Genworth Financial (GNW) Earnings Report: Q4 2014 Conference Call Transcript

The following Genworth Financial conference call took place on February 11, 2015, 08:00 AM ET. This is a transcript of that earnings call:

Company Participants

- Amy Corbin; Genworth Financial; SVP - IR
- Tom McInerney; Genworth Financial; President, CEO
- Marty Klein; Genworth Financial; CFO
- Kevin Schneider; Genworth Financial; President, CEO

Other Participants

- Jimmy Bhullar; JPMorgan; Analyst
- Suneet Kamath; UBS; Analyst
- Sean Dargan; Macquarie; Analyst
- Ryan Krueger; Keefe, Bruyette and Woods; Analyst
- Colin Devine; Jefferies; Analyst
- Geoffrey Dunn; Dowling and Partners; Analyst
- Steven Schwartz; Raymond James; Analyst
- Scott Frost; BofA Merrill Lynch; Analyst

MANAGEMENT DISCUSSION SECTION

Operator:

Good morning, ladies and gentlemen, and welcome to Genworth Financial's fourth quarter 2014 earnings conference call. My name is [Christy] and I will be your coordinator today. At this time, all participants are in a listen-only mode.

We will facilitate a question-and-answer session towards the end of this conference call. As a reminder, the conference is being recorded for replay purposes.

Also, we ask that you refrain from using cell phones, speaker phones, or headsets during the Q&A portion of today's call. I would now like to turn the presentation over to Amy Corbin, Senior Vice President of Investor Relations. Ms. Corbin, you may proceed.

Amy Corbin (SVP - IR):

Thank you, operator, and good morning everyone. Thank you for joining us for Genworth's fourth quarter 2014 earnings call. In addition to covering our fourth quarter results, we will discuss the Long-Term Care active life margin review and provide an update on our strategic priorities.

Our press release and financial supplement were released last evening. Earlier this morning, our fourth quarter earnings summary presentation, along with the investor materials covering the Long-Term Care active life margin review and our strategic priorities were posted to our Web site. Both of these presentations will be referenced during our call this morning and we encourage you to review all of these materials.

Today, you will hear from our President and Chief Executive Officer, Tom McInerney, followed by Marty Klein, our Chief Financial Officer. Following our prepared comments, we will open the call up for a question-and-answer period. In addition to our speakers, Kevin Schneider, President and CEO of our Global Mortgage Insurance Division, will be available to take your questions.

With regard to forward-looking statements and the use of non-GAAP financial information, during the call this morning, we may make various forward-looking statements. Our actual results may differ materially from such statements.

We advise you to read the cautionary notes regarding forward-looking statements in our earnings release and related presentations as well as the risk factors of our most recent annual report on Form 10-K and our Form 10-Qs, as filed with the SEC.

This morning's discussion also include non-GAAP financial measures that we believe may be meaningful to investors. in our financial supplement, earnings release and investor Materials, non-GAAP measures have been reconciled to GAAP where required in accordance to SEC rules.

Also when we talk about international protection and international mortgage insurance results, please note that all percentage changes exclude the impact of foreign exchange and references to statutory results are estimates for the quarter due to the timing of the filing of the statutory statements.

Given level of interest for today's call, we ask that analysts limit themselves to one question and one follow-up. Should you have additional questions, please re-enter the queue. Now, I'll turn the call over to our CEO, Tom McInerney.

Tom McInerney (President, CEO):

Thank you, Amy, and good morning, everyone. Our objectives for this call are to update you on fourth quarter 2014 results, provide a summary of the LTC ALR margin review and resulting outcome, and update you on steps taken as part of our strategic review process commenced over the last quarter as we explore options to maximize long-term stakeholder value.

And in doing so, address questions that some of you have raised since our last call. It is important to note upfront that we are conducting a thorough review of a broad range of strategic options with the help of external financial and strategic advisors.

In order to maintain flexibility with respect to our strategic options for all key stakeholders, we believe we need to pay down $1 billion to $2 billion of debt over time. As you can imagine, there are benefits, challenges, and trade-offs associated with each option, such as debt levels and terms, tax considerations, and the views of regulators and rating agencies.

That said, we intended to continue to work through these issues and take the steps necessary to properly evaluate and implement the options that will best support our long-term strategic priorities. We've also made decisions that resulted in certain charges in the fourth quarter that we felt were instrumental in moving forward to return the Company to profitable growth as quickly as possible.

The LTC margin is positive in the aggregate but as we indicated, might be the case in our past disclosures, the margin turned negative on acquired LTC business which resulted in an after-tax, non-cash GAAP charge of $478 million. We also incurred a moderate 2014 statutory reserve charge in our New York subsidiary reflective of a higher claim severity and lower interest rates.

Further, we also recorded net non-cash charges related to the Company's progress and plans to monetize the lifestyle protection insurance business which we have previously identified as non-core. Marty will take you through this, along with several other actions, in more detail in a few minutes.

We are also launching a very significant restructuring plan, focused on supplier and cost rationalization which we expect will generate in excess of $100 million in annual cash savings by the end of 2016. Moreover, capital and liquidity remain strong across all platforms and at the holding Company.

I also wanted to note that these charges overshadowed another solid quarter for the global mortgage insurance and fixed annuity businesses. There are a few important takeaways for our mortgage businesses.

First, the mortgage insurance business continued to show progress from our turnaround efforts, which we laid out 18 months ago, benefiting from strong competitive positions, stable to improving markets, and full-year loss ratio performance across all three primary platforms. Additionally, Canada and Australia remain strong cash generators and have been and are expected to continue to be reliable sources for future dividends to the holding company.

Second, our USMI platform continued to show improved operating performance, benefiting from a 19% drop in new flow delinquencies, as compared to a year ago, reflecting the burn-through of the older books as the new books now represent 56% of risk in-force. While this business has come a long way, we believe it will take a few more years to be a significant cash dividend contributor.

Third, the USMI business made significant progress during the quarter, working with reinsurers toward our plan compliance with the new GSE capital requirements by the anticipated effective date. Lastly, we had a settlement in our European mortgage business which significantly reduced risk and force in Ireland with minimal earnings impact.

In summary, the Global Mortgage Insurance Business is executing well and we expect it to continue to be a strong driver of operating performance going forward.

Now let me turn to the Life Division. The underlying fixed annuities performance was good and absent the reserve charge, Life Insurance showed modest improvement.

LTC remains a significant challenge. We believe the updated assumptions for the DLR and ALR are reasonable and appropriate given the experience that has emerged and the reviews undertaken.

We will continue to monitor experience, assumptions, and the resulting reserves closely, with support from outside actuarial advisors. We have made significant progress to date to re-rate the most problematic LTC blocks acquired or written over a decade ago.

However, we expect to continue to feel pressure as these blocks reach their peak loss years as our policyholders age and therefore, we will be pursuing additional in-force rate actions to recognize changes in experience. We are encouraged, however, with the positive margins on the remaining blocks and we'll actively monitor and rest unfavorable experience as it evolves.

On the rate action front, we have made good progress to date in our 2012 rate actions and based on current approach and anticipated first quarter approvals. We now project approximately $240 million to $260 million of additional annual premiums against our $250 million to $300 million objective. Now I will turn the call over to Marty to go into more detail on the fourth quarter results and the outcome of the active life margin review.

Marty Klein (CFO):

Thanks, Tom, and good morning, everyone. This morning, I will discuss our Long-Term Care margin review and impacts related to it. But first, I will briefly review our fourth quarter results.

As shown on slide 3 of the earnings summary, we reported a net operating loss of $416 million and a net loss of $760 million for the quarter. There were several factors impacting the operating loss, which overshadows solid operating performance in several of our businesses, particularly in our Global Mortgage Insurance

Division.

These items include after-tax charges of $478 million from Long-Term Care blocks acquired over 20 years ago as a result of our annual review of active life margins and unfavorable reserve adjustments totaling $48 million in our Life and Long-Term Care businesses.

In addition, reflecting our consideration of a variety of potential strategic options and current business realities, we recognize the following items in net income. First, we wrote off all remaining goodwill in both our Life and Long-Term Care businesses resulting in an after-tax charge of $274 million.

Goodwill balances are highly dependent upon projected future sales levels and with our assessment of current market realities, in addition to our active consideration of potential business portfolio changes, projected sales levels could drop in some scenarios. We concluded it was appropriate to write off the associated goodwill balances.

Second, we recognized the tax charge of $174 million, reflecting the change in our intent to permanently reinvest earnings from Genworth Mortgage Insurance Australia Limited. While we have not made any decision with regard to this asset, we are evaluating it among several other available strategic options, given its valuation and liquid state.

