Y 2020 Earnings Call

Company Participants

- Jan Willem Weidema, Investor Relations
- Lard Friese, Chief Executive Officer
- Matt Rider, Chief Financial Officer

Other Participants

- Andrew Baker, Analyst
- Ashik Musaddi, Analyst
- Farooq Hanif, Analyst
- Fulin Liang, Analyst
- Michael Huttner, Analyst
- Robin van den Broek, Analyst
- Steven Haywood, Analyst

Presentation

Operator

Good day and welcome to the Aegon Second Half Year 2020 Results Conference Call. Today's conference is being recorded. And at this time, I'd like to turn the conference over to Jan Willem. Please go ahead, sir.

Jan Willem Weidema {BIO 15133400 <GO>}

Thank you, Anna. Good morning, everyone, and thank you for joining this conference call on Aegon's Second Half Year 2020 Results. We would appreciate it if you could take a moment to review our disclaimer on forward-looking statements, which you can find at the back of the presentation. With me today are Aegon's CEO, Lard Friese; and CFO, Matt Rider.

Let me now hand over to Lard.

Lard Friese {BIO 17008174 <GO>}

Thank you, Jan Willem, and good morning, everyone. Thank you for joining us on today's call. In my part of the presentation, I will take you through the financial and strategic highlights for the half year and look forward to our strategic priorities for the coming year. Matt Rider will then go through the details of the results and our capital position. I will conclude the presentation with a wrap up. After which, we will open the call for the Q&A

session. So, let's move to Slide Number 2 and let's start by recognizing that the COVID-19 pandemic continues to affect all of us. It made the second half of 2020 challenging for our customers, colleagues, and the communities we operate in. I am proud of the continued commitment of our employees who provide support and uninterrupted services to our customers and business partners in the midst of the pandemic. Despite the impact of COVID-19 on different parts of our business, we were able to report a 7% increase in underlying earnings to EUR1.029 billion.

This increase was driven by lower addressable expenses in all our units and the benefit from higher equity markets. In contrast to the first half of this year, claims experience was broadly in line with our expectations as favorable morbidity experience in long-term care provided a meaningful offset against adverse mortality experience in our US Life business. These were both driven by the impact of COVID-19. The net loss of EUR147 million for the second half of 2020 is due to a negative result from fair value items in the Netherlands. This is a reversal of what happened in the first half of 2020. The Solvency II ratio for the Group increased slightly to 196%, which is after deducting the proposed final dividend for 2020. By proactively managing our balance sheet, we have ensured that the capital ratios of our three main units ended the year above their respective operating levels. For the Dutch Life business, we have now implemented an improvement to our internal model following approval by the Dutch Central Bank.

This significantly reduces the sensitivity of its Solvency II ratio to credit spread movements. Free cash flows amounted to EUR530 million for the full-year 2020. In 2020, we used these free cash flows to reduce leverage and pay dividends to our stockholders. We will propose a final dividend for 2020 of EUR0.06 per common share at our 2021 AGM bringing the full-year dividend to EUR0.12. Last year's rebasing of the dividend ensures that it is sustainable and well covered by the free cash flows that we generate even in reasonable stress scenarios. So, let's move to Slide Number 3. At our recent Capital Markets Day, we shared with you our ambitious plan comprised of over 1,100 detailed initiatives designed to improve our operating performance by reducing costs, expanding margins, and growing profitably. The program has had a good start with 260 initiatives delivered at the end of 2020, of which the majority relates to expense savings initiatives.

We maintained our pace with initiatives being executed up to the end of the year and we kept the rhythm and discipline into 2021 with continued good progress seen in January. As I highlighted at the Capital Markets Day, the performance improvement program is important not only because of the anticipated medium-term financial benefits, but also because of the discipline and execution capability it is helping us to build. These initiatives led to a reduction in expenses of more than EUR75 million and were the main driver behind a EUR136 million reduction in addressable expenses. This puts us firmly on track to deliver half of our 2023 target of EUR400 million savings from expense initiatives by the end of 2021. In addition, expenses benefited from reduced travel, marketing, and other spend due to the COVID-19 pandemic. We expect this to reverse once vaccines are rolled out and restrictions are lifted in the countries that we operate in.

Let's now turn to the progress we have made in respect of our strategic assets in the second half of the year. I'm now on Slide number 4. Our priority for the strategic assets is to grow the customer base and expand the margin we are able to achieve. Some of these businesses do require investments in order for us to fulfill our ambitions while others are already positioned to take advantage of market trends. In the US, we have the ambition to regain the Top 5 position in selected life products over the coming years. It is early in that transition. However, in the second half of 2020, we saw good momentum in our main distribution channel World Financial Group as a result of growth in the agency count and the introduction of a new funeral concierge benefit for Index Universal Life policies. This benefit is especially attractive for customers with higher face amount policies and results in a higher margin on new business.

Overall new sales were down, however, due to our decision to make product changes and sunset certain legacy Whole Life products. In the US Retirement business, we saw a strong bounce back in our mid-market segment in topline sales in the second half following a temporary slowdown in second quarter sales driven by COVID-19. Mid-market sales increased by 49% compared with the first half of the year to $2.2 billion as our sales team was able to quickly and effectively adapt to a virtual sales model. In addition, the momentum continues to build with ancillary product sales to our existing customers with utilization of our Managed Advice offering increasing 20% driven largely by the middle market. Stable value product adoption and asset retention rates in the Advice Center also increased. These initiatives support our ambition to expand our margin in the Retirement Plan business.

