Q1 2017 Earnings Call

Company Participants

- Luigi Lubelli, Group Chief Financial Officer
- Spencer Lee Horgan, Group Head-Investor & Rating Agency Relations
- Timothy Fabrice Ryan, Group Chief Investment Officer and Chie Executive Officer of Asset & Wealth Management

Other Participants

- Farooq Hanif, Analyst
- Gianluca Ferrari, Analyst
- Michael Igor Huttner, Analyst
- Nadine van der Meulen, Analyst
- Niccolò C. Dalla Palma, Analyst
- Nick Holmes, Analyst
- Paul De'Ath, Analyst
- Thomas Seidl, Analyst

MANAGEMENT DISCUSSION SECTION

Operator

Good day and welcome to the Generali Group Q&A session. Today's conference is being recorded. At this time, I would like to turn the conference over to Mr. Spencer Horgan, Group Head of Investor and Rating Agency Relations. Please go ahead.

Spencer Lee Horgan {BIO 4241901 <GO>}

Thank you very much. Good afternoon, everybody, and welcome to this call to discuss our first quarter results and the new strategy for asset management.

We are going to have one hour in total, and we will finish on time because I know many of you have another appointment at 1:00. Tim Ryan, our Chief Investment Officer and CEO of Asset and Wealth Management, is going to walk you through the strategy for asset management, which he's announced this morning. After which, we will take your questions on both the strategy and results.

Before we hand it over to Tim, though, I will just pass it over to Luigi, Group CFO, for a recap of the first quarter results. Luigi?

Luigi Lubelli {BIO 4108780 <GO>}

Thank you, Spencer. And good afternoon, everyone, and welcome from my side as well.

I think our first quarter results continue to demonstrate the benefits of the strategic actions we are taking and the consistency with which they are being executed. Our operating result has improved by a further 4.2% compared to the previous year despite the pressure on investment returns and the impact of natural catastrophe losses.

When you look at our KPIs, the impact of our focus on technical excellence is clear. In Life, we have been able to improve the operating results despite falling investment returns, with improved technical and expense results. Even though our New Business volumes were slightly down by 2%, our strict underwriting focus has increased New Business Value by one-third, thereby significantly raising our New Business Margin by 10 percentage points to 37.8%. This is a good indicator of the increasing economic value of the business we're writing and is, of course, directly contributing to the healthy creation of capital under Solvency II, which we could also see in this very quarter.

In Property&Casualty, we were not as like as in Q1 last year, in which we had zero natural catastrophes, whereas this year we had some win and (02:06) losses, which accounted for 1.1% of the combined ratio. If we were to leave this aside, the other components of the combined ratio, that is the latest expense ratio and both the current year and the prior year loss ratios were virtually unchanged versus their levels at Q1, not to 2016 (02:23).

The overall combined ratio remains excellent at 93.1%. And in addition, we're seeing positive growth in the top line of 1.9% on a like-for-like basis.

The net result of the group for the period is €535 million, below the €588 million we achieved last year despite the higher operating results. This reflects primarily lower realized gains that is consistent with what you have seen before and in line with our strategy, and the higher tax rate. As we highlighted in the press release, in this quarter, we have taken a specific impairment on Alitalia accounting for €42 million net of tax.

If you normalize for the realization gains and for this higher tax rate the results and the figures we just gave, you would appreciate that the profitability momentum is strengthening quite a bit. Our solvency position remained strong. The Regulatory and Economic Solvency Ratios have both been stopped (03:28) by 1 percentage point during the first three months of the year, going respectively to 178% and 195%. The contribution of operating earnings remained very healthy and more than offsets the negative investment variances, primarily reflecting sovereign spread widening on government bonds in Italy and France.

Let me finish by plugging in advance one change we're going to make to solvency ratio from next quarter onwards. Instead of booking the annual dividend entirely in the fourth quarter as we have done in the past, we will accrue it during the year. For each of the first three quarters, we will accrue one quarter of the previous year's declared dividend, that is the €0.80 (04:10) we declared for 2016. Then, in the final quarter of the year, we will trueup for whatever the annual dividend we declare will be. This will have to smooth the progression of solvency through the year.

With that, I now hand the call over to Tim, who will give you the highlights of his new strategy for asset management. Go ahead, Tim.

Timothy Fabrice Ryan {BIO 17528640 <GO>}

Good morning. Thank you, Luigi, for presenting the results.

I'm excited to be part of the Generali Group. I joined in a very exciting time, the early part of the year. And today, I have two roles. I'm the Group Chief Investment Officer, as well as the COO for Asset and Wealth Management platform.

And I really want to quickly go through the strategy for asset management today, especially for (04:56) Europe, which is 96% of assets under management. And we have ambitious and transformational targets for our business, and I'd like to walk you through using the slides that you have received this morning early on.

