Y 2017 Earnings Call

Company Participants

- Chris Figee, Chief Financial Officer
- Jos Baeten, Chief Executive Officer
- Michel Hulters, Investor Relations

Other Participants

- Arjan van Veen, Analyst
- Ashik Musaddi, Analyst
- Benoit Petrarque, Analyst
- Cor Kluis, Analyst
- Farooq Hanif, Analyst
- Johnny Vo, Analyst
- Robin van den Broek, Analyst

Presentation

Operator

Good day, and welcome to the ASR investor call annual results 2017. Today's conference is being recorded. At this time, I would like to hand the conference over to Michel Hulters. Please go ahead.

Michel Hulters {BIO 19111905 <GO>}

Thank you, operator. Good morning, ladies and gentlemen, welcome to the ASR conference call on the full year 2017 results. On the call with me here today are Jos Baeten and Chris Figee and we are here to discuss the results and give you an update on the business performance. After that we'll open up for Q&A. We have scheduled this call till 12 o'clock today, so 90 minutes. And before handing it over to Jos, please, as is customary, we have to look at the disclaimer that we have at the back of the presentation for any forward-looking statements.

So, having said that, Jos?

Jos Baeten {BIO 2036695 <GO>}

Thank you, Michel, and good morning, everybody, Ladies and gentlemen, from a management perspective, 2017 is a year to remember with a very strong set of results, happy stakeholders across the board, customers, employees, shareholders, including our former shareholder, the Dutch State. In particular, I am pleased to see that this is driven by continued solid performance of each of our business in delivering great results, but also the sale of the remaining stake, the acquisition of Generali Nederland and First Investments.

Before we dive into the financial, I would like to mention that we are also proud of the performance on non-certain, non-financial criteria. During the past year, we have seen more and more happy customers and intermediaries doing business with ASR. The net promoter score has gone up to a score of 40 points and 57 points for intermediaries and let's not forget that happy customers turn into loyal customers and they provide our license to operate and our future profits.

In addition, recognition of the ASR brand has risen in the past year and customers increasingly appreciate all of our efforts to be a social responsible insurance company. As you may have seen in the past weeks, we announced to team up with Triodos Bank and jointly committed to invest EUR600 million into ESG and sustainable projects. Another example is the ESG credit funds that we have established in 2017 and which is now open to third party investors. And these are just two examples of many initiatives we have taken in this respect. In short, we aim to be relevant for our customers and contribute to society at large as this is the foundation on which we've built our company and create long-term value for all of our stakeholders.

Having said this, let's discuss our financial performance and progress of our business and that's on slide two. Performances set over 2017 has been strong on every key metric. Let me highlight some. Operating result was up 17.2% to EUR729 million, by the way, a record high result. This yielded an operating return of 15.6 compared to our target of up to 12 and also up compared to the 14.6 of last year. Our IFRS result, net of tax, also highest on record at EUR906 million. Combined ratio of 95.1 has improved from 2016 levels and reflects continued underwriting excellence as well as the improvement in our cost ratio.

I am also pleased to see that these healthy and market outperforming combined ratios, our non-life business delivered close to 6% top line growth. Our Solvency II ratio remains robust at 196 after deduction of the proposed dividend. As you know, we are still using the standard formula. This is a 7 point increase from the beginning of the year. The main moving parts are strong organic capital generation of 377 million, and favorable financial markets that outstrip the impact of share buybacks 7 percentage points, the VA declined 9 percentage points and the re-risking of the investment portfolio which accounts for another 6 points.

Quality of our capital remains high as well with unrestricted Tier 1 capital alone representing almost 152% of the Solvency II, and then there is still plenty of headroom to maneuver and restricted Tier 1 more than 800 million. In terms of Tier 2 and Tier 3, almost 700 million. Our strong solvency position enables us to remain entrepreneurial. As we have always said, everything safely above 160 allows us to be entrepreneurial and to pursue profitable growth. Our strong solvency has also enabled us to participate three times in the sell-downs from the Dutch State. In 2017, we purchased 9 million our own shares for a total amount of 255 million. Including paid dividend, we have returned over the last year 440 million through our shares.

Speaking about dividend, given the strong results of ASR in 2017, we will propose a record high dividend of EUR229.7 million which is EUR1.63 per share. This is an increase of 28.3 compared to last year's dividends of 1.27. We assume going forward a stable growing dividend per year. I think everybody realizes that an increase of 20.3% is beyond what I would call stable growing. Hence, we assume -- sorry, hence, I would caution you on that. And I believe that in our industry, low to mid single digit ordinary dividend growth assumptions sounds more realistic.

Let's now turn to our business portfolio, and the key developments in 2017. I'm sure you are, in the meantime, familiar with this matrix in which we plot our businesses. Let me highlight some recent developments and achievements in executing our strategy. Let me start in box B on the left angle down. There you will find our large service books. Maintaining a low cost base and variablizing the cost base is crucial. In lowering the cost, we were able to decrease the cost per policy with 3% from EUR66 per policy to EUR64 per policy in 2017. This despite of a 3.2 higher than planned lapses. We continued in the same area to migrate our service books to the new platform and plan to finalize two new books in the first quarter of this year.

With the acquisition of Generali, we also acquired a new individual life book, which we will migrate towards this platform. In executing initiatives to migrate pension clients to capital light solutions, in 2017, we were able to close down nine separate accounts and to move them towards our DC solutions.

In the top left, in box A, our businesses that provide stable cash flows. Here we focus on organic growth. In P&C, we don't only talk about robotics, we actually use robotic for tender suite to make offers towards customers from an intermediary competitor portfolio which we acquired from (inaudible)

Ware learning from this how to use robotics in migrations, which is going to be helpful in future non-life migrations.

Furthermore, we saw a top line growth of almost 6%. This doubles more -- this doubles the Dutch GDP growth, which we set at our IPO would be our growth guidance in the P&C area. Within disability we see a stable top line with some moving parts underneath. As mentioned in the past, our value over volume principle let us to lose some customers due to the BeZaVa legislation. This is compensated by other segments and disability resulting in a stable top line. All in all, a satisfying growth of 8 million to 765 million in this area.

The last segment in box A is our funeral book. We completed the NIVO migration within budget and within time. So, our funeral business people is ready to migrate the 300,000 Generali policies in 2018 and is also ready to absorb any future further organic or inorganic growth if and when.

In the capital light space, box C, we have made further progress in 2017. In the asset management space, we have, as you may know, our buy and build strategy. In 2017 we acquired the First Investments, a niche investor which -- with some specialized skills and adding 0.6 billion of assets under management. Furthermore, we built this segment with the successful launch of the ASR Dutch Mobility Office Fund with external placements and the successful launch of the ASR Mortgage Fund with 0.5 billion of firm commitments already in 2017,

The pension DC solution of ASR called Werknemers Pensioen is gaining track and had a very good year in 2017 with 25.6 of new recurring gross written premiums. In terms of new business, DC is now 77% of our total new business. ASR, in the meantime, has become the number three DC pension producer in the Netherlands. Gross written premiums are up 42% compared to last year. Furthermore, with the conversion of the old DC solutions towards the new Werknemers Pensioen, the assets under management and its proposition doubled in 2017. Assets under management base is up 200 million and now close to EUR500 million in total. We're also very happy with the retention rates of our existing customers. This retention rate was last year 99.6. So lots of happy customers in the pension area.

