

Q2 2017 Earnings Call

Company Participants

- Alexander Rijn Wynaendts, Chief Executive Officer, Chairman-Executive & Management Board
- Matthew J. Rider, Chief Financial Officer and Member-Executive Board
- Willem van den Berg, Head-Investor Relations

Other Participants

- Albert Ploegh, Analyst
- Andy Hughes, Analyst
- Arjan van Veen, Analyst
- Ashik Musaddi, Analyst
- Bart Horsten, Analyst
- Benoît Pétrarque, Analyst
- Farooq Hanif, Analyst
- Farquhar C. Murray, Analyst
- Mark David Cathcart, Analyst
- Matthias de Wit, Analyst
- Nadine van der Meulen, Analyst
- Robin van den Broek, Analyst
- Steven Haywood, Analyst
- William Hawkins, Analyst

MANAGEMENT DISCUSSION SECTION

Operator

Good day and welcome to the AEGON Second Quarter 2017 Results Conference Call. Today's conference is being recorded. At this time, I would like to turn the conference over to Mr. Willem van den Berg, AEGON's Head of Investor Relations. Please go ahead, sir.

Willem van den Berg {BIO 15203834 <GO>}

Thank you. Good morning, everyone, and thank you for joining this conference call on AEGON's second quarter 2017 results and special capital update. We would appreciate it if you take a moment to review our disclaimer on forward-looking statements, which you can find at the back of the presentation.

Today's presentation will be longer than normal, but we will leave plenty of time at the end to address your questions. Our CEO, Alex Wynaendts will first cover the second quarter results, followed by CFO, Matt Rider, who will walk you through our capital plans.

I will now hand it over to Alex.

Alexander Rijn Wynaendts {BIO 1821092 <GO>}

Good morning, everyone, and thank you, all, for your continued interest in Aegon and for joining us for today's earnings call. Let me begin by providing you with an overview of the three key items that we'll be discussing today.

First, we have taken significant measures to strengthen the capital position of our Dutch business. These measures include injecting €1 billion of capital from the group before the end of September 2017, selling UMG for €295 million as announced earlier this week, and reaching an agreement with our regulator, Dutch Central Bank, on the methodology for calculating the loss-absorbing capacity of deferred taxes, as a result of which a LAC-DT is set at 75% as of the second quarter of 2017. The combined effect of these actions will bring our Dutch solvency ratio to approximately 175% on a pro forma basis for the second quarter of 2017.

Second is that we've reached an agreement with DNB to amend the conversion methodology used to translate the RBC ratio of our U.S. businesses into the group Solvency II position. This amended methodology results in a 15 percentage point increase in the group Solvency ratio, in addition to a 13 percentage points improvement on a comparable basis; this brings the group's Solvency ratio to 185% at the end of the second quarter.

And third, I am pleased to announce stronger earnings for our second quarter results and our interim dividend of €0.13 for the first half of 2017. This is part of our commitment to return €2.1 billion to shareholders over the period 2016 to 2018.

I would now like to move to slide 3 and take you through our strong operational results for the quarter. I am pleased with the clear improvement in our operating results, with underlying earnings increasing 23% to €535 million, driven by the improved claims experience in the U.S. and the higher fee income resulting from favorable equity markets.

The strong net underlying earnings for the quarter contributed to 160 basis points increase of our group return on equity to 8.4%, underscoring the progress we are making on a 2018 year-end return on equity targets of 10%.

The third area where we generated a strong increase was overall sales, which rose to €3.9 billion. This increase is a strong reflection of our successful strategic shift to fee-based businesses, in particular our UK platform. And on September 21, we will be hosting an analyst deep dive in London to discuss the recent success of our UK platform and to provide you with further insights to our UK product offering and capital position.

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During the second quarter, we announced and completed the divestment of the majority of our U.S. run-off business to Wilton Re. Through this transaction, we have achieved our objective to reduce the amount of capital allocated to run-off businesses by \$1 billion before the end of 2018. The divestment and related management actions are expected to result in a capital lease of approximately \$700 million in total.

Let's now take a closer look at our underlying earnings for the quarter on the next slide. We are continuing to see earnings momentum across all our businesses, with this quarter marking the fourth consecutive quarter of the year-on-year underlying earnings growth. During the second quarter, we saw significantly improved claims experience in both our life and our health businesses in the U.S. This improved experience reflects the benefit of management actions we've taken as part of our five part plan to improve profitability in these businesses.

