Q2 2018 Earnings Call

Company Participants

- Antonio Cano, Chief Operating Officer & Director
- Bart Karel De Smet, Chief Executive Officer & Executive Director
- Christophe Boizard, Chief Financial Officer & Executive Director

Other Participants

- Albert Ploegh, Analyst
- Ashik Musaddi, Analyst
- Bart Jooris, Analyst
- Farooq Hanif, Analyst
- Jason Kalamboussis, Analyst
- Matthias de Wit, Analyst
- Steven Haywood, Analyst
- William Hawkins, Analyst

MANAGEMENT DISCUSSION SECTION

Operator

Ladies and gentlemen, welcome to the Conference Call for the First Six Months of 2018. I'm pleased to present Mr. Bart De Smet, Chief Executive Officer; Christophe Boizard, Chief Financial Officer; and Antonio Cano, Chief Operating Officer.

For the first part of this call, let me remind you that all participants will remain on a listen-only mode, and afterwards, there will be a question-and-answer session. Please also note that this conference is being recorded.

I would now like to hand over to Mr. Bart De Smet, CEO; and Mr. Christophe Boizard, CFO. Gentlemen, please go ahead.

Bart Karel De Smet {BIO 16272635 <GO>}

Good morning, ladies and gentlemen, and thank you all for dialing into this conference call. And for being with us for the presentation of the half year 2018 results of Ageas.

I'm joined in the room by my colleagues of the Exec Committee, Christophe Boizard, our CFO; and Antonio Cano, our COO. Emmanuel van Grimbergen, our Group Risk Officer is replacing Filip Coremans, our Chief Risk Officer, who is excused today. And we have, of course, our Investor Relations team present in the room.

Ladies and gentlemen, before going into detail of the six month results, I would like to start with highlighting the important events that occurred over the last couple of weeks. First of all, we now have clarity on the put option granted to BNP Paribas Fortis, which expired without it being exercised. We highly valued the long-lasting relationship with BNP Paribas Fortis Bank as distribution partner and as co-shareholder of AG Insurance.

Secondly, the Group also received authorization from the regulator to operate reinsurance activities at the holding level, leading to higher fungibility of capital within the Group. And last but not least, the Fortis settlement has been declared binding, allowing us to regain full strategic and financial flexibility, and to help Ageas, its stakeholders and all those involved to draw a line on what has been an uncertain difficult period for everyone.

As you have seen in a separate press release issued this morning, the Board of Directors has also decided to launch a new share buyback program of €200 million that will start next week. This is the eighth consecutive share buyback program showing our confidence in the Group's financial strength. By this time next year, we will have returned €1.8 billion in total to shareholders through share buyback programs.

Let us now go into the six month results. Scope-on-scope, so excluding last year's €7 million contribution from our Italian activities, our net insurance result increased by €38 million to reach €475 million, up 9%, and this despite adverse weather events in Belgium and UK, which has an impact of €62 million and also €55 million lower support of net capital gains in the course of the first half of the year. The comparison with last year was furthermore affected by last year's €32 million change in reserve inflow interest rate in China, and the €31 million negative impact from Ogden in 2017.

Altogether, this shows an improvement of the underlying result with some €90 million or 24% compared to the same period last year. So it is fair to say that our insurance activities continue to perform very well. And barring unforeseen circumstances, we should be able to reach a net insurance result at the higher end of the €750 million (00:03:53) to €850 million range.

With respect to the dividend upstream from our operating companies, €600 million has already been upstreamed at the end of June, in line with our previous announcement. And this amount more than covers the dividend paid earlier this year, and the holding expenses, or in other words, an excess upstream of some €120 million that is added to our net cash position.

Ladies and gentlemen, I will now hand over to Christophe for more details on the results.

Christophe Boizard {BIO 15390084 <GO>}

Thank you, Bart, and good morning, ladies and gentlemen. I propose to start with the Solvency II and III capital generation figures before going into details on the IFRS results of each segment. So, on slide 7, you will find the Solvency II figures. Let us start with the Insurance Solvency ratio. The Insurance Solvency ratio stood at 202%, an increase of 6 percentage points.

The good operational half year in the Solvency II scope more than covers the accrual of the expected dividends related to the IFRS results over the period; and this despite the negative impact from the weather events in Belgium and the UK. Its improvement was also supported by 5 percentage point following the increased fungibility of own funds as a result of obtaining the license to run reinsurance activities at the holding level, as already mentioned by Bart.

The Group Solvency II ratio increased by 15 percentage point to 211%. This increase was driven by 10 percentage point of operational impact, more than covering the expected dividend. Next to this, there was a plus 7 point impact from the expiration of the put option granted to BNP Paribas Fortis, and minus 2% from the ongoing share buyback program.

Regarding free capital generation, I am on slide 8. The operational free capital generation over the first six months amounted to €392 million on the Solvency II scope corresponding to the European entities. This includes €99 million dividend upstream from the non-European NCP's. This leaves us for the European entities with a free capital generation of €293 million over the first half compared to €112 million at the end of Q1 of this year.

You might recall that last year, we had €511 million operational free capital generation on our Solvency II scope companies corresponding to an average of €120 million to €130 million a quarter. If you take into account, the management actions and risk mitigations with a decreasing effect on SCR, and the weather events in Belgium and in the UK affecting own fund, we can conclude that the underlying performance is well above the guidance indicated earlier.