For the distribution and service segment, we have medium term target of 7% to 10% growth and with this year growth of 39.5, we've significantly outperformed this target, mainly due to the strong growth of Dutch ID and the acquired companies are now fully contributing towards the operating result. This segment is well on track to achieve EUR20 million operating results.

And finally box D, the potential divestments. The real estate projects are no longer classified as held for sale, although it is still excluded from the operating result and we made progress there. IFRS result of 17 million pretax in 2017 by an increase in the sale of the residential housing and furthermore 77% of the retail space is rented, overall occupancy rate of over 80% is achieved.

So now let's turn to what the overall operating result has done for half year in the next slides, and that's slide four. As mentioned in my introduction, operating result is up 17.2% compared to last year. 2017 was a strong year and business momentum maintained at a very high level. As the chart shows, 2017 record operating result was driven by an extraordinary strong first half year of 2017 where we benefited from favorable weather conditions within non-life and the dividend season within life. Second half year showed from our viewpoints a more normalized result, because as we already indicated at the half year results, H1 went roughly 30 million above what we would considered as a normalized level.

Slide five shows the breakdown of the operational results. As said, up 107 million to 729. As you can see on this slide, all four business segments contributed to the higher results. Non-life 36 million to 172, while life was up 74 million. I will talk about those two segments in a moment, but first a few comments on the other segments. Banking and asset management improved due to an inflow of assets under management, resulting in higher fee income, partially offset by placement fees due to the launch of new funds. As mentioned, we see good business developments in asset management and this segment has the potential to grow to 20 million business in some years' time.

Acquisitions of Corins and SuperGarant contributed to an increase in the operating result in distribution and services. This segment is geared up and is gaining further mass and could potentially contribute, as said, 20 million to results this year already. To finalize, holding and other, a decline of 12 million shows impact from higher current net service cost for pension obligations own personnel due to lower interest rates. So, overall, a strong increase in operating result, driven by gains across the various businesses, and we are happy with that.

Let's turn to slide six where we highlight the developments in our expense ratio. Our ongoing focus on cost containment is one of the key drivers of operating earnings and long-term value creation. We believe we may well be the leader in terms of cost discipline and culture as demonstrated by the expense ratios in our non-life as well our life business. Overall, operating expenses increased with 2.6%, but those include absorption of the additional cost base of the acquired businesses, the additional current net service cost of 11 million and a one-off because we granted all of our staff an extra monthly salary in 2017 due to the successful privatization and the results over the last few years.

I will provide some more insight on the next slide. In non-life, the expense ratio improved from 8.3 to 7.6, driven by the strict cost discipline and portfolio growth without any FTE growth. In fact we have been able to fully absorb the top line growth in non-life in our existing platform and a nominal cost base in non-life is approximately 4 million lower compared to last year. Also, in life, the expense ratio improved from 11.7 last year to 11 in 2017 as gross written premium decreased, but operating expenses decreased even further, benefiting from the efficiencies of acquired portfolios and regular cost savings due to our migration projects and 18% lower FTE base.

Let me now turn to slide seven to provide some insight in the operating expenses related to our targets of 50 million cost savings over the medium term. This slide is to provide an overview of the development of our cost base since IPO and to assess whether we are on track to deliver our targets. At IPO, when we announced the cost saving target of 50 million, we had a cost base of 575 million. This cost base needs to be revised for acquisitions that added EUR32 million. Next year the cost base, and that's not in the graph, will also be added for Generali and for comparisons reasons, you need to adjust 44 million of additional operating expenses for Generali.

The current net service cost, which is a result of interest rates, decreased in 2016 as a result of interest rate increase in 2015 from 2% towards roughly 2.5%. This interest rate declined in 2016 towards 1.73, resulting in an 11 million additional expenses. As this is largely, interest rate development is largely outside of our control, this effect was not taken into account at the time of setting the cost saving. And then additional final adjustments we have made is what I already mentioned, the allowance we gave to all of our staff of roughly 10 million to 11 million because we did a very successful privatization and the results of ASR and that's also to consider as a one-off. If we were to correct for these items, this would lead to a 23 million cost saving in 2016 and 18 million already realized on the structural cost base in 2017 of 18 million. So, we've realized 41 million out of the 50 million planned cost savings, so another 9 million needs to be done in 2018. Now that concludes that we are well on track to achieve our targets to realize these cost savings.

Let me now turn to the next slide, where we can look deeper into the non-life segment. In non-life our expense ratio is market-leading, combined with our underwriting expertise, leading to a very strong combined ratio. All non-life product lines showed combined ratios below 100, again for the third consecutive year and as you can see in the graph -- as you can see in the graph at the bottom right hand corner. Operating results increased to 26.5% to 172 million. The increase was driven by excellent underwriting and claims handling, the absence of large claims and favorable weather conditions in the first half year of this year while last year we had EUR25 million of claims related to hail and water damages. This is reflected in the favorable development of the combined ratio in P&C.

Allow me already to make one remark on 2018. In the first half -- the first half will definitely be less favorable than last year. In January we already used our annual storm budget due to the hefty January storm on the 18th. We estimate a EUR30 million of claims in total which is equal to the annual average storms over the past -- equal to the average of the storms in the past four years.

Returning to 2017, gross written premiums rose by 6% due to the growth in P&C and health. The market developments towards more rational pricing allowed us to grow our top line while maintaining our value over volume discipline. In the P&C business the increase was mainly driven by the success of the Vernieuwd Voordeelpakket. Also in disability we stuck to our discipline and experienced a pull from the government owned UWV proposition for BeZaVa customers. Nonetheless, we managed to keep gross written premium in disability stable.

The value over volume focus resulted in switching health customers since the pricing was a bit more tailored to the top end, leading to a decline of approximately 20,000 customers. Overall combined ratio of 95.1, well below the targets of 97, an improvement of 0.5 percentage points compared to last year and this reflects improvements in the expense ratio also. Claims ratio of non-life rose slightly from 72 to 72.8. This significant improved claims ratio in P&C due to the absence of large storms was offset by higher claims in health and disability. In health, the claims ratio increased due to mainly the higher cost calculation of 2016, leading, for instance, to higher expenses for medicines in hospitals. In discipline, the claims ratio increased mainly as a result of more claims in absenteeism. In response, we raised prices on average with 20% for 2018, and this will compensate the impact going forward.

Let's now turn to slide nine. Operating results of the life segment. This increased with 13.2% to 633 million. The investment margin increase was 70 million due to higher direct investment returns. Those were up 19 million as a result of the re-risking into higher yielding investments, mainly equities and mortgages within our investment portfolio and the higher contribution from realized capital gains. Those were up 53 million, partially offset by higher interest on liabilities.

Result on cost is stable at 24 million, decline in cost coverage for the individual life is absorbed by improved cost result for pensions and funeral. Strict cost control, migration of books and cost synergies from acquisitions were partially offset by higher than expected lapses. Technical result remained stable. Despite decline in the life individual book, in the first quarter, we experienced at first mortality results due to the influenza, which has been offset by improved mortality results in the last quarter of 2017.