Our Dutch strategic assets continue to perform well. We are market leaders in both mortgage origination and defined contribution pensions and we believe that our market share continued to increase in the second half of the year. This contributed to the earnings growth of our service businesses, which now represent 12% of our earnings in the Netherlands and also generate significant asset management fees. Our mortgage origination volume for full-year 2020 surpassed the EUR10 billion mark for the first time, of which EUR7 billion was related to fee-based mortgages. This cements our position as the largest third-party mortgage originator of the Netherlands benefiting from our scale, high service levels, and diversified funding. Aegon's defined contribution pension offering benefits from the scale of TKP. TKP is our subsidiary specialized in pension administration servicing 4 million participants and is the second largest player in this field in the Netherlands.

It recently won a new contract for the administration of pension fund for workers in the Dutch metals and electronics industries. As of next year, TKP will start servicing this Top 5 Dutch pension fund representing 1,400 employers and over 600,000 participants. In the UK, our aim is to grow in the retail and workplace channels. We had net deposits in the workplace channel in the second half albeit lower than previous quarter due to one large customer moving to another provider. We did have a strong second half of the year from a sales perspective. We expect the benefits of that to appear in net deposits around the middle of the year as there is several months lead time between winning new contracts and the funds arriving. Retail net outflows shows an improvement compared to last year as a result of better retention rates. By investing in front-end portals and service for adviser and customer, we want to increase the momentum in the retail channel.

These investments will take place in the coming 18 months and are expected to lead to an improvement in net deposits over time. Let me now turn to our global asset manager and our growth markets in the Slide Number 5. Our Asset Management business performed exceptionally well in the second half both in terms of net deposits and earnings. Net deposits were up in our global platforms as well as in our strategic partnerships. As a result, 2020 was the ninth consecutive year of positive third-party net deposits. The combined earnings from Global Platforms and Strategic Partnerships increased strongly to EUR111 million for the half year mainly driven by higher performance fees from strong fund performance in our Chinese joint venture IAFMC. In our growth markets; Brazil, China, Spain, and Portugal; sales were down compared with last year.

Bank distribution in Spain and Portugal was impacted by the fallout of the COVID-19 pandemic and sales in China were down from a record high level in the second half of 2019. But despite lower sales, our in-force business continues to grow which resulted in a 22% increase in underlying earnings to EUR45 million. Let's move to Slide Number 6. On Slide 6, I'll take you through the progress we're making in reducing our risk profile and in managing our financial assets for value. As mentioned at the Capital Markets Day, we are working on extending our disclosures to allow you to better track this progress and we'll share more details with you over the course of this year. A key priority for us is to reduce our dependency on financial markets. At the end of 2020, we had already executed a quarter of the US interest rate management plan that we announced at our Capital Markets Day. This was achieved by lengthening the duration of our asset portfolio and we will take further steps in the coming quarters.

For the financial assets in the United States and the Netherlands, we are putting teams in place to continuously look for ways to maximize their value. We are for instance looking to extend our dynamic hedge program for variable annuities to the legacy block. The existing dynamic hedge program for variable annuities with withdrawal benefit, the GMWBs, was highly effective throughout a very volatile year. In each of the quarters in 2020, we achieved a hedge effectiveness of over 95% for the targeted risks. We also continue to make progress on our Long-Term Care book. After successfully completing 90% of the rate increase program initiated in 2016, we launched a new rate increase program which includes the remaining portion of the 2016 program. On a combined basis, Transamerica will be targeting to obtain approvals for rate increases for a value of $300 million over the coming years.

In the meantime, Long-Term Care claims experience developed favorably with an actual to expected ratio of 71% in the second half of the year due to the impact of COVID-19. Matt will go into more details on the exact dynamics there. For our Dutch Life business, our aim is to turn it into a low risk cash generator paying predictable regular dividends. We have taken two important steps to achieve this. Firstly, we have implemented improvements to our internal model as flagged at the Capital Markets Day. This materially dampens the sensitivity to credit spread movements. Secondly, we lowered the factors applied when calculating the loss absorbing capacity of deferred taxes to make it less sensitive to economic variances. We did see however volatility in the ratio as a result of volatility in our separate account businesses with guarantees and we are looking into ways to tame this going forward.

Slide number 7. On Slide 7, I'll summarize the steps we've taken to deliver on the two other key commitments, namely to increase our strategic focus and tightly manage the capital in small, niche, and sub-scale businesses. In the last few months we have not only announced the divestment of Stonebridge and our operations in Central and Eastern Europe, but we have also announced a right-sizing of TLB, we have restructured our businesses in India, and we've decided to cede the funding of GoBear. Our aim is to reallocate capital that we release from these businesses to strategic assets and growth markets, which offer a greater potential for an attractive return on capital and where we are well positioned for growth. An example thereof is the expansion of our joint venture in Spain with Banco Santander, which closed in July. Finally on Slide 8, I would like to spend a minute on our priorities for 2021. Our primary focus is to improve our performance across all of our businesses. That means achieving efficiencies and expense savings while at the same time investing in products and services to our customers in the various core businesses.