Furthermore, we also saw an improvement in claims experience in the Dutch disability portfolio, supported by the management actions we have taken. And another positive drive for operating results is the continued growth of our fee-based businesses, which also benefited from favorable equity markets leading to higher fee income. Although, we continue to face headwinds from lower interest rates, the effect was smaller than last year as reflected in a €10 million positive effect year-on-year. And in addition, other mainly consists of expense savings on which I will elaborate further on the next slide.

We continue to make good progress on our group expense reduction program and we are on track to reach our target of €350 million by the end of 2018. So far, we achieved run rate expense reductions of €160 million across the group, of which €130 million from the U.S., €25 million from the Netherlands and the remainder from the holding. We expect further expense reductions in the second half of this year. These savings not only enable us to improve returns, as noticeable in the previous slide, but also allow us to invest in growth.

And I would now like to turn to slide 6, which shows the development of our net income. As you can see, net income was very strong, amounting to €529 million. The significant increase from the second quarter of last year was a result of strong underlying earnings of €535 million while we also saw non-underlying earnings improve.

The loss from fair value items was mainly driven by adverse own credit spread movements in the Netherlands and the U.S., and hedges put in place to protect the capital position, which were partly offset by positive real estate revaluations in the Netherlands.

The realized gains amounted to €111 million in the quarter, and these were primarily the result of the sale of corporate bonds in the Netherlands as part of our derisking initiative to position us for a comprehensive capital plan that Matt will discuss in a few moments. Finally, other income amounted to €291 million, mainly driven by €231 million pre-tax gain related to the divestment of the majority of the runoff business in the U.S. announced earlier this year.

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Whereas the re-insurance transaction itself resulted in a book loss, the overall result also includes a €694 million pre-tax (07:52) release of deferred gains related to the discontinuance of hedge accounting for certain cash flow hedges associated with payout annuity block. Subsequent to closing the transaction on June 28, 2017, as part of our quarterly close process, we concluded to discontinue the hedge accounting treatment for previously closed forward starting swaps that were linked to the assets transferred or sold as part of the divestment.

As a consequence of the discontinuance of hedge accounting treatment, the deferred gains have been recycled from revaluation reserves to other income. In addition, there is expected partial release of the expense reserve of €82 million in the UK, following the closing of the Rothesay Part VII transfer as part of the divestment of UK annuity business.

Let me now turn to our growing deposits and solid sales on the next slide, slide 7. Gross deposits as you can see continued to be strong across all of our businesses, amounting to approximately €35 billion for the quarter. Our UK platform had a very good quarter, with strong institutional sales. In addition, asset management gross deposits increased as a result of higher inflows in both the Netherlands and the U.S.

Overall, we had net inflows from the quarter of €2.3 billion which were mainly driven by high inflows into the Dutch mortgage fund and the UK platform. Our U.S. retirement business this quarter saw fewer retirement plan takeover deposits and we continue to see reduced demand for variable annuities.

The result, we had net outflows for these businesses. In the second half of the year, we expect to continue to see increase in contract discontinuances as the process to migrate existing contracts to Mercer to Transamerica nears completion.

New life sales declined by 8% to €224 million driven by lower term life and indexed universal life sales in the U.S. and lower sales in Europe. Indexed universal life sales were lower than the same quarter last year although they were up compared with last quarter, a reflection of management actions that we have implemented to improve service levels and the launch of new products. Finally, lower sales in Europe were mainly the result of our exit last year from the UK annuity market.

I would now like to hand it over to Matt to update you on our capital position and capital plan. Matt?

Matthew J. Rider {BIO 20002664 <GO>}

Thanks, Alex, and good morning, everyone. I'm on slide 9 of the presentation, and in this section, I'd like to take you through the steps that we have taken to strengthen our capital position. As you can see, these fall under two main categories. First, we have taken a range of management actions to strengthen the Dutch capital position. This will enable management to focus on executing its strategy to grow capital generation and resume dividend payments to the group in 2018.

Second, we also reached an agreement with DNB to revise the way in which the capitalization of our U.S. business is reflected in the group's solvency ratio. The revised conversion methodology for our U.S. business leads to an improved comparability with our European peers and better reflects the capital strength of our U.S. business and increases our group ratio to 185%.

All of these actions have been taken in close cooperation with our regulator. And by removing uncertainty about the solvency ratio of our Dutch business and by significantly improving our overall capital position, we are able to reconfirm our target to return €2.1 billion to shareholders over a three-year period.

