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GNW - Q4 2011 Genworth Financial, Inc Earnings Conference Call

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PRESENTATION

Operator

Good morning, ladies and gentlemen, and welcome to Genworth Financial's fourth-quarter earnings conference call. My name is Jovan 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, speakerphones, or headsets during the Q&A portion of today's call.

I would now like to turn the presentation over to Georgette Nicholas, Senior Vice President of Investor Relations. Ms. Nicholas, you may proceed.

Georgette Nicholas - *Genworth Financial, Inc. - SVP IR*

Good morning and thank you for joining us for the first of two calls Genworth will be holding today. The first hour call will be dedicated to a discussion of fourth-quarter results. The second hour call will begin at 11 a.m. after our Canadian subsidiary completes their earnings call. In the second call we will focus on 2012 and specifically addressing low interest rates, European exposure, the statutory earnings profile of the Life Companies, and key business goals for 2012.

Also, as a reminder, we will be holding a webcast on Friday, February 10, from 10 a.m. to noon on our U.S. Mortgage Insurance business. Please note our press release and financial supplement were released last evening and are posted on our website.

This morning you will hear from two of our business leaders, starting with Mike Fraizer, our Chairman and CEO, followed by Marty Klein, our CFO. Following our prepared comments we will open the call up for a question-and-answer period.

In addition to our speakers, other key leaders will be available to take questions. They include Pat Kelleher, President and CEO of our Insurance and Wealth Management Division; Kevin Schneider, President of our U.S. Mortgage Insurance segment; Jerome Upton, Chief Operating Officer of our International segment; Ron Joelson, Chief Investment Officer; and Buck Stinson, President, Insurance Products, for our U.S. Life Insurance segment.

With regard to forward-looking statements and the use of non-GAAP financial information, some of the statements we make during the call this morning may contain forward-looking statements. Our actual results may differ materially from such statements. We advise you to read the cautionary note regarding forward-looking statements in our earnings release and the Risk Factors section of our most recent annual report on Form 10-K filed with the SEC in February 2011.

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

And finally, we talk about results for the International Protection and International Mortgage Insurance segments, please note that all percentage changes exclude the impact of foreign exchange.

And now, let me turn the call over to Mike Fraizer.

Mike Fraizer - *Genworth Financial, Inc. - Chairman, President, CEO*

Thanks, Georgette. 2011 was a year of actions designed to reposition the Company to move through an uncertain environment and provide a foundation for improved shareholder value. We recognize that the year was a difficult one for shareholders and have worked to listen, gain feedback, and intensify our efforts to improve both the performance and positioning of the Company.

We have taken important steps with the business portfolio and individual product lines to sharpen our focus, rebalance exposures, maintain or expand risk buffers, and support capital generation and redeployment. We made progress in several areas, with more work to do, and will maintain an intense execution focus in 2012.

There are many aspects of markets that one does not control. Today, I would like to highlight four important levers that we do control and actively utilize to improve future operating performance.

First, we continue to reposition the business portfolio to maximize value over the medium to long term. We are pursuing a number of steps to better align businesses, enhance risk profiles, and reallocate capital to support shareholder value.

Second, we are managing the volume and mix of new business, repricing products actively, utilizing reinsurance strategically, and managing expenses, all to maximize profitability, benefit statutory performance, and improve our capital generation use and return profile.

Third, we are managing the in-force portfolio through loss mitigation strategies, repricing actions, life insurance block transactions, and active management of investment exposures.

And fourth, we are taking actions to add to our enterprise and Holding Company strength by expanding risk buffers and managing overall risk exposures and capital effectively. A key focus here is adding to our capital flexibility and distributable earnings profile to support dividends to the Holding Company which benefit shareholders and bondholders.

As you saw in our earnings release, we re-segmented our financials this quarter. This reflects moves to align businesses to maximize operational and financial synergies. We are now operating through three divisions with six underlying reporting segments.

There are clear benefits from our new structure. On the product and risk management front, we are getting better transfer of ideas, analytics, and mortgage insurance loss mitigation strategies under this alignment. From a financial synergies standpoint, we now have an approach in place that accelerates use of our tax assets, and we have been able to improve the efficiency of capital structures.

I would like to provide some perspectives on the four key levers we control and how they impact each division. Starting with Insurance and Wealth Management, I am pleased with the progress we are making to reposition the portfolio. We have exited nonstrategic lines such as variable annuities and Medicare Supplement, to better concentrate on our strongest market positions. We continued this in January with the announced sale of our

Tax & Accounting Advisors unit, Genworth Financial Investment Services, or GFIS. This sale will allow us to focus on our core turnkey asset management businesses. We expect to receive $79 million in proceeds from this transaction and have an additional earnout opportunity.

We are being selective regarding new business. We have implemented product design changes and repriced many products across life and long-term care insurance as well as fixed annuities, and have chosen not to follow certain competitor price changes. In long-term care insurance we introduced our next-generation product with higher pricing, to reflect today's lower interest rates while continuing a focus on preferred risks.

In International Protection, we have focused on improving pricing and risk-sharing arrangements and changed the business model to withstand higher unemployment. Given revenue pressure from the low growth environment in Europe, we are entering or considering select new countries through reinsurance or small capital investments to rebalance our European concentration over time and support segment revenues.

We are managing our in-force portfolio in long-term care through care management and are executing our second round of price actions, where we have received approval in 39 states. And in lifestyle protection, margins have improved nicely over full-year 2010, given pricing, risk, and cost actions.

Finally, we remain focused on managing product mix, transactions, and platforms outside the U.S. Life Companies to maximize statutory earnings and improve capital profiles. We expect to continue shifting sales mix between life and long-term care versus attractively priced fixed annuities that are less capital intensive. We are utilizing reinsurance actively in life and long-term care insurance to optimize new business capital needs.