We will also continuously look for ways to maximize the value of our financial assets for instance, by implementing long-term care rate increases and dynamically hedging our legacy variable annuity block. We will update you of these management actions in the course of the year. In our Dutch Life business, our mindset is one of active capital management that constantly assesses ways to reduce volatility and accelerate cash flows. Capital released from our financial assets and the businesses outside of our core markets will be redeployed in our most profitable and promising businesses. Obviously this is subject to strict financial criteria in order to create value for our shareholders. We will continue to be focused on maintaining a strong balance sheet. In the near term, we want to keep cash capital at Holding in the upper half of the operating range. We will also reduce leverage by around EUR200 million in 2021 and we want to deliver on our dividend objectives. To summarize, we are fully focused on delivering the plans outlined at our recent Capital Markets Day to turn Aegon into a more enduring high performance company.

With this, I would like to hand over to Matt Rider. Matt?

Matt Rider {BIO 20002664 <GO>}

Thank you, Lard. On the next several pages, I will take you through the highlights of our second half year 2020 results, our capital position. Let me start with IFRS underlying our earnings on Slide 10. In the second half of 2020, our underlying earnings amounted to EUR1.029 billion, an increase of 7% compared to the same period last year. Earnings benefited from lower expenses in all units partly as a result of our program to reduce addressable expenses. Furthermore, we benefited from lower expenses for travel, marketing, and sales activities across the Group due to the restrictions imposed as a result of the COVID-19 pandemic. Earnings in the Americas amounted to EUR556 million and were 6% higher than in the second half of 2019 on a constant currency basis. We have seen EUR91 million better than expected morbidity experience mainly in the closed long-term care book.

This includes setting up an IBNR reserve as we expected some additional claims will be reported once the concerns of our policyholders with respect to nursing care subside. In the Life business, we experienced EUR83 million adverse mortality. This was mainly attributable to COVID-19 as the cause of death. Higher earnings in variable annuities were supported by favorable equity markets, which offset lower revenues in Retirement Plans following from outflows, lower investment margin in fixed annuities, and EUR35 million of one-time items. Underlying earnings in the Netherlands increased by 7% to EUR344 million. Lower expenses in the Netherlands were primarily driven by the change from a defined benefit to a defined contribution plan for our own employees. Higher earnings in the Dutch service businesses more than offset decreases in earnings in non-life and in the bank. In the UK, underlying earnings declined by EUR8 million to EUR62 million.

We saw higher earnings from the platform business from growth in the Workplace channel and lower expenses. These were offset by lower earnings from the run-off of the traditional pension and unit-linked business as well as lower earnings from the protection and distribution businesses due to COVID-19 impacts. Business growth in Spain and Portugal as well as in China helped to increase earnings for the international segment by 10% to EUR81 million. This increase was partly offset by adverse claims experience in our high net worth business TLB. Finally, underlying earnings from Asset Management increased by 41% to EUR111 million. This was driven by the strong performance of Aegon's Chinese asset management joint venture with performance fees net of performance-based compensation contributing EUR56 million. This far more than offset decreased earnings from the Global Platforms.

Let us turn from underlying earnings to net income on the next slide. As you can see on Slide 11, Aegon reported a net loss of EUR147 million in the second half of 2020. This was mainly driven by a EUR1.3 billion loss on fair value items in the Netherlands reversing a gain of a similar size in the first half of 2020. The main driver for this loss was a decrease in the illiquidity premium used for the Liability Adequacy Test, which led to a significant increase of the fair value of the IFRS insurance liabilities. This was partly offset by gains from alternative investments and unhedged risks in the Americas. In the current low interest rate environment, we realized EUR135 million in gains on investments from normal trading activity and as a result of our efforts to lengthen our asset duration. Despite the economic impact from the COVID-19 pandemic, impairments on our bond portfolio remained very low at EUR43 million for the Group.

Other charges include a provision of EUR125 million related to the exposure on one of our reinsurers, Scottish REIT. Its receiver is working out plans for its rehabilitation and we decided to put up a provision given the unclarity around payments to be received from the receiver. Furthermore, we incurred EUR112 million of charges in relation to the merger of two -- of legal entities in the United States. We have successfully merged our largest two US Life carriers, Transamerica Life Insurance Company and Transamerica Premier Life Insurance Company, effective on October 1 of last year. In this context, we have at the same time restructured two captives and merged them both into Transamerica Life Insurance Company. These legal entity mergers benefit our Asset Adequacy Test efficiency, increase diversification between the blocks of business, reduce the interest rate sensitivity of our capital position, and lead to a benefit to normalize the capital generation.

Assumption updates in the Netherlands had an overall positive impact and included an update to our mortality tables leading to a further alignment with Dutch industry practices. This more than offset restructuring and transformation charges and IFRS 17 project expenses. I'm now turning to Slide 12 to go through the developments of cash capital at the Holding. For the full-year 2020, the Holding received gross remittances of EUR827 million. In the second half of the year, all regions contributed to gross remittances of EUR275 million including a quarterly dividend from the Dutch Life entity of EUR25 million received in the fourth quarter. After funding and operating expenses in the Holding, this led to EUR530 million of free cash flows for the year which were used to pay the interim dividend of EUR0.06 per share and to repay $500 million of senior debt in December. After this first deleveraging step, the financial leverage of the Group stands at EUR6 billion.