Also, we are progressing on the sales process of the Lifestyle Protection Insurance business which has been a non-core business for us. Related to that planned sale, we completed an internal debt restructuring, resulting in a $108 million tax benefit.

While I won't, of course, address valuation directly, we are seeing market interest for this business and are seeking to monetize it. Given current book value, we anticipate a significant loss on sale.

Global Mortgage Insurance had another good quarter, as shown on slide 4, reporting net operating income of $83 million down slightly versus the prior quarter and prior year when adding back the non-controlling interest impact of the Australia IPO in those periods.

Let's cover Canada on slide 5 first, where operating earnings were $36 million, down $10 million from the prior quarter. We saw lower unemployment and a modest sequential increase in home prices. Additionally, tax benefits were lower versus the prior quarter.

The loss ratio increased 5 points from the prior quarter to 26% from seasonally higher new delinquencies, net of cures. The full-year loss ratio was 20% at the midpoint of our 2014 expectation. We expect the 2015 full-year loss ratio to be between 20% and 30%.

Turning to Australia on slide 6, operating earnings were $33 million, down $15 million versus the prior quarter, primarily from less favorable tax benefits. Macroeconomic conditions were generally stable in the quarter, as there was a slight decrease in the unemployment rate and overall home prices experienced modest gains.

The loss ratio remained very low at 15%. The full-year loss ratio was 19%, slightly better than the low end of our 2014 expectation. We expect 2015 full-year loss ratio to be between 25% and 30%.

In other countries, we executed a lender settlement, materially reducing risk in-force in Ireland from $700 million to $60 million, with only a minimal financial impact in the quarter. Given the size of our international operations, foreign exchange rates do impact our earnings.

While I can't predict where these rates will go, I can give you some perspective on sensitivities. For instance, its total year 2014 exchange rates were at current levels, our international earnings would have been approximately $30 million lower. Using this example, a rough rule of thumb would be a 1-point move in either of the Canada or Australian exchange rate would result in approximately $2 million change in earnings.

I will stress that this is only a translation risk, as our assets and liabilities in our international businesses are predominantly held in the respective local currency. However, we do hedge much of our foreign exchange risk associated with expected cash flows.

Moving to slide 7 in USMI, net operating income was $21 million for the quarter, up $23 million from the prior quarter. As a reminder, the prior quarter included $34 million of after-tax accruals recorded in connection with settlements, one with Bank of America , which has now received GSE approval, and another, which has now been resolved.

The reported loss ratio for the year was 62%, including a 9-point unfavorable impact from third quarter lender settlements. For 2014, USMI net operating income of $91 million was significantly improved over 2013.

Earnings and loss performance should continue to improve with the 2015 full-year loss ratio expected to be between 40% and 50%. NIW was seasonally down from the prior quarter but benefited as the business increased its single premium lender paid new insurance written, reflecting its selective participation in this market.

Future volumes of this product will vary depending on the evaluation of the risk return profile of these transactions. The Company's estimate of USMI market share increased year over year to 15%. At year end, 56% of the risk in-force is composed to 2009 and forward books of business. We anticipate this percentage will grow to between 60% and 70% by the end of 2015.

Turning to capital and the GMI division on slide 8, the prescribed capital amount, or PCA ratio, in Australia, is estimated at 159%, up from the prior quarter from continued strong statutory income. For Canada, the minimal capital test, or MCT ratio, is estimated at 225%, in line with the prior quarter.

USMI at quarter end, the risk-to-capital ratio for GMICO was approximately 14.2 to 1, down from 14.8 to 1 in the prior quarter, from an increase of $125 million in admitted deferred tax assets in GMICO, partially offset by changes in value of affiliated investigation and increased risk in-force.

Our capital goals in the Global MI division for 2015 include a PCA ratio of 132% to 144% in Australia, 220% or greater MCT in Canada, International MI dividends of $150 million to $230 million, and combined risk-to-capital ratio of less than 18 to 1 in USMI. I would also note Australia has declared a special dividend, our portion of which is approximately $40 million and will be received in the first quarter of 2015.

We have two strategic priorities for GMI in 2015. First in Australia and Canada, we will continue to look for ways to optimize capital to improve ROE, provide for growth opportunities, and return capital to the respective shareholders.

Second, USMI. It remains our priority to plan to comply with the new GSE eligibility requirements by the effective date. We still estimate the capital need to be between $500 million and $700 million. We continue to make progress on reinsurance transactions when the market appetite remains robust. However, we are waiting on finalization of PMIERs capital credit standards and ultimate reinsurance terms are subject to modification.

Turning to the US Life Insurance division, as shown on slide 9, the operating loss was $482 million, reflecting the impact of the Long-Term Care annual loss recognition review, with a net loss of $750 million after the goodwill charges mentioned earlier. Favorable mortality and life insurance was more than offset by a reserve correction on a term-life reinsurance treaty in the current quarter.

Fixed annuities showed continued solid performance. The Long-Term Care insurance net operating loss in the quarter was $506 million, driven primarily by the completion of the annual loss recognition testing review and associated charges on the acquired blocks of business, as shown on slide 10. I'll provide greater detail on the review in just a few minutes.

Although incurred loss results were primarily impacted by the loss recognition charge on the acquired blocks and other adjustments, the claim reserve review from last quarter also had an impact, as we set up higher claim reserves than new claims in the fourth quarter using the updated reserve assumptions and also had lower reserve releases on existing claims.

In addition, we had unfavorable adjustments to our claim reserves of $16 million, including a $44 million claim reserve correction. This correction was identified in the fourth quarter as an operational process control deficiency in how we implemented one of the claim reserve assumption updates. We are currently assessing the internal control environment around this issue as part of the year-end controls assessment to determine whether we have a significantly deficiency or a material weakness.

While we've not yet completed this assessment, we believe this deficiency likely constitute a material weakness in our internal controls and we plan to complete our review process and reflect the results in our 10-K as well as our plans for remediation, if we do end up concluding on such a weakness. We are highly focused on addressing this issue and taking the appropriate actions to fix the issues.

Moving to slide 11, in-force rate actions continue to favorably impact earnings, benefiting results by $41 million, $7 million higher than the last year, but $3 million lower than the prior quarter. We also received additional approvals from a second round of filings from the 2012 in-force rate action that increased the incremental premium approved to $200 million to $210 million with another $40 million to $50 million expected in the first quarter 2015 against the total anticipated annual premium increase of $250 million to $300 million when fully implemented.

Moving to slide 12, operating earnings in Life Insurance were $1 million for the quarter, down from $13 million in the prior quarter and include the reserve correction on the reinsurance treaty of $32 million that I mentioned earlier. Mortality experience is favorable versus the prior quarter and unfavorable versus the prior year. For fixed annuities on slide 13, earnings were $23 million, slightly lower than the prior quarter.

Turning to US Life statutory performance on slide 14, unassigned surplus decreased approximately $135 million and the RBC ratio decreased 18 points to approximately 430% in the quarter. There were several drivers of this decline.

First, as a result of our annual statutory cash flow testing review, we increased reserves by $39 million in our New York subsidiary to reflect an incremental $195 million negative margin on its Long-Term Care Insurance business, with the remaining $156 million to be recognized over the next four years. I'll provide more details on the review in a few minutes.

Second, we increased reserves related to secondary guarantee UL products in our New York subsidiary, which is the second and final increase related to our discussions with the New York regulator on this matter. Third, we reinsured a block of term universal life to a third-party reinsurer, providing approximately $80 million of unassigned surplus benefit.

And finally, the completion of an internal debt restructuring in the lifestyle protection insurance business, which provided overall tax benefits of $108 million on a GAAP basis, also resulted in changes to certain inner-company tax balances in US Life and in the Bermuda entities. The US Life Companies experienced a charge of $155 million while BLAIC saw a tax benefit of $230 million.

With the reflection of this benefit and other timing, BLAIC ended the quarter with an RBC ratio of approximately 345%, up from 245% in the prior quarter. We expect the RBC ratio in our US Life Companies to be greater than 400% at year-end 2015 and repatriation of the Long-Term Care business from BLAIC to the US

Life Companies remains a strategic priority for 2015.

Shifting to slide 15 and the Corporate & Other division, the net operating loss for the quarter was $17 million. International protection reported a loss of $4 million in the current quarter that included approximately $4 million of unfavorable items, including: higher claim reserves in certain contracts and unfavorable shift in the mix of contracts with profit share, higher expenses, and unfavorable foreign exchange.