I would like to make one additional comment on the effect of the expiration of the put option on the free capital. As just mentioned, there is an immediate positive impact on our Group Solvency ratio of 7 percentage points. The impact on free capital is, however, less straightforward.

Until now, we were obliged to consider from a solvency point of view to be the 100% owner of AG Insurance. This is no longer the case, and we are therefore, no longer obliged to cover the 175% of the full SCR on our own.

Let me clarify with some concrete numbers. At 100%, AG Insurance has €6.7 billion of own funds and €2.9 billion of SCR. Based on our 175% target, this leads to a free capital of €1.7 billion. 25% of these or €0.4 billion is for our co-shareholder. However, Solvency II regulations require us to deduct €1 billion as non-transferable own funds, but we consider that the difference, €0.6 billion can now be recognized as free capital.

After these detailed explanations on the solvency and the free capital generation I propose to come back on the IFRS results.

As you can see on slide 10, the net Insurance result for the first six months of 2018 amounted to €475 million, which represents a 9% increase compared to last year scope-on-scope if we exclude our Italian operation, still consolidated last year. The result in the second quarter amounted to €176 million. The net result of the Life business increased to €373 million compared to €312 million last year, thanks to strong results in all segments and in particular an exceptionally high result in Ageas (00:10:51).

The net result of the Non-Life activities decreased to €102 million compared to €133 million last year due to the negative impact of €62 million related to the adverse weather in Belgium and the UK. Last year's results also included €7 million contributions from Cargeas, our former Italian operation.

Total inflows increased slightly at constant exchange rate and exceeded again the €20 billion threshold with strong inflow growth in Belgium, offsetting lower inflows in the UK. In Belgium, inflow growth outperformed the market in Non-Life, and in the Belgian Life activity we reversed the trend observed in previous quarter with strong growth, mainly thanks to unit-linked inflows considerably up year-on-year and driven by successful sales campaign. Inflows of the Asian non-consolidated partnership returned to growth at constant exchange rate during the second quarter, and this was the result of successful sales campaign and continued channel development.

On the technical side, everything also remains on track as we experience solid operating results across all our segments with a strong guaranteed and unit-linked margin respectively at 110 bps and 28 bps. The group combined ratio stood at 97.8%. But as mentioned before, both in Belgium and in the UK, the first six months of this year were marked by poor weather impacting the group combined ratio by 4.7 percentage points. In other words, excluding the weather impact, the combined ratio would have been an excellent 93.1%.

As usual, I will now give you a bit more details on each segment. In Belgium, slide 11, the net result stood at €220 million with a strong net result in Life at €181 million. It remained at the same high level as last year, despite a lower level of net capital gains. This reflects a strong technical performance with operating margin above target in guaranteed business and on target in unit-linked with respective value of 108 bps and 43 bps.

The operating result remained in line with last year, marked by a better underwriting performance and supported by a high investment result. Similar to last year, the annualized impact of the capital gains is expected to level out over the remainder of the year. As mentioned, the Non-Life business was impacted by adverse weather in January and May, June for an amount of €29 million. The underlying performance continues to be strong, and excluding the weather events, the combined ratio would have been 93.1% with a lower level of prior year releases compared to last year.

In the UK, slide 12, the situation continues to gradually improve, and despite a negative €33 million impact from bad weather, the net result amounted to €31 million compared to €11 million last year, helped by higher prior year releases. In a softening market environment, we continue to focus on pricing and underwriting discipline, which obviously weighed on inflows.

In Continental Europe, slide 13, our net result went up 3% scope-on-scope, meaning without our Italian operation in 2017. Our operating performance remained solid in our Life business despite lower volumes while we delivered a strong performance in our Non-Life activities with a combined ratio at 91.6%.

Finally, in Asia, slide 14, as mentioned before, we recorded an exceptional performance with a net result at €170 million compared to €113 million last year. This performance was driven by an exceptionally high first quarter result in China, which benefited from a positive evolution in the interest rate, partially offset though by equity impairments following the negative development of the China equity market during the second quarter.

The net result of the General Account on slide 16 amounted to €34 million negative compared to €161 million negative last year, primarily driven by a positive revaluation of the RPN(I) for €9 million compared to a cost of €122 million last year, so a variance of €131 million from 2017 to 2018. This brings the Group net result to €441 million compared to €284 million last year. The total liquid assets of the General Account stood at €1.8 billion, of which €0.9 billion remains ring-fenced for the settlement.

Ladies and gentlemen, I'd like to end my comments here and to leave room for questions.

Q&A

Operator

Ladies and gentlemen, we are ready now to take your question. The first question comes from Jason Kalamboussis from KBC Securities. Sir, please go ahead.

Q - Jason Kalamboussis {BIO 4811408 <GO>}

The first question is on Asia. If we exclude the realized gains, the result seems to be at a relatively good level in the second quarter on an underlying basis. And I would like your thoughts and comments on it, i.e., is it something that we should rely for the second half because at the end of the day, if we exclude the impairments, we are at above €80 million? And also if you could remind us the realized gains and impairments notable in China, how does that work and if there is any difference with Ageas?

The second question is on the General Account. Should we expect any legal costs relating to settlements in the second half? And what should be a normalized level ex legal costs that we should use as a guidance for 2019?

And the final question is if you could comment, I mean, rating agencies have given a positive outlook at Group level. So the three-notch difference with Insurance operation normally should at some point be reduced, notably now that you have put behind the whole litigation issue. Could you comment on that? When do you expect changes there? And how would that change? How you are going to run the Group and notably the reinsurance business? Thank you very much.