As announced, we are planning to further reduce leverage by about EUR200 million in 2021, which puts us well on our way towards our gross financial leverage target of EUR5 billion to EUR5.5 billion. Cash capital at the Holding was EUR1.1 billion at the end of the year in the upper half of our operating range. As mentioned at the Capital Markets Day, we expect to manage cash capital at the Holding to the top half of the operating range in the near term considering the current risks in the macro environment, the ongoing restructuring of our business, and our target to reduce leverage. Moving to Slide 13, which shows the capital position of our main units. I'm pleased that the capital ratios of all our main units are above their operating levels. US RBC ratio increased by 25 percentage points following strong normalized capital generation driven by the same factors that positively impacted IFRS underlying earnings in the second half of the year.

Markets also had a positive impact on the RBC ratio mainly from rising equity markets while adverse impacts of rating migration and credit defaults were limited. As a result of the sale of Pyramid complex in October, the US regulated entities paid a dividend to the US Holding which in turn was used to reduce the affiliate notes to a little over $100 million at the end of 2020. Today, the affiliate note balance is zero, which represents a reduction of $1 billion from the half-year mark. We will continue to use the affiliate notes going forward for liquidity management purposes. In the Netherlands, we were able to implement the proposed improvements to our internal model as flagged at the Capital Markets Day. To remind you, this will materially reduce the sensitivity of the Dutch Life solvency ratio to credit spread movements going forward. Sensitivity or a 5 basis point change in the EIOPA VA has for instance reduced from 10 percentage points to 1 percentage point on the ratio.

You can find the full list of updated sensitivities in the appendix of this presentation. Having said that, the Solvency II ratio of the Dutch Life entity fell by 15 percentage points to 159% in the second half of the year as we decided to lower the factor applied when calculating the loss absorbing capacity on deferred taxes from 65% to 45%. Our decision to lower this factor makes the ratio less sensitive to economic variances going forward. We also took into account recent industry-wide guidance on this topic published by the Dutch Central Bank. Furthermore, the decline in the ratio reflects some volatility in the separate account business with guarantees and an increase in required capital as we invested more in corporate credit. This is to move our asset allocation more towards EIOPA's VA reference portfolio and will benefit capital generation in the future. In the UK, our main legal entity Scottish Equitable increased its capital ratio to 156% and it's now above the operating co.

The increase was mainly driven by updated expense assumptions reflecting part of the expense savings initiatives we are implementing. On Slide 14, the changes in the capital positions of the units come together in the Group Solvency II ratio. Overall, the Group Solvency II ratio increased by 1 percentage point to 196%. Next to the developments in our three main units that I just described, there were three elements that impacted this ratio. First, we not only paid the interim 2020 dividend, but have already deducted the proposed final dividend for 2020 which is in line with industry practice. Second, we included Aegon Bank in the calculation of the Group's ratio in accordance with industry-wide guidelines from the Dutch Central Bank. And thirdly, we invested in the expansion of our joint venture with Banco Santander.

This brings me to my final slide on Slide 15 on the proposed final dividend for 2020. We intend to propose a final dividend of EUR0.06 per share for 2020 at the Annual General Meeting in (multiple speakers) our policy is to return free cash flows to our shareholders (multiple speakers). However, we expect near-term growth of capital distributions to shareholders to be muted as we prioritize deleveraging and want to maintain cash capital at the Holding in the upper half of the operating range. Finally, let me remind you that we are going to move back to quarterly reporting as of the first quarter of this year. Lard and I are looking forward to updating you on a more regular basis about the progress of Aegon's transformation. To facilitate the transition, we are planning to publish an updated financial supplement with the quarterly figures for 2020 and additional disclosures on our strategic and financial assets well before the first quarter 2021 results.

With that, I pass it back to you, Lard.

Lard Friese {BIO 17008174 <GO>}

Thank you, Matt. And before I close off, let me reflect on yesterday's announcement that the Supervisory Board will propose to the Annual General Meeting of Stockholders to reappoint Matt as our CFO. I am pleased that he will continue for another term and I really look forward to executing our strategic plans together with him and the rest of the organization. Today's presentation shows that we are progressing well in this respect. We have significantly increased our strategic focus. The teams that we are establishing to manage our financial assets will continuously look for ways to maximize their value and opportunities to release capital, capital that we will reallocate to businesses with better growth opportunities. Our performance improvement program has had a good start and we enter 2021 with momentum. Supported by a reduction of our addressable expenses, we have delivered an increase of 7% in our underlying earnings in the second half of 2020. By actively managing our balance sheet and reducing leverage, we improved our financial strength and reduced the volatility of our capital position. This provides a strong foundation to deliver on our dividend objectives.

I would now like to open the call for your questions. And in the interest of time, I kindly request you to limit yourself to two questions. Operator, please open the Q&A session.

Questions And Answers

Operator

Certainly. (Operator Instructions) We will now take our first question from Farooq Hanif from Credit Suisse. Please go ahead, the line is open.

Q - Farooq Hanif {BIO 4780978 <GO>}

Hi, everybody. Good morning. Thank you very much. Just first question is on the operational capital generation, which is clearly well ahead of consensus. Can you give us some sort of sense of what operational variances are in that number and just whether for example are we likely to see -- I mean the 29 percentage points capital generation in the US, is that a good guide to the normalized capital generation in the business? That's question one. Question two in terms of the modeling change that you've done in the Netherlands to reduce volatility, how does that change your risk appetite and growth appetite? So, is this going to just make it easier for you to re-risk without seeing the volatility in that business? Thank you.

A - Lard Friese {BIO 17008174 <GO>}

Thanks Farooq. Matt, can you please take those?

