Acquisition of Generali Nederland by ASR Nederland NV Call

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Company Participants

- Chris Figee, Chief Financial Officer
- Jos P. M. Baeten, Chief Executive Officer

Other Participants

- Albert Ploegh, Analyst
- Bart Horsten, Analyst
- Benoît Pétrarque, Analyst
- Cor Kluis, Analyst
- Matthias de Wit, Analyst
- Robin van den Broek, Analyst

MANAGEMENT DISCUSSION SECTION

Operator

Good day, and welcome to the a.s.r. Conference Call on the acquisition of Generali Nederland. Today's conference is being recorded. At this time, I would like to turn the conference over to Mr. Jos Baeten, CEO of a.s.r. Please go ahead, sir.

Jos P. M. Baeten {BIO 2036695 <GO>}

Morning, everybody. Thank you for joining us at this early moment, especially the people calling in from the UK and possibly USA. As you may have read this morning, we've announced the acquisition of Generali Nederland. We, of course, are very pleased with this transaction as it's, to our opinion, demonstrates our ability to act decisively on attractive opportunities as we see them in our marketplace. It also shows that there are indeed possibilities in the Dutch markets to supplement organic growth with profitable and value-creating acquisitions.

Before Chris and I will discuss directional and the financial transaction highlights, I would like to thank the team of Generali in Italy and in the Netherlands for negotiating with us on an exclusive basis already since May. Over the course of the past month, we have been able to thoroughly review the business to assess the synergies and the potential value of this transaction. We have confidence this will result in a transaction that is beneficial to both parties.

So, let us now turn to the rationale of this transaction. The acquisition of Generali Nederland is in the heart of our M&A strategy of acquiring mid-sized and smaller companies. As you may know, Generali Nederland has been active in the Netherlands for more than 145 year. With a staff of about 350 employees, it provides a broad range of Life and Non-Life insurance products in our markets.

In 2016, Generali Nederland generated a premium income of roughly €380 million, of which €270 million (sic) [€275 million] was in Non-Life and roughly €100 million in Life. So, this transaction will especially boost our position in the Non-Life markets. With a combined ratio year-to-date below 100% already from the beginning, this will positively affect our earnings in the Non-Life business.

Generali Nederland strengthens our overall position as being the number three in the Dutch insurance market, will add roughly 2.1% of market share in Non-Life. This will bring us to a market share of 16.5% in the Non-Life area and will add almost 1% in our market share in Life and our market share in Life will be around 15.4% after closing of the transactions.

The transaction rationale, in our opinion, is quite compelling. The activities of both companies show an overlap which offers attractive business synergies and diversification benefits. In addition, the combination of the two organization also eliminates capital tiering restrictions as they are today within Generali Nederland.

Overall, there is a significant synergy potential. In total, we expect to realize approximately €140 million in cost and capital synergies by the end of 2021. With this transaction, we take advantage of a.s.r.'s strong solvency position and financial flexibility. The cash consideration, as you may have read in our press release, which we, by the way, will pay out of existing funds on closing will amount to €143 million.

After closing, we will also recapitalize the acquired entities to at least 130% and after capitalized – capitalization of Group Solvency II ratio on a pro forma basis remains strong at 185%. So, an effect of roughly 9 points compared to our reported solvency end of half year.

When we take into account the additional capital that we will inject in the acquired business and benefit of the expected synergies, we estimate a total investment, and Chris will come back to that in a moment, of fungible capital of roughly €200 million. As you know, we attach great value to our financial discipline and have maintained this when assessing this transaction.

Therefore, we expect an attractive return on investment exceeding 12%, and we wouldn't be surprised if the final return on equity will be in the 15% area. The all-cash deal, by the way, received already approval by Generali Group, as you may have seen in their press release of this morning, and had the full support of the Generali Nederland's board and supervisory board as, of course, our two boards.

Also, we had a constructive dialogue with both workers councils, ours and of Generali Nederland's, and both workers councils have approved with a positive advice this acquisition. Of course, as is customary, this transaction is subject to approval of the Dutch Central Bank and the Dutch competition authority, ACM. We expect to close somewhere in the first quarter of 2018.

We have confidence in execution of this transaction given our very strong track record in integrating businesses and ongoing cost management. During the recent years, we have already acquired eight companies and successfully completed migration onto – into a.s.r. For example, the last one we integrated was NIVO and this will be completed for the end of this year. So, we are ready for the next one.