So, the first element I want to go on slide number 1 is clearly we have two important elements on our strategy. Number one is to broaden and deepen our investment capabilities that we have. We have very strong investment capabilities on the insurance side; thanks to the balance sheet of Generali, as well as part of it distributed through the unit-linked and the variable annuities. But we don't have a full spectrum of capabilities yet and we have, as a group, and I would come back to this, needs to invest, and I will explain in which direction we're going to emphasize on building those capabilities.

Number one, broader and deeper investment capabilities. Number two is using those investment services to bring solutions to very specific group of clients, mainly in Europe and on the continent. So, this is a way to accelerate the built-up (06:11) that we will have over the next figures. Talking about years (06:14), let me give you the financial ambition that we have on the asset management for Europe.

As you can see on that slide number 1, on the graph, we are starting from a base that is low in many ways, low in terms of net result, €84 million of net result at the end of 2016. We will be at more than €300 million of net result after tax in 2020, which is a sizeable increase of more than €200 million, and I will explain how we get there. This will have an impact for the group after consolidation and after tax of €150 million. This will be done by improving a combined cost/income ratio from 71% today to 55% and lower. 71% is a bit high, 55% would be very competitive in the marketplace. That will be an improvement of 16 points on the cost/income ratio and mainly driven by revenue expansion.

The other part is the growth of asset under management will be from – growing from €446 billion to €500 billion. And this is not taking into account any market movement appreciation during that period of time. I want to be very clear about this. So, when we build the strategy, we start with where are our strength, and the strength is the Generali Group.

So for a few minutes, I will take my hat as a Group CIO. And the Group CIO, when I look at this type of challenges that we have in Europe, which are low-interest-rate environment, inflation in terms of price linked to monetary policy being very accommodative in Europe, the yields are quite low, as well as the corporate spreads are low; this is one element that is of worry for many insurance company, but not for Generali. And when we look at those aspect of dealing with a low interest rate environment, we are dealing and looking at two sides of an asset over an insurance balance sheet, the A and the L.

On one side, we need to find better solution on the asset side. And when we say better solution, we are talking about risk adjusted yield and return for the asset. On the other side, we have the liability aspect, and Philippe has been very clear in November 2016 about the necessity for the group to move more towards more than Life, i.e., moving from traditional Life to unit-linked and fee business.

So, in order to solve the conundrum around A and L into what we called ALM, we need to look at both side and the asset management piece is a critical element. Once you'll be able to deploy capital smartly and quickly and a very effective way in terms of capital charge, not just capital (09:12), so risk liquidity aspect. And on the liability side, the transformation of liabilities will come from the fact that we have a stronger asset management capability.

So, I'd like to move on that slide number 2. Clearly, the ambition is to help Generali Group. Now, I take back my hat as CEO of Asset Management and Wealth Management, where listening to the fact that we need to improve the risk adjusted yields on one side, it means for us, we need to offer, as an asset management company, access to real assets, and I will come back to what I mean by real assets in a few minutes.

The second part is the transformation of the liability structure will be driven by innovative investment solution, and I will come on this as well because we have a huge opportunity if we look at how much market share we have among our unit-linked from the asset management of Generali.

So, let me move to slide number 3, which actually highlights those potentials. So, I mentioned that one key element to be able to address the needs on the insurance side of the management of the main funds (10:24) is increasing real asset; and what we'll talk about real assets in this case. Well, traditionally, real assets have been real estate exposure. But today, banks are not so much taking risks on long-term dated loans. There's a lot of financing gap, where actually insurance company can step in and help the system – the financial system to be quite effective.

We, as insurance company, will be supporting this in different dimension. So, real asset means private debt, private equity investments. On the private debt side, think about infrastructure debt, infrastructure equity and SME lending, and different aspect. But you need very special skills to be able to underwrite those type of asset to analyze that, to source them and to bring them into a friendly capital environment for an insurance company and accounting operations. So, the real asset is a key component today at Generali. We have 7% of real assets and we are increasing this allocation.

The second aspect of the need from Generali, I mentioned, is transformation of the liabilities. Today if I look at the unit-linked business, over the €78 billion of assets that we have on behalf of our policyholder, we outsourced 86% to external managers. Our share of the wallet is 14%. We definitely can do better. We are not going to be 100%, but you will see what the level of penetration that we are expecting to have by 2020. So, those are two key important opportunities we have within Generali. But we need to deliver as an asset management group to be able to either invest in real assets and provide innovative solutions to our customer. So, how do we do this?

Well, we're going to innovate by creating a multi-boutique insurance asset management platform, this is slide number 4, and there will be two aspects of the multi-boutique. The multi-boutique will focus on one side on real assets; on the other side on high conviction strategy portfolio managers.

On the real asset, I mentioned already a few key assets or expertise we want to bring on board. On the high conviction strategy, the biggest focus will be on bringing on board multi-asset expertise and global equities across different geographies not just on Europe, but as well U.S. and emerging market, for example, as well on fixed income. This will be done in a very simple way.

We already have some expertise within Generali, but this expertise is only confined today to the needs of the insurance group and we want to open this to different set of customer. I will come back in a few minutes to this.