A - Matt Rider {BIO 20002664 <GO>}

Sure. With respect to the normalized capital generation, really if you look at it half year over half year in -- I think we speak mainly about the US business; first half of the year we had EUR230 million of normalized capital generation, second half we had EUR540 million. So, basically the operational variance here relate mainly to the mortality and morbidity experience. So in the first half of the year, we had serious mortality. In the second half of the year, mortality has been a little bit better but offset by claims. So, I think you really need to normalize this out. One thing to maybe keep in mind normalized capital generation for the second half of the year in total for the Group, this is after holding and funding expenses, was about EUR873 million. If you take away the holding and funding expenses or if you put them back in I should say, that gets you to about EUR1 billion and that's the normalized capital generation before the holding and funding.

I just need to remind you of a couple of things there. For next year and again relative to the Capital Markets Day, we figured that Central Europe and Stonebridge will reduce that number by about EUR100 million. And we also have just a gentle reminder that from next year, we're going to be removing the UFR impact on the Netherlands and that's going to be about EUR200 million. But really just the seasonality in our business reduces that -- let's say that if you wanted to do a run rate based on the second half results, probably reduces it by more than EUR300 million. So you have to take those sort of one-time impacts into account. And it's a -- it is an important question that you have. With respect to the modeling change in the Netherlands. The reason why we did it is to moderate that the massive amount of sensitivity that we had to credit spreads within our Solvency Ratio.

So if you look at those sensitivities in the back of the presentation, for anything that is credit related you will see that those have massively declined. So, it doesn't necessarily help us to re-risk. We will do that on the economic basis as let's say circumstances permit like we did in the second half of year when EUR4 billion moved into corporate credit, but this is going to stabilize the ratio and basically put it in a position where it can pay a normal dividend over time. Now we will aggressively manage the capital position within the Netherlands through additional management actions, but this should stabilize the ratio and sort of calm it down.

Q - Farooq Hanif {BIO 4780978 <GO>}

And just one quick follow-up on the Dutch ratio. It's probably a third question actually, sorry about that. But just in the move to the lower LAC-DT presumably you weren't asked to do this, but you did it because you could. Is that right or I mean what was the driver of the reduction?

A - Matt Rider {BIO 20002664 <GO>}

The driver was us. So what happened was that the Dutch Central Bank two days prior to the Capital Markets Day had issued some guidance that was not anything -- it was very -- it was industry specific, it was nothing that was directly related to us. But what we saw is that they were giving some, let's say, best practice with respect to how you should treat the excess spreads in your calculation and the release of the risk margin. So, we decided -- and also I think importantly is they gave the industry guidance to take into account adverse scenarios when you calculate that number. So, we decided to do it ourselves to get it out of the way and frankly to make the LAC-DT in the future a bit more resilient because again now you're taking into account some adverse scenarios in your calculation so it will make it more resilient for the future.

Q - Farooq Hanif {BIO 4780978 <GO>}

Okay. Thank you very much.

A - Matt Rider {BIO 20002664 <GO>}

Maybe one more important point on that one is that so by reducing the LAC-DT effectively you're increasing the SCR and over time that's a stock and flow type issue. So, we'll get the capital generation.

Q - Farooq Hanif {BIO 4780978 <GO>}

Okay. Good point. Thank you very much.

Operator

Thank you. We will now take our next question from Robin van den Broek from Mediobanca. Please go ahead, the line is open.

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

Yes. Thank you very much. Good morning, gentlemen. My first question is a little bit about the bigger picture. I mean when you came out with your Capital Markets Day when you reset the dividend last summer, I think there were a lot of uncertainties around mortality, macro, equity markets, credit cycles. If I look at your results today, I mean it's clear there's high equity markets and cost savings are already helping and the new stimulus in the US I guess makes sense to expect a better credit cycle on the back of that as well. I'm just wondering how these things could resonate into your expected payout ratios because it seems that over last year you have significantly improved at least the capitalization -- quality of the capitalization in the US. So, I was just thinking about your overall remittance ratio in the plan. I mean you're working towards the 70s level in 2023. Just wondering should we be expecting any upside to that shorter term?

I appreciate that you probably still want to stay cautious and I've seen your reiteration of the muted dividend growth, but I'm just trying to tie the things together. So, that's question one. Second question is on your financial assets and more specifically on TLB. I mean it feels there's a little bit of a change in the narrative in your presentation today where before I think you clearly had the intention to sell it and now it feels like you're more leaning towards just managing it more efficiently. And in connection to that, can you maybe talk a little bit about which assets within financial assets would be more suitable for an actual disposal and which ones are not? I mean for example you talked about maybe doing back book deals in the Netherlands. Maybe some more thinking around those potentials will be very helpful. Thank you.

A - Lard Friese {BIO 17008174 <GO>}

Yes. Hi Robin. Good morning and thank you for your questions. So, let me start by -- I'll just take them one by one. That maybe the easiest way. So, we said at the Capital Markets Day that our objective is to grow our dividends in line with the growth of the free cash flows to a level around EUR0.25 per share over the year 2023. We also said that we want to operate in the beginning of our journey at the higher end of our capital range to allow us financial flexibility to delever the Company and to also have financial flexibility for some management actions that we may want to take around financial assets for the A book and the like. And obviously we also need to bear in mind we are still in a pandemic. We all hope it's behind us soon obviously, but we're still in the pandemic environment so we're also taking that environment into account. So, we have got good momentum. At the moment, we're working hard.