Runoff earnings were higher by $11 million compared to the prior quarter, primarily related to favorable taxes. We had favorable taxes in Corporate & Other related to timing with the full-year operating tax rate of 34%.

Moving to investments on slide 16, our general account continues to perform well. The Global Portfolio core yield was down slightly from the prior quarter at 4.38% due to the impact of lower rates and other factors and there were no impairments in that quarter.

As shown on slide 17, at the holding company, we continued to maintain significant liquidity with cash and liquid assets of approximately $1.1 billion, representing a buffer of approximately $685 million in excess of our target of 1.5 times debt service and well above our $350 million risk buffer. We anticipate maintaining this target and risk buffer in 2015.

Unfortunately, our leverage ratio increased to 25.9%, given the Long-Term Care Reserve increases, goodwill write-downs and other impacts to equity this quarter. Stepping back, in addition to our current excess liquidity at the holding company and the solid capital levels across our operating platforms, we have significant levers benefiting our financial flexibility.

These include monetization of our non-core businesses, additional life block sales of refinancing, and reinsurance of MI business risks. We also have other sources of capital available that we could consider such as the additional sell-down of Australia MI business, among others. We currently believe these are more attractive sources of capital than outright equity raise and we have no current plans to do such a raise at this time.

Let me now turn to Long-Term Care and discuss our annual margin testing. Please refer to the separate presentation of Long-Term Care annual margin testing. In the third quarter, we made significant updates to our Long-Term Care claim reserves to reflect our updated view on our claim severity assumptions.

After a review of this experience, expected claim termination rates are expected to be lower and benefit utilization rates are expected to be higher than had been assumed before in the third quarter. As a result of the updated assumptions, we expect claimants are staying on claim longer and using more of their available benefits.

We made these updates to our claim reserve assumptions in the third quarter and they have informed the assumptions made in our margin analysis. With these updated claim severity assumptions, we have and will continue to pursue actuarial adjusted rate actions to attempt to offset the higher expected claims costs.

These new claim cost views and associated rate actions represent the most significant updates from a margin analysis last year. Genworth's reviews of Long-Term Care active life margins are substantially completed. We were assisted by two leading external actuarial firms with strong Long-Term Care experience.

One firm work closely with our actuaries on the detailed assumptions and reserve changes and the second firm conducted an independent peer review of our assumptions and approach. Both firms concluded that the assumptions in the aggregate were reasonable and supported by experience.

Slide 2 summarizes our active life margin conclusions. First, GAAP loss recognition testing margins were positive in aggregate; however, we must test our acquired block, representing business acquired before 1996, separately from our other business.

The margin on the acquired block, which as we previously disclosed had very thin margins, was a negative $735 million pre-tax, as future in-force rate actions, either incremental premium rate actions or risk benefits, depending on policy holder behavior, have less impact given the higher age of the block.

Net GAAP liabilities for this block had been approximately $2.6 billion before adjusting for the negative margin. The other much larger block tested had a positive margin of $2.3 billion. Net GAAP liabilities for this block are approximately $15.7 billion.

Second, statutory cash flow testing margins were positive in aggregate, using our policies in-force as of September 30, and adjusting for year-end interest rates. As a reminder, we test each legal entity separately on a statutory basis governed by the specific rules of the regulator in the state of domicile.

The margins in our General Life Insurance Company, or GLIC, and Brookfield Life & Annuity Insurance Company, or BLAIC, were a positive $4.3 billion, in aggregate, before adjusting downward for about $1.9 billion for provisions for (inaudible), or PADS.

Given the requirements for cash flow testing in New York, we increased reserves by $39 million in our New York subsidiary to reflect the $195 million incremental negative margin on the Long-Term Care Insurance business and net annuity, with remaining $156 million to be recognized over the next four years.

For call, we have had negative margins in New York in the past, for which we have previously held reserves of $80 million. Our statutory capital levels remain solid, with an RBC ratio of approximately 430% at year end, reflecting these results.

The components of the statutory and GAAP margins are laid out on slide 3. The present value future premiums, claims and expenses are projected based on assumptions reflecting our own experience and actuarial judgment.

As I mentioned, the most significant updates were to claim-related assumptions, such as claim termination rates and benefit utilization rates, informed by assumptions which were updated in our third quarter claim reserve review as well as the inclusion of additional assumed future premium increases and reduced benefits which offset most of the expected increase in claims cost.

We developed a new series of anticipated in-force premium increase requests based on updated claim severity assumptions and these premium increase assumptions were informed by our historical track record what we have achieved in previous rate actions in review of the relevant regulators as well as our third-party advisors. It is important to note that if an actual claim incidence or severity in the future is different than expected, the projected in-force rate actions will change accordingly, as these projected rate actions were developed reflect claims cost being experienced.

Other significant impacts related to investment assumptions given the current low rate environment. As a reminder, Genworth began hedging interest rates starting in 2000 for Long-Term Care. We have after-tax terminated hedge gains that resided in accumulated other comprehensive income on a GAAP balance sheet of approximately $1.7 billion and this amount will amortize in to GAAP income over time.

Similarly, we have approximately $830 million, primarily from after-tax hedge gains on a statutory basis that reside in the Interest Maintenance Reserve, or the IMR, on the statutory balance sheet, and the IMR amortizes in to statutory income. While our hedging program has dampened the effect of lower interest rates, during 2014, we revised our reinvestment strategy given that environment and adjusted our reinvestment strategy for Long-Term Care business to pick up additional spread.

This new reinvestment strategy is reflected in our cash flow testing analysis and I'll provide additional perspectives on this revision in a few minutes. In addition, we reviewed other assumptions and in some cases, made updates. In particular, we reviewed claim frequency, lapse rates, morbidity and mortality improvement, and expenses. The margin impact from updates on some of these items was modestly favorable.

Slide 4 provides a summary of the key updates we made to both our assumptions concerning claim termination and benefit utilization rates. As a reminder from our third quarter earnings call, claim termination rates refer to the expected rates at which claims end and benefit utilization rates refer to how much of the available policy benefits are expected to be used.

Also, as you'll recall, there are numerous assumptions for claim termination and benefit utilization rates based on several characteristics, such as type of policy, as well as policyholder and claim characteristics. Assumptions developed in the third quarter claim reserve review informed our active life margin analysis and we projected them forward over the 40-year-plus projection period.

Subsequent to our third quarter claim reserve review, we continued to assess our assumptions concerning claim termination rates in connection with our active life margin review. After review and consultation with our third-party advisors, we increased the assumptions concerning claim termination rates slightly in the later durations, given that the statistical credibility of our data from claims and durations severed and beyond, while much better, is still limited.

As we noted in our earnings release and commentary, we also updated our assumptions for this refined view in our Disabled Life Reserves in the fourth quarter. The combined impact of changes to the assumptions for claim termination rates and benefit utilization rates reduced GAAP margin by approximately $5.4 billion. As we discussed in the third quarter, we have developed management actions regarding premium rate increases that we expect will offset much or possibly most of the reduction in margins from the updated assumptions.

Turning to slide 5, a key change from last year's margin testing is the inclusion of future rate actions in our GAAP loss recognition tests as well as in our GLIC and BLAIC legal entities. Inclusion of such premium increase and associated benefit reductions is consistent with actual guidelines, GAAP accounting, and the regulatory framework in almost all states. In addition, we consulted with our regulators on these assumptions for our cash flow testing work.

Before discussing the future rate action assumptions, I want to give some context for our actions today. First, we have a good history of achieving premium rate increases on our in-force blocks. In 2007, we filed for an approximate 10% rate increase and achieved about 90% of our requested filing that resulted in incremental premium of about $50 million to $60 million.

In 2010, we filed for an approximately 18% rate action and achieved about 94% of our requested filing that resulted in incremental premium of about $40 million to $50 million. Additionally, we have made good progress with the 2012 rate actions that represent about $200 million to $210 million of incremental premium, which we'll fully implement it by 2017 and have also received or expect to receive approvals in the first quarter, reflecting $40 million to $50 million of additional premium increases.

We still anticipate additional premium increases from 2012 rate actions of $250 million to $300 million when fully implemented. Second, as part of our strategy, beginning in 2013, we have filed for premium increases on our Choice 2 block.

We have seen good progress to date on our Choice 2 filings, where we've heard back from 30 states and received approval from 22 states. We believe the Choice 2 approvals received so far, will ad an incremental $20 million to $30 million in annual premium increases once fully implemented.