Our integration plan, by the way, which we will develop further together with the people of Generali Nederland includes the relocation of all Generali Nederland's management and employees to a.s.r.'s main office in Utrecht in the course of 2018, and of course, the merger of all the legal entities. We plan to merge the – to do the merger of the legal entities in Life somewhere in 2018, and Non-Life will be done at the latest in the first half of 2019.

We expect the integration to offer a cost synergy potential, representing at least 50% of the Generali Nederland cost base, which is just below €50 million. So, roughly €23 million per annum and that's before tax. The main driver of those cost synergies will be the relocation of employees and the closing of the current building of Generali Nederland, the IT migration and, of course, scale advantages in Non-Life, Life and the several group functions.

Before handing over to Chris, one final remark I would like to point out that this transaction will have no impact on our earlier stated commitments to participate in a final sell down for an amount of circa €100 million, if and when the Dutch states should decide to sell down the remainder of their position further in this year. And as said, this will, of course, depend on the market conditions and the solvency at the moment of the Dutch states' decision.

Having said that, Chris, the floor is yours and Chris will start at slide number...

Chris Figee {BIO 18815839 <GO>}

Four. Okay. Jos, thank you very much. Back to slide number 4 to walk you through the financial elements of this transaction. As you would expect from us, we are applying very strict financial criteria to evaluate this investment.

Next, we're strengthening the a.s.r. business franchise. We believe that this business, this transaction will also raise our financial profile and create real and tangible value. We have evaluated this transaction along two yardsticks. One is, does it meet our base ROI hurdle of 12%? So is the earnings contribution devalued by the capital commitment? Does it exceed the 12% hurdle? And secondly, is it robust? Does it stack up to alternative way to deploying this capital, for example, buying back our own shares?

And we're very pleased to say that we are firmly convinced that this transaction meets both criteria. Please note that this deal has very specific transaction parameters, very specific transaction scope. The entity that we are acquiring is today still has an intragroup reinsurance arrangement with the parent company in Italy that will be eliminated upon closing, as was also indicated in the press release by the signing entity, by Generali. So, we're buying the business excluding this quota share arrangement, after which we will inject capital in the various entities to compensate for the solvency level.

We expect the ROI to exceed 12% based on operational and capital synergies. Synergy potential to be around €17 million. Contribution to operating result, which is the base earnings plus synergies, around €30 million with a reasonable conservative calculations. We didn't go overboard in assessing the synergy potential of the group. There's always a potential haircut when you make those deals work. Out of this, we estimate that the additional generation of organic capital, additional OCC, for those who like to use that phrase, is around €25 million per annum upon realization of the synergies.

Total expected capital deployment, there are €200 million. 6 points of SCR, at least 6 points of the SCR of a.s.r. to date i.e., divide €200 million by €3.5 billion SCR, you get to 6 points. In the next page, I will walk you through that buildup. Out of €200 million, €143 million is a net cash payment. The remainder represents capital injections and cost and capital synergies. So, again, we believe this makes a very attractive deal at 12% hurdle and Jos alluded to potentially even 15%, if we divide €30 million additional earnings by €200 million of capital commitments, you get to something that's very close to 15% upon delivery.

So, let me walk you through our capital commitment on page number 5. We have outlined here the various steps how we get to the €200 million of fungible capital commitments. Block one, our net cash price is the amount of cash we will transfer as considerations to Generali, €143 million. We will inject around €200 million of capital into the Life and Non-Life subsidiaries, mostly in the Life business, a bit in Non-Life to compensate for the termination of the quarter share contract and there will be cost and capital synergies of €140 million that are beneficial to us. And net-net, that gives a fungible capital deployment of €200 million.

To zoom in on those cost and capital synergies, I tend to divide them into three blocks, some will realize upon closing of the deal immediately. Some will realize upon the legal merger between the entities and some will realize upon the finalization of the synergies.

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In terms of this block one, realization upon closing which is a tiering benefit. As you have – we may recall, we've outlined in our various analyst presentations that we have tiering headroom in eligible or room to top (00:12:54) eligible capital. One could argue tiering headroom in itself doesn't feed any children unless you deploy it, enter it into earnings. We believe these transactions allow us to turn tiering headroom into actually as tangible earnings, so tiering benefits will recognize and exist upon closing of the transaction. Upon legal merger, there will be various capital synergies, mostly diversification benefits, possibly a LAC DT benefits that will realize upon legal merger of the entities.