In addition, targeted transactions have improved and will continue to add to Life Company unassigned surplus. These include the gains from unwinding and resetting forward starting interest rate swaps, and the first life block transaction, which Marty will discuss in more detail.

Finally, sound operating dividend generation by International Protection and Wealth Management benefit the Holding Company.

Turning to International Mortgage Insurance, we continue to move forward with our planned minority interest IPO of up to 40% of Australia Mortgage Insurance. We still anticipate second-quarter 2012 execution. We have not encountered any regulatory or market conditions that would change that timing.

The planned IPO supports objectives to rebalance the portfolio, maintain control of our strategic Mortgage Insurance platforms in Australia and Canada, add to risk buffers if conditions warrant, and redeploy capital.

Regarding new business, we have maintained pricing discipline and guidelines in a competitive environment. In Canada, we are working to gradually rebuild share as government guideline changes, such as lower amortization product and lower LTVs and refinancings, have contributed to a smaller market. Australia has seen a larger origination markets, and we renewed a number of key commercial relationships during the year while maintaining pricing discipline. In Europe, we reduced new business over time, given the economic environment, and stopped writing in some countries.

We continue to manage the in-force portfolio to minimize losses through our loss mitigation activities such as workouts, settlements, and asset management. On the capital front, International Mortgage Insurance achieved its dividend goals and remains a strong generator of capital, as large older book season and smaller new books are written. We are also managing our capital and risk through the establishment and use of global external reinsurance markets in certain countries. So, as we look forward over the next few years, we expect capital generation to increase from these platforms.

In U.S. Mortgage Insurance we saw improved financial performance over the past two quarters, but there is still a way to go here for recovery given a tough market. Our focus remains on risk containment of the in-force portfolio and claims-paying ability. On this front, we remain active in the area of loss mitigation and continue to derive substantial results, with year-to-date benefits reaching $567 million.

In assessing our in-force book, we place a strong emphasis on internal and third-party analysis of our claims-paying ability. And we continue to see adequate claims-paying ability and positive value in the business platform, which Kevin will discuss in greater detail on our February 10 call on U.S. MI.

We saw an increase in flow new insurance written over the prior year and prior quarter. Mortgage Insurance penetration is up versus the FHA, especially in the purchase market. We estimate that our market share is flat, despite reallocations after exits by competitors, as we have maintained our pricing and guideline discipline. And our post-2008 books of business are very profitable, significantly outperforming expectations.

Regarding our ability to write new business, a complete evaluation must take into account several factors including risk to capital, claims-paying ability, assessment of where books of business are in the loss curve, and finally capital alternatives. We invest appropriate time with regulators, customers, and others to help support this comprehensive assessment approach.

We have the following alternatives to support new business currently. First, we currently maintain regulatory waivers or other authorizations from 44 states that permit the Company to continue writing new business while its risk-to-capital ratio exceeds 25-to-1. Second, we have a subsidiary called Genworth Residential Mortgage Assurance Corporation, or GRMAC, which has capital supporting approximately one year of new business capacity nationwide, depending on new volume levels. This entity can be used with GSE approval, and currently five states are being written out of GRMAC.

Third, we continue to work constructively with GSEs and regulators on creating additional flexibility through alternative structures that support future business, which could be funded internally, externally, or through a combination of the two. We also maintain the four demanding screens discussed on prior calls, which would inform any future decision to provide additional capital support to the U.S. MI business. As we outlined last quarter, given the alternatives in place and our adequate claims-paying resources, we have no plans to contribute capital to U.S. MI.

Finally, we have made ongoing progress in building buffers and managing overall capital and risk profiles at the Holding Company and operating businesses. At the Holding Company, we ended the year with approximately $950 million of cash or highly liquid securities, up $250 million from third quarter. The increase was driven by a series of actions taken throughout 2011.

We have continued to actively manage our investment portfolio, reducing certain exposures, particularly in financials, and believe our European portfolio is well positioned. We have also managed our capital levels carefully at the operating platform level and been very active over the past 10 years in executing forward interest rate hedges to protect against low rate environments. We will go into further detail on the second call later this morning on how we are managing our exposures on the European asset and liability side, as well as how we are addressing the low interest rate environment.

We have also streamlined costs across our platforms to enhance competitiveness, adjust to the realities of slower markets, and match a more concentrated product and distribution focus. All of our strategies and steps across our four levers -- to improve business alignment and reposition the portfolio, be selective regarding new business, manage the in-force intensively, add to risk buffers at the Holding Company, and pursue targeted capital strategies -- support our goal of accelerating redeployment of capital and improving shareholder value.

It is fair to say that 2011 was a challenging year from a market standpoint, and a humbling year from my seat. Through the year, we intensified our focus and actions to improve Genworth. While we have made progress, we recognize that more work remains and so must our intensity. Through enhanced focus, our business platforms today are deeper and stronger within their large target markets.

We also have made a number of moves on the people front to strengthen the team and our capabilities. So our commitment remains one of driving execution, taking the steps we need to, and building value.

Now, let me turn it over to Marty. Marty?

Marty Klein - *Genworth Financial, Inc. - SVP, CFO*

Thanks, Mike, and good morning. I will begin today with the segment results in the fourth quarter, then provide an update on the Holding Company, and wrap up with a discussion on accounting changes impacting future quarters. I will start with the Insurance and Wealth Management Division, where operating earnings increased 12% from the prior year to $145 million, driven by results in the U.S. Life Insurance segment.

Our operating earnings were down sequentially, mainly from International Protection and results in the Life Insurance business. Insurance earnings were $60 million for the quarter. We continued to see sound new business performance impacting our results as well as favorable mortality experience versus pricing.