A - Bart Karel De Smet {BIO 16272635 <GO>}

Okay. Thank you, Jason, for the questions. The first one, we had indeed in Q2 and it could be part of the miss towards consensus, the €44 million impairments in China. The reason is that we use for impairment the Ageas rules which is as soon as it's minus 25% and so on, whereas local rules are less conservative. So, that also explains if you look through the local cost accounts of Taiping Group that you will see not the same figures as ours.

So we, of course, cannot predict how the markets in China will evolve in the second half of the year, but we can, let's say, repeat our guidance that we expect for the Asian entity a total profit of €250 million plus. There, of course, with respect to China, you have to take into account that, for instance, the second half of the year is also a period where we already start preparing the next campaigns for the next year. So there might be some investments to further increase growth. But we are confident on the results in Asia, having one caveat and that is, of course, how markets will react and what the impact could be on the equity portfolio.

Positive also to mention is that where we were far behind our, let's say, last year's figure in sales mainly in China. That is being fully recovered in the second quarter, and we are confident that we will further grow for growth in that region.

The second half, yeah, on maybe last point in CTIH, we publish later in August. So you will have a bit more also view on, for instance, the commercial results of June, July.

The General Account, the normalized cost level, we take and you can count on this something around €70 million on a yearly basis.

A - Christophe Boizard {BIO 15390084 <GO>}

Yes. Because there is almost no cost recorded during the first six months regarding litigations. So it's a clean General Account, I would say. Now the last question, on the rating implication. So, here, we expect some good news because the ambition is to gain three notches on the holding. So Ageas SA/NV presently rated by Standard & Poor's at BBB. And the ambition is to reach a full A level and with the following – for the following reasons. The first notch is gain through, I would say, the positive expectation on the proposed settlement and the homologation of the proposed (00:23:23) settlement. This would give us one notch.

And then on the two additional notches, it relates to the reinsurance activities that we want to launch. So it means that the holding will become an operational entity, and our plan is to have the concept of core entity being recognized by Standard & Poor's. And in that case, the holding would benefit from the core entity rating of the group which is A like AG and like the UK. So three notches up, and you will guess that the benefits are really huge in term of financial flexibility, cost of financing for future financial operation, emission of sub debt or all these potential things. So the fact that we could reach this full A is really a key element for the financial flexibility. And if you have read the Standard & Poor's press releases, it was already preannounced. There was a press release from Standard & Poor's stating that there was a potential upgrade of three notches. So, that's not something that we are affirming on our side. This is also taken into account by Standard & Poor's.

Q - Jason Kalamboussis {BIO 4811408 <GO>}

Many thanks. Just a quick one on Asia, just as a follow-up. Do you find that with things that have changed in the market, structurally you would expect that the earnings or the underlying earnings are going to be better? So if I ever look through the second half and I look to next year, do you find that this is a genuine trend that is helping you and was this confirmed in the second quarter?

A - Bart Karel De Smet {BIO 16272635 <GO>}

Most important change in China already entered in the market beginning of the year with what you could call kind of a ban on low profitable single premiums. And if we reach at the end of Q2 almost the same volume as last year, it's, let's say, exclusively regular premiums and very strong, let's say, renewals where also – where, as I indicated, profitability is higher. This is good for the market, and we are quite confident that this will help us in the future profitability of that company. We also reach for the comparable insurers, in the meantime, a number four position coming from the eighth position some years ago. So we are growing stronger than the market. We are characterized by a very efficient sales force that is growing with, let's say, quality of sales that's high so that we have few lapses. So we are very confident on the future profitability of that market.

Q - Jason Kalamboussis {BIO 4811408 <GO>}

Thank you very much.

Operator

The next question comes from Bart Jooris from Petercam. Sir, please go ahead.

Q - Bart Jooris {BIO 3470300 <GO>}

Yes. Good morning. Some more general questions, if I may. Now that with the expiry of both the Fortis settlement and even maybe, let's say, an increase of your rating, you will have more free usage of the cash, you have more possibilities regarding growth investments or shareholder reimbursements. Does it change the way you look at things? Are you more actively studying certain sectors or certain countries? Could you give us an idea on that?

And then on the opposite side, there was some rumors, if you may say, of a possible bet on Ageas by Fosun. Could you give us some insight at what that could mean for the JVs? Are there change of control clauses and then how do they work?

A - Bart Karel De Smet {BIO 16272635 <GO>}

Okay. With respect to the first part of your question, so I believe we can confirm today that we are a company that in the first time for the first place is looking to deliver on the promises which are to go for a strong, stable, increasing dividend with this clear dividend policy where we also try to go for further growth where, of course, mainly the Asian market is our growth engine and that we have – let's say, we want to have a stable solvency level and a cash position that permits us to keep flexibility, be it for further acquisitions or be it for, let's say, returning to shareholders. It's of course – your question is more than relevant with the expiry of the put option.

So the potential use of the cash we had or a big part of that for the put option is off the table. So you could say that is cash that we can now use again for those two goals, M&A and/or returning to shareholders. And we will have on the 19 of September, let's say, the update of our strategy or the launch of a new two-year plan. We'll give more clarification on that. And capital management is, of course, part of that Investor Day.