And if and when we realize the planned synergies, that will ultimately be reflected in the best estimate liabilities and lead to reduction of capital. One could argue that it's possible to bring forward those capital synergies, but historically, we've never done that. We've only recognized capital synergies if and when they are there, not just when they exist on paper. And we try to stick to that more responsive (13:52) approach to capital management.

Adding it all up, by the way, also – we also have some alignment of actuarial assumptions, which will be a small negative upon closing. So, block four has closing synergies, legal merger synergies, cost benefits and alignment of actuarial services. Net-net, the commitment of fungible capital of a.s.r. is €200 million and we compared the ROI on a €200 million of alternative ways -- deploy this €200 million, and we think this deal will stack up against it.

So, we believe that we are – we will be effective owners of the Generali balance sheets and that effective ownership will help us make a very attractive ROE on this transaction.

That is -- concludes my portion of the financial analysis and elaboration on the capital commitment. Back to Jos.

Jos P. M. Baeten {BIO 2036695 <GO>}

Thanks, Chris. Well, to summarize, as said, we are very happy with this transaction. It will strengthen our market position in the Netherlands, especially in Non-Life. And as you may know, we are focused on creating a stronger Non-Life business. And it shows also that we are able to deploy our capital in a value creative way for our customers and our shareholders. So, we're happy and we will start to integrate this business as soon as we have closed the transaction and that will happen as said in the beginning of 2018.

So, as from now, the floor is open for questions.

Q&A

Operator

Ladies and gentlemen, we will start the question-and-answer session now. First question, Mr. Cor Kluis, ABN AMRO. Go ahead, please.

Q - Cor Kluis {BIO 3515446 <GO>}

Good morning. Cor Kluis, ABN. A couple of questions. First of all about the solvency ratio. You mentioned in the press release is minus 6% on the solvency ratio. Could you give the split out effect of – on the Own Funds and the – on the SCR? So, the SCR rises by how much than the owned funds? How does that change?

And also related to debt, you said minus 6% and then at the end of Q2, the solvency was 194%, so then I don't comment the 185% solvency ratio, so what do we miss there?

Another question is about the capital generation is €225 million, this is the UFR of 4.2%, so obviously, on a UFR, where you were always very transparent about -- of 2.7%, the capital generation would be higher than the €25 million. How much higher would that be?

And my last question is about the hybrids of Generali. You mentioned that some of that hybrids is being now accounted in the capital in Tier 1, Tier 2. How much hybrids that Generali have and in absolute terms, how much extra benefit do you have in your Own Funds due to debt? That were my questions, and by the way, great acquisitions.

A - Chris Figee {BIO 18815839 <GO>}

Okay. Cor, it's Chris. Thanks. Let me take that question. First one on the solvency ratio. The numbers would be pre and post transaction. If you look at our half year results and I guess you have pen and paper with you, and Own Funds were €6.8 billion, SCR requirement, €3.5 billion. You divide one by the other, you get 194%. Post-transaction, the Own Funds will go up and the SCR will go up. Own Funds estimate €6.950 billion (17:42), SCR up €3.8 billion. Divide one by the other you get 185%.

So, we believe that the move is kind of the dilution effect that you're adding a business that has a little bit lower solvency ratio than we have, so you dilute in terms of ratio. Impact is (18:01) that the required capital goes up. If you think about the cap – the fungible capital commitments for us, we define this fungible capital with a solvency ratio up 140%, which is our dividend payment trigger. So, if you multiply the required capital by 1.4 and now you calculate the gap between the Own Funds and the solvency floor, so basically, 1.4 times the required capital, and you then take pre and post, you get to a delta of €200 million. And that's a €200 million difference. And we relay that €200 million to the current required capital that we have, so that's actually 6 points.

So, in summary, we gave you the pre and post Own Funds and required capitals, you divide one by the other, you go from 194% to 185%, which is simply is the dilutive effect you're adding businesses that have a lower solvency ratio as such. And because the required capital goes up, you think what it does to our fungible capital in euro terms, the only difference in euro terms really is the fungible capital commitment and there, we always multiply the required capital by 1.4, which gives us a solvency floor in this model, so 140% is our official formal dividend trigger.

If you then look at the delta between Own Funds and floor measured in euros, you get actually to a €200 million difference and that €200 million is indeed the actual additional capital commitment that we have. And (19:35) to us, we relate €200 million to €3.5 billion required capital we have today, which is 6% application of our solvency, so that is the difference between the dilution effect because you're acquiring a business with lower required capital -- a lower solvency ratios and the actual capital that we commit to this – to the deal.