Term UL and other universal life sales were down approximately 4% from the third quarter. We expect sales to continue to moderate in the first-quarter 2012 due to our previous pricing actions and capital discipline.

We continued to use reinsurance on new business to manage capital effectively and expect a capital benefit of approximately $25 million per quarter in 2012. In addition, we are completing our first life block transaction, which will generate approximately $100 million in initial after-tax capital benefits for the Life Companies. We have executed the reinsurance treaty and are redeeming associated bonds under the terms of last month's successful bond tender. The transaction will be completed in the next few weeks.

Long-term care earnings were $38 million for the quarter. The reported loss ratio of 67% improved over the prior year and the prior quarter. We experienced low claim termination rates versus the prior year, but we did see lower new claims compared to the third quarter as well as an increase in active policy terminations, primarily in our older issued policies.

Additionally, our previously announced premium rate increase on a majority of the older issued policies has begun to take effect. We still expect the continued impact in 2012 will add about $50 million in additional premium in 2012, and about $60 million in 2013 when fully implemented.

We are closely watching the performance of the older business and will assess potential additional rate actions accordingly. We continued to see sound performance across the block of newer issued policies, with a loss ratio of 50%, in line with prior quarters. As we manage capital and risk we use reinsurance on new business, reinsuring about 40% of the new long-term care product.

Fixed annuity earnings were $16 million as we adjusted for the state guarantee funds assessment. In December we launched our new suite of indexed annuity products, designed to further enhance our annuity product offerings. We expect to increase sales in 2012 by approximately 10% as we adjusted the sales mix of our products to build capital and statutory earnings in our Life Companies.

International Protection reported earnings were flat to the prior year and decreased 24% sequentially due to top-line pressure, as European economic concerns reduced consumer and related insurance product sales. Despite the top-line pressures, full-year operating margins improved more than 360 basis points over 2010 results, returning to 2008 pre-recession levels.

Wealth Management earnings were $12 million for the quarter. All-in, 2011 full-year net flows were a positive $1.4 billion, despite a challenging environment and the negative net flows in the fourth quarter.

Last month we announced an agreement to sell Genworth Financial Investment Services, or GFIS, to Cetera Financial Group. GFIS accounted for about 14% of Wealth Management's earnings and about 11% of assets under management in 2011.

Turning to capital, International Protection and Wealth Management paid $199 million in dividends to the Holding Company in 2011. With respect to statutory capital for the U.S. Life Companies, the unassigned surplus at year-end is estimated to be in excess of $50 million.

The RBC ratio topped 400% as we completed the sale of our Medicare Supplement business during the quarter and also realized tax benefits from locking in gains on our forward starting interest rate swaps. We still intend to dividend up to the Holding Company a significant portion of the proceeds from the Medicare Supplement sale over the course of this year, subject to regulatory approval.

As an important part of our strategy to reestablish ordinary dividend capacity from our Life Companies by 2013, we are working on executing several initiatives to grow capital, statutory earnings, and unassigned surplus in order to restore this capacity. And we will expand on these in our 2012 business goals call.

Moving to the International MI segment, reported earnings were down by $20 million from the prior year, and earnings decreased 24% when excluding FX. Underlying performance for the quarter was mixed.

Unemployment rose slightly in Canada and was flat for Australia, while the housing markets are performing as expected. In Europe, the uncertain economic environment is creating pressure in some countries, particularly Ireland.

In Canada, excluding FX, operating earnings for the quarter were down 15% from the prior year. The loss ratio increased 4 points sequentially to 40% from a reserve strengthening associated with higher severity on existing delinquencies.

In Australia, excluding FX, operating earnings were down 9% from last year. The loss ratio decreased 2 points sequentially to 46%, reflecting a decline in new delinquencies.

The delinquency rate improved across all regions sequentially. As part of our risk and capital management strategy, the Australian business continued to expand its reinsurance program.

Combined, Canada and Australia paid dividends of $215 million to the Holding Company in 2011. And both platforms continue to generate capital as smaller books are written and the larger books continue to season.

The operating loss in other countries in the International Mortgage segment was $15 million from losses driven by the European economic environment, primarily in Ireland from higher delinquencies. Ireland is seeing increased new delinquency development from prolonged economic stress and significant home price declines.

After several years of limiting new MI business in Ireland, we stopped writing the business altogether midway through last year. In addition, we have been working to manage our exposure in Ireland through loss mitigation. We will expand on this subject as part of our discussion of the impacts of European exposure for our Company on our second call this morning.

Turning to U.S. MI, results continued to be impacted by weakness in the US economy. Flow NIW increased 23% over the prior year and 19% sequentially, reflecting the continued gradual shift away from the FHA and higher refinancing activity. Our estimated market share remains flat at about 14% as we maintain pricing discipline.

Our total flow delinquencies decreased 1% sequentially, with new delinquencies down both year over year and sequentially, reflecting the continued burn-through of the 2005 through 2008 book years as well as a favorable impact from the geographic mix of new delinquencies in the quarter. Redefaults on modifications continued to be within our ultimate expected range of 25% to 30%.

Shifts in the payment status, or aging, was relatively stable, while we did experience fewer net cures, driven by declining loss mitigation, consistent with our reserve strengthening in the second quarter. Our average flow reserve per delinquency is relatively flat at $29,100; and our total amount reserved for flow delinquencies by category is consistent with the third quarter.

Loss mitigation savings in the quarter eased to $147 million with workouts declining 16% as HAMP modifications wind down.

Our combined U.S. MI statutory risk-to-capital ratio increased to 28.8-to-1 in the quarter. GEMICO currently maintains waivers and other authorizations in 44 states, and we are now writing business in five states out of Genworth Residential Mortgage Assurance Corporation, or GRMAC, which is a subsidiary of GEMICO. Those five states account for about 10% of NIW.

