PERSPECTIVE
FINANCIAL GROUP LLC

DUE CARE BULLETIN

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M Financial Group Due Care Review of the Manulife USA* Closed Block

*Effective 1/1/05, the Manulife USA name was changed to John Hancock USA.

Life insurance due care requires an understanding of the factors that impact policy performance and drive product selection.

M Financial Group continues to lead the industry in life insurance due care and client advocacy, providing valuable insight and analysis that delivers significant value to clients.

From 1987 until 1990, M Financial Group maintained a marketing agreement with Manulife Financial Corporation (MFC), known at the time as Manufacturers Life Insurance Company (MLI). In connection with this marketing relationship, M Member Firms wrote approximately 2,000 policies representing $2 billion of face amount. The relationship was terminated in July 1990.

In 2004, MFC acquired John Hancock Financial Services (JH). M Financial has had a marketing relationship with JH since 1992. In light of M Financial's relationship with MLI and JH, and our commitment to in-force management, the M Product Management team performed a due care review of the Manulife USA Closed Block, which includes policies sold by M Member Firms during the marketing relationship with MLI. The results of this review are provided as part of this M Due Care Bulletin.

Demutualization of Manufacturers Life Insurance Company

In 1999, MLI converted from a mutual ownership structure (owned by the participating policyholders) to a public ownership company (investor-owned, publicly traded stock company). This process is called demutualization.

Closed Block - At the time of demutualization, a Closed Block was formed to protect the performance of participating policies issued prior to the demutualization. To achieve this protection, assets in the Closed Block may not be transferred or reallocated to any other portion of the insurer's general account, except under very limited circumstances. To protect dividends, all assets in the Closed Block must be fully distributed to policies within the Closed Block.

At the time of demutualization, assumptions are made regarding investment results, persistency, mortality, and expenses in order to calculate the amount of funding required for the Closed Block liabilities. These liabilities were established in accordance with accepted actuarial methods and assumptions used to provide for guaranteed benefits, dividends, and other non-guaranteed benefits that meet the reasonable expectations of policyholders.

Closed Block Funding Assumptions - Certain assumptions were used to fund the Closed Block:

- One dividend scale and one set of funding assumptions are applied to all Closed Block products.
- Mortality is based on company experience at time of funding.
- Expenses are based on company experience at time of funding. The amount

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per policy is fixed and adjusted with the U.S. CPI inflation index.

- Persistency is based on company experience at time of funding and is in line with industry lapse rates reported by LIMRA.
- For the investment yield on underlying assets, the characteristics of assets selected for the Closed Block are similar to those of assets used to support policy benefits and dividends prior to demutualization. The assumed investment yield was based on experience at time of funding.

Closed Block Dividend Policy Tenets

- The Closed Block dividend policy will be consistent with the previous dividend policy, but amended to reflect changes required in connection with demutualization (such as the assumptions used to fund the Closed Block).
- Experience gains and losses will be reflected in changes to future dividends.
- Dividends shall be paid with the objective of exhausting assets with the final payment to the last policy.
- In the dividend allocation process, the Manulife USA Board of Directors will endeavor to achieve reasonable equity between classes of participating policyholders by allocating in the same proportion as they are considered to have contributed to the total distributable amount.

Closed Block Review at Time of Funding - The Appointed Actuary for MLI determined that the liabilities were established in accordance with accepted actuarial practice and reflect methods and assumptions that are appropriate to circumstances of Manulife USA. Further, the Appointed Actuary determined that the assets retained in the Closed Block to support such liabilities are sufficient for such purposes.

In addition, an Independent Actuary from Ekler Partners Ltd. endorsed the opinion that the Closed Block Assets are expected to be adequate to meet policyholders' reasonable expectations. Further, because Manulife USA is domiciled in the State of Michigan, Manulife sought and received approval from the Michigan Insurance Commissioner on the amount of Closed Block Assets.

Ongoing Closed Block Review - The dividend scale is established by the Manulife USA Board of Directors from time to time, and is reviewed annually. The dividend policy is intended to—at all times—comply with applicable law and regulatory requirements and accepted actuarial practice in the State of Michigan.

Manulife USA provides to the Michigan Commissioner the required reports and opinions regarding the operation of the Closed Block Account and compliance with the dividend policy provisions.