The other aspect that we want to do is we want to have an entrepreneurial spirit within this framework of multi-boutique because we believe that people make the difference in terms of performance and that's the key element for success of the strategy on the asset management in the active space. One thing that we will not compromise on is the control, and the controls are very specific for us. It means controlling compliance, risk management, and as well as audit and governance.

So, multi-boutique will be the enabler for us, obviously, in addition to a very strong asset management expertise we have on the insurance side, and we want to use this platform in terms of investment engines as we talked about broader and deeper investment capabilities and what we are doing it for. We're going to do it for Generali, first, as I've said, and secondly, leveraging this in two very specific segment of client analysis (14:16) moving to slide number 5.

Slide number 5 shows that we're going to specialize ourselves in the insurance asset management segment. As you know, insurance asset in Europe represent €9 trillion of assets and they are quite fragmented around more than 4,000 insurance and mutual companies in Europe. So, the mutual is quite an important institutional player, fragmented. And we have a know-how on how we can actually deliver not only ALM advice but also provide investment solution with a real asset experience that we have around a buildup of an insurance solution team to help us speak the same language as insurance company across Europe. The main focus will be Continental Europe for this business and segment.

The second part of the growth expansion that we will have is on individual client and savings. Definitely by bringing onboard high conviction, active managers will be a differentiating factor for all of our customers, and that will give us also discipline in terms of execution. The fact that we're going to benefit from the expertise, their track record will help us to offer better investment solution to our clients within Generali Group, as well as through different banking channel in terms of distribution, wealth management platform, IFAs. This will be done again in Europe.

Now, how can we move from an €84-million net result after tax for the asset management business into €300 million in 2020? We have five key levers, and we have a control on most of them.

Let me start with the fact that on one side, if I look at slide number 6, we're going to have a revenue expansion, but the fact that the insurance needs are growing within the real asset path, and we will optimize those fees. The contribution will be €70 million of net result from this expansion of revenue and relocation of asset.

The unit linked I mentioned to you, the unit linked is a huge opportunity for us. We only manage a portion of this today. We can expand further. Our assumption is we'll improve our penetration by 15 percentage points and that will give a contribution of €30 million by 2020.

Last not but least in terms of where we have a very strong control is operational efficiency. The way we are set up today, I mentioned that the cost/income ratio was relatively high. But we have really room for improvement on this by €20 million in 2020. And this is an action that I've already analyzed and took initial steps for us in the asset management business.

So, that's the first element. Three elements that is within the control. We will benefit from the growth of Generali and also of external clients. If you look at the growth that we can benefit from Generali, we will talk about the fact that we need to allocate more going forward as well to real assets and special skills and that will contribute to €60 million net result.

And the external plans, which is an important part to grow for us, but in this environment, like we are talking about the next three years (17:49), we'll contribute $40 million (17:51), it's not a very big stretch. It is attached to €20 billion of new assets mainly coming from the insurance side, but not only. And this is going to help us basically, if I look at €84 million to €300 million of net result after tax for the asset management business, triple the net result by 2020.

So, I wanted to share those elements in terms of strategy, in terms of focus. We're going to first build the investment capabilities across real assets, as well as high-commission portfolio expertise. And based on this, leverage the strength of Generali Group that is being in business since 1851 with €446 billion today of asset under management, we have the scale. We can actually grow. And those numbers are actually quite conservative numbers, have high conviction in delivering at least €300 million by 2020.

With this, I think it will be time for me to take some question with Luigi about the Q1, as well the asset management, and thank you for listening.

Spencer Lee Horgan {BIO 4241901 <GO>}

Thank you, Tim. Thank you, Luigi. So, yes, operator, please, now if we could take questions.

Q&A

Operator

Thank you. We will now take our first question from Gianluca Ferrari, Mediobanca. Please go ahead.

Q - Gianluca Ferrari {BIO 15042989 <GO>}

Yes. Hi. Good morning. I have some questions on the asset management project. The first one is, what is the CapEx to finance that project and the phasing of those costs? And if we can assume that you will use part of the proceeds from the current disposal plan to finance that project?

Second question is on the €150 million additional net profits in 2020, if you can guide us for the phase-in of those additional profits? So, from 2018 to 2020, what is the journey to get there?

My last question is on M&A. We read this morning on El economista (20:02) that you might evaluate some acquisitions in Spain and in particular, in Life. If you can tell us if you are looking at an agency network or bancassurance business? Thank you.

A - Timothy Fabrice Ryan {BIO 17528640 <GO>}

So, I will be able to answer the first two questions. I will leave Luigi to answer the third question because that's more around the insurance side. Let me answer on the first one, and it's a very good question.

On the CapEx side, we are not looking at spending a lot of money. This strategy is more an organic strategy, acquisition of team and talent. The budget we have decided (20:37) will be €35 million over the next three (20:42) years. So, it's a very small budget and will be spread with opportunities that we will have and we're already engaged in quite a few. That's the number one element to your question, and thank you for it.