In the quarter, GRMAC's capital increased modestly to approximately $76 million, and its risk-to-capital ratio is 1.6-to-1. We continue to believe that we have about one year of new business capacity across 50 states in GRMAC.

Moving to the Corporate and Runoff Division, improved variable annuity results driven by better market performance were offset by lower earnings from the sale of the Medicare Supplement business, as well as an after-tax goodwill impairment of $19 million related to the reverse mortgage business. This business was acquired in 2007 and offers products that provide liquidity and retirement income to senior market consumers.

Shifting to investments, the global portfolio is performing well. Core yields were down slightly at 4.6% in the quarter. Results reflect the lower limited partnership income as well as higher cash balances, which are being reinvested over the next few months.

Impairments were down slightly in the quarter and from the prior year. We have $700 million or less than 1% of the portfolio in European periphery exposure, which is down $185 million from the third quarter primarily due to opportunistic sales.

Turning next to the Holding Company, we remain very focused on maintaining appropriate risk buffers. We also are making headway in our strategy to create further dividend streams to the Holding Company, particularly in U.S. Life Insurance. These are important steps in maintaining our financial strength for policyholders, bondholders, and shareholders.

At the end of the fourth quarter, the Holding Company held cash and liquid securities of approximately $950 million, which is about $400 million over our cash buffer target of 2 times debt service coverage, and we expect to maintain a similar excess in this uncertain economic environment.

While we are moving forward with the minority interest IPO of the Australia Mortgage Insurance business, our risk buffer plans are not dependent on this transaction. We continue to navigate the Company towards a long-term leverage ratio in the 24% to 26% range, which is equivalent to our previously communicated range of 22% to 24%, adjusted for the new DAC guidance. The Holding Company received $478 million in dividends in 2011.

Let me now cover some accounting changes being made in 2012. We are adopting the FASB's new DAC guidance and expect the impact will be a reduction in retained earnings and stockholders equity of approximately $1.4 billion. We will defer fewer costs, but record lower amortization.

In describing the earnings impact going forward, there are four main drivers -- sales growth, product duration, product mix, and distribution mix.

Relative to our competitors, we believe the expected impacts are similar in our life and annuity product lines, but different in long-term care. Over the last couple of years, sales of our long-term care product have generally grown faster than many others in the industry.

Additionally, the retail distribution channel is a relatively large percentage of our sales volume and is more negatively impacted from lead generation expenses that are no longer deferable. While not impacting economic or statutory results, in 2012 we expect a negative impact on GAAP earnings from the new DAC guidance of about $65 million to $75 million or about $0.13 to $0.15 per share, with an impact of approximately $20 million to $25 million in life insurance and $25 million to $30 million in long-term care. We continue to evaluate a number of options for adjusting distribution and marketing structures to mitigate the effects of this new standard.

Separately, we have changed our accounting for reserves on our level term life insurance products, which we no longer sell. Under the prior approach, profits emerged as a level percentage of premiums; and given the increasing premium stream in these products after the level premium period, policy reserves could become negative.

While the amount of the negative reserves at year-end was immaterial to the current balance sheet, over the years the negative balances would have become much larger. While this approach is certainly compliant and consistent with industry practice at that time, more recent accounting models for long-duration contracts follow an approach which emphasizes the balance sheet over the income statement. We believe accounting policy under these more recent models is preferable, and so we will be flooring individual policy reserves at zero. We are making no changes to the assumptions which were locked in at the time these policies were issued.

There will be a negative earnings impact of this new accounting policy of approximately $20 million to $30 million after-tax annually in 2012 and in the following several years. However, we believe this approach is more conservative and reduces balance sheet risk.

As with the new DAC accounting guidance, this policy affects only GAAP reported results, not statutory or economic results. The impact from future lapses, if higher than assumed, will be significantly reduced.

In closing, with the transitions made through 2011, we are very focused on improving performance of our businesses and generating capital while managing our risks in an uncertain environment. I would now like to open it up for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Andrew Kligerman, UBS.

Andrew Kligerman - *UBS - Analyst*

Great, good morning. So, with the MI risk-to-capital ratio at 28.8-to-1, and you mentioned the 44 waivers, the GRMAC in five states where you have about a year of new business writing that can be done, have you gotten indications that you can continue writing at the same pace that you have been over the last several quarters? I mean, are you pretty confident that over the next, say, two years you are not going to have to put any new capital in, given these scenarios?

Mike Fraizer - *Genworth Financial, Inc. - Chairman, President, CEO*

Good morning, Andrew, and thanks for the question. Let me turn that over to Kevin Schneider.

Kevin Schneider - *Genworth Financial, Inc. - SVP, U.S. MI President & CEO*

Andrew, as we said before, we don't think there is a bright line test on risk-to-capital. We think the actions we have taken over the last year and the contributions we have made in the last 12 months to the capital levels provide us with a nice corridor to navigate through.

We have shared all of our forecasts and our expectation on risk-to-capital development with both our regulators and with the GSEs. And at this point in time, we think they are considering things beyond just risk-to-capital when they assess our ability to continue to write.

So they look at the strength of our reserves, they look at the quality of our portfolio, they look at the profitability of the new business which adds to our claims-paying. They look at where we stand on the loss curve and other capital alternatives. So I can't give you any assurance of -- in a two-year period, the second part of your question. I think that is a little long.

But I can tell you at this point in time we expect to be able to continue to write. We have got the benefit of GRMAC, our wholly owned subsidiary below GEMICO, in the event that GEMICO runs into some problem on the waivers. And that gives us a little bit of extra cushion which perhaps puts us out into that second year that you asked about.