The second part of – and maybe I add also that, okay, the fact that we renewed buyback is also confirming that, okay, put or no put. Our strategy so far did not change. On the control clauses, indeed, we have a lot of joint ventures where you have change of control clauses, but we, for evident reasons, say also because the shareholders' agreements are not for publication of disclosure. We don't give details on disclosures, but you can, let's say, note that all of our joint ventures have a number of clauses with respect to change of control and what are then the consequences if that might happen. But we – okay, sorry for that, but we don't disclose this.

This also, let's say, related to the rumor that we had earlier or even last week. That also we can confirm that a rumor is a rumor. In principle, we do not react on rumors and the only additional comment we have given is that we have not received any concrete indication of interest from Fosun with respect to Ageas. So, more than that, it's not – we cannot say.

Q - Bart Jooris {BIO 3470300 <GO>}

Okay. Thank you.

Operator

The next question comes from Matthias de Wit from Kempen. Sir, please go ahead.

Q - Matthias de Wit {BIO 15856815 <GO>}

Yes. Good morning and thanks for taking the questions. First on capital generation, I've got two questions. The first one is on the minorities. I think you disclosed it separately in Q1, but I don't think I'd find them again in Q2, so could you provide the share of minorities in the operational capital generation, please? And then secondly, also on capital generation, there is again an operational SCR released in Q2. I wondered if you could provide more details on that one. And then the third question is on liquidity and link to litigation. So now that everything is behind in terms of litigation, is there room to upstream the excess capital sitting in Belgium to the holding company? Thanks.

A - Christophe Boizard {BIO 15390084 <GO>}

I'll take your first question on capital generation and the treatment of minority interest. So I especially mentioned Q1, because in Q1, we were already of the opinion and we guess that there was a fair chance for the put not to be exercised. And we, I would say, prepare the ground. And if you go back to the disclosure at the end of Q1, we were still obliged to disclose a 100% roll forward. And because the free capital generation is backed by Solvency II where we are seen as owning 100% of AG at the (00:32:23) cost of the value of the put.

But we isolated the – what belong, if I may say so, to the minority interest. And we tried to isolate what the Group share would be. And the Group share was precisely this €112 million. So this €112 million correspond to 75% of ownership of AG, which makes it fully comparable to the figure we are releasing today. And so it's the reason why I especially mentioned this €112 million as a comparison, but it's a comparison on the same scope. So it is quite a valid comparison.

Then the second part of your question was on the SCR release in Q2. It was – the main thing was that we took some management actions, and you referred to the €34 million, which is on slide 59 and also on slide 9, by the way. And so this is due to some reduction in risk and I'll give you two example. In the UK, there was something done on the balance sheet on the assets side to reduce the risk on some receivable.

And then on the Intreas side, due to the fact that the weather impact is quite high this year, the Intreas team decided to buy additional protection during the year. You know that in the insurance sector, you can buy during the year additional covers with slightly higher prices. But if you buy additional cover, you suddenly had the impact in the SCR which is reduced because you are better covered. So the two main things are some protection on some asset receivable in the UK, and on Intreas, they bought an additional protection vis-à-vis exceptional events.

A - Bart Karel De Smet {BIO 16272635 <GO>}

Okay. The second question with liquidity link to litigation and more specifically the request or the question whether there's more room for upstream cash at the holding level. First of all, we have our solvency in capital management policy, which determines what dividends we expect to operate the companies to upstream depending on the solvency level. You have seen that this year, we already received €600 million. And we also mentioned in the press release and in the table as a footnote that we expect another €60 million from Malaysia and there will also still be a dividend going through Intreas. So we will be definitely above the €600 million which more than covers our dividend and corporate cost, and you could say that even gives an additional €120 million, €140 million cash to strengthen the cash position at the holding company level and, okay, what will now happen also after the reinsurance application, the rating changes and all these things give us some time to further work on this. But we will keep a strong solvency position in our operating companies also because we are market leaders in most of the countries where we are, and at the same time, be sure that there is sufficient cash upstream, let's say, to deliver on our promises with respect to dividend and with respect to buy back if there are no M&A files.

Q - Matthias de Wit {BIO 15856815 <GO>}

Okay. Thanks a lot.

Operator

The next question comes from William Hawkins from KBW. Sir, please go ahead.

Q - William Hawkins {BIO 1822411 <GO>}

Hello. Thank you for taking my question. Can you just remind us your target of being better than 97% combined ratio, how are you thinking about weather within that number? So if we take the, I think, 4.7 points that you have flagged for this half, should we take that to zero within the 97% or do you have a view about normal weather?

And then secondly, could you talk a bit about the outlook for the UK in the second half of this year and into 2019? I think you talked on the first quarter about becoming a bit more focused on returning to growth to improve your economies of scale. If you're doing that in terms of being more price competitive, does that inevitably mean that there's going to be upside pressure to your combined ratio simply because you'll still be reserving conservatively with regards to Ogden or is there a compensating factor?

And then lastly, could you just talk briefly about the meaningfulness in your view of the 175% Solvency II ratio. I mean, you set that a few years ago. At that point, it seemed to be a more realistic target. You're now comfortably above that level. But many companies themselves kind of moving the goalposts in terms of thinking about that cushions for market sensitivity and other stuff like that. So, to what extent is the 175% actually a useful figure for us to take as a gauge? Thank you.

A - Bart Karel De Smet {BIO 16272635 <GO>}

The combined ratio, Antonio, you take that.