Life segment premiums decreased mainly due to the one-off effect of the two acquired portfolios in 2016. Recurring premiums decreased 2.8 as higher gross written premium and pensions DC were offset by lower premiums in the individual life. So going forward, growth in life premium should come from DC business. In 2017, we added more than 500 employers to our portfolio, and we have become, as said, the number three pension producer in the Netherlands. So we trust we can continue to grow our DC business going forward.

And on slide 10 and let me provide with an update on the Generali acquisition. The closing has been finalized on the 5th of February. So this is for us the starting point of integrating the business. Let me remind you of the strategic rationale for this acquisition. This is a compelling opportunity to further consolidate the Dutch market and the bolt-on acquisition of the type we prefer. The cash consideration has been paid after the closing and the recapitalization of the operating companies has been done. The guidance from the announcement still stands. And therefore there will be a pro forma impact of 9 percentage points on our Solvency II ratio in Q1.

A few remarks what we have done. Since the closing already, we already established the reporting lines towards ASR. All control functions in the meantime are reporting to ASR. Control of asset allocation and interest rate hedge is now over to ASR and we, as said, injected capital according to earlier commitments and started the re-risking of the Generali portfolio.

On the progress going forward, the merger of the top holding Generali NL within -- into ASR will be before the summer. Legal merger of the non-life and life entities will be right after the 30th of June this year. Re-labeling of all the businesses from Generali to ASR brands will be done within six months.

And finally, all the staff will be moved this summer to the ASR building and the Generali building is available for sale and we already identified the first interested buyers. Please bear in mind that we will first have restructuring expenses in 2018 before Generali can fully contribute to its potential. This will happen over time with an expected impact of 25 million of organic capital generation in 2020 and EUR30 million contributing to the net operating result at the latest in 2020.

So on slide 11, the comparison with our targets and I will cut this short a little bit. We have met and exceeded all of our targets and we are proud on that. And before I hand over to Chris for further details on our capital and solvency, I would like to conclude with the final slide on our dividends. Clearly, as this slide -- as this chart demonstrates, over the past year, we have built a very solid track record in paying dividends. Our ambition is to pay a stable growing dividend. The strong increase in operating results drives the higher proposed dividend for 2017, maintaining at a payout ratio of 45% and this leads to the already mentioned 229.7 million dividend payout. Proposed 2017 dividend per share is, as you know, EUR1.62 per share, an increase of 28.3 on the 2016 dividend per share. This year, we will introduce an interim dividend with a payout ratio of 40% of the last year's dividend. Based on proposed 2017 dividend, this would amount to 0.65 interim dividend per share payable in 2018.

We've also proven not to be hoarders of capital. In 2017, a total of 9 million owned shares have been purchased for the amount of 255 million. Since the IPO in June 2016, 672 million of capital has been returned to shareholders including proposed 2017 dividend and as we have mentioned before, we are keen to deploy capital first both in organic or inorganic growth opportunities. Should those not materialize, then we will explore appropriate ways to return capital over time.

Chris, the floor is yours.

Chris Figee {BIO 18815839 <GO>}

Very good. Jos, thank you so much. I will continue our presentation and move to the solvency and capital section. If you follow me, and flip to page number 14, where we will discuss and elaborate on our multi-year equity and own funds movements. These are the book values that we report, book values from an IFRS perspective or a Solvency II perspective. We're proud to show a continued growth in book value. IFRS equity grew again even excluding hybrid capital instruments. Book equity moved up by 652 million, especially when we consider that absorbs a cash distribution to shareholders in the year of over 453 million. That means net 652 after we shared with our shareholders EUR450 million in cash. And we're proud that we are able to combine an increase in IFRS equity with also 100 basis points increase in our ROE.

So the numerator and the denominator both went up, which is confirmed by the prospect on Solvency II. You can see the eligible own funds moving up to 5.3 billion unrestricted Tier 1 and 6.8 billion of full own funds. Hybrid instruments now compose only 23% of our total own fund. So again solid growth, solid development in book values and we still believe that developing the book values in the long run provide a good indication of where companies are heading.

Now that we're talking about stock, I'd like you to turn to page 15, on our solvency, the solvency stock. This page shows own funds and required capital to 196% solvency ratio, up 7 points in the year. If you look at the longer term perspective, up from 186% in the first quarter of 2016. If you go back two years end of Q1 2016, we are at 186%. Today we are at 196, despite us returning in that very period almost 700 million in cash to shareholders. So we gave back 20 points of solvency to our shareholders roughly, and to we increase our solvency to 196.

We're proud of the level of capital and the composition of capital. It's 196 in the standard formula. Unrestricted Tier 1 is 77% and the Tier 1 ratio -- unrestricted Tier 1 ratio would be 152 or Tier 1 as a total is 166. No Tier 3 capital at this point, so there is no tiering risk. We don't use any Tier 3 element in our solvency and we have headroom in all the available solvency categories, and the combined Tier 2 and Tier 3 headroom is now at 697, increased against since last year. So significant amount of financial flexibility.

Market risk is still under 50% of required capital at 47. Appendix E in the presentation gives more feeling on the composition of the SCR, and the required capital and the deltas and there you can see the market risk is still below 50%. So our claim that we are an insurance company not just an investment fund is by that sense still substantiated. And finally, the LAC DT, the ever famous loss absorbing capacity of deferred taxes is at 74%. It increased, we moved the LAC DT of life from 60 to 70 and non-life from 75 to 90. Please note that increase is solely due to the increasing of the DTL. There are no future profits in the substantiation of our LAC DT.

In this year we made various efforts and we created a significant DTL in the year. As a matter of fact, both our life and non-life entities now have a net DTL position, so no DTAs in the net DTL position. And the increase in the deferred tax liability that we felt comfortable to use to further strengthen our LAC DT ratio, so very well founded, no future profit and delta, we use only a DTL movement, moving our LAC DT to 74%. In a later page in the pack you can see the solvency of the underlying entities both life and non-Life are Solvency II at 185% mark. So in terms of solvency stock, we feel comfortable with the level of solvency that we hope.

Moving from stock to flow. Page 16. As you know, there are various ways to decompose or to bucket the delta and solvency. From beginning of year to end of the year, our ratio improved by 7 points. One way of analyzing that delta is by using capital accretion, which is on page 16 where we define sources and uses of capital. Source of capital is operational capital generation, what does the business generate in terms of long-term investment margins and additional returns, what is the book release of capital and what are the deltas or net effects of assumption changes in business developments, that would generate 1.1 billion organically and 300 million operational Tier 1 issuance.

And then the use of capital while it's absorbed by the UFR unwind, absorbed by the cost of hybrids and capital that we required -- that we invest into market risk leads to a capital accretion of 742 million, out of which in the last year we paid out roughly two-thirds, 255 in share buybacks, two-thirds in dividends and we retained one-third in our balance sheet. So one way of depicting or decomposing the delta and solvency is capital creation sources and uses of funds.

The alternative more classical way is on page 17 which is the organic capital generation. As said, our solvency increased from 189 to 196 or about 7 points. Of this, in our definition, which is reasonably conservative, define an organic capital generation creation of 377 million or about 11 points of starting solvency. Appendix G in the pack, that gives more information on that very number. There is lot of analysis going out there on the assumptions that are embedded in your OCC, especially around market returns. I think it is a great piece of work by (inaudible) actually on looking at various metrics that people use. In the appendix we tried to give you alternative use.