To your second question on the UFR effect of 2.7%, the honest answer is, Cor, I have literally no idea, but my best guess is the Generali business is more tilted towards Non-Life than Life. If you look at their premium level, it's about two-thirds is in – but yeah, three quarters is within Non-Life, one quarter is in Life. The Life business has a substantial turn life component to it, so this business has less dependence on UFR, both in stock and flow.

So, a low UFR will push up the organic capital generation a bit, but not something that would make us really rich is not that hard of the deal. So, at a few meetings too, it is my best guess but not material to our increase.

Fine in terms of hybrids, there were no so much – not so much hybrids in the Generali NL capital structure, but an amount of DTA that was not recognized. So, the business brings in a DTA that is ineligible, because it exceeds norms for Tier 3 capital. And because we have Tier 3 headroom that we are able to absorb that DTA in our balance sheet. And as we said, we're very pleased because this allows us to have -- convert tiering headroom into actually earnings because this is solvency that is not -- it is there. It is not recognized in the Generali balance sheet, but will be recognized, it will exist on our balance sheet without us doing real hard work for it.

Q - Cor Kluis {BIO 3515446 <GO>}

Very clear. Thank you very much.

Operator

Next question is Benoît Pétrarque, Kepler Cheuvreux. Go ahead please.

Q - Benoît Pétrarque

Yes. Good morning. Couple of questions on my side. The first one will be on the capital generation. So, the timing we – I think you said that it's going to be €25 million by 2021. It seems that most of the capital generation in effect comes from cost synergies. Could you confirm that and also could you talk about the timing of the synergies. Are we going to start to see some positive effect already in 2018 and 2019 or will that be more back-end loaded? And could you also talk about whether you anticipate also in your new capital generation figure a turnaround of the combined ratio which I think was pretty high at Generali? That was the first question.

Second was on the kind of capital injection you do there. I thought that Generali recapitalized the business in Q1 2017. I think I saw reports showing that the Solvency II ratio in excess of 130%. So, which level of Solvency II ratio do you buy the business before recap? That will be the question.

Then the last one was on the – to come back on the Solvency II impact. So, you said 9 percentage point negative on day one, what will be kind of the positive in the coming years on Solvency II ratio? So, now it's minus 9 percentage point. Can we expect capital synergies and cost synergies to have a positive effect and how much will that be? Thank you very much.

A - Chris Figee {BIO 18815839 <GO>}

Benoît, on your first question on the OCC, I think it's a gradual improvement. I agree that what the current – we will need to enhance the earnings of the Generali Group, enhancing the cap generation or these realizations will be important (23:30) gradually – I think gradual movement towards the 21 number. There will be bit of a re-risking opportunity which will be front-loaded.

For example, there is an amount of cash on Generali in our balance sheet, which is waiting to be reinvested. There are also some tax rulings around of it, forced to reinvest it relatively quickly. So, you see the first year benefits from re-risking and investing some of the cash. And then, I think the cost synergies will gradually fade in over the year and gradually move towards the target level. So, re-risking benefits in the beginning, putting the cash to work and then gradually over time towards our target.

A - Jos P. M. Baeten {BIO 2036695 <GO>}

Second part of the first question was about the combined ratio of Generali. Well, you already said, Benoît, that it was above 100% last year, that's true. As far as we have seen the numbers, the first half year, it developed in a positive way and it is currently below 100%. We will start integration in Non-Life as from the next year, 2018, after closing. And we don't know yet whether we will be able to merge the two entities already in 2018 or at the beginning of 2019. If and when we have combined the two, the cost level of Generali will be more matched with ours. So, we are convinced that we will be able to bring the combined ratio as far as it is not already below 100%, more towards our own levels in the due course of 2019.

A - Chris Figee {BIO 18815839 <GO>}

Benoît, to your third question on the incoming solvency levels of the entities, indeed, Generali injected capital into its Life subsidiary in Q1. But remember, it also had a quota share arrangement between subsidiary and parent company. The quota share arrangement was eliminated, the intragroup reinsurance arrangement. So, the incoming solvency of the entity is just below 100% because of the elimination of the quota share. So, we're looking at recapitalizing Life entity.