A - Antonio Cano {BIO 16483724 <GO>}

Your question, William, was what the impact is on weather on a combined ratio on a stable basis. I think if you look back, you could expect 2% to 3%, that will be a normal impact of weather and that's Belgium, UK, and Portugal. Your second question was on the outlook for the UK. So we are indeed growing again parts of the business. In the total numbers we showed to you, you will see that because they're part of the business where we're still kind of in a restructuring mode or coming back to profitability, and outlook for the UK remains what it was. I think at previous sessions we already indicated that for this year we aim at a result of about €60 million, 6-0 million euros, so we maintain that. And growth, there is a bit of growth, but expect that not to be huge certainly not this year, certainly also given the soft market in the UK.

A - Bart Karel De Smet {BIO 16272635 <GO>}

And so the combined ratio of 97% is indeed including a normal expected weather impact as Antonio said of 2% to 3%.

A - Christophe Boizard {BIO 15390084 <GO>}

So, on the target of 175%. So, first of all, let's not forget that it is still based – the target is still for the insurance activity. And I would like also to remind you, on the Investor Day of 2015, all that this target has been set up, it is basically to be able to absorb a shock of 1 in 30 (00:39:42) and that we are then still well above the 100% solvency capital requirement.

Now for the rest, of course, we are very comfortable with the current level of capitalization at group level, at insurance level, but also certainly within our operating company. And as already mentioned, in September we have our next Capital Day, and there we will also give an update on our capital management.

Q - William Hawkins {BIO 1822411 <GO>}

Can't wait. Thank you.

Operator

The next question comes from Ashik Musaddi from JPMorgan. Sir, please go ahead. He hung up the line. So the next question comes from Steven Haywood from HSBC. Sir, please go ahead.

Q - Steven Haywood {BIO 15743259 <GO>}

Thanks very much. Just a quick follow-up and a couple of other questions as well. You mentioned that your weather impact is 2 to 3 percentage points of your combined ratio and normalized sort of impact throughout the year. And in the Q2, you had 2.3 percentage points of adverse weather in it. Can you just confirm whether this is within normal limits, or is this on top of your – in addition to normal kind of 2 to 3 percentage points of weather?

And then a couple of questions on your operational sort of capital impact. The €293 million, I don't know if you addressed this early, but could you tell me whether this includes the 25% minority's amount as well, or if it – and if it now excludes this? And then also, on the €99 million dividend upstreams from your non-European NCP's, can you tell me where these have come from? Because I can only see China at €62 million and Thailand at €14 million. Thanks very much.

A - Bart Karel De Smet {BIO 16272635 <GO>}

I'll take the first question on the combined ratio and clarify that a bit. So the 2% to 3%, that is a part of our 97% target. So within the 97%, you could expect 2% to 3% coming from weather events. You referred to that, after six months we're slightly – well, we are above 2%. Bear in mind the reinsurance treaties that there are in place. There are various aggregate treaties in some companies. So as you build up weather-related claims, there is a point in time when you start (00:42:24) with the retention levels and then you will see no more net impact from the weather.

Up until the six months, it was mostly within our retentions and there are a few treaties where we have reached retention levels, but it's not huge. Saying that, going forward for – certainly for Belgium, if we still would have another big flood or storms or whatever, that would mean mostly in the reinsurance treaties. I hope that clarifies it a bit.

A - Christophe Boizard {BIO 15390084 <GO>}

So Steven, on your free capital generation question. So on the first one, I can confirm that the €293 million is indeed after the deduction of the 25%. So it means that it is our share. After the expiration of the put, we are the owner of 75% of AG. So this figure corresponds to our holding of AG. So this is after deduction of the 25%.

Then as regard to the NCP at €99 million, the lacking components are Malaysia where we received €16 million of dividend; and Turkey, €7 million. So you had China and Thailand, but we have Malaysia and Turkey as well, to be added in that case. If you adapt all these four numbers, you arrive at €99 million.

Q - Steven Haywood {BIO 15743259 <GO>}

Okay.

A - Christophe Boizard {BIO 15390084 <GO>}

And then on the – it was not precisely your question, but this €293 million relates to the European entities. And please take into consideration the fact that we have free capital generation under Asian business as well, and please refer to the footnote material. And here we can confirm that on the non-controlled participation with JVs from Asia in terms of free capital generation, we are very well on track with the guidance of around €250 million.

Q - Steven Haywood {BIO 15743259 <GO>}

Okay. Thanks for the clarification. I appreciate that.

Operator

There are no more questions in the queue. We have a question from Farooq Hanif. Sir, please go ahead.

Q - Farooq Hanif {BIO 4780978 <GO>}

Just wanted to know in terms of the improved capital fungibility due to reinsurance. Is this going to change anything in terms of how you manage group liquidity or upstreams in the future? So, will we see kind of any immediate impact from that on cash flow?

And also, going back to the points made earlier about your improving financial flexibility, I know you gave some sort of guidance around your debt-raising capability in the past when we were discussing potentially raising debt for the BNP option. Could you kind of update us on where you think that is now according to the S&P model, for example? Thank you.

A - Christophe Boizard {BIO 15390084 <GO>}

So on your first question on capital fungibility, so that's internal capital management because what we call reinsurance is more a financial operation, but based on quota share. What we will do is that we will take a share of the operation or the controlled entities within the holding. So it means that the dividend capabilities of the corresponding entities could be reduced – will be reduced, but we will have to add back what we will recognize directly within the holding. So all-in-all, there will be no change; no change. It's really an internal management of the group.