Page 17 is our definition on our long-term investment assumptions the way we run the business, but we don't mind providing a service to the analyst community. So we've done some work for you in aligning it to market consistent numbers. On the pack, please note, the total own funds in the year increased by 712 million, 712. So if you add the numbers above the line delta EOF, 712, which includes the absorption of the decline in VA. In the standard model, the VA during the year declined by 9 points, which shaved off 9 points of solvency, so I could say, even excluding the VA, we would have generated growth almost 30 points of solvency in the year.

Other points to note, the risk margin release is kind of similar to the UFR unwind. It's not our achievement, but it's a nice coincidence which means UFR unwind and risk margin release is roughly similar, so I mean the SCR release actually really contributes to free capital. Also note that our dividends at the 230 million of ordinary dividends, represents about 60% of the organic cap generation and 80% of the operating and business cap generation which means the 60% is a number that those of you who have been following us since the IPO are familiar with. Although we pay our dividends based on operating profit, 45 of operating profit, but given that the OCC tends to be around 70%, 75% of the operating profit, 45 times 70% equal roughly 60% which is the payout ratio as a function of capital. So our ordinary dividend is about 60% of the total organic capital or 80% of the operational cap generation. That's the capital excluding book release. So that means our dividend payment to our perspective is sustainable and well founded in replicable capital generation.

Page 18 shows the sensitivity of the Solvency II ratio to the UFR. As you know, the UFR will be lowered, actually has been lowered in the beginning of the year from 4.2 to 4.05. That will cost us 3 points of solvency which is it's a given. Interesting to note that we steer the business increasingly on an economic UFR. We've talked about it before. At this point, we've estimated economic UFR at 2.2 because 2.2 is -- a UFR it has consistent -- safely consistent with the investment yield that we are generating today.

At that level, our Solvency II ratio would be 150% and we believe that number should be compared to 100 plus a margin, 100 plus the buffer. We could even see throughout the year that if interest rates continue to go up, that 2.2 might be gradually moved upwards. We'll do some careful homework before we go out with formal guidance, but the direction on that number, the direction (inaudible) was up rather than lower, so the 2.2 should go up rather than down given where markets are which should give you comfort on the economic UFR adjusted solvency position of the Group.

And if you were to strip out UFR and the VA altogether for what some people claim to be an exit value for the group, that's safely over 130% and for the life business also significantly above zero. So ex-UFR, ex-VA, the group is at 133% and if you adjust for tiering, we would be 122, but then you can do the refinement of the model, safe to say ex-VA, ex-UFR, this group is still very solvent and very well able to pay any dividends. I am proud to say that the UFR ratio at a 2.2, so our economic UFR actually also increased by 8 points, in line with the headline increase.

From solvency to balance sheet, page 19, shows you numbers on our balance sheet. We would think, or we are convinced that we have a strong and resilient balance sheet. You can see the solvency position and the headroom that we have, the leverage and the maturity profile. Couple of points to make. You can see the financial leverage of the group stable 25.2 to 25.3. Despite adding a 300 million RT1, the financial leverage ratio stayed stable and to preempt your questions, if you had a debt over equity, so very basic D over E calculation, that also, ratio would have stayed stable at 33.7 to 33.8. So there is no numerator/denominator play at hand here. So it's levered the group very, very stable.

Actually if you look at our leverage, we report 25.3 on an IFRS basis. If you adjust for the fact that we have a shadow accounting IFRS scheme in which we do not add realized capital gains to our book value, if you were to adjust for that, the leverage ratio would be in the low 20s, around 20%.

If you think that -- if you take into account that the S&P leverage ratio is 18% and norm for the group is 40%, although very well below the single A norm.

And finally, if you look at solvency as a percentage of a cap or leverage as a percentage of solvency, it's about 28% of unrestricted Tier 1 which is low for the industry. So in summary, headline leverage 25.3. Actually if we redeem the Tier 1 note that if -- where we refinance the call, the leverage will go down to 22. Shadow accounting adjusted, let's put that way, is low 20s. S&P leverage 18, only half of the 40 and Solvency II basis only 28% of unrestricted Tier 1. Again it's a long way of saying we have substantial financial flexibility. We have room to add leverage and because we've got all the instruments out there, we've got headroom, we can pick and choose the instrument that we like. We have headroom in Tier 1, Tier 2 , Tier 3, and we've got various T1, T2 instruments. So we can pick the instrument we like. Were we to add leverage, there is no constraint from our balance sheet whatsoever.

Page 20 is called unencumbered access to pools of liquidity. Not sure who came up with this title, but I guess our IR team was close to its karma when they made the pack. Anyways I think what we are trying to say is that we have been able, and are able to upstream cash to the Holding. You can see the bridge from holding cash beginning of the year to the end of the year at 518 million. Totally, upstream funds up 27% in the year from 407 to 518, which is excluding by the way the benefits that we have from creation of DTL. The DPL creation led to inflow 200 million of cash, which we deliberately kept in the life insurance business. So upstream is up from 518 to the holding. Whilst we upstream cash, think about the 518, roughly 400 in life, the remainder in non-life, whilst we upstreamed, the solvency ratio of the entities are at 185 and 186, up plus 5 or plus 4 during the year.

So the life and non-life entities upstreamed cash during the year and still increased the solvency by 4 to 5 points. And our remittance, it exceeds the organic cap generation and it actually exceeds the result after tax and after hybrids, and finally also low double leverage. So to compound and to build on the previous sheet's message, we can raise debt if we want to. We've got substantial flexibility and also there is no blocking issues to cash, we can and upstream cash to the holding. We just decide strategically [ph] to hold the cash in our operating entities. But the combination of upstreamable cash, solid solvency levels at the operating entities, low double leverage gives a huge amount of financial flexibility for the Group.

Happy to take your questions if you have those in the Q&A. Jos, back to you for wrap-ups and some final words of wisdom.

Jos Baeten {BIO 2036695 <GO>}

I hope that's not a message according to my age. Thank you, Chris. I will conclude with the key takeaways. From a management perspective, we are pleased, as said, with the strong operating results. We had truly a very good and record year driven by strong performance in all of our business segments. We deployed the capital -- the capital profitability, generating an operating return on equity at 15.6% and we can offer our shareholders quite a considerable increase in the dividend per share and the prospect of an attractive interim dividend starting in this year.

Our balance sheet is strong, as Chris explained, and we have substantial financial flexibility. The insurance entities are highly capitalized, offering ability to upstream cash to the holding if and when needed. On all counts, we are outperforming current medium term targets. Put differently, our business is delivering top quartile performance while these provide us a comfortable start into the New Year. However, while we strive for nothing less, it does represent a level that is very challenging to outperform this year.

Before we open up for questions, a few words on how we look at 2018. Based on the strength of our balance sheet, our financial flexibility and current high performance of our operating businesses, we believe we are in excellent shape to seize all key insurance opportunities over the medium term. Our businesses are simply doing well. Our dividend-paying capacity is strong, and we assume a stable growing dividends going forward.