The second one, additional profit, what's the journey (20:57) and how it grows. It grows in a linear fashion from 2016 to 2020. We'll grow from first around the insurance side and then the third party after we have built up and we'll have a momentum, will contribute at the end of 2020. So, that's to give the answer to both questions. I hope I answered this. And, Luigi, you want to answer on Spain?

A - Luigi Lubelli {BIO 4108780 <GO>}

Yeah. In terms of Spain, I mean, there is nothing to announce. The statements made by the CEO of Spain were, generally speaking, within the framework of the group's aspiration. I mean, Generali does not have an M&A target per se. But really, it doesn't mean that we would not be considering acquisition opportunities in Spain or elsewhere if they were aligned with our strategic goals. But I would rather take that statement as a general statement of what the group is after made in (22:08) Spain rather than actually specific Spanish goal.

Q - Gianluca Ferrari {BIO 15042989 <GO>}

Thank you.

Operator

We will now take our next question from Paul De'Ath, RBC.

Q - Paul De'Ath

Yeah. Hi there. A couple of points, firstly, on the asset management strategy. So, you're looking to sort of expand the external client base, third-party assets under management. Do you need (22:39) a track record in order to bring those clients across? If you're hiring new teams, is there any sort of delay before you can actually start winning mandates, or can you use there, I guess, that track record from wherever you're buying them in from?

And then the second point on the asset management piece, just kind of how much is it going to cost to bring in (23:08)? I know you said in terms of CapEx it's only €35 million, but presumably, in order to bring in the right people, you're going to have to pay them more than the people you currently have. So, is there additional underlying cost elements to come through?

And then finally, just on the quarterly results as well then. In the Life business, the New Business Value and the New Business Margin sort of increased dramatically. Can you give us any idea of how much of that is clearly based on the mix of the business – as you're changing the business mix and how much is due to higher asset pricing or those (23:54) macro environment? Thanks.

A - Timothy Fabrice Ryan {BIO 17528640 <GO>}

Thank you, Paul. This is Tim, and I will address your first two questions and Luigi the third one. On the asset management aspect, there's two different situation. One is real assets and the other one is high conviction portfolio management expertise. On the real assets, you don't really need to have a track record. You need to make sure that the people who are working, who are interested in working with Generali have an experience and analytic around those assets.

So, if I take SME lending, those people are usually coming from a bank experience, and we will – and we are checking their background and capacity testing this, for instance. So, you don't really – dependent on track record. You are more dependent on the quality of the people and the ability for them not only to source, but also to understand the asset management dynamic, number one.

Number two question in terms of attracting talents and the aspect of CapEx. The multi-boutique framework in which we're going to operate is a system where actually we are not going to integrate those managers within Generali. We're going to take stakes or help them to develop those stakes into the – to help them to foster (25:21).

So that means that those individual will be entrepreneurs that will have an equity ownership as well as a revenue sharing. Therefore, we'll be fully aligned in terms of success on the delivery between client performance, their performance and shareholder. So, this is the aspect of the boutique model.

The last thing I want to mention going back to your point on track record, because it's important that we link this with the boutique is when we look at high conviction asset managers, we are going to look at people who can bring their track record on the high conviction side. So, I explained about the real asset, that's more about people expertise and the high conviction. We are definitely going to engage and make transaction with individuals that have a track record that can be used and can be leveraged, and we are confident that they can continue to perform well.

So, this is a very key element to hear. We're not talking about incubating teams. This is much more about leveraging the skill set, the track record, gives compliance to be able to make sure that it can offer investment solution to our customer. So, I'm hopeful I've answered your question. I'll leave it to Luigi to answer the third one.

A - Luigi Lubelli {BIO 4108780 <GO>}

Thank you, Tim. As far as the New Business Margin, both if you compare to the same quarter of the previous year or if you compare to the last quarter, to the fourth quarter of the previous year, the improvement in margins is largely due to a business and product mix. There is a (27:00) compared to the fourth quarter, we have a positive impact of economic guaranties (27:05) because we began the quarter with a better – generally speaking, better financial variables, while compared to the last year, the (27:14) happened, but in both cases, the overwhelming majority of the improvement comes from business.

Q - Paul De'Ath

Excellent. Thank you.

Operator

We will now take our next question from Michael Huttner from JPMorgan.

Q - Michael Igor Huttner {BIO 1556863 <GO>}

Thanks very much. I have three. On the solvency, can you explain, again, the bit about accruing the dividend? I didn't catch whether this happened in Q1 or will happen in Q2?

And also on solvency, can you say what the figure is for the organic growth this quarter? It's lovely (27:48) to see the solvency rise, but trying to guess how much is market potential (27:52) is a little bit tricky.

And then my third question would be on the – you had announced as part of your strategic project and reiterated last year that you would dispose of operations worth €1 billion, and I just wondered in terms of timing or how much or when or will it improve solvency? I mean, if you give us a feel for it and whether you might use that money to make some of these asset management transactions? Thank you.