In terms of group financial flexibility, what we have in mind is that there is room for additional leverage and our assessment is that it is around €1 billion from the – if you take the regulation about Tier 2 capability, we have additional room for €1 billion.

Q - Farooq Hanif {BIO 4780978 <GO>}

So that's based on the Solvency II regulation, presumably?

A - Christophe Boizard {BIO 15390084 <GO>}

Yeah. Yeah. Yes. Because we have limitations imposed by the Solvency II.

Q - Farooq Hanif {BIO 4780978 <GO>}

But just – I mean, presumably you...

A - Christophe Boizard {BIO 15390084 <GO>}

You have the capital credit under Solvency II. If you want to have the capital credit and to take that into account in your Solvency ratio, you obviously have to follow the Solvency II rules and you have limitations based on your Tier 1 amount, and this put limits on Tier 2. And with this, our very rough calculation is that the room we have is around €1 billion.

Q - Farooq Hanif {BIO 4780978 <GO>}

But to maintain the upgrade of notches of the holding, presumably you won't go to a full €1 billion. So I was wondering if there's another constraint that's...

A - Christophe Boizard {BIO 15390084 <GO>}

No. No. When I told you there is a potential upgrade of three notches, it is based on the present capital structure. So, this is a potential. If we want to increase the leverage, it's another discussion with the rating agency. But at this stage, we don't have the intention to raise this €1 billion of debt. So we will present our fight (00:48:24) to S&P with the present balance sheet structure, and it is where based on their capital model, we are, let's say - we are eligible - theoretically eligible to gain these three notches.

Q - Farooq Hanif {BIO 4780978 <GO>}

Okay. That's very kind. Thank you very much.

Operator

The next question comes from (00:48:48) from JPMorgan. Sir, please go ahead.

Q - Ashik Musaddi {BIO 15847584 <GO>}

Hi. This is Ashik Musaddi from JPMorgan. I'm just using Kunal's (00:48:55) line. Sorry, I had a - look, I was on the queue earlier, but missed it somehow. I have a few questions. So first of all, could you just remind us about your M&A? How do you see M&A at this point? I mean, in past you have mentioned that you would like to do something in Indonesian Non-Life. So, where are we on that? And is there anything happening in Fidea, in Belgium? Is there something happening in Portugal, because still there is a lot of consolidation expected in Belgium, Portugal and your aspirations around M&A in Indonesia as well? Any thoughts on that would be great.

The second thing is, you mentioned that it looks like you're still low on capital gains this year for Belgium compared to what you have done last year. So, shall we be expecting more cap gains in Belgium in second half or, give or take, you're done for this year in first half in Belgium?

And the last bit is, I mean you're growing very rapidly in China. I mean, €12 billion flows is a pretty big number for first half. I mean, if I annualize that it's €20 billion, €25 billion a year. Do you ever get worried about such growth? I mean, is (00:50:07) relaxing some of the underlying behavior or they say, (00:50:12) underlying features of the product to deliver such a massive growth. Any thoughts on that would be great. Thank you.

A - Christophe Boizard {BIO 15390084 <GO>}

Thank you, Ashik, for the three questions. The first one, M&A. Okay, maybe summarize. When we look through the mature markets, our core markets, Belgium, Portugal, UK, we can say in Belgium, yes, we will look to whatever opportunity that permits us to increase our stake in Non-Life primarily, because we are at 25% plus market share in Life. So that's not really where we are looking for expansion in organic growth. And if Fidea would be a file that comes through the market, we will, in any case, have a look at that.

In Portugal, okay, there are also indeed rumors indications that in the coming quarters one or more files might come to the market, as we have chosen Portugal to become our third home market after Belgium and UK. And we have been quite advanced in our transformation plan in Portugal. We also there will, in any case, look to those opportunities and see whether they can match also there again, primarily in Non-Life because also in Portugal in Life, we have a market share of more than 20%.

The UK, for the evident reasons, we continue, as Antonio said, to first of all finalize the restructuring, which is really very well-advanced. And we will look how we can take up again with growth after two years of decline, growth in a smart way. So that's with Europe. If you then go to Asia, we indeed expressed already a number of years our interest for Indonesia. We have been looking to multiple files in the past and – or we declined because they were not fitting our financial criteria, or we sometimes also not withhold because we don't want to pay the price (00:52:24)

So it's a difficult market to find a target that is giving us enough confidence that we can become, let's say, a top player in the market and also (00:52:37) conditions. So we continue to screen the market, but not an easy one. And then there are other countries in Asia where we are present or not present, where we continuously see how we can increase our footprint. But we will keep this discipline knowing that, okay, prices, if you really want to make it jump in the market, you probably have to, from time to time, pay a strategic premium. But we are, as you, I believe, have all seen in the past, we are not ready to do (00:53:13) decisions in this perspective.

In Belgium, the capital gains, you can see – and it's on slide 25 in the pack, that we realized so far €79 million compared to €101 million last year. Part of our cap gains and/or a big part are always real estate. We can never, let's say, plan them in equal part per quarter. So you could say that compared to last year, you can expect a bit more in the second half than what we had last year. In the second half last year, we only realized, if I remember well, €6 million or €7 million in the second half. So I think you can count on a bit more.