At the same time, when taking into account the already high level of operating result in 2017, which is partially driven by exceptional favorable operating conditions in 2017, and the low amount of large claims in Q1, the uncertain developments in today's financial markets as a result of which direct investment yields have been reduced and the 30 million impact from the January storms, we reckon we have a slightly moderated earnings level in 2018. This will be partially countered by the earnings contribution from the Generali acquisition and selected re-risking. The earnings contribution from Generali will normally grow over time as synergies are received. Also, we will act responsibly in further re-risking our balance sheet, given the state of financial markets.

With that, ladies and gentlemen, we are happy to take all your questions.

Operator

Thank you. (Operator Instructions) We will take our first question from Cor Kluis from ABN AMRO. Please go ahead.

Questions And Answers

Q - Cor Kluis {BIO 3515446 <GO>}

Good morning. Cor Kluis speaking, ABN. Couple of questions. First of all about the Solvency II ratio, the roll forward from the third quarter toward the fourth quarter and the outcome is around of course now 193, but the dividend is minus 6, the VA is minus 3. So could you give all the components in specifically in the fourth quarter? Second question is about operational capital generation, especially for the own funds piece. I think if I calculate it that come to around EUR40 million in the fourth quarter. It was somewhat lower than previous quarter, so could you give some indication why the own funds was a little bit less enhanced by that? And my last question is about this Solvency II ratio year-to-date that we had followed through the start of the year. Of course, the VA probably went up somewhat, I think at least at the market effects year-to-date for your Solvency II ratio. Those were my questions.

A - Chris Figee {BIO 18815839 <GO>}

Okay, Cor, it's Chris. When it comes to the roll forward of Solvency II in the third quarter, net-net we moved up from 193 to 196. You are roughly thinking that the VA took out about 3 points from that number in the quarter, the dividends took out about 7 points in the quarter and the LAC DT addition added about 5 and the remainder is the combination of three things which is business capital generation, excess return in markets and further investments into required capital into especially real estate.

So in the fourth quarter, in the required capital, we added more real estate to our balance sheet. And the lowering interest rate in the fourth quarter increased the SCR requirement, simply because the capital charge on longevity our lapses go up. Simply it's an NPV phenomenon. When rates go down, life capital goes up, so basically you take out 10 for VA and dividends at 5 for the LAC DT which will get you to 188, we got to 196 and the remainder really is the company -- is the combination of operating cap generation, good financial markets and addition of capital.

And the own funds development in the fourth quarter was lower than expected. I think it was roughly in line with where we were. The fourth quarter, as you see on the business, was slightly lower contribution from non-life in the fourth quarter from disability, but in line with previous -- with the average of course of earlier quarter. So to us nothing peculiar or nothing that was out of the ordinary in the fourth quarter.

In terms of market development this year, solvency, couple of things happening, three. One is, the UFR was officially lower, so that takes up 3 points out of your solvency. Secondly, markets were down a bit that shaved a bit of solvency out as equities were lower and the VA was up a bit. So basically the solvency take out the UFR of 3 points, will bring you from 196 to 193. And then I think the market are a very small drag, but the last time I looked was a week and a half ago and since that the markets are up, so we don't really look at it on a weekly basis, think of it as, yeah, roughly stable in the year.

Q - Cor Kluis {BIO 3515446 <GO>}

Very clear. Thank you.

Operator

We will now take the next question from Arjan van Veen from UBS.

Q - Arjan van Veen {BIO 5197778 <GO>}

Thank you, gentlemen. Couple of questions on the life side and one on the integration, please. The life re-risking of the asset side, did that helped your investment margin in 2017, I was just curious as to how much more to go and then should we expect that to drive earnings a bit more in 2018? The second question is more on the reduction in the life gross written premium as well as new business AP, so just curious as to whether that's kind of in line with your plan or are you a little bit disappointed with the growth in the life given it missed consensus on program, both metrics. And then finally just on the Generali acquisition, what do we assume the -- what they do [ph] earnings start coming through into the numbers just for our modeling purposes. And then I assume you will update on that in more detail at the Capital Markets Day on the 10th of October.

A - Chris Figee {BIO 18815839 <GO>}

Okay, Arjan, let me talk about life and re-risking. The Appendix L, from Leo, has actually more details on the life segment. There you can see the direct investment income in the year, so it moved up from 981 to 1,000, to 1 billion equity direct cash income during the year. So we really received coupons, rents et cetera, so no capital gains et cetera at all. So you can see how this thing developed during the year. Normally the first half tends to be higher than second half because the dividends are recorded in the first half, but you can see if you read that there was 19 million of additional direct investment income, partially as a consequence of the re-risking of the business.

How to think about it going forward? Best estimate is to have it stable. There are couple of things at play. One is your yields are still depressed and falling, meaning it's getting more and more expensive to buy a certain earning stream these days in the markets. Whether it's you buying a stream of rental income, or whether you are acquiring mortgage income, whether you are acquiring credit spread, so there is some downward pressure on direct investment yields, mostly because in a mortgage book, some of the very profitable vintages here, since 2008 the vintage here is being redeemed as we speak and replaced by lower rate mortgages. So that is inevitable return that all financial institutions have. However, we see some room to continue to add risk to our balance sheet. At 47% market risk, we can continue to add risk to the balance sheet of ASR, so we can probably cover up or compensate the gradual downward push on yields with gradual re-risking. We're putting through a number of initiatives like the Triodos initiative Jos mentioned to acquire more illiquid assets. We believe there is opportunities to do, continue to add to real estate business to keep the direct investment income in the life business stable, but that will require some gradual re-risking in the year. Where we see opportunity is mainly in the real estate space, so stable and if we continue to re-risk during the year there might be a bit of upside, but depends a bit on how markets develop.

Before I give to Jos, on the Generali earnings, we indicated a 30 million potential net operating profit contribution from Generali. That number still stands. In our work on the integration overseen so far confirms that opportunity. I would safely say that is not going to come overnight, so say it would be a third, a third, a third in the next three years. We have some room to move to little bit faster in the first year as we start cutting costs and add the investment business to our book. So 30 million at one-third each of the three years with some upside in the first year. If we indeed succeed on the moving of staff and the legal merger that we plan to conduct in the second half, I mean the moving of Generali staff into ASR buildings, the legal merger, that will be important triggers, and if we indeed succeed in that, we may outperform that rough timeline,

Q - Arjan van Veen {BIO 5197778 <GO>}

Sorry, just on Generali. From an IFRS and to see, so your account starts from the 5th of February or is there a different date we should think about?

A - Chris Figee {BIO 18815839 <GO>}

Well, maybe in the 5th of Feb, the 1st of Jan. 1st of Jan, it's a full -- we mean that the one --

Q - Arjan van Veen {BIO 5197778 <GO>}

Okay, you would be backdating it to 1 Jan actually.

A - Chris Figee {BIO 18815839 <GO>}

On the Generali earnings, the first half cutting [ph] are not so big that one month will make that much of a difference, so 1st of year.

Q - Arjan van Veen {BIO 5197778 <GO>}

Okay, thanks.