We have also received, or expect to receive approvals in the first quarter reflecting $20 million to $30 million of Choice 2 premium increases. Also, we are going back to states that did not approve our Choice 2 filings to ask them to reconsider increases based on the new claim assumptions.

We anticipate additional premium increases of $40 million to $60 million when fully implemented from the 2013 Choice 2 rate action. These actions we have been taking just since 2007 should result in additional expected premium of about $380 million to $470 million. We have developed a plan for future premium rate increases for all older blocks up to and including PC Flex that were informed by historical track record, reviewed with the regulators and consistent with projected future claim costs.

These rate actions projected, to be implemented over the next 15 years, assume we achieve incremental annual premium, which grows to $525 million to $625 million at the peak before declining significantly over the subsequent years as the number of active lives declines. The corresponding GAAP margin impact of these rate actions, reflecting both additional premiums as well as reduced benefits, is approximately $4.9 billion pre-tax.

Before I move on to other assumptions in our margin analysis, let me provide some perspectives on future rate actions and corresponding potential reductions and benefits. We believe providing alternatives to policyholders so they can choose between accepting higher premiums or electing benefit reductions in these guaranteed renewal policies is important.

And we expect to see even more focus on and receptivity of reduced benefits as an alternative to higher premiums. We believe regulators and policyholders generally are more receptive to this approach and certainly prefer having choices.

Such reduced benefits generally are expected to be actuarially equivalent to higher premiums and so the margin impact should not be significantly different. However, with reduced benefits, our exposure to changes in future claims cost is lower. In other words, our tail risk is reduced.

In the low inflation world, some policyholders may find it more attractive to lower their benefit increase option or biowriters on their policies in lieu of higher premiums. Choice 1 and 2, representing our largest blocks, have a higher proportion of bio features than do older product generations.

Electing risk benefits, such as choosing reduction in the bio feature, may be easier for those policyholders to accept than paying higher premiums and regulators increasingly prefer that carriers provide such choices to policyholders. Certainly, different people have different views on the subject of rate actions and the ability of Genworth and other long-term care providers to obtain them.

We believe regulators are generally more receptive to acknowledging the need for such rate actions and we've been working with them to gain approvals in forms that they think are more beneficial to policyholders, to approaches such as staged increases or providing alternatives for risk benefits. Our assumptions on future rate actions are in line with what would be actuarially justified, while reflecting our own historical track record as a model of corresponding additional premium.

Now let's shift to slide 6 and investment assumptions. Our cash flow testing projections assume a 10-year treasury rate of approximately 2.2%, in line with levels at year end, rising to approximately 4.7% in 2028 to 2030 before gradually declining over the remaining projection period to 4% to 4.2%.

During 2014, our investment risk and asset liability management team modified our reinvestment strategy for long-term care. In order to increase spread in a lower interest rate environment, we've made changes to our reinvestment allocations, which will lower the overall credit quality one notch to BBB+ over time.

Also historically, we have invested very little in alternative investments but we do plan to build up an allocation of up to 5% over time. We've reflected these changes and reinvestment strategy in our cash flow testing analysis.

For GAAP loss recognition testing, we utilize the static discount rate that is in line with our current portfolio yield, as has been a practice for many years. As a result of the reserve increases in the third quarter and the fourth quarter, the asset is required to back the liabilities increased as we needed to contribute assets so that assets equals liabilities.

In this low rate environment, these additional assets were lower yielding and decreased the PGAAP and HGAAP discount rates by 35 basis points and 23 basis points, respectively. This impact on GAAP margins of the year-end discount rates was an unfavorable $1.5 billion.

Long-term care is a long duration product and movements in any number of assumptions can impact performance over time. With that as the backdrop, we've provided selective sensitivities on our updated assumptions on slide 7 but actual experience may differ.

The claims cost sensitivity, or sensitivity A, further increases the claims severity or claim frequency above what we have included in our updated assumptions. This sensitivity does not include future rate action or benefit reductions that we would likely put in place to offset much of this impact.

Given the potential impact of interest rates on margins, we're providing two sensitivities. The first interest rate sensitivity, or sensitivity B, assumes that the 10-year treasury rates are 2.5% on a statutory basis for the entire projection period.

The second interest rate sensitivity, or sensitivity C, assumes that discount rates affecting PGAAP, HGAAP and statutory cash flow testing are reduced by 25 basis points. Finally, the in-force rate action sensitivity, or sensitivity D, assumes that we only achieve 90% of the planned future rate actions that we have modeled.

Next, I will cover two GAAP accounting implications that emerged as a result of our margin testing and are summarized on slide 8, first, given the negative margin on our acquired block, GAAP reserve assumptions were unlocked and reset so that the expected margin is zero. With zero margin, this block has a higher likelihood of a future unlocking.

Second, as I discussed earlier, the loss recognition testing margin on our other block, the HGAAP block was $2.3 billion on a GAAP basis. However, given the new claims severity and in-force rate actions assumptions, the earnings over the projection period display a pattern of profits for the next 15 years or so, followed by losses thereafter.

The profit period has a present value of approximately $3.5 billion while the present value of the losses is a negative $1.2 billion netting to the $2.3 billion margin. This is a result of the active life reserve assumptions being locked in under GAAP and the increased premium or associated reduce benefits falling to the bottom line in the analysis, while the higher claim severity assumptions contribute to losses in later years.

This expected pattern has emerged for the first time during this year's margin testing, given our updated view on claims severity. Therefore we will use a portion of the expected benefit from future in-force rate actions to fund the expected future losses during the expected profit periods rather than being fully recognized in the period received. This change should help limit the loss recognition testing margin deterioration in the future as we accrue additional reserve liability for the future loss periods.

We've provided a lot of information this morning so let me sum up on our margin results. Our GAAP and statutory margins are lower than last year but remain positive in aggregate. We must, however, recognize a GAAP charge on our block of policies acquired before 1996, that, that block must be tested separately. We also have reserve increases in our New York subsidiary due to its including negative margin which excludes future rate actions.

Finally, our US Life Capital and RBC levels remain solid, even after reflecting our new claim cost assumptions in our claim and active life reserve processes. With that, I'll turn the call back over to Tom.

Tom McInerney (President, CEO):

Now let me take a minute to discuss, in a bit more detail, our strategic review and priorities. As discussed already, we have and continue to analyze a range of strategic options to maximize shareholder value, working with our Board. We have engaged external financial and strategic advisors to assist us in our reviews. We have made candid appraisals of our business' strengths and weaknesses and are taking proactive measures to rationalize our overall portfolio.

We believe that our Mortgage Insurance businesses are our strongest businesses and we expect them to continue to perform well in 2015 and beyond. We must continue to take steps to mitigate LTC risks given the pressures on the older LTC blocks and impacts we're seeing on sales given rating pressures.

To that end, we continue to capitalize on our industry leadership in order to drive regulatory and market changes that are necessary to sustain this business over the long term. By far the most important action we can take to make LTC a viable business is to continue to work with all state regulators to seek significant actuarially justified premium rate increases and benefit reductions on the existing in-force LTC blocks.

We think that future premium increases or benefit reductions on the older blocks of business is critical to maintaining positive ALR margins. In addition to securing future premium increases or benefit reductions, we will continue to develop higher return, lower risk, new LTC and combo products to address the growing LTC needs and increasing size of the aging US population.

And we will press on regulators the need to consider more frequent and smaller premium increases on current and future business, as experience dictates. We believe that the result of the costs and portfolio rationalization efforts we are pursuing will improve our ability to reduce debt levels, increase capital buffers, improve operating earnings and ROE, and the life businesses and grow profitable mortgage business.

We remain actively engaged with our Board, key stakeholders, and external advisors to ensure appropriate evaluation of growth opportunities, capital structure, regulatory actions and rating considerations. We will provide investors with regular progress updates and now Marty, Kevin Schneider, and I are happy to answer your questions.

QUESTIONS & ANSWERS

Operator:

Ladies and gentlemen, at this time, we will begin the Q&A portion of the call.

(Operator Instructions)

Jimmy Bhullar, JPMorgan .

Jimmy Bhullar (Analyst - JPMorgan):

Hi, good morning. I just had a couple questions. First, you mentioned the plan to by $1 billion or $2 billion. Obviously, you're going to get dividends from the Australia and Canadian MI businesses, but what are you going to get other than that? I'm assuming you might not be able to get much dividends from life. That's my first question.

Tom McInerney (President, CEO):

Let me take the first part and say that working with our Board and our external financial and strategic advisors we determine when we're looking at all of the options that we might consider to raise shareholder value, we don't have as much flexibility as we'd like because of the level debt of the holding company.