A - Luigi Lubelli {BIO 4108780 <GO>}

Hi, Michael. Thanks for your questions. The accrual of the dividend will be starting from the first half results .So, the figures that we are presenting today are not adjusted for that. So, I think that answered the first question.

We have not provided an actual split, but qualitatively we have an increase, albeit by 1 percentage point in the solvency compared to the year-end. And I told you that the recurring earnings generation offset the impact of the financial variable. So, you can somehow guess that one was slightly larger than the other. As an impact (29:12), I'm afraid I cannot tell you more than that.

Obviously – and I think this is common knowledge and understandable knowledge, this was driven by the behavior of spreads in Italy. I think what might come as a surprise compared to estimates I think that also you should factor in the impact of spreads in France, which also had an impact on the development of the solvency ratio. Of course, all of those reasons have receded as we speak.

And lastly, with respect to the disposals, there's no further news with respect to what we said when speaking which was basically a month and a half ago about the full year results in that all processes are under way. And we are making – we're satisfied with the progress we're making on them. But clearly, as you can appreciate, M&A processes take their time. And we'll be informing you about them once we can give good news. The amounts obtained, of course, can be deployed for investments in asset management or for any other kind of investments that we'll find attractive at the time.

Q - Michael Igor Huttner {BIO 1556863 <GO>}

Fair enough. Thank you very much.

Operator

We will now take our next question from Farooq Hanif from Credit Suisse.

Q - Farooq Hanif {BIO 4780978 <GO>}

Hi, there. Thanks very much. I've got two questions for Tim and one on the Life business. I'm a little bit - slightly confused about the numbers. So, the €84 million going to €300 million, first question is kind of how will you account for that? So how will we see that in operating profits? Are you going to split that between Life and another line? Are you going to have your own kind of asset management number separated out?

And secondly, related to that, if you're essentially saying that you're going to move into higher fee structures, for example, private debt.

Surely, that's kind of - yeah, you're gaining money in the asset management operation, but you're then taking a higher fee from the Life business. So, we're internal assets concerned, I don't understand how that creates extra profit. Maybe I'm just being really stupid, which is quite likely.

And third question, net inflows. They've come down quite a lot, and it seems that this is because you're shifting away from traditional business. I was wondering if you could comment on Italy, in particular, kind of what the level of net inflow decline has been there and whether you think this could continue as you shift business mix, or we should expect perhaps net inflows to come down further. Thank you.

A - Timothy Fabrice Ryan {BIO 17528640 <GO>}

Yes, Farooq, this is Tim. So, the aspect of disclosure will be done. We'll have for the first time a disclosure on asset management results contribution. Now, to answer your question is, we have an increase of the net result of asset management beyond €200 million. After consideration net of tax, it will be a contribution on earnings of €150 million.

So, one is, yes, we will disclose now the asset management business - line of business. Secondly, the consideration aspect, I've just given you the number.

Number two - which is a very good question, it's not at all silly, it's very appropriate is that the fact that we are investing in real assets is because we are expecting higher return. Let me take you - let me give you an example. On private equity side, the fee that you will have on private equity that we put actually on the Appendix as a net margin is around 80 basis points. But if you look at the portfolio that we have of private equity, the way that we manage private equity, we are able to actually extract, compared to traditional equity in that listed equity index, more than 15% of outperformance on the like-to-likes, so on the cash flow, is called a PME index, basically looking at the cash flow of a private equity profile versus every single cash flow within an index.

So, the value that we create out of investing into the real assets is basically giving - sorry for the American analogy, but giving more bucks for the bang. So, for us, it's really an element of having more return for both the policyholder as well as for the shareholder. Yes, it's a higher fee, but today, those returns, you cannot really have them and you cannot spend a little (34:11) to actually perform well. So, this is the answer to your question, which is a very good question.

Now, Luigi, would you like to take the net inflows?

A - Luigi Lubelli {BIO 4108780 <GO>}

Absolutely. The flows in Italy, you are correct in reading that. I would say – thank you for the question because it serves (34:28) me to basically describe Life and how Life is behaving. In reality, what you've been seeing in the first quarter is entirely aligned with what we saw in the year, granted the fact that in the year the inflows were larger than in the year before, but this is the first quarter.

But, what I mean, we announced a strategy, and the strategy is directed, as Tim was saying before, at looking for products, which are more capital-light products, which have a better return features relative to the risks we are taking, and we are progressing along those lines. So, we have outflows of traditional savings, but we've had a very good performance, and relative to the market as well in high risk (35:21) and unit-linked. Banca Generali was an especially successful channel in this quarter. You may have seen the result. So, actually, the kind of business that we're selling is much better in terms of quality compared to that.

So, I would say that you have to interpret this as a – call it the moment of switch in terms of the product mix. But definitely, directionally, it's going exactly where we want it to go. And those New Business Margins we've been able to deliver, we are extremely pleased with.

Q - Farooq Hanif {BIO 4780978 <GO>}

And may I just quickly follow up on one thing. So...