Let me now show you how we plan to increase the capitalization level of our Dutch business on the next slide. As promised at our first quarter results conference call, we're today presenting a comprehensive plan to increase the Solvency II ratio of our Dutch business. The plan consists of the sale of UMG, risk profile enhancement at the Dutch level, and a capital injection from the group.

Together, these actions add around 40 percentage points to the Dutch ratio, and as a result the pro forma ratio amounts to 175% as of the second quarter, well within our new target range of 150% to 190%. This allows us to better manage potential uncertainties and take reasonable risks while also consistently paying an attractive dividend to the holding.

Over the last couple of months, we've had extensive discussion with DNB on our plans and have worked very well together to close outstanding methodological matters. One of the key items we agreed on was how to interpret DNB's guidance on the famous LAC-DT. While we will follow an approach in which we complete a quarterly review of LAC-DT level going forward, we can confirm our LAC-DT factor at June 30 at 75%. Nevertheless, I should emphasize that Solvency II will continue to evolve.

EIOPA is expected to review some of the key elements of the regime in 2018 and 2021. This is yet another reason to maintain sufficient capital buffers in our units. Let me now take you through the key steps of our capital plan and the benefits for our Dutch business on the next slide. Increasing the Dutch capital ratio not only enables Aegon the Netherlands to resume dividend payments to the group, it allows it to accelerate the execution of its strategy. The Dutch business intends to pay a dividend over 2017 of €100 million in the first half of 2018, of course, subject to market conditions and regular governance in line with our capital management policy.

Thereafter, Aegon the Netherlands intends to resume a normal pattern of interim and final dividend. The higher capital ratio enables us to make the planned investments to capture opportunities we see in the Dutch market, an important one of which being the market-wide shift from defined benefit to defined contribution pensions.

As part of our strategy, we aim to maximize the value of our back book by optimizing our risk-return profile. To achieve this, we are executing an illiquid investment program of €3

billion to €4 billion over the period 2017 to 2019 to increase the returns of our Dutch business and to improve capital generation going forward.

The illiquid investments are expected to lead to an increasing capital generation of around €50 million per year once it is fully completed. And the next key step in the capital plan is the recently-announced divestment of UMG, which I'll discuss on the next slide.

As announced on Tuesday, the sale of UMG to Aegon increases the capital ratio of the Dutch business and will provide a good home for both our customers and employees. We acquired the business in the early part of the 2000, a very challenging time for independent financial advisors and since then, we have transformed it from a loss maker into a profitable business. It's important that this transaction is seen in both the context of the evolving insurance landscape in the Netherlands and our own strategy to optimize our portfolio. We're very pleased with this divestment for €295 million. This both increases our financial flexibility and enables us to focus on those businesses that are core to our strategy.

As we have discussed with you before, a fundamental element of our strategy is to use retirement products to build a lifelong relationship with our 4 million Dutch pension customers and guide them through their choices and financial decisions they need to make. This is just one example of how we are increasingly transforming into a service provider with a fee-based business model, be it in asset gathering, pensions, or mortgages where we're now a top three provider in the Netherlands.

On December 1, we'll be holding a deep dive for analysts and investors, in which the management team of Aegon in the Netherlands will provide an update on the opportunities for Aegon in the Dutch market.

On the next slide, I'd like to outline the risk profile enhancements, an area in which we've made strong progress in recent months. First, we completed de-risking of the general account to create room for the planned illiquid investments. We'll update the credit shock for non-safe haven sovereigns in the third quarter following approval by DNB. And thirdly, we're on track to implement further actions such as additional credit risk hedging related to separate account liabilities with guarantees.

Taken together, these actions are expected to improve the Dutch solvency ratio by between 5 and 10 percentage points in the remainder of the year.

Finally, I'll show the funding plan for the €1 billion injection into our Dutch unit from the group on the next slide. The largest element of the comprehensive capital plan is a capital injection of €1 billion from the group by the end of the third quarter. Importantly, our solid excess capital position, together with the actions we have taken to increase our financial flexibility, enable us to inject capital without having to issue shares.

During the second quarter, excess capital in the holding increased to €1.7 billion, driven by regular dividends of €400 million from the U.S. and CEE, and a €176 million special dividend from Asia. The special dividend from Asian operations is a result of the ongoing

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capital efficiency program. Going forward, we expect Asia to contribute positively to capital generation.