So based on working with rating agencies, regulators and our feedback from external advisors, we believe that a target of $1 billion to $2 billion of debt reduction frees up a lot of additional options to consider. So as we look at strategic options, we are looking at those that will allow us over time to reduce that debt. I'll turn it over to Marty I guess to give you a little bit of specifics in terms of the 2015 operating dividends that we're expecting.

Marty Klein (CFO):

Hey Jimmy. It's Marty. I think what we have in our cash plans are really the dividends, planned conservative depends we have coming from Australia and Canada.

As you know, we expect that to be in the range of $150 million to $230 million, and remind you our annual debt services order magnitude around $280 million. We're also obviously going in to the year here with significant liquidity at the holding Company, probably close to $400 or $350 million to $400 million over our cash buffer.

That obviously provides lift there. We do expect Company balances to be relatively stable with the dividends we're giving. Obviously the other thing we're working on as we mentioned in the remarks is we are launching our sales process of lifestyle protection. We're not managing our cash reflecting that but obviously if we execute that, that will create some up side.

Jimmy Bhullar (Analyst - JPMorgan):

And the $1 billion to $2 billion, you're planning on doing that this year or is it more of a longer-term target?

Kevin Schneider (President, CEO):

It's more of a longer-term target. And we're looking at things, as Marty said, like selling API, as we said last year we're looking at selling blocks of life annuity.

We are looking at our Australia business and should we sell further down there, that was part of the reason for that PRI tax charge. Obviously there are other options but all of those we're looking at in conjunction with our Board and external advisors to do over the longer-term.

Jimmy Bhullar (Analyst - JPMorgan):

It's sort of a reasonable assumption that paydown, you would need to sell as reinsured businesses, because from the operations the cash flows are somewhat limited.

Unidentified Company Representative:

That's right.

Jimmy Bhullar (Analyst - JPMorgan):

And another question related to that, are there any implication physical you determine there's an weakness in your control to do anything else in the short term?

Tom McInerney (President, CEO):

Jimmy, I think this came up really in the third quarter related to our long-term care life reserve charge and we had a manual process introduced for the first time with that adjustment. And that's really where the issue is. We obviously have been working on addressing that. When we have our 10-K we'll provide more details on that error if it is in fact a material weakness.

We're still assessing that. If it is material weakness we'll provide remediation plan. We're still going over our overall assessment. At this point I anticipate if it is a material weakness it's pretty isolated to that particular situation. If that is the case I wouldn't make any broader issues as you describe.

Jimmy Bhullar (Analyst - JPMorgan):

Thanks. And one last one. You did change the for Australia and that sort of gives you some flexibility to sell down your stake. Wondering why you did not do that for the Canadian business and is that something you'd consider?

Marty Klein (CFO):

The first thing I'd say on all three MIs is we think all three are performing well and they're our strongest businesses. In looking at Australia and Canada, in our holdings of those, we looked at the percentage of ownership that we have of those. We looked at whether the banks in those market receive explicit or implicit credit for the mortgage insurance.

We looked at our market share versus competitors in the overall competitor environment. We do think in Canada there is the potential based on what the housing regulators have said that they may look to recuse the housing authority corporations guarantees and therefore the taxpayer exposure.

We think that's a potential in the Canadian market to grow. Then obviously for management oversight and synergies between Canada and Australia are different. So all of those went in and so our conclusion was we're looking -- we haven't made any decisions yet on Australia.

But we are looking at options to sell down further. Right at this point we're not currently looking to sell down in Canada. So that's the difference in the tax treatment.

Jimmy Bhullar (Analyst - JPMorgan):

Thank you.

Operator:

Suneet Kamath, UBS.

Suneet Kamath (Analyst - UBS):

Thanks. Good morning. Marty, I was hoping you could help us reconcile the statutory active life margin in terms of what you showed us in the last presentation and what you're showing us today. Just in terms of the pieces.

So you start with the -- whatever it was, the $2.6 billion I think, what was the impact of the revised claims assumptions, and then separately what was the impact of the future rate increase benefit that ultimately gets you to I think what the comparable number is this quarter of $2.1 billion?

Marty Klein (CFO):

Yes, you're right, your beginning and ending balances are right, Suneet. We called out in my prepared remarks the pieces on a GAAP basis and those assumptions are really the same on a cash flow testing basis with one slight change.

That's the slight change I'll speak to in a moment. I don't want to get in to specific amounts but discounting rates a little bit different. So those amounts are same.

$4.5 million negative effective margins on updated claims utilization rates about $1.5 billion for interest rates as a decreased margin. Then on the positive side, $4.9 billion pre-tax of premium rate action in the future.

Then about -- we didn't really call it out but roughly $500 million to $600 million of sort of other adjustments and those kind of really get you in the GAAP walk. On the statutory side it's really those same items. The present values are a little bit different.

I think the difference in stat is that with the interest rate approach that we use, different than statutory testing where we use a variety of randomly generated interest rates and take the average of that and we've described in the presentation what that average gets to.

That's obviously a different approach than what we do in GAAP where we just use our current portfolio rate and use that back to discount back the cash flows. The other adjustment in statutory which is not reflected in the GAAP margin testing is the new reinvestment strategy are articulated where over time, and really takes a long period of time as we're reinvesting in bonds and the reinvestment strategy is BBB+.

That takes 15 to almost 20 years in the model to get fully in to that triple B plus category on average. Similarly we built in small allocation to alternatives that builds up over time. I think it takes 10 to 12 years to get up to I think 5% allocation.

So those are really the differences on stat. Really if you think about that billion and a half interest rate hit in margin on GAAP, it's a bit less on a statutory basis for those reasons.

Suneet Kamath (Analyst - UBS):

And frankly, I think a lot of us are more focused on statutory so if at some point you could give us a clear reconciliation of how that ALR on a stat basis change, that would be really helpful. The second question I have is on the anticipated rate increases, I guess it's slide 5 of your LTC presentation.

So it looks like you have prior approved or anticipated rate actions of $280 million to $370 million. When we think about the $625 million of peak incremental annual premiums, is that in addition to the $380 million to $470 million or does that include the $380 million to $470 million?

Marty Klein (CFO):

That is in addition to the $380 million to $470 million. So those are future premium increases or benefit reductions that we'll seek over the next 15 years or so. I do want to make a comment there.

I've been here for two years and I think there's been a significant change from a regulatory perspective in terms of where the states are. I think two years ago I think a number of regulators were still working through what was actually justified. I think now there's a recognition based on our recent experience, our experience in competitors, that there is a need for significant increases on the old business for us and other companies.

Long-term care is a guaranteed renewable policy. Regulators are required to approve appropriate actual changes. I think there is a change in the last two years in terms of regulators and all the states look at it.

Suneet Kamath (Analyst - UBS):

When you say in your prepared remarks that you've run these price increases by the regulators, who specifically is that? Is that just your main insurance regulator or have you sort of discussed this with all of them that you have to go back to and ask for price increases?

Marty Klein (CFO):

Suneet, it's really with the regulators for US Life Companies. We do anticipate having a call with all the insurance departments here shortly to go over this type of information. It's really in conjunction with consultation with the regulatory -- regulators of our states.

I'd point out one of the things in our future rate actions which is part of the overall block that we haven't had historically as much rate actions on is Choice 1 and Choice 2 which really represent about a billion 4 of the overall 2.4 $2.4 billion of in-force. As we think about the termination rate and updated assumptions we have, that's an area really I think a big chunk of the future rate actions comes in to play. Historically we haven't had as much focus on that if you think about the 2007 and 2010 rate actions. They were contained to the much older blocks.

Suneet Kamath (Analyst - UBS):

Got it. Makes sense. And a last quick one on long-term care. If we back out the charges and then we back out the benefits from the rate actions of I think $41 million, it looks like the normalized earnings excluding rate actions for LTC in the quarter was negative $53 million which is the worst we've seen. Why we saw some significant deterioration relative to what we saw in the third quarter. I'd expected the DLR charge would improve earnings because you're front loading some benefits but maybe that's not right.

Marty Klein (CFO):

Yes, Suneet, let me just -- I think the core is really -- we could maybe talk about this a little bit off line, but the core is a little bit higher number but it is negative. That's the first time we've seen it negative.

There are a number of kind of nonrecurring things between the reserve, the margin impact at this time. The adjustment that we're having and the reserves we talked about earlier. The error is worth about $44 million. So we do have those things.

But you back all that out, it still is a negative P&L number. I think a couple things are driving that. Really part of it is really related to the claim reserve assumptions we put in place at the end of the third quarter. And there's a couple aspects of that.