A - Luigi Lubelli {BIO 4108780 <GO>}

Sure.

Q - Farooq Hanif {BIO 4780978 <GO>}

On the revenue expansion number, the €70 million, basically, Tim, what you were saying was that you will charge more. But because you generate high return for the Life business, there'll be an incremental profit.

A - Timothy Fabrice Ryan {BIO 17528640 <GO>}

Correct.

Q - Farooq Hanif {BIO 4780978 <GO>}

Okay. Thank you.

Operator

We will now take our next question from Thomas Seidl from Bernstein. Please go ahead.

Q - Thomas Seidl {BIO 17755912 <GO>}

Yeah. Thank you. Good day, everyone. First question is on return on investment, 10 bps drop year-on-year in just one quarter. That's probably even more than we forecast. I wonder how the in-force guarantees have developed in Q1. In other words, had you been able to keep the investment spread stable as you announced at the Investor Day in November, or are these spreads continuing to come down.

Second question, quite some news coverage on your investment in commercial lines in the U.S. during the quarter. I wonder why you feel it's a good moment to enter commercial lines when we are probably at the peak of the soft market there. And thirdly, reserve releases, I think in the press release and all the – during the call, you said it's flat year-on-year around 4%. I guess, this means – does this mean that for the full year, we should expect the same very high level of 5.7% (37:35) reserve releases? Thank you.

A - Luigi Lubelli {BIO 4108780 <GO>}

Hi, Thomas. Just to see if I can answer your questions based on information. What I can tell you is that, on the New Business, the trends in guarantees that you saw last year are continuing into this year. So, the New Business that is being booked is at lower guarantees than the New Business that was booked last year. And we're actually quite pleased with the development in that sense. So, of course, if we book New Business at lower guarantees, the average guarantee gets diluted down. I wonder if I'm answering your question this way.

Q - Thomas Seidl {BIO 17755912 <GO>}

No. I think we discussed this before, right. I mean, a 10-bp drop on (38:29) one quarter. So, if you extrapolate this to the year, I struggle to see how the investment spreads can stay stable, and that is basically what you told us at the Investor Day.

A - Luigi Lubelli {BIO 4108780 <GO>}

Firstly, I think there's also an element of rounding here, which we should not forget which can make a difference on these balances. But what I can tell you is that in terms of what we said at the Investor Day, what is happening is very much aligned with what we've stated. So, from a management standpoint, we are achieving exactly what we were saying in terms of guarantees. At the first half results, you'll be able to see more details about that. I cannot give you figures because they're not published, but I'd say that the development, especially on the New Business is quite pleasing, I would say. That's what I could say now.

Is it a good moment to enter the commercial business? We actually have not entered the commercial business. We were already there. We have been doing that. It's part of it – it's not a large part of the Generali activities, but we do have a commercial insurance business and they're operating. It's being developed under the new GBL and International Management (39:45) line headed by Mr. (39:49), and it's doing well. But we are not entering the business. We have been there or we were there already.

Q - Thomas Seidl {BIO 17755912 <GO>}

And talking about the U.S., where you have recently opened a number of offices, and in the press, there was quite some estimates about the growth you expect to do in the U.S.

A - Luigi Lubelli {BIO 4108780 <GO>}

Well, as I said, that is part of the development of the business. But honestly, I would not get too carried away in that sense because the actual volume of business that we do in commercial relative to the total business of Generali is relatively small, but clearly, (40:28) wants to develop the business and it's pushing on that to the extent possible and reasonable, of course.

With respect to the reserve releases, we clearly – with respect of the figures for the first quarter, you're right in the interpretation. I mean, we've not given the figure, but qualitatively, we're telling you that basically everything is aligned with a year ago. And honestly, there's no forecast for year-end. I mean, (41:01) – I know this topic comes again and again. It's part of the development of the claims payment. So, there's no target or forecast for the end of the year.

Q - Thomas Seidl {BIO 17755912 <GO>}

All right. Thanks, Luigi.

A - Luigi Lubelli {BIO 4108780 <GO>}

You're welcome.

Operator

We will now take our next question from Nick Holmes, Société Générale. Please go ahead.

Q - Nick Holmes {BIO 3387435 <GO>}

Hello. Hi, there. Thank you very much. Just a couple of quick questions on solvency. The first is, can you tell us what your plans are for the solvency and financial condition report? Well, I mean, we're going to get a lot of information here. I wondered, can you guide us what we should be focusing on?

And secondly, looking at the economic solvency ratio. Just wondered, Luigi, whether you could update us, again, when we can expect to have this fully approved. Is it on end of 2018? Is that kind of realistic? Thank you very much.

A - Luigi Lubelli {BIO 4108780 <GO>}

Hi, Nick. Well, it's not as if we have plan (42:12). I mean, that's kind of required by law. They are going to be released on the due date of the 19th of May, and the fact is, I cannot guide you in the sense that I don't know how (42:29) will compare to the rest because it's the first time we're all coming out on the market with this.