In the remainder of the year, we expect to receive another €1.3 billion in regular dividends and proceeds from recently announced divestments. This is more than sufficient to also cover our group dividend and holding funding and operating expenses in addition to the capital injection.

We will soon issue €500 million in senior debt to prefund some of the cash flows coming into the holding later this year. This will temporarily increase our leverage ratio, but we still expect to remain within our target range of 26% to 30%. And over time, we are committed to reducing leverage back into the midpoint of our range.

As announced this morning, we have reached an agreement with Athene to sell our business in Ireland. We expect the deal to close in the first quarter of 2018. Therefore, the proceeds of the divestment are not taken into account in the roll forward you see on the slide.

The transaction is in line with our strategic objective to maximize our portfolio, including divesting non-core activities and those that lack sufficient scale.

Let me now turn to our updated capital management policy on the next slide. The decision to operate the Netherlands at a higher level of capital resulted from a fundamental change to our capital management policy. As you can see, we have recalibrated our capital zones to put a greater focus on protecting capital generation and the sustainability of dividends.

At the same time, we want to be able to continue to make optimal risk return tradeoffs even after moderate or economic or other shocks. To achieve this, we have both lifted and widened the target zone to 150% to 190% for the Netherlands. If we would approach the low end of the target zone or even slightly below the target zone, we would no longer be forced to take derisking actions that would have an impact on current and future capital generation.

Instead, we've built in additional buffers which if required would enable us to maintain our risk profile and pay a partial dividend while using capital generation to gradually return to the target zone. The sensitivities that are the key drivers behind the target zones can be seen on the next slide.

Looking at the sensitivities, the key point is that the pro forma capital position of 175% for the Dutch business enables us to absorb market shocks. One of the starting points in setting a new capital management policy for Aegon the Netherlands was that it needed to be able to absorb the expected lowering of the UFR, while also being able to pay a sustained dividend to the group.

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The lowering of the UFR is a tradeoff between the stock and flow of capital. If the ratio would go down, then the recurring capital generation would increase. For other scenarios, such as a decline in interest rates, the ratio and recurring capital generation would both be adversely impacted. We can also confirm that the main Dutch subsidiary Aegon Leven is expected to return to dividend paying status with a solvency ratio of over 160%, meaning that it will be operating at the higher end of its own target range of 145% to 175%.

That brings me to our updated capital generation and dividend expectations for the Netherlands on slide 17. Now there's a lot going on in this slide, so I want to take you through the key points. We expect normalized capital generation of around €300 million going forward for Aegon the Netherlands, excluding the temporary strain from the illiquid investment program and the impact from the step-by-step lowering of the UFR as proposed by EIOPA.

Putting these exceptional items aside, normal capital generation is expected to increase as a result of the uplift from excess spreads due to the illiquid investment program. The increased Dutch capital ratio, together with growing capital generation, will enable Aegon the Netherlands to resume dividend payments to the group.

I would now like to focus briefly on capital for the group as a whole on the next slide. In the second quarter, our group solvency ratio increased significantly from 157% to 185%. On a like-for-like basis, the ratio increased by 13 percentage points as a consequence of three key drivers. First, the majority of the capital release from the U.S. run off deal was realized as a result of the reinsurance agreement and related management actions

Second, the Rothesay Part VII transfer is the first of two final closings on the sale of the UK annuity book. Second transfer related to the Legal & General transaction is expected on the second half 2017, and will further add to the UK solvency position.

Third, total capital generation for the group amounted to approximately €600 million and included a benefit of approximately €300 million from market impacts and management actions. These management actions included the derisking of the Dutch general account, as I discussed earlier, and lower capital requirements for equity risk in the UK, where we have put in place additional hedges to protect fee income.

In addition, the ratio benefited from a change in the conversion methodology for our U.S. business under Solvency II, which I will discuss on the next slides.

As Alex highlighted, following discussions with our regulator, we obtained approval to amend the deduction and aggregation methodology for our U.S. business, which will be reviewed annually. This includes both the lowering of the conversion factor from 250% to 150% of company action level RBC, and own funds by 100% RBC to reflect transferability restrictions.

The updated methodology is therefore more in line with that used by our European peers and this, of course, greatly enhances comparability. As a result of the change in

methodology, our group Solvency II ratio has increased by 15 percentage points. Furthermore, the quality of capital has also improved as reflected by the increase in the relative share of restricted and unrestricted Tier 1 capital.