And then the last point on China, rapid growth. Okay, we can confirm that in any case the intention of our joint ventures, so as well our partner as ourselves to further invest in growth. So you can expect in the coming period a further increase of sales teams. As I mentioned earlier in the call, coming from a number eighth position some years ago, I think last year we were sixth. In the meantime, we're number four in total premium in commercial, not in new business.

So first of all, we see that our company is – locally there, is very well equipped to recruit thousands – I would even say, ten thousands of agents in a short period of time to train them very efficiently and also to be very selective after three and six months to, let's say, take out those agents that are not productive.

So it's impressive, the growth we make there, as well the number of sales as in premium income. But I can assure you that it's done in a very, let's say, disciplined and measured way. So we feel comfortable with that and don't see that as a specific risk.

Q - Ashik Musaddi {BIO 15847584 <GO>}

Okay. That's very clear. Thank you.

Operator

The next question comes from Jason Kalamboussis from KBC Securities. Sir, please go ahead.

Q - Jason Kalamboussis {BIO 4811408 <GO>}

Yes. Hi. Just a quick follow-up on the combined ratio in Belgium. You had – I mean, I can appreciate that you have lower reserve releases versus last year, but you had in the second quarter relatively large reserve release, I think above 10%. But you also mentioned that – and I'm not sure if I understand it well that you had reserve strengthening still in workers' compensation. So if you could give a bit more color there, that would help.

And the second thing is, there is an – the expense ratio in the UK and Continental Europe has been increasing over the last year. Are there any main reasons behind it? I know you're expecting it to be a bit lower as you're going to the second half.

A - Christophe Boizard {BIO 15390084 <GO>}

So I think your first question was on the combined ratio of Belgium and in particular, the workers' comp, lower releases from previous years. There's nothing really specific there. It's a business line where there isn't had any (00:56:44) some volatility. And if I remember well, it was a specific type of contract where we had a review of reserves, but it's nothing really very, very special. I would say, it's part of the normal volatility.

Q - Jason Kalamboussis {BIO 4811408 <GO>}

Okay. But do you still have much larger releases in other businesses presumably, because you're making up for that, and also it was like a high release – prior-year reserve releases quarter?

A - Christophe Boizard {BIO 15390084 <GO>}

No, the releases are not really managed in a global way. So (00:57:16) product by product. So the fact that in one product there is a higher or a lower release, will never impact the way that the other releases are managed.

Q - Jason Kalamboussis {BIO 4811408 <GO>}

Okay. Thank you.

A - Christophe Boizard {BIO 15390084 <GO>}

So, there's nothing really – there's no real story behind that. The second question was on the combined – no, on the expense ratio for Continental Europe and the UK, I believe? I think for Continental Europe...

Q - Jason Kalamboussis {BIO 4811408 <GO>}

Yes, which increased over the last year or so. How do you see that progressing over the next 6 months (00:57:50) 12 months?

A - Christophe Boizard {BIO 15390084 <GO>}

I think Continental Europe, you are probably comparing a slightly different scope because last year at Cargeas,...

Q - Jason Kalamboussis {BIO 4811408 <GO>}

Correct.

A - Christophe Boizard {BIO 15390084 <GO>}

...our Italian operations were included there, which was like really a bancassurance type of operation which typically had lower expense ratios. So now actually you are looking at just Portugal which still has a higher expense ratio. So their work is ongoing, particularly to make the business we bought from AXA more and more efficient (00:58:22) potentially also bancassurance business, that's a very efficient business.

In the UK, the expense ratio is really about to drop in both premium income, so your net earned premium goes down. And also (00:58:38) other income and commissions or ancillary income, that would typically kind of correct for in our expenses. So we'd also see a drop the last two years of this ancillary income and that has also an impact on the expense ratio. But we're working hard in actually resizing the operations in the UK to fit the current volume levels (00:59:06) business we want to have in the future.

Q - Jason Kalamboussis {BIO 4811408 <GO>}

Okay, great. Thank you very much.

Operator

The next question comes from Bart Jooris from Degroof Petercam. Sir, please go ahead.

Q - Bart Jooris {BIO 3470300 <GO>}

Yes. Thank you for taking some follow up questions. Coming back a little bit on Asia, and some of these things have been said, the second quarter, you had the impairments, you also made up for a large part in your gross inflows regarding, okay, the loss of the single premiums in the first quarter. So, I assume you had quite some more commission expenses, given that Q2 inherited is a low figure.

If we take Q2 just as a run rate, that is for the following quarters, we already arrive above your guidance. So, could you give any comments on that? Because despite – in case there are no, let's say, dramatic stock exchange movements in Asia, you should exceed your guidance rather easily, I think this year. And then secondly, is there any update on the Ogden rate discussion in UK?

A - Bart Karel De Smet {BIO 16272635 <GO>}

Okay. Asia, if you take the Q2 result, which was €46 million, as mentioned, we have something like €44 million negative on cap gain. So, you could say you are more in underlying of €90 million. We keep the €250 million guidance as being, let's say, what we normally – and I think your words – that maybe easily should achieve. But reminds a number of elements. First of all, we are not sure what the markets will do in the coming months. So you have the trade war and the potential consequences on stock exchange. That's also what partly hit us in Q2.

In a country like Malaysia, our result is already, to a certain extent, impacted by IFRS 9. So also there, the durations in markets have an impact on the – our IFRS profit. And then you have what you already commented a bit, the fact that we will have investments and further growth in China in the coming two quarters, so that will also have a kind of a dampening effect on the profits.