So, I can only tell you that, of course, our respect the legal requirements for this kind of documents are most accurate interpretation of them. And they will provide - of course, they will provide information on the companies as required by Solvency II on the various aspects of how the risks are managed, how risks are measured, what are the figures on solvency under Solvency II, that's kind of what the reports say. We will set up a centralized approach so that you'll be able to speak to my IR colleagues, and they will be handling the questions you may have on the SFCRs once released. I wonder if this answered your question, Nick.

Q - Nick Holmes {BIO 3387435 <GO>}

Yeah. I mean, that's very useful. I wonder is the group ratio something that you will delay until - I think it's 1st of July, isn't it? It has to be released.

A - Luigi Lubelli {BIO 4108780 <GO>}

As I said, I mean, there's no matter of delaying of planning. This is not a voluntary disclosure. This is required by law and we have to do it by - as required. So, we'll be coming out in July with the group.

Q - Nick Holmes {BIO 3387435 <GO>}

Okay, okay. And then, sorry, with the economic, just a quick update where you are?

A - Luigi Lubelli {BIO 4108780 <GO>}

And once again, this is a popular question. And I'm afraid we try our best, but the outcome is not in our hands. So, we certainly are progressing on the IMAP's processes in a number of countries, and they take their own time.

I'd say that end of 2018 would probably not be realistic in the sense that for to have all companies approved by the internal model under 2018, we'd love to. But there are technical times and dialogues with supervisors, which might be but possibly will take a bit longer than that.

Q - Nick Holmes {BIO 3387435 <GO>}

Okay. Great. Thanks very much, Luigi.

A - Luigi Lubelli {BIO 4108780 <GO>}

Very welcome.

Operator

We will now take our next question from Niccolò Dalla Palma from Exane BNP. Please go ahead.

Q - Niccolò C. Dalla Palma

Hi. Thank you. All my questions are for Tim. So, first question is on the unit-linked revenue increase. I would have expected maybe something more from that. Can you maybe explain if there is some contractual constraints in terms of in-sourcing more of the unit-linked business? And are you planning to move 100% in-source for all the New Business? And also, maybe a quick reminder of how much is today managed by Banca Generali, which I suppose is not included in the 14% of slide 3.

Second question is on the optimization of fees. Just to make sure I understand this correctly. So, the €70 million all stemmed from bringing the fees to market level, i.e. – so, it suggests that today, you are below the market level that we see on slide 11, which you kindly detailed, while the mix effect is captured by the €60 million that we see further below in the growth of Generali assets and the allocation to real asset. Is that the correct interpretation? And the follow-up for that is, so why – don't you think there's a risk the market may move towards your fees rather than you being able to move to the current market level?

And then the third question is maybe a big picture (46:41) and also for Luigi is, what is the risk that some of these additional earnings will be offset by some pressure on the fees that you can charge on the products in the Life business? So, how much is actually recapturing a part of the value chain, which is absolutely crucial, but more to offset expected pressure in the business? Thank you.

A - Timothy Fabrice Ryan {BIO 17528640 <GO>}

Thank you, Niccolò. So, there's definitely a lot of good questions here. Let me address them. First of all, the way that we engage with clients is first – they are first in a way that we proceed with business. So, we look at the interest of clients first and foremost. So, to your point of either contractual aspect that will refrain us from increasing the wallets of our penetration, the answer is in a few jurisdiction, yes. But when we come up with the plan to increase from the level we have today to 16% to 30%, the answer is we took that into account. Some of those relationship on the unit-linked is also linked with our distributors, so we are very mindful of where is feasible and not feasible when we come up with this plan.

But again, the plans and the offerings that we have, will have to be competitive and will be competitive. So, that's a really important point.

And on the points on Banca Generali, Banca Generali is using the Generali asset management for €0.8 billion of assets that are sourced. Most of it is open architecture. This is out of scope of the presentation today. So, I'm just giving you that as an information point. But Banca Generali will continue to thrive with its own business model. And there may be some synergies, but at this stage, we didn't take into account any synergy with Banca Generali.

Niccolò, did that answer your first question before I go to the second question?

Q - Niccolò C. Dalla Palma

Yes.

A - Timothy Fabrice Ryan {BIO 17528640 <GO>}

Okay. So, the second question on fee optimization and so on. What I want to stress is that the Appendix slide that you have on 11 is the net revenue margin, not for Generali but the market. And it's really important that you keep that in mind it was just an illustration that we were giving you, and it's based on survey done by BCG over 2016. So, those are net margin on different line of products, not the fees that we have in Generali, or we will have with the multi-boutique platform.

So, the question is around the market and the risk of pressure on fees, let me address those two questions separately depending on the assets. If we talk about real asset, we're talking about most of the assets have scarcity. And therefore, they are not going to be hundreds of billions of assets on this front. They will be very selective, so therefore, the competitive nature that you have here, A, is around being rare services or asset that you can attract and deploy; two, therefore the pricing pressure is fairly low; and two, there's no index linked to those real assets. So, I want - I mean, the competitive pressure is - the most important point to your question is the scarcity on this and that gives a competitive edge in terms of not earning fees on that level (50:04).