One is as new claims come on to the books, we're now setting up significantly higher reserve than we did in the past. So that's a pretty big difference that we're seeing this quarter. Then along the same lines with the new claim reserve approach that we have, we had less in the way of reserve releases on existing claims.

Again, you'll recall we updated our claim termination rates. We think people stay on claim longer. So those dynamics this quarter had a pretty big impact on the quarter. I think that obviously has a current period impact presumably if we have the claim reserve right, that means there will be a lot less drag in future period or hopefully no drag in future periods from the claims that go on the books.

Then the final thing is we have less in reinsurance benefits. I want to say after tax probably $15 million less in reinsurance benefits quarter over quarter if that's helpful.

Suneet Kamath (Analyst - UBS):

My core number just backed out the benefit of the rate actions. That's how I got from your minus 12 to my number. Thanks again. We'll follow up.

Marty Klein (CFO):

The only thing I'd say on that is I think you have to count the premium increases of benefit interruptions we're getting and there's no question going forward we will based on the new claim termination rates and benefit utilization we do need to go back to the old blocks and take that in to account. That's part of why you need the premium increases to benefit reductions going forward that we've laid out in slide 5.

To me, that's a critical part of it. And we obviously would expect -- and these are all the numbers shown on page 5, the annual incremental premiums. So it's a lot of incremental premiums or going forward we think there may be more benefit reductions depending what policyholders decide. I think those are very important to restore the profitability of the in-force Long-Term Care business.

Suneet Kamath (Analyst - UBS):

Understood. Thanks for the time.

Operator:

Sean Dargan, Macquarie.

Sean Dargan (Analyst - Macquarie):

Thank you and good morning. I just want to follow up on the present value of future premiums embedded in your margins. As far as I'm aware, you're the only company assuming future rate increases that have not been either filed or approved.

And Tom's commentary that getting these rate increases are critical, I think puts a seed in some investors' mind that you may have to walk away from the estimates of the benefit that you're going to be getting from these in your margins. So just to be clear, this methodology was signed off by the Delaware regulator and two separate actual actuarial firms?

Marty Klein (CFO):

Hey Sean, it's Marty. I don't want to speak to individual companies but I think those are a number of companies, more than a few that do include future rate actions in their GAAP analysis. It looks to be in the statutory basis as well.

So I don't want to talk about specific companies on this call but certainly can follow up and give you some direction on that off line. I'd also say that on a statutory basis with exception in New York if you look at the guidelines in cash flow testing they typically point to actuarially guaranteed renewable.

Beyond that we did speak with the regulators specifically about this. They agreed it's appropriate to include it with the exception of New York which does not allow for it. And after we developed the plan we then spoke again with them and reviewed it. If that's helpful.

Sean Dargan (Analyst - Macquarie):

Sure. And the actuarial firms you mentioned are also okay with this methodology?

Marty Klein (CFO):

They reviewed all of our assumptions including this and they believe the margin tests and aggregate or margin results and aggregate are appropriate.

Sean Dargan (Analyst - Macquarie):

One follow-up. You wrote down all Goodwill associated with LTC and life but you did not write down DAC or take a DAC charge. Can you just remind us what the difference in accounting in which you have to impair to DAC versus goodwill?

Marty Klein (CFO):

Certainly. It is a different approach. For us as we test goodwill, it's really kind of a two-prong test. One is a test that looks at the overall value including in-force and projected sales and for a while both our life insurance and long-term care lines have failed that particular test so then you segue to another test that really is very much focused on the value of new sales in both life and long-term care as you recall we did partially impair or write off some of the goodwill balances in life insurance and long-term care.

As we now look at where we are this quarter with potentially reduced sales from where we are given rating and other things we may do, we decided to write down all the remaining goodwill. Shifting to DAC, it is a different analysis.

That really frankly is part of the overall margin testing. When you do your GAAP margin testing, if the margins are negative, you first write off the DAC. After the DAC is written down you go to reserves and reset those.

Our margins as you saw on the more GAAP block are still quite positive. Obviously in the future if we decide to report parts of our long-term care business separately from a GAAP accounting standpoint and certain investors have different opinions on that if that makes sense to take some of the older business and put it in a different block and report separately, it would be tested separately and would be DAC write-offs in that scenario.

Sean Dargan (Analyst - Macquarie):

Thank you.

Operator:

Ryan Krueger, KBW .

Ryan Krueger (Analyst - Keefe, Bruyette and Woods):

Thanks. Good morning. On the sensitivities you provided the active life margins, I had a couple questions there. How should we think about the lower interest rates and lower discount rate? In other words if interest rates were lower than your assumption would that also likely lead to a discount rate reconduction on top of that as well?

Marty Klein (CFO):

The discount rate is really a focus of interest rates and spreads. Basically it's effectively the portfolio rate. For GAAP it's the current portfolio rate and we just use that all the way through. And for stat it's whatever the portfolio rate is year by year depending on the test or scenario that's being used in a cash flow testing but it is effectively the portfolio rate and obviously the portfolio rate does depend on interest rates as well as the spreads you're getting on your portfolio.

Ryan Krueger (Analyst - Keefe, Bruyette and Woods):

Okay. I see. So if interest rates are lower as had portfolio yield comes down, you also lower your discount rates so there's essentially two impacts.

Marty Klein (CFO):

Right.

Ryan Krueger (Analyst - Keefe, Bruyette and Woods):

Okay. You show the sensitivities relative to the $4.3 billion statutory margin that's before pads. Can you help us think about what the sensitivity would be to the number that's already after the pads? The sensitivities would be lower BAZ you're already assuming some of this in the pads.

Marty Klein (CFO):

It's a very good point. After pads I think our margins are right about $2.1 billion. The pads are largely for a couple reasons. One is for future rate actions. And the other is really for what we're expecting have on the asset side, the return side. I think you make a good point that the close to $2 billion in pad that we have, actually $2.2 billion in pads we have, those go directly to interest rate related aspects and conservatism there as well as rate action pads.

Ryan Krueger (Analyst - Keefe, Bruyette and Woods):

Got it. Then if the BLAIC, can you give us an update on how the statutory and capital is on BLAIC and what the anticipated impact of repratriaing that would be?

Marty Klein (CFO):

Sure. BLAIC's RBC did go up about 100 basis points during the quarter to about 345% at year end. The biggest part of that had to do with this tax benefit we got from this LPI kind of restructuring and that really contributed most significantly other BLAIC's RBC increase this quarter. In addition there was a smaller timing impact related to a repatriation of small block term business that was in there. So BLAIC's RBC is now 345%. The overall capital level in BLAIC is just over $800 million.

Ryan Krueger (Analyst - Keefe, Bruyette and Woods):

Thank you.

Operator:

Colin Devine, Jefferies.

Colin Devine (Analyst - Jefferies):

Good morning. I guess a couple questions. First, Marty, you intimated the possibility you're considering a closed block and based on your comments that there would be a DAC impairment. Is it fair to conclude if we do look at what you defined as the old block here, it would fail the margin testing, so there is a deficiency on that is the first question.

Second, and perhaps can talk about this, when you're looking at the changing the investment strategy, how much is that impacting the margin testing you've done here? And what I'm getting at, how dependent on it -- how dependent is the testing on the success of that strategy? So if we could clarify that.

Then for Tom, I guess, Tom, I'm scratching my head here because you're telling me the MI businesses are getting better and yet I'm looking at your guidance for next year and you're guiding for lower loss for weaker loss ratios in both Australia and Canada versus what they had in 2014? So maybe you can reconcile that since frankly I think you're forecasting some fairly significant increases in the loss ratios for both of them.

Marty Klein (CFO):

Let me start off on your first question. The historical GAAP block really except for the acquired block, business acquired in 1996 and before, represents a lot of the older generation as well as the newer generation, everything modeled in aggregate. I think it's very fair to say that the older blocks are performing much less well, in fact losing money versus the newer block.

The overall margin we have on GAAP clearly -- well, maybe not that clearly, is a function of some of the newer business that has very, very positive margin and that offsets to some extent what would be presumably negative margin in the newer block.

So if we did at some point, and I notice this is in your note, take some part of the old long-term care business and report it separately and manage it differently that would likely create a DAC loss. We're looking at a lot of different things right now as Tom mentioned and so that would be something that could happen. We're still assessing that along with a variety of other things.

With respect to your second question, I'd say the reinvestment strategy and cash flow testing, it's a reinvestment strategy that is pretty typical with insurance companies. We've had a very high credit quality portfolio in long-term care, particularly given the long duration nature of it. In fact, in the new reinvestment strategy the credit quality in the long duration stuff is still very high.