Andrew Kligerman - *UBS - Analyst*

Okay. Thanks a lot. Then, another question to Marty maybe, on the Life Company and the statutory surplus. I guess last quarter you mentioned that you had a negative statutory unassigned surplus; and then I think I heard correctly today that you have a $50 million positive now, and that you wouldn't be able to dividend money from the LifeCo to the HoldCo until next year.

I guess just one little bit of clarity on a phenomenal 405% RBC ratio would prevent -- you would still be prevented from dividending money to the ParentCo. I want to understand that, maybe a little dynamic there.

Then secondly, just given the activity -- you mentioned the block transaction and so forth -- what would you anticipate being able to dividend up in 2013?

Marty Klein - *Genworth Financial, Inc. - SVP, CFO*

This is Marty. Thanks for the question. Let me start off and then I will turn it over to Pat. Just first of all, hitting the RBC ratio, it really did benefit primarily by a couple different things.

One is the Medicare Supplement sale. Those proceeds were about $214 million in capital; and that transaction closed early in October. So RBC is benefiting from that.

It is also benefiting from some deferred tax assets benefits around some of the forward starting swap gains. So those two together really contributed largely to the increase.

But really, paying a regular dividend doesn't relate so much to RBC ratios as it does to the level of unassigned surplus as well as to the statutory earnings that the companies have. We will be talking more about this on our second call, but let me turn it over to Pat just to give you a little bit of a sense for the development of unassigned surplus over the year and some other considerations.

Pat Kelleher - *Genworth Financial, Inc. - EVP, Insurance & Wealth Management President & CEO*

Thanks, Marty. In the third quarter, we reported the negative unassigned surplus after we had seen, I will say increases in variable annuity reserves on a statutory basis given the market environment and as well given the drop in interest rates. We saw that rebound in the fourth quarter, in addition to the factors that Marty described, as well.

We will go through on the next call that there are a number of impacts in terms of shifting our mix of business, greater use of reinsurance. On a full-year basis I would say the 2011 statutory earnings were below the level achieved in 2009 and 2010, primarily due to the equity market and low interest rate impacts, and a moderately higher long-term care loss ratio.

But I would say that moving into the new year with the block transactions, with the shifts that we have made in our new business capital allocation we are expecting to see that level climb to at or above the historical levels and position us very well for our target of returning to ordinary dividend paying on an ongoing basis in 2013. Does that help?

Andrew Kligerman - *UBS - Analyst*

What were the historic levels of unassigned surplus?

Pat Kelleher - *Genworth Financial, Inc. - EVP, Insurance & Wealth Management President & CEO*

We will go through that in the second call. They were elevated above $500 million back in 2007. They came down during the financial crisis due to investment losses. That was offset or mitigated by product-related earnings through that period.

And as we build the product-related earnings and complete the block transactions, we expect to rebuild the unassigned surplus to positions that will support, I will say, healthy, ongoing ordinary dividend capacity starting in 2013 but also in future years. And the block transaction as well as the value creation from the new business and the capital allocations to that are part of that picture.

Andrew Kligerman - *UBS - Analyst*

Perfect. Then just lastly, maybe some color on the size of the interest rate swap that benefited Genworth in the quarter.

Ron Joelson - *Genworth Financial, Inc. - SVP, Chief Investment Officer*

I will take that one, Andrew. So effectively what happened in the fourth quarter is that we unwound swaps generating cash of about $950 million. Those swaps are qualified hedges, so the market value gains flow directly to the balance sheet, and the income recognition would be deferred over the next 20 to 30 years.

Additionally, the unwind monetization of the swaps and reinvestment of the cash will generate about $20 million of additional earnings per year for the Life Companies. We also, I should note, re-struck those swaps to provide protection in the future in case there are further rate declines. And we will also be discussing those income effects in the second call at 11 o'clock Eastern.

Andrew Kligerman - *UBS - Analyst*

Perfect. Thanks so much.

Operator

Donna Halverstadt, Goldman Sachs.

Donna Halverstadt - *Goldman Sachs - Analyst*

Good morning. I wanted to start with a follow-up to Andrew's U.S. MI question. Can you give us any sort of specifics on the time frame over which you will continue to assess that business before making a definitive decision on the ultimate resolution of U.S. MI? Whether that be at some point in the future, starting to feed it again, versus starving it, versus killing it.

Mike Fraizer - *Genworth Financial, Inc. - Chairman, President, CEO*

Donna, this is Mike. Thank you for participating and thanks for the question. A couple perspectives.

First, we think we have made a lot of progress in managing our portfolio, as I think Kevin emphasized and I tried to touch upon in our prepared remarks. The whole focus on containment, maintaining strong claims-paying ability, and moving through the current in-force block is a key focus for us.

Again, as part of that you want to make sure you understand a block, how it is performing, how it can perform under various conditions. And that is one of the important reasons we augment not only our analysis of that but use third-party analysis to do that.

So, we think we have a strong claims-paying ability in place. We think we have a good corridor for new business that takes us out a year-plus, as Kevin talked about.

We have touched upon constructive discussions going on with GSEs and others about some alternative structures that add to that capital flexibility. So, I think we're in a good position right now to write this profitable new business, manage through our in-force with strong loss mitigation. And then we will always actively assess the business and see if something changes on that front, but I think we have got good runway right now.

Donna Halverstadt - *Goldman Sachs - Analyst*

Okay. I also, Mike, wanted to follow up on a comment I think I heard you make in your prepared remarks. I think you referred to Australia and Canada as strategic positions. If that in fact was the label you used, does that mean you have definitively decided to remain a hybrid Life/MI company, albeit with reduced exposure to MI through the partial IPOs?

Or is the potential alternative of a more complete split between Life and MI still something that might be on the table?

