Manulife Financial Corp.: What to Expect in 2017

Description

Shares of **Manulife Financial Corp.** (TSX:MFC)(NYSE:MFC) ended 2016 roughly 16% higher than where they were at the beginning of the year. Going forward into 2017, I expect this momentum to be carried on the back of its growing Asia division and yield-curve steepening in the United States.

However, despite growth in Asia and macroeconomic tailwinds, Manulife's U.S. segment continues to be a thorn in the company's side, and we could very well see a divestiture within this underperforming segment in the coming quarters.

Momentum to continue; Asia is the crown jewel

The consensus forecast for Manulife's FY 2016 core ROE stands at 9.4% — up from 9.2% in 2015. The growth in ROE is expected to come mostly by way of Manulife's Asia segment, which had a 13% increase in year-over-year core earnings in Q3 2016. Moreover, average assets under management and assets under administration for the Asian segment increased over 20% year over year compared to just 8% and 5% for the Canadian and U.S. segments, respectively.

Manulife's recovery of investment gains was also quite notable. After Q1's $340 million worth of investment losses, primarily due to energy write-downs, Manulife has recorded $60 million in investment gains for Q2 and $297 million in gains for Q3 as energy prices began their recovery, thus resuming the six-year trend of $300 million investment gains per quarter.

As to its financial position, we can expect Manulife to continue with its sector-leading MCCSR ratio north of 230% thanks to higher earnings growth going into 2017 (an MCCSR of 100% means a financial institution has adequate capital to meet its financial obligations).

Finally, while management did not provide solid commentary regarding any possible dividend increases, with a target payout ratio of 30-40% of core earnings, we can expect a dividend hike in 2017 should core earnings continue their momentum.

U.S. still a laggard; LTC divestiture a possibility

Although the much-feared actuarial-review charge for U.S. long-term care (LTC) came in at $455 million, under Q2's guidance of $500 million, the U.S segment as a whole continues to lag, as evident by the 4% decrease in U.S. core earnings year to date for FY 2016.

That being said, a steepening U.S. yield curve and strong performance in the U.S. equity markets should alleviate some pressure in this division. Moreover, management has also hinted at exploring possible divestitures for its U.S. segment during the Q3 earnings call, which, if undertaken, would be welcomed by the market.

The bottom line

The rising tide of U.S. interest rates has lifted the shares of financial companies, and Manulife is no exception. I expect the momentum to continue going into 2017 because of the strength of its Asia division and investment gains. I also expect at least one dividend raise this year and possible asset sales in the U.S. segment.

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