To some extent, the Non-Life entity had a solvency above 100%. So, I think in our planning, I think we capitalized at 130% on closing, achieve or aim to have the Life business move to 140% in the course of the year. That's at least is assumed in our capital synergies that we will just retain some of the synergies and move the Life business to 140%. With that, they should be able to run standalone and speedily, as quickly as possible integrate into our own a.s.r. legal entities.

And your final question was on when do we see some capital synergies fit in? I think if you look at the last page, page 5, the €140 million, think about €50 million in tiering benefits, think about €70 million, €80 million in like the TSCR (26:53) benefits, but think about €50 million to €70 million of actuarial assumption alignment that will take place as that will be realized at the time of the legal mergers.

Then there is cost benefit which is the remainder, is around €80 million which is near the cost synergies which will gradually fit in over time. So, I think especially the cost benefits in our solvency level will fade in over time upon delivery and we will choose to realize and when delivered, not upon when you put them on paper.

Q - Benoît Pétrarque

Great. Thank you very much for that.

Operator

Next question, Albert Ploegh, ING. Go ahead, please.

Q - Albert Ploegh {BIO 3151309 <GO>}

Yes. Good morning. Yeah, a few questions left from my side. Maybe first on the Non-Life, which is still two-thirds of the need of the premiums. Can you give a little bit more detail on the composition of the book and potentially also, let's say, the different combined ratios for PNC, for example?

And I also have a question on maybe to get a little bit understanding on your thinking of weighing an acquisition against the alternative of a buyback. I think you made some comment on slide 4 where you refer to the accretion exceeds the impact of a €200 million buyback. Can you give a bit more color around that statement to also going forward to understand better how you weigh these alternatives?

And the third question is and I would just sense this is the first big bolt-on acquisition. I know you have alluded to some potential pipeline on funeral, so can we expect maybe by year-end some more capital allocation to other bolt-on acquisitions?

A - Chris Figee {BIO 18815839 <GO>}

Albert, let me get to your question on capital deployment first. We did check in our assessments to what extent deploying €200 million of share buybacks (28:57) earnings per share, dividend per share and cap generation per share. And of course, buying back shares does accretes EPS, DPS and CPS, if you wish. We felt that if you look at these numbers deploying it to M&A naturally outperform that -- those metrics.

However, I could simply say very crudely and I'm not giving any opinion about the value per share price here, mind you, guys. But if you take the operating profit that we're making this year or that we've made so far this year, if you think about the underlying operating profit that we alluded to in Q2 around

€175 million per quarter. Simply divide that by the market cap of a.s.r., you get to something which is around 11% to 12%. So, we think effectively, when you have a deal that exceeds that...

Q - Albert Ploegh {BIO 3151309 <GO>}

Yeah.

A - Chris Figee {BIO 18815839 <GO>}

...you get more bang for your buck. But we deliberately and explicitly asked ourself the question, earnings per share, dividend per share and cap gen per share, what would happen if you buy back shares for €200 million? What would happen if you buy Generali and we felt that this actually does outperform that metric?

A - Jos P. M. Baeten {BIO 2036695 <GO>}

And on your first question, some – a bit more insight in the Non-Life business. Out of the €280 million of gross written premium, 16% of that is in disability. The remainder is in rest of Non-Life, so in PNC, of that 84% roughly half is car, is car insurance, 17% is in commercial lines and 15% is in personal lines. The average – I don't know all the combined ratios by heart, but the average combined ratio of the total Non-Life business is in the -- just above – just below 100 areas and is already set. As soon as we have converted the business to our platforms and to our business lines, we are pretty sure by adding our cost levels that we will be able to move them towards our own combined ratio levels.

Q - Albert Ploegh {BIO 3151309 <GO>}

Okay. Thank you.

A - Jos P. M. Baeten {BIO 2036695 <GO>}

And on your third question to elaborate on a potential pipeline, I think we already, in earlier calls, explained that we only start talking about them as soon as we are sure that we can present a transaction. We are convinced there are more opportunities in the Dutch market, but never elaborate on names and timelines whether they will be done by us.

Q - Albert Ploegh {BIO 3151309 <GO>}

Thank you.

A - Jos P. M. Baeten {BIO 2036695 <GO>}

But we see still opportunities.

Operator

Next question, Matthias de Wit, KBC Securities. Go ahead please.

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

Yeah. Good morning and thanks for taking my questions. I first wondered if it would make sense to develop an internal model considering that the business will become bigger and bigger following all the acquisitions you did and so it might make sense to develop one given the current size of the company.