Mike Fraizer - *Genworth Financial, Inc. - Chairman, President, CEO*

Well, Donna, again thanks. Let me break that on two fronts.

First, what I wanted to convey regarding Mortgage Insurance is that we have seen benefit in having multiple platforms because of the diversification of risk that provides; certainly we move know-how around the world. In fact, that diversification has helped us be able to work with third-party reinsurers and -- really from nowhere -- create an external global MI reinsurance market that we think can benefit certainly ourselves and over time the entire industry.

So, that is what I wanted to convey.

We will, as I think we have over time, always reassess our business portfolio and see what the optimal mix is of businesses. We have a lot of execution to do and a value to rebuild right now.

We get some financial synergy out of the diversification of cash flows to the Holding Company from both the MI side and also -- back to our last conversation of what do we see on Insurance and Wealth Management, that we really want to get the Life Companies back to paying a regular dividend to the Holding Company.

So, we will evaluate any changes in the portfolio, including -- do you get a better value for shareholders with a pure-play type structure down the road? But right now we have a lot of execution to do with our current portfolio, so I hope you find that helpful.

Donna Halverstadt - *Goldman Sachs - Analyst*

Okay. Yes, thanks. Then the last question is just a more day-to-day type question. Marty, I was wondering if you could just update us on the status of the renewal of the credit facilities that expire in May and August of this year.

Marty Klein - *Genworth Financial, Inc. - SVP, CFO*

Sure, I would say that -- a couple things. One is that the Company's balance sheet and its liquidity needs are very different now than they were a number of years ago. We are no longer having outstanding commercial paper. We are no longer in the funding agreement business. So the need for a facility the size that we have currently is a lot less, I would say. If and as we renewed it still, we'd be looking at something that's probably order of magnitude maybe a third or perhaps even less than the current size.

As we think about where we are with our risk buffers and Holding Company liquidity, we have really developed those and really don't actually need the credit facilities as that stand now, given the liquidity that we have. What we will do is we will revisit credit facilities later in the year as we make progress on some of the things we're working on including the Australian IPO.

Donna Halverstadt - *Goldman Sachs - Analyst*

Great. Thank you very much, gentlemen.

Operator

Geoffrey Dunn, Dowling & Partners.

Geoffrey Dunn - *Dowling & Partners - Analyst*

Thank you. Good morning. A specific question on the MI side. Sequentially you saw your claim severity come down about 12%, 15%, which is pretty unusual even from a geographic shift. So can you discuss what is going on there? Particularly, are you seeing any kind of material emerging curtailment opportunity that you think is sustainable?

Kevin Schneider - *Genworth Financial, Inc. - SVP, U.S. MI President & CEO*

Thanks, Geoff. This is Kevin; I will take that. When you think about our overall loss mitigation efforts, we have through this cycle been focused on, number one, what was coming through in the delinquencies, and investigating those and making sure loans were properly underwritten. So that sort of worked itself through the system. As of about the second quarter of 2010 most of our material benefit was gone from rescissions.

Now the loans are starting to make it through the delayed foreclosure process and starting to be perfected claims. And as we look at those claims and as we look at the way they were serviced, we are certainly looking at them very closely in terms of making sure that the servicers performed to the standards that are required in our Master Policy. And where we see that there was some problems in that servicing or breakdowns in the way it was done in the marketplace -- and we all certainly read about that on a regular basis -- we have been doing some curtailment of the claims. You know, trimming back on interest rated expense and other things, where frankly there was no focus put on the consumer.

So we have beefed that up a little bit and are going to continue to look at all claims, make sure we are paying every single legitimate one, but make sure we are paying them consistent with our Master Policy.

Now if you look in our supplement, to your -- just to give you a little bit of perspective on it, on the quarter, we probably paid 5,600, 5,700 claims in total, something like that. That, with an average improvement from the prior quarter, as you referenced, of about $6,000 per claim, you can get some handle on the impact that that might have over time.

Geoffrey Dunn - *Dowling & Partners - Analyst*

Okay. I know with rescission denials you tended to have a little bit of forward insight given the pipeline of investigations. Do you have a similar insight on the curtailment reviews? Is there reason to believe that the severity level could at least be more towards this level than third-quarter level as we look into the beginning of '12?

Kevin Schneider - *Genworth Financial, Inc. - SVP, U.S. MI President & CEO*

Based upon what we are seeing coming in the door right now, I think it has largely been consistent with the numbers you see in the Q4 trend. And I wouldn't expect any material difference on that at least early on in the year.

Geoffrey Dunn - *Dowling & Partners - Analyst*

Okay, great. Thank you very much.

Operator

Jeffrey Schuman, KBW.

Jeffrey Schuman - *Keefe, Bruyette & Woods - Analyst*

A couple questions. On the life reinsurance transaction that you were working on in first quarter, you have talked about the statutory gain; but presumably you are monetizing some future earnings. So I am wondering what the go-forward GAAP earnings impact would look like.

Secondly, I think you mentioned the earnings implications of the swap gain, but I didn't quite follow that. So I was wondering if you could just quickly review that for us again, please.

Mike Fraizer - *Genworth Financial, Inc. - Chairman, President, CEO*

Thanks for the question, Jeff. Let me turn that over to Pat Kelleher. Pat?

Pat Kelleher - *Genworth Financial, Inc. - EVP, Insurance & Wealth Management President & CEO*

Yes, with respect to River Lake III, if you look at it from a GAAP perspective, I think we indicated it is expected to result in a GAAP loss of $37 million, which is really net of the write-off of DAC associated with the sale of this business.