Three years after the Effective Date, and every five years thereafter, Manulife USA retains, at its own cost, an independent actuary to examine and report on the operation of the Closed Block Account and make a report to Manulife USA management and the Michigan Commissioner. The report of the independent actuary includes such data and opinions as may be required by the Michigan Commissioner.

Each year, on or before April 30, Manulife USA provides a separate income statement and balance sheet for the Closed Block Account to the Michigan Commissioner. The statement is prepared in accordance with statutory accounting principles as prescribed by the Michigan Commissioner.

M Financial Group Review of the Manulife USA Closed Block

As part of our analysis of the Manulife USA Closed Block, M Financial compared the Manulife USA Closed Block dividend scale to the dividend scales of other prominent insurance carriers.

Dividend Rate History

Year	Manulife USA Closed Block	Metropolitan	New England	Northwestern Mutual
1999	8.50%	7.60%	8.00%	8.80%
2000	8.50%	7.60%	7.75%	8.80%
2001	8.50%	7.60%	7.75%	8.80%
2002	8.50%	7.35%	7.50%	8.60%
2003	8.25%	7.10%	7.25%	8.20%
2004	8.25%	6.60%	6.75%	7.70%
2005	8.00%	6.60%	6.75%	7.50%
2006	7.75%	6.25%	6.00%	7.50%
2007	7.50%	6.25%	6.00%	7.50%
2008	7.50%	6.25%	5.50%	7.50%
2009	6.85%	6.25%	5.50%	6.50%
2010	6.35%	5.75%	5.25%	6.15%
Cumulative Change 1999-2010 2005-2010	 (2.15%) (1.65%)	 (1.85%) (0.85%)	 (2.75%) (1.50%)	 (2.65%) (1.35%)

The Manulife USA Closed Block dividend interest rate has held up well over the last decade relative to dividend interest rates from other prominent life insurance carriers, including a cumulative rate drop at least 50 basis points (bps) less than both Northwestern Mutual and New England. However, over the last five years Manulife's dividend interest rate has dropped more precipitously than other dividend interest rates, including 30 bps more than Northwestern Mutual's dividend interest rate.

Interest Rate History - In addition, M Financial reviewed the Manulife Closed Block dividend interest rate to the history of 10-year U.S. Treasury yields, where the 10-year rolling average provides an asset portfolio benchmark for the interest component of dividend scales. Insurance companies typically invest in investment grade bonds and mortgages to best match the insurance liability profile and due to regulatory constraints. New money bond yields have been decreasing since the early 1980s. Consequently, portfolio earnings have been under downward pressure, resulting in decreased dividend interest rates. Most dividend interest rates are based on the investment earnings of a seasoned portfolio. Because it takes time for investments to mature (and ultimately roll off the portfolio), there is a lag between the change in new money rates and the resulting change to portfolio earnings and the dividend interest rate.

Year	10-year U.S. Treasury Portfolio Benchmark*	Manulife Closed Block Dividend
1999	6.61%	8.50%
2000	6.41%	8.50%
2001	6.13%	8.50%
2002	5.89%	8.50%
2003	5.70%	8.25%
2004	5.42%	8.25%
2005	5.19%	8.00%
2006	5.03%	7.75%
2007	4.90%	7.50%
2008	4.70%	7.50%
2009	4.46%	6.85%
2010	4.18%	6.35%
Cumulative Change		
1999-2010	(2.49%)	(2.15%)
2005-2010	(1.01%)	(1.65%)

** 10-year Rolling Average of 10-year U.S. Treasuries represents a benchmark for the interest component in dividend scales.*

Similar to the comparison to peer dividend interest rates, Manulife's Closed Block dividend interest rate:

- Has held up well relative to the dividend interest rate benchmark over the last decade.
- Has not done as well over the last five years.

Other Dividend Interest Rate Influences - The extent to which portfolios have allocations to other investments, such as equities and real estate, will impact portfolio earnings and dividend interest rates. Some insurers, including the Manulife Closed Block, are known to have higher allocations of equities and real estate, which have impacted rates credited to policies.