But as we are looking to, like many other insurance companies, get a little more spread, we intend to reinvest in a little bit lower credit quality things such as the average portfolio with triple B plus.

Similarly we also have had historically next to nothing in term of term investments. I think a number of insurance companies have 3, 4, 5, 6, 7%. We've had close to zero. So we'd build that up to about 5%. I think those things in the model because it's the reinvestment strategy and it's a very long duration portfolio, it takes quite a long time in the model to build up and make a bigger impact.

In the case of bond portfolio, I think it takes 15 to 20 years and on the case of alternatives, it probably takes about a dozen years or so to build up to that 5% allocation. Clearly alternative investments have a higher return in them than do fixed income bonds these days. That was what was the remodel. Now I'll turn it over to Tom for your last question.

Tom McInerney (President, CEO):

Colin, I would say that first of all, we were pleased with the performance of all three of the MIs in 2014. If you look at that one slide that Marty showed in terms of how they performed against the targets we set at the beginning of the year, it's all green on that page. I would say we think they're good businesses. They're performing well.

The loss ratios in 2014 were well below what our target were and so I think my feeling, I'll let Kevin talk specifically about 2015 in the guidance that they were very low. We think over time based on the historical performance in those markets that those loss ratios in 2014 were so good that they're probably not sustainable at that level. We still think 2015, the loss ratios will be good but I'll turn it over to Kevin to give more specifics on 2014.

Kevin Schneider (President, CEO):

The guidance as stated in Marty's remarks, in Canada we're expecting it to be between 20% and 30% next year. Had great experience this year. I think the thing, and to Tom's point, I don't think it's sustainable. It's still even in our guidance, it's well within the range on our pricing expectations on Canada where we price the business. I think we just need -- we're a little cautious as we observe the impact, through 2015 what the oil price is going to do to the country.

That's something we're watching very closely. We think that's probably going to tap down the overall home price appreciation experience in Canada. And might have some pressure relative to the oil price. In fact on overall unemployment. So I think we're a little bit more cautious on it but still a solid loss ratio performance. In Australia we're targeting a 25% to 30% range in Australia.

I think it's a lot of the same type dynamics. The Australia economy is holding up pretty well but obviously the RBA is concern would the strength of the economic growth. They've reduced cash rates and cut their rates. I think they're expecting some challenges to the economy. We think there's absolutely going to be a moderation in home rates down there.

We've benefited significantly in 2014 from curates in Australia where we've sold houses and not even experienced any losses associated with it because of the high home price appreciation level. I think that's going to tap down. Still very solid pricing, well within our pricing expectations.

But it is going to moderate I think off of what have been two very, very favorable years from a loss ratio perspective. And the US business is going to grow. It's going to continue to grow and experience I think a decent year in line with Tom's comments.

Colin Devine (Analyst - Jefferies):

Thank you. One follow-up for Marty. Marty, lifestyle protection, I think you acknowledged there's going to be a significant loss, I think that was the adjective used if you're able to sell it. Given that, why wasn't DAC impaired at a minimum? It seems to me effectively you acknowledged that $248 million has gone so why not clear the deck at this quarter?

Marty Klein (CFO):

Yes, in a sense it would be nice to clear the deck but we do have to follow GAAP accounting rule. I'd say where we're launching a process, the GAAP accounting for this really means it to do what you describe would really entail calling it discontinued operations and I think to do a lot of that, so if you have to have a pre-tangible plan where you feel extremely confident that you actually would execute a sale within about a year time frame.

So while we're launching the sale and hopefully we'll be in position where later on in the year we'll be in position to execute the sale, I think we're not quite to that point where we can get to that GAAP accounting threshold and do that. I would say certainly our intent to sell it hopefully later this year. We've launched that process.

I don't want to comment on the evaluation we expect to get from LPI but we do want to make sure you and our investors and analysts all understand that I think it's quite likely to be below and probably well below the current GAAP book value. But we're not really quite at the point yet from a GAAP accounting standpoint where we're able to make that change in our accounting.

Colin Devine (Analyst - Jefferies):

I hope you can get there in the next quarter. Thanks.

Tom McInerney (President, CEO):

The farther along we get the better along, we hope we move it along too. Thanks, Colin. By the way, the definitive on your question on the cash flow testing, yes, we absolutely would pass cash flow testing without this reinvestment strategy handily. So it didn't have so much of an impact that we'd have negative margins.

Colin Devine (Analyst - Jefferies):

But it is fairly dependent on the assumptions of the new business and it's still early days for those to be fair too, right?

Tom McInerney (President, CEO):

Yes. I think the impact on a GAAP basis 4.9, it's pretty similar on stat so you can certainly wind it in. We wanted people to know in that assumptions in the amount of premium in the assumption. Absolutely.

Colin Devine (Analyst - Jefferies):

Okay. Thanks.

Operator:

Geoffrey Dunn, Dowling and Partners.

Geoffrey Dunn (Analyst - Dowling and Partners):

Thanks. Good morning. A little change in questioning. I was a little confused on domestic MI this quarter. Was there or was there not an additional loss of accrual this quarter?

Tom McInerney (President, CEO):

Geoff, there was not an additional loss of accrual. What we've seen in the US business, what we're continuing to see positive emergence of our early term delinquencies. We made no adjustment to our factors associated with that.

We'll continue to watch for sustained performance before we make those adjustments but we're probably reserved at the 1 in 6 times from a frequency standpoint, trending more toward 1 in 7 but we need to see more sustained performance on that. On the other side of it we still got to be prudent I think as we watch severity.

Severity has been kind of sticky. The older adults continue to age. When you look at that all together, our reserves are performing, our business is performing consistent with our reserve expectations but we had no adjustment this quarter.

Geoffrey Dunn (Analyst - Dowling and Partners):

Okay. Then you also alluded to discussions with reinsurers. Are there any new reinsurance agreements this year? And are you still looking at O?

Tom McInerney (President, CEO):

We put no insurance in place. We made nice progress working in the US business, if that's your question, with re-insurers consistent with our plans to be compliant from a PMIER standpoint. So we've made a lot of progress with the re-insurers. Where we stand though is we still don't have the PMIER standards. They're not final. Until they're final, we won't know exactly how they're going to gauge the insurance. So we're working on that and good review right now with the GSEs as well as with our state regulator.

Geoffrey Dunn (Analyst - Dowling and Partners):

At this point you're still going down the quota?

Tom McInerney (President, CEO):

At this point in time that would be our approach.

Geoffrey Dunn (Analyst - Dowling and Partners):

Great. Thank you.

Operator:

Steven Schwartz, Raymond James.

Steven Schwartz (Analyst - Raymond James):

Good morning, everybody. A lot has already been answered already. Marty, your description of the profit pattern for GAAP on LTC, are you basically referencing SOP-301? Is that how this is going to work?

Marty Klein (CFO):

Not exactly and I was wondering when this question would come up because it is a new phenomenon for us. And again, what we're seeing here in our margin testing for GAAP is the kind of expected pattern of earnings is over the next 15 or 16 years we have positive earnings then it becomes negative after that kind of under the way we've been reporting and that as those losses kick in after about year 15 or 16, the value of those losses is about a billion 2. You take the 3.5 billion and negative, you still have positive margin at 2.3 billion.

But GAAP accounting, under GAAP accounting when you have a period in the future where there are losses, you do need to accrue liability for that. Beyond that though there's not really any clear GAAP accounting guidance on exactly how to do that so we're working with our accounting teams and our auditors to develop the approach and I think there could be a variety of approaches depending on how we decide to do that and working in conjunction with our auditors.

I think what we'd anticipate doing is that -- what we'd anticipate doing is taking, given that we now have a different view of severity on existing book, we'd probably take some of the future rate actions on this existing book we're tending to get and rather than having the normal course as we would do, have it all hit the bottom line as we get those additional premiums or as you get reserve releases, we'd rather take some of that benefit and fund liability for those future losses.

Again I'd remind you this really relates to the business, the margin testing, year end so any new business we'd write is really not part of this. It's really reflective of the block we have on the books right now. Basically what we'll take is part of the benefit we'd get from future rate actions, rather than hitting the bottom line, we'll take some of that and build up an incremental liability to fund those losses so that billion 2 of losses would be effectively zero with that liability we'd build up.

Steven Schwartz (Analyst - Raymond James):

Okay. So the use of benefit factors and what have you that you might do for GMIB or SG is not necessarily -- that's not necessarily the way it's going to work?