If you look at it as a sale of a business and a release of GAAP capital, it is a sale at about 80% of book value. And that is a good trade, considering that after the impacts of increases in financing costs there is a relatively low level of GAAP earnings that has been emerging from this block. On average, we see it as a mid-single digits per annum GAAP earnings give-up associated with the sale. So from our perspective the capital generation and the impact on shareholder value is very positive.

Jeffrey Schuman - *Keefe, Bruyette & Woods - Analyst*

I'm sorry; mid-single digits millions of dollars of earnings? Is that what you said?

Pat Kelleher - *Genworth Financial, Inc. - EVP, Insurance & Wealth Management President & CEO*

Per year, yes.

Jeffrey Schuman - *Keefe, Bruyette & Woods - Analyst*

Per year? So some number $4 million to $6 million, something?

Pat Kelleher - *Genworth Financial, Inc. - EVP, Insurance & Wealth Management President & CEO*

On average, yes.

Jeffrey Schuman - *Keefe, Bruyette & Woods - Analyst*

On average. So the stat gain is a pretty big multiple of that. Okay.

Pat Kelleher - *Genworth Financial, Inc. - EVP, Insurance & Wealth Management President & CEO*

That's exactly right. I will turn it over to Ron for your question on the swap gains.

Ron Joelson - *Genworth Financial, Inc. - SVP, Chief Investment Officer*

Yes, so thanks, Jeff, for the question. What I referred to with respect to the $20 million relates to the proceeds of the swap unwinds. Those proceeds can be reinvested, and the reinvestment effect is a $20 million run rate for the US Life Companies. That does not include the amortization effects of OCI in our swap program; and we will be covering that piece along with really the entire picture when we do the 11 o'clock call. So there is a second income effect that also occurs with respect to that program.

Jeffrey Schuman - *Keefe, Bruyette & Woods - Analyst*

Okay. I will wait for that. Thank you.

Operator

Joanne Smith, Scotia Capital.

Joanne Smith - *Scotia Capital - Analyst*

Yes, good morning. I have two questions. One is for Kevin, with respect to the wind down of the HAMP program, and what do you see going on in Washington with respect to additional actions to work through loan modifications and obviously the backlog of foreclosures? And that is my first question.

Kevin Schneider - *Genworth Financial, Inc. - SVP, U.S. MI President & CEO*

Let's start with that one, Joanne, because that is a mouthful in itself. I think the latest thing around HAMP I would view as net positive for the mortgage insurance industry. The HAMP program has been extended for another year. There has been additional flexibility provided around debt-to-income levels to qualify, which will bring more potential borrowers to the modification program potentially. Investor properties are available.

So those things are all sort of net positive to us and I think should give us some additional run room on HAMP, which we thought was really declining and petering out by the end of the year.

The government has also offered some additional incentives by the Treasury to investors who would write down -- do some principal reductions. So far, none of that has really been taken up by the GSEs; and so I don't know that we will get any additional benefit out of that, really.

But there is a lot of activity going on in Washington on trying to make sure you stay focused on the borrowers. The big huge refinance program that was offered up by the administration this week doesn't really -- the GSEs and the agencies don't qualify for that. So I don't think we will get a lot of benefit out of that, as most of our portfolio is with both Fannie and Freddie, and I think that one has got a little bit of political headwind it's got to play through before those things get approved.

But a lot of activity. We are staying focused on the activity that we have known has worked, which is keep working with those borrowers and with the servicers to try and drive as many workouts as we can.

Joanne Smith - *Scotia Capital - Analyst*

Kevin, just on the loss mitigation savings that you realized, how much of those were directly related to efforts around HAMP? And where do you see mitigation savings going in 2012?

Kevin Schneider - *Genworth Financial, Inc. - SVP, U.S. MI President & CEO*

Most of those savings for us were driven by -- think of it this way. It is any rescission-related savings, any workout-related savings, and then any claims settlement savings really that we -- or short-sale type things that improve what our otherwise loss position might be.

As this year, it was -- again, we had about $567 million, something like that, in savings directionally I think. We will talk about that on the next call. But at the highest level, it's sort of $300 million to $400 million worth of anticipated savings next year.

Most of it coming from -- continuing to come from modifications, whether they are HAMP mods or some other type of mods outside of the government's HAMP program.

Joanne Smith - *Scotia Capital - Analyst*

Okay. Then just do you see that curtailments could potentially offset the reduction in mitigation savings?

Kevin Schneider - *Genworth Financial, Inc. - SVP, U.S. MI President & CEO*

Well, there will be some improvement potentially vis-a-vis curtailment. We don't have a lot of rescission-related savings anymore in our numbers and really didn't this year. If that is what you mean I think there might be a little bit of offset there.

But again we are just trying to make sure we are only paying claims that -- paying all the claims that are owed and paying them in accordance with our Master Policies.

Joanne Smith - *Scotia Capital - Analyst*

Okay, thank you. Thank you, Kevin. And, Pat, a question for you with respect to the market conditions for potential block sales on the Life Insurance business.

Pat Kelleher - *Genworth Financial, Inc. - EVP, Insurance & Wealth Management President & CEO*

Sure. We have found in the course of the work that we have done to date that the portfolio reinsurance market is alive and well. That is the market that we tapped for our first transaction.

We are actively working on the follow-on transactions and don't really have anything material to report at this time. So we will look to update you on future calls.

Joanne Smith - *Scotia Capital - Analyst*

Okay, thank you.

THOMSON REUTERS

Operator

Thomas Gallagher, Credit Suisse.

Thomas Gallagher - *Credit Suisse - Analyst*

Good morning. Just wanted to follow up on how the mechanics of unwinding the forward starting swaps works. I ask because, if I recall correctly, that was predominantly used to hedge your long-term care liabilities.

Just curious how that interplay works. Are you now less hedged against long-term care when you monetize that forward starting swap? Or is it just changing the geography of it? Can you talk a little bit about how that interplay works? Thanks.

