Does John Hancock Spinoff Make Manulife Financial Corp. a Buy?

Description

Under pressure from shareholders to deliver better returns, **Manulife Financial Corp.** (TSX:MFC)(NYSE:MFC) is reportedly looking to hive off its John Hancock unit in the U.S. through an IPO or spinoff.

If the rumours turn out to be accurate, should investors look at Manulife's stock in a more favourable light with John Hancock no longer a drag on the rest of its business?

That's a tough call. Here's why.

John Hancock's business

Lately, everyone in financial services seems to be laying off staff to become leaner while simultaneously becoming more technologically advanced.

Great-West Lifeco Inc. announced 1,500 job cuts in late April; **Royal Bank of Canada** announced 450 cuts to its Toronto head office staff in June.

"Put up or shut up" seems to be the rallying cry among insurance investors in this country, and it appears management is listening.

How big a drag is John Hancock on Manulife's overall business? Let's have a look at its fiscal 2016 results to get an idea.

In 2016, Manulife's U.S. division (John Hancock) generated US$1.2 billion in core earnings, which was 6% higher than in 2015, but 2.7% less than 2014. However, thanks to the depreciation of the loonie, the U.S. division's core earnings over the past two years jumped 16.8% from $1.4 billion in 2014 to $1.6 billion in 2016.

Can you see where I'm going with this?

Now that interest rates are moving up, and the Canadian dollar is starting to strengthen, Manulife wants to strike while it still can extract some additional proceeds from an IPO or spinoff.

Also, have you seen how well the IPO market is doing in both Canada and the U.S.? It’s hard to know when it will get another opportunity to hive off this segment of its business at a reasonably compelling multiple.

It’s got to act before the door closes, possibly for good.

Asia is the future

In the U.S., John Hancock is a small potato compared to its peers.

In 2016, although the U.S. division was responsible for 40.4% of Manulife’s overall core earnings and 38.5% of its overall revenue, its net premium income was $7 billion, or just 28.8% of Manulife’s overall net premium income.

Yes, insurance companies are becoming more holistic in their business models with every major insurance company working hard to build the wealth management side of the financial planning process, but at the end of the day, Manulife is going to live or die with insurance, not wealth management.

Asia is where its future growth lies — a market where it’s been active for 120 years.

Now consider the numbers for Asia in the last two years. Core earnings have grown 48.3% to $1.5 billion (without much of a currency bounce) with revenue growth of 61.4%.

It’s not hard to see why it’s focusing a lot of its attention on Asia.

Bottom line on spinoff

While it’s giving up a big chunk of business, it’s the right thing to do.

John Hancock hasn’t been a dog like some acquisitions Canadian companies have made in the U.S. over the years, but it hasn’t been the home run management hoped for when it bought the company in 2003.

If you own Manulife, I would continue to own it. If you don’t, should this happen, you ought to at least contemplate buying it.

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