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A second question is on the capital generation of €25 million. I'm not sure if I understood it correctly, but does that include any SCR releases or is that purely Own Funds generation? And can you also elaborate a bit on what you have assumed in terms of pre-risking because the Generali portfolio is still significantly overweight in sovereign, so I would have expected, yeah, even a higher capital generation assuming that you could shift part of these assets to liquids or mortgages.

And maybe a last one. Can you, yeah, elaborate a bit on what you have exactly assumed in terms of LAC DT for? Because I think there is currently none in the Life business and a bit in Non-Life. But if you could be a bit more specific of what you expect to get over time it would be helpful. Thank you.

A - Chris Figee {BIO 18815839 <GO>}

Hey, Matthias. Good morning. On your question on the partial internal model. I think I foresee our standpoint data has not changed because of Generali transaction. So, we believe, it's something we watch with interest, but there is really no plan to date to move to an internal model. And that may change in the future, but at this point in time, where there is no real plan or intention to move there. At this point, I mean, this transaction doesn't change yet.

In terms of the post of the capital generation of €25 million, it is mainly Own Funds, (33:58) Own Funds. There are some SCR (34:01), but the bulk of it is Own Funds because Generali is predominately a Non-Life business. So, it's all technical result, underwriting results and your long-term investment margins as well (34:11) could generate on this business. So, a limited contribution from SCR really is the majority of it is really addition of operational, operation of Own Funds above the line. It's numerator stuff, if you wish.

In terms of the reinvestment side and risk, re-risking, it's actually limited fair point. There's €150 million of cash in the Generali balance sheet at this point in time, which is there from a transaction previously one day aborted or sold some of the real estate. That needs to be in reinvested in order to get the tax credit that's part of this. We've assumed that reinvestment takes place and for the rest, a very limited re-risking. At this point, we think that is still possible. So, there is some upside in our numbers as part of this. But the cap gen that we have here is really the business as it is, reducing the cost, further improving underwriting result, and re-risking the cash. It does not yet assume a massive turnaround of their sovereign, sovereign portfolio.

We will assess that annually when we do our annual SAA, Strategic Asset Allocation study in October and November. And by that time, we'll have both balance sheets or at least we have an assumption of both balance sheets. And then we will run the group-wide risk allocation program, so. we felt it was right not to run ahead of debt assessments, but assessed those numbers when we do the group-wide annual Asset Allocation study.

But the €150 million real estate is actually there and rest assured, a.s.r. is already working to fill it. We have a pipeline of potential real estate transactions that will enable us to very swiftly move ahead and fill the -- we just take the entity in Generali and replace the cash with actually earnings.

LAC DT, your final question will assume that all those LAC DT levels at the Generali will move to the 60% level that we have as a.s.r. and substantiate that with an increased earnings base, lower cost level, better underwriting profits and some re-risking results. And we've believed that given the plans that we have, moving towards a 60% LAC DT as we deploy across our business is definitely and definitely feasible.

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

Okay. Thanks a lot.

Operator

Next question, Bart Horsten, Kempen & Co. Go ahead, please.

Q - Bart Horsten {BIO 2390919 <GO>}

Yes. Good morning. Most of my question have been answered. I have two left. First, on the ROI of the investments. If I'm correct, the initial ROI is around 4% excluding the synergies,obviously. When do you expect until 202 you will exceed the 12% hurdle rate? So, that's more in terms of timing of both the cost synergies and the capital synergies.

And my second question relates to the Solvency II position of Generali after your capital injection. I think you just mentioned it will be around 130%. Do you think that's sufficient from there or will further strengthening be necessary and will it be mainly through our organic capital generation or does it require more capital,maybe in the mid-term? Thank you.

A - Chris Figee {BIO 18815839 <GO>}

Bart, on the ROI, good question. I think, I don't care -- I mean, what we'd look for is to quickly move the ROI to deal above 10% because we believe 10% is our best estimate of the hurdle rate or the cost of capital. We believe that taking out some costs, improving pricing and the re-risking I just discussed, we believe that the ROI moves to something in the north of 10%, probably early 2019 would be my best estimate, if you exclude any restructuring charges, of course. But the OpEx restructuring charge is somewhere in 2019. We should move this thing towards the 10% hurdle and (38:11) at the value creation level and then quickly pull through towards 12% and 15%. So, that's my assessment there.

