Manulife Financial Corp.: My New Top Pick for Dividend Income

Description

On August 7, a day marked by gloomy economic headlines and a brutal stock market sell-off, insurance giant **Manulife Financial Corp.** (TSX: MFC)(NYSE: MFC) delivered one of the few pieces of good news.

While investors were bracing for more bad times ahead, Canada's largest life insurer announced a 19% dividend increase, with management citing that its turnaround plan "is unfolding very well" and that expansion initiatives are expected to "yield results for our shareholders".

Surprised? You should be. The last time Manulife increased its distribution was in the second quarter of 2008. However, following six quarters of losses stemming from the financial crisis, the company was forced to slash its payout 50% in a bid to preserve capital. Needless to say, the stock had lost a lot of goodwill among the dividend investment community.

However, the distribution hike signals that Manulife's turnaround is playing out faster than anyone anticipated, and that the company is once again on a solid financial footing. Better yet, this might only be the beginning. A number of catalysts suggest that more dividend hikes could be on the way.

First, Manulife is continuing to build out its Asian operations. What separates Manulife's international business from other insurance companies is that it's not concentrated in Japan, a mature and low-margin market. Rather, the company's business is centred in a number of fast-growing emerging economies like Indonesia, Malaysia, and Vietnam. These businesses now account for a larger share of the company's earnings than Canada.

In the years ahead, this story line could change how the market sees Manulife. For years, the company has been seen as a stodgy Canadian life insurance company that generated steady premium income. As investors start to wrap their heads around the company's expanding Asian operations, they could reward the stock with a premium valuation multiple.

Manulife is also well-positioned if interest rates start to increase. Insurers make their profits on the returns they earn on premiums received from policy holders. As rates rise, insurance earnings explode higher because the bonds they hold as investments suddenly offer higher yields.

The way I describe it to investors is that bond yields are to life insurers what oil prices are to energy companies. With U.S. Federal Reserve Chair Janet Yellen winding down emergency stimulus measures, interest rates are bound to start moving higher. That could mean more dividend hikes and share buybacks from Manulife.

Of course, Manulife is hardly a slam dunk. Emerging markets can be a bumpy ride, and a slow economy could kick interest rate hikes further down the road.

That said, Manulife's shares — which currently yield about 2.9% — are temping. With more dividend hikes likely on the way, this stock could become a new income investor favourite.

CATEGORY

1. Investing

TICKERS GLOBAL

1. NYSE:MFC (Manulife Financial Corporation)
2. TSX:MFC (Manulife Financial Corporation)

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Date
2025/09/12
Date Created
2014/08/11
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