We're having our nose down and we'll keep our nose down to ensure that we focus us fully on the implementation of our granular operating plan that we have to improve the business. And as I said in the Capital Markets Day, look any free cash that comes out over time and that is more than what we need for the fulfillment of our plans has a clear priority, which is that as a priority it goes back to stockholders. But at this point in time, I would say we're of course pleased with the progress that we're making, but it's the start of a journey and we are fully focused at implementing our plans. That's number one. On TLB, we have said at the Capital Markets Day that we focus -- that we make choices and that we focus on three core markets, three growth markets, one global asset manager and that all the other businesses and ventures including TLB in this case are being run tight capital with a bias to exit. Now what we've done is exactly that.

So in the back end of last year, we have stopped the funding of GoBear. We've started to unwind the traditional distribution channel in India. At TLB we've appointed new management, restructuring the cost base to ensure that they run -- that we run them at tight capital and that they focus on products with low capital intensity. So, we're doing exactly with those ventures and assets what we have explained in the Capital Markets Day with a bias to exit over time. Then thirdly, your point around Financial Assets. Financial Assets, we have classified in the US the Financial Assets for especially the VA book with living benefits and guarantees and a long-term care book. And when it comes to the financial assets with the variable annuity book, we have said that we are doing a lot of work, which has commenced and it's well underway, to ensure that we analyze how we potentially expand the dynamic hedge program that we have for the GMWB book to the wider legacy block of VA.

And that is, as Matt I think outlined earlier, for us a very important first step to then subsequently see in what ways we can extract capital and maximize the cash flows by reducing risk, make them less risky, by make them emerging earlier and faster, or by making these cash flows bigger and more beneficial to us. So, we will look of course at internal options, but also if possible we will also be opened for external options there. Then we have the long-term care book, which is the next piece of our Financial Assets in the US. We focus very much on improving the quality of that book. We have seen that our assumptions are tracking actuals well as was I think explained during the presentation. We have -- we are launching a -- have commenced start for approval requests for improving the quality of the business further through rate increases and that is something that we will focus on there.

For our Dutch Financial Assets. I think Matt has just explained how we're prioritizing the stability of the capital turning it into a reliable may I -- forgive me the word, boring capital payer over time and obviously we will actively manage that under our ownership as these long-term cash flows along their long-term liabilities are a nice funding -- internal funding vehicle of course as well. So, that's what we focus on. And with that, I think I've taken all three questions. So, thank you very much, Robin.

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

Thank you.

Operator

Thank you. We will now take our next question from Michael Huttner from Berenberg. Please go ahead, the line is open.

Q - Michael Huttner {BIO 21454754 <GO>}

Fantastic. Thank you so much. Traditionally I always say well done, but these are really good numbers. So I have three questions, but choose which ones you want to answer. The first one is going back to Bermuda. Can you give us -- can you say -- I didn't look for it, sorry -- how much money they made in 2020 and what could be a kind of run rate? The second is on COVID, what should we expect in terms of impact to 2021? You sounded a little bit cautious saying we're still in middle of the pandemic, but I thought that there's positive offsets but I may be wrong. And then the last one is on kind of relating to the Financial Assets. I'm always optimistic you could sell off the US to the A book more quickly or reinsurers or something. Devising interest rates in the US, how beneficial are they to this kind of increased cash return, maybe other options, et cetera? So it's three questions, please choose If you don't want to answer them.

A - Lard Friese {BIO 17008174 <GO>}

Thank you very much, Michael, Matt, think of the TLB question and what's run rate earnings?

A - Matt Rider {BIO 20002664 <GO>}

I think we can cover all three.

A - Lard Friese {BIO 17008174 <GO>}

Okay. Please go ahead.

Q - Michael Huttner {BIO 21454754 <GO>}

Thank you.

A - Matt Rider {BIO 20002664 <GO>}

Maybe on the first -- just for the TLB business. We did EUR49 million before tax in 2020 on about EUR600 million of IFRS equity. With regard to the, let's say, COVID expectations for 2021, we are still quite cautious. We are expecting still to have let's say maybe in the first -- enhanced claims in the first and second quarter. I would say in the first quarter something like $100 million would be something reasonable. That would be based on an assumption of 200,000 total US deaths. So, something in that range. And then the important one also is on defaults and credit migration and we're still expecting something for next year something in the area of $300 million. Even though we've had very low impairments in 2020, we're still expecting that there could be knock-on impacts once we come out of COVID.

So something in the $300 million range with, let's say, commensurate credit migration that you would see come through solvency. Now for the rest of the macro environment, obviously very unclear. You've seen unprecedented levels of government support so far in 2021, which is making the credit losses very small and equity markets are really almost surrealistically high at this point. So, that's why we need to be a little bit cautious with respect to let's say dividend expectations and performance in 2021 because we don't know the knock-on consequences of COVID yet to the financial markets. Your third one was the US VA book as a financial asset. What we need to do here is we need to implemented a dynamic hedging program as Lard had outlined and it's going to take some time to do the full evaluation of what the implications of that are.

But a big thing and let's say our ability to put that dynamic hedging in place and let's say the economics of it are going to be based on the interest rate levels at the time that we would execute that kind of a thing. So right now we have seen -- I think in the first half of the year, we saw the 10-year treasury at 66 basis points. We ended the year at 93 basis points. I think today we're somewhere in the 113 basis points range, something like that. That is helping us. We're getting actually quite a big help in the economic value of these businesses and that helps us to execute on the hedging and again we'll come back likely in the -- at our first half results and give you an update where we stand.