The number two element to your question is on the high conviction level. As I said, I'm really focusing on actively managed portfolio. When we look at boutique managers, so for the last 20 years in the U.S. on the equity space, you will see that boutique outperformed by a minimum 50 basis points the traditional asset manager. And there's a very specific reason for this is that those people live and die to perform. And if they don't perform, they won't be able to survive.

Now, they need an infrastructure. They need a compliance structure. They need a systems structure. That's why with Generali we can help. And that element is really a performance aspect. And the last thing I want to mention is for us, it's not about performance against indexed, that is really important. The real cause of all what we're doing is to be able to combine different source of returned assets to provide solution and to package them on the individual investors. So, for example, income-driven solution rather than to say that we are here to give a performance against EURO STOXX 50, and so on. We are going to combine those expertise to be able to deliver very important solution to our customers.

So, therefore, the pricing that we have embedded into those product is in line with what we have already with external manager even lower than what we have with external manager. So, we know exactly what the dynamic is. But we also are quite confident that on one side on the real asset, we can keep and we will keep the pricing element because of the trades (51:43) I mentioned before. And on the active management side, it will be not just providing one product, but a series and combine them to provide a long-term savings solutions.

I wanted to maybe address the question around additional earnings offset by fee charge (52:03). And could you elaborate a bit more, Niccolò, on this point?

Q - Niccolò C. Dalla Palma

I'm thinking, if I take the specific example of Italy and the hybrid products they have, the product launch in 2017 seem to have lower cost to the client than the one launched in the previous two years (52:22), perhaps stemming also from the very high level of fee (52:27) reached in 2016.

So, I was just wondering whether you need to accelerate the move on the asset management to recapture a part of the value - an important part of the value chain that you manage and whether the €150 million will be fully accretive or whether you feel the - and whether you're really comfortable there will be no risk of some offset from the gradually lower fees on some of the very profitable hybrid products?

A - Timothy Fabrice Ryan {BIO 17528640 <GO>}

Niccolò, let's say, I can understand why you may have guessed this explanation on your own, but in reality, we did not go on - in our minds, the - and I'll let the team (53:21) to explain better essentially. Life - let me put it in very plain terms. At Generali, Life had a strategy and it had a clear strategy. What we lack was a strategy for asset management, and that is what is being delivered today. So, it wasn't because of a shortage elsewhere. It's because everything else was taken care of and this one was, to begin, taken care of, but go ahead.

A - Luigi Lubelli {BIO 4108780 <GO>}

Absolutely. And we will continue to provide to our customer different solution in different needs, including passive and so on. So, I mean, this strategy is being put in place to accelerate the fee business not to offset. So, it's more a continuum of our strategy rather than anything else.

Q - Niccolò C. Dalla Palma

Okay. Thank you, and look forward to meet you tomorrow.

A - Timothy Fabrice Ryan {BIO 17528640 <GO>}

(54:18)

Operator

We will now take our next question from Nadine van der Meulen from Morgan Stanley. Please go ahead.

Q - Nadine van der Meulen {BIO 15200446 <GO>}

Good afternoon. Just one question from me. On the cash flow generation, just in light of the target of €7 billion from 2015 to 2018. At the end last year, you are already sort of achieving half of that, and particularly 2016 was strong on operational improvement in France (54:48), and I remember at the time there were comments on similar operational improvements elsewhere as well. So, wondering if you could comment on the development on the cash flow generation.

A - Luigi Lubelli {BIO 4108780 <GO>}

Hi, Nadine. As I said before, I think the good thing, certainly the thing I'm pleased with and we are pleased with is the fact that the underlying trends of Generali are stable and remain the same. So, what we are doing on the business is fully aligned with what you saw for the year and what we said in Investor Day.

So, also in terms of cash generation, I would say we are steering the business in the direction we wanted to go. As I was answering to somebody else's question before, the first quarter especially the drop in inflow I wouldn't take that as anything – meaning anything else. The business is doing well. We're having good cash flows. Most importantly, the business we are booking is a business that will be generating better cash flows going forward. So, we're actually quite happy with the position in that sense.

A - Spencer Lee Horgan {BIO 4241901 <GO>}

Thanks, Luigi. It's Spencer here. So, we're almost up at 1:00. I just wanted to add one thing to the question that Nick asked earlier about the SFCR. It's a logistical point. But what we will do is set up a central page on the generali.com group website, where you'll be able to download all of the SFCRs of the relevant companies as a group. As Luigi mentioned, we will do that on the 19th of May. And then if you do have questions coming from that, the IR team is ready to take them.

So, with that, I think we better wrap it up to allow you to get on to the next one. Thank you for joining us. Sorry, we've been a little bit time pressured, but I guess you're under more time pressured than us today. But hopefully, we'll get to see many of you over the next days.

And with that, operator, if we could close the call, please. Thank you.

Operator

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