So, it is – if you look to last year, we were at under €13 million profit in Asia after six months, and we ended the year in more than €290 million. We are now at €170 million, so we are indeed very confident that, €250 million is reachable, and with no doubt, not hesitate to do better. On Ogden, Antonio?

A - Antonio Cano {BIO 16483724 <GO>}

In Ogden, we can be very brief (01:02:15). And so, we hope and support that this gets resolved as soon as possible. But looking at the legislative calendar of the UK, where we already said, I think at previous calls that we did not expect any change in 2018, so definitely not. So, we hope that somewhere in 2019, this might be done. And more than that, I cannot say. I will just repeat what I said other times, don't hold your breath for now.

Q - Bart Jooris {BIO 3470300 <GO>}

Okay. Thank you.

Operator

The next question comes from Albert Ploegh from ING. Sir, please go ahead?

Q - Albert Ploegh {BIO 3151309 <GO>}

Yes. Good morning, and thank you for still taking my questions in the call. Two from my end, first of all, on the share buyback, I know you delivered clearly on expectations. But I guess, it must have been in a way an economically more difficult decision to continue at – with the same program given simply what the share prices, and if I simply look at metrics like book value.

So how do you look at that decision in the light of what the share price is? And then maybe you already alluded to something of new flexibility that has been obtained, and then what we can expect on the Capital Markets Day in terms of, let's say, special distributions. Maybe you can already give us some kind of preview there?

And the second question is on the BNP decision not to exercise the put. I remember, you saying that you tried to start some dialog before June 30. So (01:03:58) been any form of discussion with BNP? And if not, yeah, what do you think the reason simply was for BNP just to lapse the put, because I still believe, it would have been an excellent way for you guys to redeploy capital and to use the balance sheet? Thank you.

A - Bart Karel De Smet {BIO 16272635 <GO>}

With respect to the share buyback, of course, we took the process as we did it in the past. However, we have the timing in our board with half year results where we present and discuss our half year results. We come out of management with a (01:04:39) proposal for a buy back where we look at, of course, the cash position. We look at our solvency position. We also look through the economic environment then, and in all honesty, there are maybe a bit more uncertainties in the markets than what we had in previous years. But we also look to - well I would say that the return on equity of a program. And it's clear that the return on equity of the program, with the current share price, is lower than what it was, let's say, the first time or even a number of previous years.

And so, all these elements together brought us to a decision to re-launch share buyback, because it's still considered a much better investment than keeping the cash as such. And also, let's say, by a lack of immediate M&A files, where we have to put the money on the table. So, all these elements together brought us to a decision on new buyback of €200 million.

We will, of course, again, and sorry to repeat that, but in our Investor Day, I gave clearance on our view on this for the coming three years. The put option, first of all, it was an option that was granted to BNP. So, they had the choice to exercise or not. I think, we always have been talking with BNP locally, with the headquarters in Paris on a number of topics. Of course we sometimes (01:06:19) to the put option, but there never have been difficult or a harsh or even discussions on whether to exercise or not. It was fully up to them to take a decision. And we were correctly informed at the moment that the expiry date was there. That they - have not the intention to exercise. And so, I think both parties are happy with that decision. It clarifies something, so we don't have this uncertain element anymore, not now, never anymore because there is no kind of renewal of an option.

So, they are a 25% shareholder. They also, by doing that, somewhere showed their belief in AG Insurance and also believe in the value of distribution agreement, the distribution agreement that is now, you could say, a kind of a perpetual agreement with a notice period of two years.

So, the end date of - end of 2020 is not valid anymore because it's every day moving up for at the earliest three years from the day of the potential decision to cancel the agreement. But also there, we can confirm that there is no indication at all that our important distribution partner in Belgium being BNP Paribas Fortis Bank would not be happy with the way we first of all work together, okay, pay decent commissions for good products with good service. And I think, you already are invested in a company that has a good solvency position and pays a nice dividend. So, I would say everybody seems to be happy.

Q - Albert Ploegh {BIO 3151309 <GO>}

Okay, thank you. Thank you very much.

Operator

As there are no further question, I would like to return the conference call back to the speakers; Mr. De Bart and Mr. Boizard (01:08:21)?

A - Bart Karel De Smet {BIO 16272635 <GO>}

Okay. Ladies and gentlemen, thank you for your good questions. To end this call, let me summarize the main conclusions. Over the past couple of weeks, major milestones have been reached with almost all the legacy stocks (01:08:37). We witnessed also a commercial turnaround in Asia in particular, in China and returned to growth in Life inflows in Belgium. The Insurance net result is strong despite adverse weather and substantial lower support from net capital gains. We showed a continued solid operating performance across all segments with UK making encouraging progress. The Solvency II ratio for Insurance and the Group is strong, well-above target. And we also showed a strong operational free capital generation.

And finally, we launched eighth consecutive share buyback program of €200 million. One last thing, another day to keep in mind is the 19th of September, Wednesday, where we will host our Investor Day in London. On that occasion, we will update you on our new strategic plan for the future following the successful completion of our Ambition 2018 plan.

Now, with this, I would like to bring this call to an end. Don't hesitate to contact our Investor Relations team should you have outstanding questions. Thanks for your time. I would like to wish you a very nice day and for those who still have it in front of them, a good holidays. Goodbye.

Operator

Ladies and gentlemen, this concludes today's conference call. Thank you very much for attending. You may now disconnect.