Q - Michael Huttner {BIO 21454754 <GO>}

Lovely. Thank you very very much.

Operator

Thank you. We will now take our next question from Steven Haywood, HSBC. Please go ahead, the line is open.

Q - Steven Haywood {BIO 15743259 <GO>}

Thank you very much. I think you mentioned about the volatility in your separate account in the Dutch and how this is impacting Solvency ratio. Can this volatility be addressed in the future? I assume that the internal model update that have been done don't really address any kind of volatility really from this account. And then my second question sticking with the Dutch business again. There was mention about the remittances also came from the mortgage business in the second half of 2020. I'm just wondering how this aligns with the dividend band from the ECB assuming that the mortgage business has a banking license. Thank you.

A - Matt Rider {BIO 20002664 <GO>}

Let me pick up the first one. So, what we had signaled was if you think about the -- we ended up at 159% on the Dutch Life Solvency ratio and that was probably lower by maybe 10 percentage points than what people have been thinking about. 6 percentage points of that related to the reduction in the LAC-DT, the worst case tax factor for that one. The remaining 4% really came from volatility in that separate account that's LAC with guarantees. And indeed there are some things that we can work from demand standpoint and some things that are going to be difficult to do. But the idea here is that most of that can be dealt with through management actions. That's one of the things that when we say that we are going to have dedicated teams working on the Financial Assets books, this is one area that a dedicated team is going to really be digging into in terms of finding the management actions. With respect to the remittances from the mortgage company, no, this has no impact. We have freedom within the Group to be able to pay dividends and that's why we took I think it was EUR47 million dividend out of the mortgage company in the second half.

Q - Steven Haywood {BIO 15743259 <GO>}

Okay. Thanks very much.

Operator

Thank you. We will now take our next question from Fulin Liang from Morgan Stanley. Please go ahead, the line is open.

Q - Fulin Liang {BIO 21126177 <GO>}

Thank you. Good morning. So, I have three questions. The first one is just a bit of clarification. The $300 million LTC pricing program, is that something new or is it just implementing the remaining pricing and did you say also that kind of you changed your regulatory assumption to reflect this program? So, this is like out because you normally do the assumption review in the second half -- sorry, in the second quarter of the year so this is out cycled stuff. Is that right? So that's the first question. And the second question is also a bit of a clarification. So, the way you implement, you reduced the volatility to the spread movement. If I interpret the whole thing correctly is you bring your portfolio more in line with reference portfolio.

Does that mean actually you lower the allocation to government bonds, increase allocation to credit assets, and probably also slightly lower the allocation to Dutch mortgages? Is that interpretation correct? And if that's the case, what's the impacts to your incremental normalized capital generation because presumably this new portfolio would have higher yields? So, that's the second one. The last one -- sorry, my question is a bit long. The last one is just in terms of the outlook of your remittance from Netherlands given your Solvency is already approaching the kind of 150 level and also we will have a drag from lower UFR, we will have potentially some drag to prepare for the good long term to review changes in maybe two or three years' time. Does that mean that the outlook from the Netherlands remittance will be kind of low in the next three years? Thank you.

A - Lard Friese {BIO 17008174 <GO>}

Matt?

A - Matt Rider {BIO 20002664 <GO>}

Okay. So thanks, Fulin, for your very detailed questions there. So, let me first clarify $300 million in rate reductions. Back in 2016 Transamerica had implemented a rate increase program and we took credit for that for about $1.1 billion in our reserving and premium deficiency reserve testing. Of that $1.1 billion, we have currently executed on that with state regulators $1 billion of that. There is still some outstanding leaving that $100 million stub. So when we say the $300 million, it's effectively we're rolling in those states that had not approved the previous rate increases for $100 million

And then we have an additional rate increase program that we are reflecting in our -- in this case, our premium deficiency reserve testing of $200 million. So, the total between the stub of what was left over from 2016 and what we're now doing is about $300 million. Now that's not an assumption change. This is actually a management action.

And what we do is when we do a management action and we have been very good at getting these things approved in the local state insurance departments, we are able to bake those into our premium deficiency reserve testing or reserving for those kind of things much like we would be able to bake in management actions on expense assumption changes that we do and like we saw in both the Netherlands and in the UK. So, what we're seeing here is with the management actions in place, we're ready to file, we're ready to go, and it's going to take some time to get those and obviously we haircut what we think we can get -- from what we think we can get for putting in the provisions so put it in at a conservative level. Your next question with regard -- was with regard to the changes that we made to our internal model to reduce the volatility of the Dutch Solvency ratio and the important thing here to remember is that these are -- this is really a move within the SCR. It's within the SCR.

So what we're doing is we have -- there is basically a change that we have made which allows let's say the SCR to move more in line with our own asset portfolio. So, it does not require like massive portfolio changes. Now yes, we did invest more in corporate credit opportunistically in the first half of the year EUR4 billion. We might bring down the mortgages just a little bit, but they're not going to be any material impacts in terms of the -- let's say, the capital generation ability of that business other than to the extent that you have a higher SCR, then it's more of a capital release over time. I think that's all.

Q - Fulin Liang {BIO 21126177 <GO>}

Okay. Thank you. The second -- the last question is about outlook of Netherlands because of the solvency...