In terms of solvency of the operating entities, I said we inject capital immediately to get the two entities upon closing or just the minute after closing to 130%. We'll assume that the Life business will then be further strengthened to 140% and that's enough because by then, we will integrate into a.s.r. and the legal merged entities will cease to exist.

So, 130% in Non-Life, ultimately pulled to 140% in Life and then it becomes no longer meaningful because they will be integrated and be part and parcel of the a.s.r. legal entities.

A - Jos P. M. Baeten {BIO 2036695 <GO>}

And as said, Bart, the legal merger in the Life entity is foreseen already in 2018.

Q - Bart Horsten {BIO 2390919 <GO>}

Okay. Okay. Thank you.

Operator

Next question comes from Robin van den Broek, Mediobanca. Go ahead, please.

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

Yes. Good morning, everybody. Sorry, did I sound like I'm about to die, but I hope that's not the case. Most of my questions have been answered as well. Two remaining. Just very clear, the 185% pro forma you mentioned, so I understand correctly that it only includes basically the net cash price of €143 million or does it also include the actuarial alignment and the tiering benefits you mentioned before? And secondly, I was just wondering your holdco cash target of €350 million, how does this transaction and potential participation in the state sell down affect that level for this year and or do you expect to upstream some more capital from your subsidiaries to get to that target?

A - Chris Figee {BIO 18815839 <GO>}

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Well, Robin, thanks for your question. And first, where is your health insurance or where is your funeral insurance? (40:07) take an additional hit this year. No, I hope you get back soon.

In terms of the capital flow, it's page 5 and €200 million actually is a net cash out plus and minus all the movements in capital. So, as you see, the €200 million is a cash prize of €143 million plus the capital injections plus aligned with an actuarial synergies minus the various capital synergy that we have. So, it's a net figure after all that's been said and done. So, I think that – to your first question.

What does it do to our holdco cash targets? We believe at this point that the holdco cash target is still feasible, although we're not married to the holdco cash target in the sense that as long as our business continue to operate very effectively, we believe it's also probably when (40:57) explainable that there's cash in the operating entities. In a sense that in our point of view, managing very tight for holding cash makes sense if you've got an international group with various subsidiaries under various regulators who have different management teams where they might be a discipline question. In our situation, we're still in one country, one jurisdiction, one regulator, and the management team of a.s.r. Group is the same as the management team of different legal entities, so there's little to be disciplined there.

So, as a principle, we're not as tied to holdco cash as some of the others are, but we do believe that holding cash is not something that is going to be changed a lot because of this. Although, we will be exploring, I think that's in our pack. We'll always explore whether the funding for this deal should be done by OpCo upstreams or could it also be done by raising cash in the capital markets.

We haven't made a decision there yet, but if you look at the actual return on capital in our business, and if you look at the estimated cost of capital in the hybrid capital markets, the latter could be an option to smoothen the funding of this transaction. Again, we haven't made our decision on that yet but it's something we explore to see if we have – what is the most value creating way to fund this cash out.

So, Tier 2 security, even Tier 1 options are, of course, in play because, I mean, we've shown to you the benefit of having Tier 3 headroom and one can convert tier headroom into value creation and tangible earnings. So, to make a long story short, holding target is unchanged, although I'm less married to that holding target than some of my peers would be and exploring whether upstreaming cash or effectively raising capital in the capital market is the most value creating way to support this business and that is something we'll explore further.

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

I'm sorry just to come back on the Solvency II ratio. I thought you mentioned before that you don't recognize cost synergies, for example, before they are actually realized. So, I think you said that the €185 million is net including all the synergies, but that doesn't seem to coincide with your previous statement or am I getting something wrongly here?

A - Chris Figee {BIO 18815839 <GO>}

€185 million is at closing, Robin.

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

Yeah. Okay. So that doesn't include any of the synergies that you mentioned before?

A - Chris Figee {BIO 18815839 <GO>}

Yeah.

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

Okay.

A - Chris Figee {BIO 18815839 <GO>}

Well, it does – not the cost synergies. The others are there. The cost synergies will only be realized upon delivery. The tiering synergies, the legal merger synergies, the SCR benefits will be there (43:39) cost synergies that will show in your best estimates, we will only recognize those when we actually deliver them.

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

Okay. Thank you. That clarification is very welcome. Thank you.

Operator

Last question comes from (43:53) of JPMorgan. Go ahead, please.