A - Jos Baeten {BIO 2036695 <GO>}

And, Arjan, this is Jos on your second questions on the development of the gross written premium in the life area. To judge that you should take into account in 2016 we had to add, in total, roughly 500 million of one-off single premium due to the acquisition of NIVO and a large pension contract called Astra contract. If you strip those two out and you would compare the organic development of the life premiums, we are relatively satisfied, given the fact that in the Dutch market, the individual life books are declining and we were able to almost compensate them and not fully by the growth in our pension book, so the total decline of life premiums if I take out those two one-offs in 2016, it's roughly 2.5% to 2.6%, which is in line with our expectations. And we will not be able to fully compensate the decline of the individual life book by growth in our pension business, as long as we keep up to our strategic value over volume. We only want to do business in this area if we can offer prices that enables us to deliver the value also from a shareholder perspective. So nothing unexpected from our perspective. Yes, it is down a little, but we are happy that we were able to compensate those gross written premiums that declined in individual life with the new business in DC, in pension DC.

Q - Arjan van Veen {BIO 5197778 <GO>}

Okay, that's very clear. Thank you.

Operator

We'll now take the next question from Farooq Hanif from Credit Suisse.

Q - Farooq Hanif {BIO 4780978 <GO>}

Hi, there. Thank you very much. Just wanted to go back quickly to Generali Nederland. I remember you talked about roughly, I think, 15 million to 17 million of synergies which I think are included in your 30 million already. As you look at the business, I mean what are the main areas that you've allowed for that, and what have you not allowed for in that? And then secondly, in the disability business, at what stage will you get an indication from UWV on pricing for the base of 2018? And do you anticipate a time where that will become more reasonable given the data that's coming through and it will allow you to step into that market to grow more? Thank you.

A - Chris Figee {BIO 18815839 <GO>}

Hi, Farooq, it's Chris. On the Generali synergies, those are -- the 15 to 17 are all cost synergies, the real cost that's in there because this really is a cost play. So that's within that. What is not in there is the benefits from re-risking because we think that additional -- there could be potential values from that, but I'm required a commitment of capital. At this point, we have reserved 2 to 3 points of solvency capital to add to re-risk the Generali business, but we'll do it carefully. Given the state of financial markets we are not going to go overboard and play risk. The business case in Generali should be a cost game, so we want to meet our targets based on generating cost synergies as we planned. So the 15 million to 17 million is cost and those are all on track and with that we will meet our return hurdles. That could be on top of that additional room for re-risking which will gradually feed-in during the year. Think about 2 to 3 points of solvency that we could add, think about between 5 million and 10 million of potential additional investment earnings that will feed in during the year.

A - Jos Baeten {BIO 2036695 <GO>}

And, Farooq, I am happy to take your second question on the visibility. The UWV calculates its premium based on the claims cash out in a certain year and they divide this through the number of customers they have and that is the actual premium in a certain year. As an insurance company, we have -- when we calculate the premium, we have to take into account future claims solvency developments, et cetera.

So to your question, it will take a number of years before we will be able to compete with the cash-based system that is used by the government. But as soon as their customer base grow, their claims will grow. And so the average premium they have to calculate will go up and somewhere in near future the premium level of the government will meet ours. So we are in the market. We have customers in the BeZaVa, but the growth was not as big as we projected at the IPO, because we also need to make money. So we want to be careful to compete with structural unprofitable premium from an insurance point of view. So it will be not from the 1st January of this year to the 1st January of next year, but it will grow gradually over the next two to three years.

Q - Farooq Hanif {BIO 4780978 <GO>}

Very clear answer. Thank you very much.

Operator

The next question comes from Robin van den Broek from Mediobanca.

Q - Robin van den Broek {BIO 17002948 <GO>}

Yes, good morning, everybody. Referring to slide 19, it seems that you have quite a bit of firepower on the S&P framework, but on your website, you've also disclosed a document on the RT1 issuance which stipulates a cover of only 5.7 times. And I think that S&P in the past did indicate that if you drop below 4 times that would mean a downgrade for the Group. So how does that tie into the flexibility on financial leverage these slides are telling us? That's question one.

And then question two, if you have that much pace on financial firepower, what should we think about what you will do with it? I mean, I think you have been quite clear that you have a focus on M&A at the moment, but you've thus far always focused on small bolt-on. Could you consider larger deals? I think press was recently indicating that (inaudible) and maybe even (inaudible) books could be up for sale. Is that something you would look at, or would you remain committed to small bolt-on M&A and how would that affect your capital distribution policy? I mean, the DPS announcement today is very welcome, but it seems you could do more. Last year you indicated that your capital distribution would be capped, that's the capital being generated in the year. Is that something we should also consider for this year or will you deviate from that path? And my third question is on the life operating results for the fourth quarter came in at 167 million. Is this -- do you feel comfortable with this level going forward excluding the potential add-on effects from Generali or are there some one-offs in that 167 number per quarter? Thank you.

A - Jos Baeten {BIO 2036695 <GO>}

Let me start with the middle question and Chris will come back to the first and the last one. The way we look at the market currently in relation to our capital position is that the base of our strategy is organic growth combined with inorganic growth in certain areas and like we have said in the past that there is, in the funeral business, we like non-life portfolios. That's why we acquired the Generali book. And if we would find further potential investment opportunities in the asset management area, we would certainly look at that. So that is the core of our strategy.

In terms of would you be willing to look to other opportunities, and like you mentioned, the potential individual life books from Dutch competitors they are going to get rid of it and now we almost have concluded the conversion of our own books to the software as a service platforms. We are perfectly willing to look at further consolidation of the Dutch individual life market. I think we are well positioned. As far as I know, we are the only insurance company in the Netherlands with a variable cost platform in life, but we've always said we first want to do our own books and that's not fully done, but we are now convinced that we are able to transfer a portfolio to this platform.

The first one will be the Generali portfolio going forward, but if and when there are interesting opportunities in the Dutch marketing regarding to life, individual life books, we certainly will take a look at those. And that's the way we would love to deploy capital. So we are happy with our current capital position and willing to deploy towards all kind of organic and inorganic growth. On top of that, we have announced the interim dividend stating that we are willing to deploy capital also to shareholders. And as said in my presentation, if and when we can't find any organic or inorganic growth opportunities and our capital continues to grow, we are willing to deploy -- to look how to deploy this capital and that's why we, as said, have announced the interim dividend already.

And the last remark to make is if and when there would be something big in the Dutch market, we've always said that's not our primary aim. We're not calling people, but if somebody would call us, we are always willing to have a talk, and to have a discussion whether it fits within our strict financial criteria.

A - Chris Figee {BIO 18815839 <GO>}

Now Jos has to think how we will plan to deploy the funds. Let me shed some light on how we can raise. Your point on fixed charge coverage is valid, although the prospectus really had pro forma numbers, as I recall, using last year's operating profit divided by the interest charges of the hybrid including tier 1. This year's operating profit number is already substantially higher. So if you run this number I think you end up 5.9 or 6 times interest cover. And on an IFRS basis it's 16 times. So it's not 100% clear which number S&P will look like. I think S&P does not necessarily look only at operating profit, they look at a sustainable earnings power. So probably in their prospective the number is between the operating cover and the IFRS cover, so operating is now at 6 times, IFRS coverage at 16 times. Also note that, in that is two very expensive hybrids at 10% coupon. If those are being called or refinanced or even called, because we did (inaudible) aim of calling these core Tier 1s. That 20 million pre-tax interest charges drop out, so the very expensive ones drop out. So it means if you do that, the interest cover goes back to 8 to 9 times on an operating basis and on an IFRS base even higher.