A - Matt Rider {BIO 20002664 <GO>}

Sorry, apologies. So, we do want to maintain a cautious stance with respect to their regular dividend and we do have to take into account the outlook. So, we are going to have UFR drags for the next three years. The EIOPA review is I think probably the earliest that that then could be even enacted would be 2024. So, that's even -- that's sort of even beyond our own what you would say our planning horizon and what we put out for target. So, that's not much of a big deal for us. And also we've looked at least the EIOPA advice, it looks like it has about a neutral impact on the Dutch Solvency if you looked at it today at today's current interest rate level. So, that's not so much of a concern. But the idea is that Dutch Life business is a financial asset and we are going to run it as such, which means try to get as much capital as we can over time, increase the net present value of the proceeds.

Q - Fulin Liang {BIO 21126177 <GO>}

Got it. Thank you.

Operator

Thank you. We'll now take our next question from Ashik Musaddi from JPMorgan. Please go ahead, your line is open.

Q - Ashik Musaddi {BIO 15847584 <GO>}

Yes. Thank you. Good morning, Lard. Good morning, Matt. I just have couple of questions. First of all, going on your Financial Assets. Now sorry to be a bit pushing on this. I know you have a clear strategy that you want to run those for value with a bias for exit at some point, but at the same time I think what Matt you suggested is that interest rates are going up which are helping the economic value of these assets. So, can you give some clarity as to how long will you wait for interest rates to go up to see more value out of these assets? I mean or would you say that what matters is how much you're getting it today and then -- and that's what you will take a call rather than just keep waiting for interest rate in US to go higher? So, that's the first question. The second one I would ask would be capital generation. Just to get a bit of clarity. If I understood correctly, what you mentioned was EUR800 million was the second half capital generation and we need to take away EUR300 million for the Central Eastern Europe, Stonebridge, and lower UFR impact so that's EUR500 million. Should we like do times two of that and that's what the normalized capital generation is EUR1 billion a normal run rate or am I missing anything on this? Would be great. Thank you.

A - Lard Friese {BIO 17008174 <GO>}

Thanks, Ashik. Matt, you take both.

A - Matt Rider {BIO 20002664 <GO>}

Okay. So on the Financial Assets, are we waiting for interest rates to go up to take action? No, we're simply not. Now we're benefiting from higher interest rates now and clearly the higher interest rates go at the moment that we would put on a dynamic hedge so that would include interest rates, we would get a benefit of higher levels of interest rates. But we are not waiting. The plan here is to implement a dynamic hedging program. We need some time to evaluate the circumstances. But what you're really seeing here is the fact that the economic value of that block really is sensitive to interest rates and we need to know what the implications of that are in order to put the dynamic hedging program in place and then ultimately to do something with the block. And again we're benefiting now from higher rates, but we're not waiting for them to go up. That's not the point.

We're going to management action targets. With respect to normalized capital generation, I would start with that. I mean I'm probably going to ask you to go back to IR and walk you through this in granular detail. But again we did -- for the second half of the year, we did that. We did about EUR870 million of normalized capital generation after holding and funding expenses and you do have to take away the effects of Stonebridge and the CEE which is about EUR100 million, got to take away the UFR impact EUR200 million. There is some seasonality in there so we get much better capital generation in the second half of the year from the US than we did in the first maybe EUR300 million and that gets you I think to more of a normalized number if you could -- if you have (technical difficulty).

Q - Ashik Musaddi {BIO 15847584 <GO>}

Okay. That's great. Thank you.

Operator

Thank you. We will now take our next question from Andrew Baker from Citi. Please go ahead, the line is open.

Q - Andrew Baker {BIO 20402705 <GO>}

Great. Thanks guys and thanks for taking my question. So, just two please. The first one, Matt, on the EUR100 million you mentioned earlier for Q1 mortality. Maybe you just clarify is that what you're saying ex this mortality claims or is that net with the favorable morbidity that you expect? And then just secondly on the VA book. If you were to explore third-party solutions for this, do you see it as a single book so the GMWB and the GMIB --GMDB book or could you potentially look for solutions for those two as separate books? Thank you.

A - Matt Rider {BIO 20002664 <GO>}

So, on the first one. The excess mortality, let's say, in the first quarter would be the gross earnings impact and it only relates to mortality. It would not reflect any, let's say, benefit for morbidity. But we don't know what morbidity is going to do, we're just signaling the fact that that's what we're thinking in terms of excess mortality for COVID. With respect to the VA book, I mean again first step is to dynamically hedge it and second we could look at options. So you could do the whole book, you could do parts of it, slices -- vertical slices frankly, lots of different options there. But again we can take this a little bit in sequential order and worry about the hedging first.

Q - Andrew Baker {BIO 20402705 <GO>}

Sorry, Matt. Just one follow up there. But if you were to look at in slice, why would you need to wait for the dynamic hedge for the GMWB book if you were to look at that separately?

A - Matt Rider {BIO 20002664 <GO>}

I'll give you a quick example. You see the economic value of that book that is changing quite a lot due to levels of interest rates. So, let's say you got into a transaction situation today and you're not dynamically hedged and the interest rates go up 50 basis points or go down 50 basis points, the purchase price would be just whipsawing all over the place. So step one, get it in a position so that an external buyer would be willing to take it on and any external buyer is going to dynamically hedge.

Q - Andrew Baker {BIO 20402705 <GO>}

Right. Thank you.

Operator

Thank you. We will now turn the call back to your host.

A - Jan Willem Weidema {BIO 15133400 <GO>}

Thank you, everyone. This concludes Aegon's second half year 2020 results call. Thank you for your interest and bye.