Hi. Good morning. Thank you for taking my questions. I have a question on the earnings. I mean, currently, the Generali Dutch business is getting around €9 million and then you're saying that it will reach to around €30 million post-tax – post the synergies. I mean, it seems like a big difference. Can you just help me bridge this? How is it coming and where is it coming from? That's my question one.

And the second question I have is, if I look at slide number 5, the capital investment to transactions. I mean, the net cash you pay of €143 million is today and the gross capital injection is also today of €200 million. So, is it fair to say that you've actually injected €340 million on this? Obviously, there is capital and cost synergies, but the cash, which goes aside from your current business is around this much. Thank you.

A - Chris Figee {BIO 18815839 <GO>}

Okay. On the operating result bridge, indeed today, if you look at the IFRS profit, its 4 in Non-Life and 13 negative in Life. But, in IFRS profits, it also includes some reserve strengthening LAT issues at Generali.

We reported the operating result, so the bridge from IFRS earnings today to operating result in the future is one IFRS to operating and operating from year one to year three. We think there is definitely opportunities to gradually, as Jos said, the combined ratio in the Generali business today is at or below a 100s. Last year, we're still above 100% .Today is on the run rate improvement, there was not yet in the 2016 figures. But I guess it will show up in 2017 figures simply because the hardening of the Non-Life markets.

As we strengthening – as we strengthen provisions, the gross capital injections and the alignment of the actuarial assumptions, that will just lead to much less pressure from LAT shortfalls and actually support the earnings of the group and finally, there's the investment from the reinvestment of the €150 million cash.

So, to me, the bridge from the IFRS loss in 2016 to operating results in 2016 to an operating profit in 2020 is partially already ongoing improvements in Non-Life earnings. The strengthening of the reserves that will take place and the alignment of the actuarial assumptions that will just eliminate continuous negatives from LAT shortfalls. And finally, there is the returns from the reinvestment of cash, so that means that the standalone Generali business, excluding synergies already move into positive operating earnings territory and from there, we can pull them to actuarial full synergy potentials, full operating earnings including synergies. So, that's the bridge.

In terms of your point of what is a cash investment, well, actually, the cash out, the cash that leads the group has €143 million. When you buy a business and then we move cash around from a.s.r. Life into Generali Life and from a.s.r. Non-life into Generali Non-life, but both are 100% subsidiary. So, there's no cash out. The cash out of the group is €143 million. Then indeed we strengthen the

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capital base of the acquired entities by €200 million, but again, we earn it back, back to real intangible synergies and the DTA will be recognized on day one.

The LAC DT and SCR mergers, the benefit, will be realized upon legal mergers. I mean, I leave to anyone who wants to see the glass half full or glass half empty. The facts are that the cash out is €143 million. Fact is €200 million of capital injection, but fact is there is a LAC DT benefit, the diversification benefit and a DTA benefit that actually tangibles here and there. So, I believe that is the capital commitment.

The remainder then is, I think, your actuarial assumption alignment which we'll take into account, so the one thing you could discuss is the recognition of the cost synergies. €80 million and indeed that will happen only upon [Technical Difficulty] (48:20).

Interestingly, if you think about the delivery of those delivery synergies, if we were not to realize them, we'd still would be able to make the hurdle rate on this transaction and so we would realize them because we believe strongly in the synergy potential in this case. So, fact is, there are real tangible capital synergies that will limit the actual capital commitment of our group.

Q - Operator

Okay. Yeah. That is clear. Just following up on cost synergies. I think if I'm not mistaken throughout the presentation you said that the cost synergies are around €80 million in the future, so I was just wondering then in that case, am I – did I listen to that correctly or is it something else?

A - Chris Figee {BIO 18815839 <GO>}

Yeah. The cost synergies are €80 million, but that's after inclusion, by the way, of the restructuring cost. So, think about a cost synergies minus restructuring costs and some tax impact and then you get €80 million of cost synergies, net of restructuring cost.

Q - Operator

Okay. All right. Thank you.

A - Jos P. M. Baeten {BIO 2036695 <GO>}

Well. Thanks. Thanks, everybody for joining our early morning call. This last question concludes our call. And again, thank you for listening and we look forwards to all your reports and if you have any further questions, please don't hesitate to contact one of our IR colleagues. Good morning, everybody.

Operator

Ladies and gentlemen, this concludes the a.s.r. conference call. You may now disconnect your line. Thank you.

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