And my IR people tell me that actually S&P tends to look at IFRS rather than the operating income. So operating is our own conservative view. So if you take into account from a leverage perspective or from an interest cover perspective, there is no limitation or there is some limitation, but not an immediate limitation on the horizon. If we were to raise 500 million to 1 billion that is something that the group could bear. And if you allow me to make a statement about the 30% mark, there is some misconception on the 30% leverage norm. We said we strive to have a norm that's below or around 30% on an IFRS basis. In my little speech, I showed to you that there are various metrics that we could look at. I think we should not take, given where rates and yields are today, given where the interest cover is today and given the way our balance sheet is structured, I think we could even look with something at north of 30 doing -- below 40, between 30 and 35 leverage would also be definitely feasible for us. So in terms of financial flexibility, we should not feel ourselves to be overly constrained.

Q - Robin van den Broek {BIO 17002948 <GO>}

Final question was on the --

A - Chris Figee {BIO 18815839 <GO>}

On the life earnings. I think, as I said, the dividend, the income from investment is probably stable. As I said, the income from the -- the operating income from the capital gains reserve is stable at now 3.2 billion, so it has been north of 3 billion for -- so I think for four years, so as long as I can remember. So it's substantially above 3 billion. So we think the release on cap gains reserve should be there. The only thing we -- and to think on the cost side, our cost resources is likely to be stable. The one thing where you can see some downward pressure is the mortality reserve simply because the book will shrink over time, so you may see some downward pressure on the mortality result. So fair to say, stable to a gradual downward pressure from the inevitable shrinkage of the book over time. But we feel pretty comfortable with that. Are there one-offs in the life business, yes, a few positive one-offs, but my history tells me, you always have one-offs. So even if they don't reoccur, there will not be such a massive change in life earnings.

Q - Robin van den Broek {BIO 17002948 <GO>}

Okay, thank you. Those are very clear answers.

Operator

(Operator Instructions)

A - Chris Figee {BIO 18815839 <GO>}

Jos just tells me, in the end we are all one-offs, that's a very good way of looking at our business.

Operator

(Operator Instructions) We'll now take our next question from Kunal Zaveri from JPMorgan.

Q - Ashik Musaddi {BIO 15847584 <GO>}

Yeah, hi. This is Ashik here, I am just using Kunal's line. Just couple of questions I have. So first of all is, your IFRS book value has gone up considerably in 2017. Can you give us some sense about what is the reason for that? I can understand that operating profit and dividend, there is a bit of difference, but I think there is something to do with cap gains as well. So why is cap gains reflecting in IFRS book value if you follow shadow accounting, so that -- what are we missing here? So any thoughts on that? And secondly, just for modeling purpose again, if I look at your amortization of this realized gains reserve, should we keep it at stable at 2017 level which is around 320 million or do you reckon that it could go up or down? Any color on that will be great. Yeah. Thank you.

A - Chris Figee {BIO 18815839 <GO>}

Hey, Ashik, well, the book value went up because of a couple of points, retained earnings, non-pay of [ph] dividends. Secondly revaluation of those assets that are not shadowed in a shadow accounting reserve, so shadow accounting has fixed income, but those assets that are not in fixed -- not fixed income, i.e., real estate or equities, those revaluations are reflected in our IFRS equity, because they are not in our operating profit, right. I mean, operating profit only has direct investment yield, so no cap gains, but in the IFRS equity, the cap gains on those asset classes are not part of shadow accounting are a positive contribution. And finally, there is IAS19 deduction, which declined a tiny bit during the year, so it's a smaller negative actually becomes a positive. So those three elements, retained earnings, revaluations of asset classes not part of shadow accounting and a smaller deduction from IAS19 pension accounting, those account for the delta in IFRS book value and your capital gains reserve release. I plan with a stable number. I mean, if you look at our multi-year budget that has a number stable over time. So we feel comfortable sharing that message with you, stable number

Q - Ashik Musaddi {BIO 15847584 <GO>}

Yeah. Thank you.

Operator

We will now take the next question from Johnny Vo from Goldman Sachs.

Q - Johnny Vo {BIO 5509843 <GO>}

Yeah, hi. Thank you very much for letting me ask my questions. Just a couple of questions. Just, look, if I look at the solvency of the life entity alone and forget about the consolidated solvency which is influenced by debt issuance and so forth, it actually declined by 1 percentage point half on half despite you actually adjusting the LAC DT, which added north of 5 percentage points to solvency. And then it looks like you've significantly paid out more than you generate. So is this remittance coming from the entity abnormally high? That's the first question.

The second question just comes back to like further buyback potential. If I look and I take into consideration your solvency like reduced by 9 percentage points for the transaction with Generali, you will have some negative adjustments for UFR of 3%. Cash in the holding will have to reduce by the dividend you are yet to pay. Also your dividends are going up and there's a bond that you need to redeem in 2019. Unless you raise further debt, it doesn't look like you have that much cash available. And given the pressure on solvency, it also doesn't look like you can sustainably transfer high remittances out of the entities. Can you comment on that as well? Thank you

A - Jos Baeten {BIO 2036695 <GO>}

Johnny, Thank you. When it comes to our solvency in the life business, it declined by 1 point during the year, but note it increased by 1 point in the last half year, but has increased by 4 points during the year. In spite of in total I think about 400 million that we upstreamed from the life entity during the year. So in spite of a 400 million upstream, it moved up by 4 points year-on-year. 1 point decline half year, I don't -- the solvency ratio is at 186%. If we were to eat 1 point per half year we could continue to eat for a long, long time. If you think about our solvency in the life business ex-UFR or ex-UFR and VA, that's still substantially high. Ex the UFR of 2.2, the life solvency level is about 122 of the life insurance entities. So the economic solvency of the life business is still safely well above 100, ex than with the UFR of 2.2 and as said, the 2.2 is more likely to go up and to go down, so with that feel that the life insurance entity itself is very well capitalized with 200 million of upstream -- 400 million upstream in the year.

If you think about further about the solvency in the -- the EOF during the year is about 5 billion, it declined by 100 million in the first quarter -- in the second half of the year because of upstreams. So what happened to the solvency ratio especially the addition of risk, so we added more real estate risk in the fourth quarter. We added higher charge from longevity capital and from lapses because the rates fell. So the below the line numbers increased from real estate asset allocation and from longevity and from lapses. So we are not at all concerned about the solvency level of life at 186 standard formula increasing by 4 points during the year. At 122 standard formula, at 2.2 UFR, these are just very solid levels that give no concern about what if and how we can upstream to the markets. And if you look at the amount of fungible capital or the amount of EOFs, still 5.1 billion.

So, in that sense, we are not concerned about further upstreamability. When we look at share buybacks and our potential, I mean, fair enough, I mean, we ended the year at 196 solvency, take out an initial 9 point of Generali which will add back -- add solvency back during the year of integration, but the first closing of the deal and the merger of a lower solvency business with the higher solvency business, it erode 9 points of solvency from our group. They got 3 points of solvency from the UFR. We'll give you slightly lower solvency level, but the UFR decline will also add back to OCC. So it will basically move from stock to flow, so the UFR decline as such I am really not worried about and that's the way we have taken into account when we look at the 2.2 metric.

