROE was 18.9% up from 16.6% in Q3/06. Dividend increased by 9% to \$0.96 annually from \$0.84.

Our 2007 and 2008 EPS forecasts have been lowered to \$2.80 and \$3.08 from \$2.83 from \$3.14 respectively. We expect that the stronger \$CDN relative to the \$US will be a larger negative for the balance of 2007 and 2008, however MFC's more aggressive share buy back program should be a partial offset. MFC is focused on increasing its dividend and maintaining a significant share repurchase program. Excess capital is still over \$3 billion. We expect the dividend could be increased further over the next 12 to 18 months to the \$1.10 per share level for an increase of 15%.

We continue to recommend MFC as a BUY based on (1) earnings are extremely well diversified globally (50% U.S.) and well positioned in Asia, (2) we are very impressed with the growth in wealth management and believe MFC is pushing more in this direction (3) Canada remains solid, (4) excess capital in excess of \$3 billion should support acquisitions, share repurchases and dividend increases and (5) an aggressive share buy back program. Total 12-month expected return is 13.0%.

### Valuation

We believe MFC has very strong fundamentals as discussed above and continues to justify a 5% premium valuation to its peers. We have increased our 12-month share price target to \$46.00 from \$45.50.

**Currency Impact**

The strong CDN\$ stripped away \$0.03 per share on Q3/07 such that the EPS increase would have been 18% on a constant currency basis versus the 13% increase reported. During Q3/07 the CDN\$ averaged \$1.045 versus the US\$ or up 7% on a Y/Y basis. Assuming an average of \$1.05 through to the end of 2008 the average Y/Y increase for 2008 would approximate 9% or over twice what we had forecast. If we were to alter our forecast to reflect the current level of the CDN\$ versus the US\$ our EPS would be lowered to \$3.00 from \$3.08.

**Closed Berkshire-TWC (Berkshire) Acquisition**

Manulife completed the acquisition Berkshire's mutual fund and securities dealerships in Canada consisting of over 700 Advisors and 237 branches across Canada. When combined with Manulife Securities, the transaction is expected to create a sales force of 1,500 independent advisors (doubling the current number at Manulife Securities) and will triple the Assets Under Administration (AUM) to \$19 billion. This transaction is more of a bulking up exercise for Manulife as we do not expect much in the way of earnings contribution.

**No Direct Exposure To U.S. Sub-Prime Market – But \$860 Million Indirect**

Manulife disclosed last quarter that it has no direct exposure to sub-prime residential mortgages or sub-prime CDO's but that it has \$860 million in Residential Mortgage Backed Securities (RMBS) related to sub-prime which are all high quality and mostly pre-2006 in origin.

**Other Quarterly Highlights**

- MFC reported operating Q3/07 net income of \$1,070 million or \$0.70 per share (fd), down modestly from last quarters \$1,102 but up 13% Y/Y.
- Total FUM (Funds Under Management) at quarter end were \$399 billion up 5% Y/Y, however again if the currency impact is removed the increase was closer to 15% Y/Y. The underlying growth continues to be very impressive.
- Total U.S. Protection reported Q3/07 net income of US\$138 million down from US\$169 million or down 18% Y/Y or down 12% in constant currency. Earnings were hurt by a decline in long term interest rates (the reverse of the situation in Q2/07). Of the total, JH Life's net income was US\$100 million down 23% Y/Y. JH Life sales were a record US\$197 million up 17% Y/Y. JH Long Term Care (LTC) net income was US\$32 million in Q3/07 up 60% Y/Y driven by favourable investment gains and solid sales driven by market share gains.
- U.S. Wealth Management reported Q3/07 net income of US\$257 million down 3% Y/Y. The Variable Products Group net income contribution was strong at US\$166 million up 42% due strong sales and the positive impact of equity markets on seg-funds guarantees. Fixed Products net income was US\$92 million down from US\$133 last year due to the level of investment related gains and lower funds under management due to scheduled withdrawals and restricted sales..
- Canadian division reported strong earnings with net income in Q3/07 of \$333 million up 45% Y/Y. The strength was largely attributable to the positive impact of real estate appraisal gains on reserves (the extent to which was not disclosed). Management did indicate that it was significant but offset in part by a write-down of BCE bonds. Individual Insurance sales were strong at \$68 million in the quarter up 6% Y/Y and up 15% YTD. Strong equity markets helped as AUM in wealth management jumped 15% Y/Y. Manulife Bank experienced strong loan growth.

- Asia excluding Japan reported an earnings gain of 25% Y/Y in line with the 25% YTD earnings increase. The earnings were driven by strong equity markets as Asia (ex Japan) saw an earnings increase of 60%. Japan was weaker than expected due to turbulent equity markets.
- During the quarter MFC repurchased 21.2 million shares for \$849 million for a YTD total of 53 million shares or \$2.1 billion. This level of share repurchase significantly exceeded our forecast of 40 million for 2007 and we have revised our share repurchase assumption for the current year to 60 million shares. For 2008 we have revised our share repurchase estimate to 50 million from 40 million.

No representations, express or implied are made by **eResearch** as to the accuracy, completeness or correctness of its research. Opinions and estimates expressed in its research represent **eResearch**'s judgment as of the date of its reports and are subject to change without notice and are provided in good faith and without legal responsibility. Its research is not an offer to sell or a solicitation to buy any securities. The securities discussed may not be eligible for sale in all jurisdictions. Neither **eResearch** nor any person accepts any liability whatsoever for any direct or indirect loss resulting from any use of its research or the information it contains. This report may not be reproduced, distributed or published without the express permission of **eResearch**.