Year	Manulife USA Dividend	Manulife USA Annual Dividend Change	Equity (S&P 500) Annual Return	Real Estate (NCREIF) Annual Return
1999	8.50%		21%	11%
2000	8.50%	0.00%	(9%)	12%
2001	8.50%	0.00%	(12%)	7%
2002	8.50%	0.00%	(22%)	7%
2003	8.25%	(0.25%)	28%	9%
2004	8.25%	0.00%	11%	14%
2005	8.00%	(0.25%)	5%	20%
2006	7.75%	(0.25%)	16%	17%
2007	7.50%	(0.25%)	5%	16%
2008	7.50%	0.00%	(37%)	(6%)
2009	6.85%	(0.65%)	26%	(17%)
2010	6.35%	(0.50%)	15%	13%

It appears that for Manulife the relatively large dividend rate decreases in 2009 and 2010 have been influenced by the simultaneous large negative returns for both equities and real estate. This may also explain Northwestern Mutual's large dividend interest rate decreases over the last two years which totals 135 bps (versus 115 bps for Manulife).

Note that a complication with dividend interest rates is that many insurers, including the Manulife Closed Block, incorporate mortality and expense experience as well as investment earnings. As an example, if investment earnings have declined, they may be offset with better mortality experience, resulting in less of a reduction to the dividend interest rate. Credits and charges are typically not transparent with bundled Whole Life products. However, mortality and expense experience is typically more predictable and has less fluctuation, therefore having less of an impact on changing dividend interest rates.

Manulife Commentary

We have asked Manulife to provide commentary on the Closed Block performance. Manulife's observations—decreasing new money interest rates, negative equity market returns, and negative real estate returns—are consistent with M Financial's.

Manulife has provided the following commentary regarding the Manulife Closed Block dividend interest rate decreases in 2009 and 2010:

- Fixed Income Returns: Each year, some fixed income investments will mature, and the proceeds will need to be reinvested. As some of these maturing investments had higher rates of return than currently available, the reinvestments will be at a lower rate, and will lower the total investment return.
- Real Estate: The returns from real estate investments have been the largest driver of the drop in the dividend interest rate over the last couple of years. Even though other sectors have started to recover, real estate has not yet bounced back.
- Equities: Equities remain a mixed bag. The poor performance in 2008 and into 2009 helped cause the large drop in the 2009 dividend rate, while the rebound later in 2009 and into 2010 helped dampen the decrease in 2010 (50 bps in 2010 vs. 65 bps in 2009).

For 2009, the poor performance of both real estate and equities contributed to the decrease in the dividend scale. For 2010, the poor performance of real estate was partially offset by the improvement in the equity markets. The low fixed income returns available also contributed to the dividend scale decrease for both years.

Survivorship Plus and Survivorship Life @95 - In addition to the general analysis of the Manulife Closed Block dividend, M Financial reviewed two products—Survivorship Plus and Survivorship Life @95—that have received favorable treatment. Specifically, these two products have a dividend interest rate that has not decreased as the dividend rates for the other Closed Block products have. Manulife provided the following commentary explaining the non-guaranteed "floored" dividend:

- In 1996, Manulife provided an extensive coverage review on Manulife's Traditional Whole Life products. The Survivorship Plus product series and the Survivorship Life @ 95 product series were updated to bring more of the expected dividends forward in time, so that the policyholder would receive them earlier in the life of the policy rather than later. This way the dividends would be far more effective in being used to offset the policy premiums.
- This dividend re-structure included a couple of constraints. A floor was added to the Base Dividend, which is implemented when the dividend interest rate hits a specified minimum that varies by policy. When the floor is implemented, the Base Dividend would not decrease during the premium paying period. In addition, the Base Dividend would never be greater than the initial gross annual premium on the Base policy (excluding rating and riders), assuming there was no loan on the policy. Therefore, the Base Dividend does not change

with a dividend reduction. If there were paid-up additions on the policy, the dividend on bonus would change with a dividend reduction, therefore reflecting a decrease in the Total Dividends.

- Although the dividend re-structure is not guaranteed, Manulife has no plans to remove these floors and allow dividends to decrease below levels of the previous years. Changing the dividend floor requires board approval.

The information contained in the analysis is a compilation of information and data that has been published elsewhere or made available to M Financial Group for inclusion in this document. The analysis is based on interest rate information available at the time of preparation. Our best efforts have been applied in the preparation of this analysis. M Financial Group makes no representation regarding the accuracy of the information included and assumes no responsibility for any erroneous information. Nothing contained in this analysis should be construed as a positive or negative recommendation regarding any insurance policy.

For More Information

To learn more about the Manulife USA Closed Block, please contact:

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