So we see no impediments to return capital to shareholders. The Generali will take us some capital in the beginning, but there will be capital synergies during the year or later on as the integration takes place. And the Generali business will add to earnings. So you should see our business as a dividend stock with substantial dividend-paying potential. Dividend as a function of organic capital generation, of own fund generation is still very, very safe. We've committed to you this year or we aim to give over 300 million of capital back to shareholders in a base dividend and an interim dividend. I do not see why that would not be sustainable. As even the combination of this year as base dividend, plus interim dividend is less than the OCC that we generate. So if we continue to do this and distribute 300 million plus to shareholders, which I think is about 6% of our current market cap, that means then still the life business would not erode solvency except for the gradual decline in the UFR that will get back to flow in higher OCC. So, Johnny, I hear your point, but in terms of numerical analysis, you are probably correct. In terms of what the business is doing and our policies, we see no limitations there.

Q - Johnny Vo {BIO 5509843 <GO>}

Okay, thank you.

Operator

We will now take the next question from Benoit Petrarque from Kepler.

Q - Benoit Petrarque {BIO 15997668 <GO>}

Yes, good morning. It's Benoit Petrarque from Kepler Cheuvreux. Yes, couple of questions on my side. The first one will be on your long-term investment return assumptions. Any updated levels into 2018 on your assumptions, what do we need to plug in our models on that one? On the cost base, so you have a cost-cutting target of 50 million, you've reached 41. Out of the 41, I was curious how much is actually coming from the M&A you have realized since the IPO? So much has been coming from the inorganic, well, basically consolidation of the cost base and your cost reduction on M&As versus what is coming from the organic growth of the cost base? And then maybe last one will be on the (inaudible) models. Can you update us on potentially your view on the standard formula, also looking at the EIOPA plan changes on the formula, any thoughts on that, any plans to move to (inaudible) models? Thank you,

A - Chris Figee {BIO 18815839 <GO>}

Okay, Benoit, thank you. I will take the questions. Finally someone asked the question about (inaudible) I thought that you guys would be all over it but apparently it is clear. Let me go to Appendix G and our mark, because this is an assumption we will not change our long-term investment assumptions, I mean, they are public and we look at our business to move up. It measures across the cycle. So, we believe these are across the cycle assumptions. So where did they move, over time where have they moved. What we're seeing, if you look at the actual spreads and the model spread that the government bond spreads has moved closer towards our model. The small drag from core govies to what we assume, but they've moved very close to where we are, so that drag is actually kind of meaningless today which by the way also means that our swap spread hedging trade has worked well. I mean, remember in this year, we hedged the swap spread risk and that trade has come out very well as the swap spread between core governments and swaps has narrowed. So we're seeing the drag if you wish from govies, core government has narrowed substantially. At the same time last year these credit spreads have also tightened. So there is a bit of a drag from the credit side. There is still a plus from the mortgage side, mortgage is still more than OCC assumption and non-core peripherals have also tightened a lot, although that has changed in the past few weeks.

So we don't change our long-term investment assumptions. We believe they are fair over the cycle. Where core governments are getting closer to our model, credits have drifted away a bit. Sovereigns have drifted away, but are recovering. And on the mortgage side there is still substantive spread. But if you look at the page number, page Appendix G, the net-net of all of it there is still about 9 million to 10 million understatement of the OCC from this perspective. On equities and credits, the 300 basis point or 330 basis points are still fairly conservative. If you work with 7% as some of our peers do, that would add substantive more to the OCC. We continue to work with these spreads, but this is actually what has been realized. And the actual return on equities last year was even larger than that.

Maybe if you allow me to make few other remarks, we've also showed the impact of our hybrids, I mean it's unclear where industry is landing in terms of hybrid expense and OCC. If you exclude the 56 of hybrids, this is the number, of this 20 million base stuff it goes through the P&L, 36 is (inaudible) and go through OCI. So you can play around with these numbers. And finally, it's the UFR drag. We have noted that there is also various ways to deal with the UFR drag in the industry. We take really conservative view. 31st of December pinpoints or actually Q4 of last year UFR drag and Q4 this year's UFR drag, gives 101. If we had done a more frivolous calculation, I could have argued the number was at 10 million better. That will gradually show with the numbers as we develop.

So we still believe we've got fairly conservative way of doing stuff. The way I do UFR drag, you could argue it's 10 million less, we could have argued part of all the hybrids up in the OCC, you could have argued how you work with spreads, but we work with a long-term across the cycle assumption. That's kind of in line with how we run our business. So that's going to -- we will stick to that. But we hopefully Appendix G gives you a bit of our handle on to analyze these numbers.

Should I also take your question on the standard model?

A - Jos Baeten {BIO 2036695 <GO>}

Yeah. And then I will take the cost question, Chris.

A - Chris Figee {BIO 18815839 <GO>}

We are running on a standard model. We firmly believe in that. It's the best and it's a very cost efficient way to measure capital. However, we are aware that EIOPA will come with a review of the model sometime soon. It's probably expected any day, any week now. That could give us potentially reason to revisit the standard model if we feel it is no -- much less appropriate than what it was today and sometimes we look at where some of the numbers are that other players use, would give us slightly different outcome. So it's not that we are -- it's not in principal against -- it's internal [ph] certainly not. For now we think it's the most cost effective way to use the standard model, but we will keep a close eye on the EIOPA rules and regulations. We will keep a close eye on the progress on IFRS 17, because moving to an internal model will keep the same people busy, but also the IFRS 17 implications. But we certainly will not -- do not rule out, we certainly do not rule out ever moving to an internal model.

A - Jos Baeten {BIO 2036695 <GO>}

Thanks, Chris. Benoit, on your question on which part of the cost reduction is already realized, 41, which parts came out of the M&A and which part is, let's say, organically. The larger part is organically. And it's not exactly to pinpoint how big the exact numbers are because an integration never takes place overnight. They flow in gradually. But let me give you a few examples. Last year, for example, we did no integrations in the P&C business and there the cost reduction was 4 million. In the non-life business, we reduced the cost per policy from 66 to 44, that was mainly organically. And there was one cost reduction which I can put a number on and that was the cost reduction on AXENT, that was last year 5 million. So let's say roughly two-thirds to a bit north of that is organic cost reduction and the remainder is due to already in 2015 announced M&A transactions.

Q - Benoit Petrarque {BIO 15997668 <GO>}

Okay, great. Thank you very much.

A - Jos Baeten {BIO 2036695 <GO>}

Does that answer your question, Benoit?

Q - Benoit Petrarque {BIO 15997668 <GO>}

Yes, thank you very much.

A - Jos Baeten {BIO 2036695 <GO>}

Okay, thank you. Well, we've understood there are no further questions. So thanks everybody for joining us today. As said, we were very happy with the results we were able to present. Some of you we will meet over the next few days. So we are looking forward to that. Others we may meet at the 10th of October when we will organize our first Capital Markets Day. In the meantime, we continue to do all the good work to deliver the results as promised. And as said, we are fully convinced that our underlying business will deliver performance again in 2018. However, we of course see the movements in the financial markets and we already have had our first storm in 2018. But having said that, we are fully convinced that we will be able to deliver a healthy and market outperforming results going forward. Thanks everybody.

Operator

Thank you. That will conclude today's conference call. Thank you for your participation. Ladies and gentlemen, you may now disconnect.