Marty Klein (CFO):

No, no, no, not at all. This is all within the existing block we have of long-term care. Basically as we're projecting forward we'd take our new view of claims which creates some losses in future years along with our new view of future rate actions and kind of change the accounting recognition for those future rate actions so that some of that would be building up as a liability or reserve against those billion 2 losses. It's all within the long-term care of business.

Steven Schwartz (Analyst - Raymond James):

Right. I understood that. I guess my question goes back to -- I don't have a page number on here. Page 3 of the long-term care insurance margin testing. The present value of future claims and expenses is $40.7 million. The present value of future premiums is $27.3 million on the H gap block. Does that mean I'm going to have a benefit ratio benefits divided by premium of -- I think that's 150%?

Marty Klein (CFO):

Yes, I'm not sure I'd look at it quite like that. In fact, this doesn't really change the margin testing. What it does is it changes the pattern of GAAP earnings recognition for the future rate actions. I think that's maybe a way to think about it. Let's go on the status quo where we'd change nothing.

Where we'd see is over the next 15 or 16 years we'd get these premiums or reserve and that would hit the bottom line and that would help benefit the next 15 or 16 years. Then you get to those later periods beyond 15 or 16 years and a lot of that benefit would already be recognized in our GAAP P&L and then you've got these higher claim actions and higher severity expectations would lead to losses in future years.

So rather than doing that, what we need to do is set up an accrual for a liability to fund that period of time where those were future losses. The way that we'll do that is we will not recognize the full benefit of those additional premiums or the full benefit of reserve releases but rather we'll recognize only part of that benefit and set aside the remainder of that benefit and kind of accrue reserve or liability.

Steven Schwartz (Analyst - Raymond James):

So profit liability is what you'll set up. Okay. Then for Tom, I can't find the number here, but I thought I saw the debt total capital is currently 25.9%. Was that correct?

Tom McInerney (President, CEO):

That's correct.

Steven Schwartz (Analyst - Raymond James):

That doesn't strike me as ridiculously high. I mean a lot of companies are around 25%. I don't understand why you think you really need some significant action here.

Tom McInerney (President, CEO):

So again, I'd say, Steven, it's based on the options we're considering. Including a number of investors and shareholders over time have talked about a split. With $4.6 billion of debt at the holding company and today Australia and Canada being the primary sources of cash capital to service the debt, our feeling is to have a broader array of options that we could consider, again, we've made no decisions on any of these.

We believe we have more flexibility if the debt was 1 to 2 billion lower than it was today. We have talked to the rating agencies. We've talked to regulators and certainly we've heard from a number of investors over time and I do think that given the level of debt and given today's payers if you will of the debt service, now USMI we think in a few years as the loss shares goes away, it will also be a payer of dividends.

We don't think -- we have long-term care. We are looking to improve the capital RBC capital supporting long-term care and therefore we don't expect a lot of ability at least in the next few years to pay dividends. It's really to have flexibility to consider a broad array of options that are feasible we believe and are outside financial advisors have also confirmed we'd have to reduce the debt around that range given the current cash capital generation of our operating subsidiaries.

Steven Schwartz (Analyst - Raymond James):

Tom, you referenced a split. I assume you were reference the split from life insurance.

Tom McInerney (President, CEO):

Right. A number of investors have talked about that.

Marty Klein (CFO):

Again, we haven't made any decisions and I think the debt paydown Tom talked about would give us flexibility to do other options whatever they are. I think with our current earnings streams amid the businesses, I think that lower is quite manageable.

What we'd like to do is pay down a billion or couple billion to have more strategic flexibility. I think with the status quo of what we'd have, we certainly think it's very manageable with the flows we'd be getting from Canada, Australia, US life we're going to really sit tight on as far as dividends for the next year or two and let that capital base build back up.

Steven Schwartz (Analyst - Raymond James):

Okay. Thank you.

Operator:

Scott Frost, Bank of America .

Scott Frost (Analyst - BofA Merrill Lynch):

Thanks. Just wanted to make sure I understood this, on slide 3, you're talking about for example, $32.7 billion is the PV of future claims. You're saying that increased by $5.4 billion. Is that what you called out in the release? You're offsetting that by $4.9 billion of additional premium increases. This leads to the second question here. Is that the right -- am I thinking about that the right way?

Tom McInerney (President, CEO):

Right, the $5.4 billion is really represented in the present value future claims expenses lines. So that's larger by that $5.4 billion. There's one distinction on the GAAP versus stat. One is GAAP is pre-tax and $5.4 billion is a pre-tax number. Then similarly the additional premiums, $4.9 billion pre-tax future premium benefits are really reflected in the present value future premiums row.

Scott Frost (Analyst - BofA Merrill Lynch):

That's what I wanted to ask about. You talked about earlier the premium increases that you're going to get that have already been approved plus incremental expected additional premiums, it looks like about if I look at sort of midpoint it looks like a billion annually or whatever is what you're supposed to be getting, am I assuming kind of a similar ratio in that $4.9 billion of rate increases you've already gotten versus rate increases you expect to get?

Marty Klein (CFO):

To be clear, and I'll refer folks to I guess it's slide 5, that 4.9 billion of benefit, pre-tax margin references is really associated just with the incremental premium that we would get in the future. At its peak, that's $525 million to $625 million. What happens is as we implement that, you look at that in our modeling, it kind of builds up over time.

Takes us about 15 years to get that fully implemented. It ramps up pretty slowly and actually ramps down pretty quickly as the number of active lives paying that premium comes. It's really about four, five, six years we're getting additional premium in that neighborhood. The $4.9 billion is associate would the anticipated peak actual additional premium.

So the other premium that we reference that we've gotten to date, the 380 to 470 is trying to give context to folks what we've already achieved the last few years with the rate actions. That's already because it's been approved. Already built in to our margin testing.

Scott Frost (Analyst - BofA Merrill Lynch):

Okay. I should have asked more simply. Of the $4.9 billion of premiums you expect to get, how much of that has already been done?

Marty Klein (CFO):

That's all in the future.

Scott Frost (Analyst - BofA Merrill Lynch):

That's all in the future. But that has to be requested from regulators and approved?

Marty Klein (CFO):

That's right.

Scott Frost (Analyst - BofA Merrill Lynch):

For your debt reduction, what I count, it sounds like over time, and I'm looking at your debt maturity schedule. Looks like you've got $300 million, $600 million in 18, $400 million in 20. Is that the time period I'm thinking about for your debt reduction plan? Is it normal amortization? Is that the timeline we're talk about? And do you consider the 6.51%, 66 to junior subs, is that contemplated as part of the plan of reduction?

Marty Klein (CFO):

You know, there's different ways to pay down the debt. One is just with the passage with time really just pay off the maturities and really the next item maturities we have a $300 million and $600 million respectively.

That's certainly one way to do it. I think what Tom described as we look at the strategy, is there anything we should be doing differently and options we should be looking at that if we did choose those, those might accelerate those paydowns if we sold the business or did something different or a variety of different things, would that create capital to give us the opportunity to do it quicker? So obviously how we think about the paydown of debt is going to be a function of what we decide to do strategically and they're very intertwined.

Scott Frost (Analyst - BofA Merrill Lynch):

So again that sounds like -- that implies tenders or open market purchases?

Marty Klein (CFO):

Exactly right. For example, if we sold a business and had some capital, we might say then let's -- rather than waiting for the maturity, we might do a tender. And again we have different tenors with different maturities and different costs. And we'd look at all that in that particular market and decide if we wanted to do a tender or open market purchases or what have you.

Scott Frost (Analyst - BofA Merrill Lynch):

Okay. Great. Thanks a lot. That's it from me.

Marty Klein (CFO):

Thank you for your question.

Operator:

And ladies and gentlemen, I'll now turn the call back over to Mr. McInerney for closing comments.

Tom McInerney (President, CEO):

Thank you, [Christy]. And thank you for everybody on the phone today for your time and your questions. And although we may not have answered every question about all of our future actions, we hope you have a sense of our focus and priorities and that you found today's discussion helpful.

While our challenges are both complex and substantial, we are confident that our actions to date and this strategic review of future actions we're now looking at will serve to continue to grow our mortgage insurance businesses, will rationalize our life insurance business while leveraging our leading position in long-term care to significantly improve in-force profitability and improve the way the LTC industry is regulated. I can assure you our management team is determined to build businesses for the benefit of all of our stakeholders. Thank you very much.

Operator:

Ladies and gentlemen, this concludes Genworth Financial's fourth quarter earnings conference call.