Ron Joelson - *Genworth Financial, Inc. - SVP, Chief Investment Officer*

Sure, Tom, this is Ron Joelson. I will take that one.

So, essentially what we do, what we have done with the forward starting swap program is we locked in or monetized some of the gains that were existing in the program. But we re-struck the swaps, and the reason we did that is we felt that we still needed additional protection should interest rates fall further.

So we have in fact re-struck those swaps. And you will even see if you look in our disclosures, you will see that we have continued to have and enjoy gains on those swap positions, mainly because rates fell somewhat even afterwards. So, we have exactly the same or approximately the same notional swaps outstanding today as we did before we undertook the unwind.

Thomas Gallagher - *Credit Suisse - Analyst*

Got it. Then Ron, is it fair to say since you recognized a gain that you just got different strike prices, or the swap is more expensive? Or how should we think about that?

Ron Joelson - *Genworth Financial, Inc. - SVP, Chief Investment Officer*

Yes, you have it right in the sense that we now have strike prices or we have effectively lowered the protection point. As I said, because rates fell a bit further we continue to have gains -- close to $500 million of unrealized gains that continue to sit in the Other income or derivative section of our disclosures.

Thomas Gallagher - *Credit Suisse - Analyst*

Got it.

Ron Joelson - *Genworth Financial, Inc. - SVP, Chief Investment Officer*

(multiple speakers) Balance sheet.

Thomas Gallagher - *Credit Suisse - Analyst*

Got it. Then can you just talk a little bit about how the year-end process went for low interest rate-related pressure on the Life Insurance business on a statutory basis with cash flow testing? How did you come through that? And did these hedges have a meaningful impact for you there?

Pat Kelleher - *Genworth Financial, Inc. - EVP, Insurance & Wealth Management President & CEO*

This is Pat, I will take it. Hedges, of course, have a very meaningful impact on cash flow testing in terms of the margin analysis that we have had. We haven't completed the process for all of the Life Companies at this point in time; but I can say that based on the interim results we feel very good about where we are.

Thomas Gallagher - *Credit Suisse - Analyst*

Okay, thanks, Pat. Then just lastly, as we think about just your capital management, you look at Holding Company debt, consider the Australian IPO, I guess the one thing that I am wondering is -- when you look at potentially monetizing a piece of the Australian business and using the proceeds to perhaps buy back stock, maybe a portion to retire debt, I presume that is going to reduce the ongoing cash flow coverage when I think about it from an interest coverage standpoint. Just because at least to date the Life Insurance business generates GAAP earnings but hasn't been generating stat earnings. I appreciate that you guys are monetizing some gains on the statutory basis, and that is good that you are building capital.

But is there any -- beyond that sort of capital build, is there visibility on cash flow recovery or statutory earnings improvement on a more sustained basis?

Mike Fraizer - *Genworth Financial, Inc. - Chairman, President, CEO*

Tom, this is Mike. First, thanks for the question, and let me break it down on a few fronts. I would like to start statutory and then move -- at the Operating Company level and then move towards the Holding Company and your redeployment question in trying to give you as thorough an answer as we can.

First, on the statutory side, as we have laid out and we're going to lay out in quite a bit more detail on the second call today, in fact providing you some exhibits that I think the investment community will find very helpful to see how we are thinking about statutory earnings, unassigned surplus, and the path towards both improvements on both the unassigned surplus and the stat front, and how that results then in the common dividend. You will see a roadmap, if you will, on that front.

So we are very focused on that, and that is really an underpinning. Because if you look at it we have had good dividend flows -- well, good capital generation and then subsequent dividend flows from the International Protection business. We have it from our non-insurance business, Wealth Management. And then reestablishing that on the U.S. Life side, all aids what comes up through the Insurance and Wealth Management Division.

And then again out of Canada and Australia we have seen good capital generation and dividend performance along with that. So those statutory and capital generation underpinnings are the foundation.

When you get up to the Holding Company level and you think about the risk buffers we have, as Marty laid out, we are running about $400 million above our 2 times debt service coverage cushion we want to have. And then what we do is we basically look at a stress environment and then say -- what would happen if the bulk of your dividends didn't come up from your Operating Companies for, say, 18 months because of some macro event out in the environment? And what type of buffer would you want to have to be able to handle that?

That would equate to about -- when we talk about that risk buffer -- about $300 million. So that is a way to think about that and, hence, Marty's commentary.

Now, as you move over that, because you still have the Med Sup dividend that Marty talked about, we still have the closing of the GFIS sale coming, we have the minority IPO of Australia that is moving down the track right in accordance with our plans, and you look at therefore additional amounts, you would say -- well, how would you think about those proceeds?

Well, first you would look at the environment and say -- did something change from the risk environment that changed your perspective on that risk buffer I just laid out?

Second, there would be what I would say would be a proportional deleveraging. And if you do a proportional deleveraging for a piece of a business you sell, then you're protecting your coverage ratios; and then you are protecting your leverage ratios within that 24% to 26% range that Marty talked about. And then you move to redeployment.

So it is quite rigorous. Statutory, looking at the dividend, going to the Holding Company, making sure we have the risk buffers, targeting redeployment because we see shareholder value creation in that redeployment, but maintaining the appropriate coverage and debt ratios along the way. So sorry for the long explanation but hopefully that is very helpful in seeing how we'd walk down that path.

Thomas Gallagher - *Credit Suisse - Analyst*

That was helpful. Thanks, Mike.

Operator

Ed Spehar, Bank of America Merrill Lynch. Your line is open.

Ladies and gentlemen, this concludes Genworth Financial's fourth-quarter earnings conference call. Thank you for your participation. At this time the call will end.