I'd like to stress that these changes will have no impact on how we manage the capital of our U.S. business. We continue to target an RBC ratio of between 350% and 450%, and normal dividends are still expected to be at a similar level.

This leads me to the updated capital zones for the group and for our main units. As you can see in Europe, we've updated the capital target ranges for both the Netherlands and the UK. In the Americas, the RBC target zone remains the same. The new 150% to 200% target range for the group reflects both the updated target zone for the Netherlands and the UK, and the new conversion methodology for the U.S. All in all, we're at the high end of our target zone at the group level, which means that we are in strong position to return capital to shareholders as planned.

The next slide shows our normalized group capital generation. We expect that our units will generate €1.4 billion of normalized capital in 2018 and that this number will continue to rise over the medium term due to the decisive actions that we have taken and will continue to take to grow capital generation. Examples of such actions include, first, executing the five-part plan in the U.S. including our ambitious \$300 million expense savings program.

We're also transforming our UK business to the number one platform player in the market through the integration of Cofunds and we want to optimize the risk return profile of Aegon the Netherlands by shifting investments to illiquid assets. The expected capital generation is more than sufficient to cover the group funding and operating expenses, as well as our dividends to shareholders.

In summary, over the past few months, we've been fully focused on increasing the capital position of Aegon the Netherlands to enable us to execute our strategy and to improve operating performance.

We've resolved a number of open Solvency II methodological matters with our regulator to remove uncertainty going forward. We have achieved a level of playing field with respect to the way in which our U.S. business enters into our group solvency ratio and we've recalibrated our capital zones to put more focus on the sustainability of capital generation and dividends. We can be pleased that we have been successful on each and every one of these fronts and I'm confident in our ability to return €2.1 billion to shareholders over the period from 2016 to 2018.

Alex and I are now ready to take your questions.

Q&A

Operator

Thank you. And our first question comes from the line of Farooq Hanif, Credit Suisse. Please go ahead.

Q - Farooq Hanif {BIO 4780978 <GO>}

Hi there. Thanks so much for taking my questions. Firstly, could you explain the kind of variability of the LAC-DT methodology that you're suggesting and whether if it's going to be a big impact across the quarter?

And secondly, when you talk about in the Netherlands opportunity for capital deployment above the 190%, what do you mean by that?

And lastly, can you explain the nature of illiquid investments in the Netherlands? Thank you.

A - Matthew J. Rider {BIO 20002664 <GO>}

Yes. Sure, Farooq, maybe first on the volatility of the LAC-DT factor, I think that so first of all, we are going to recalculate the number on a quarterly basis. We actually come up with a number that we could rationalize as even a bit higher than 75%. So, I think that that would be reasonably stable. But again, we have to recalculate it every quarter. With respect to the new capital zones for the Netherlands, the 190% top is basically opportunity to pay additional dividends. And the third question?

A - Alexander Rijn Wynaendts {BIO 1821092 <GO>}

Nature of the illiquid...

A - Matthew J. Rider {BIO 20002664 <GO>}

Nature of the illiquid investments. Yes, probably in three main categories, I would say, continued investment in Dutch mortgages, infrastructure debt, and private lending – direct lending.

Q - Farooq Hanif {BIO 4780978 <GO>}

Thank you very much, that's it.

Operator

The next question comes from the line of Robin van den Broek from Mediobanca. Please go ahead.

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

Yes. Good morning, gentlemen. Thank you for taking my question. Firstly I appreciate the granularity you've given, the capital generation for each business unit. I was just wondering if you could share some more light on remittances per unit because I think slide 17 shows that for 2018, for example, for the Netherlands, you will be eating into your Solvency II ratio if you remit more than €50 million, so yes, from the €300 million, could

you maybe share some light on the remittance ratio expected in the midterm and maybe the same for Americas, United Kingdom, and Asia?

Yes, the - sorry, I was dropping a pause there, but secondly, I was wondering it seems that the capital plan for the Netherlands has triggered you to do a lot more portfolio focus in the last quarter. I was wondering is that going to be an ongoing process and could we expect more or are you basically done with reevaluating your total portfolio?

A - Matthew J. Rider {BIO 20002664 <GO>}

Yes, on your first one remittances from the group, you're correct. So, we would expect to generate approximately €50 million of capital in the Netherlands. We're also absorbing obviously the UFR decrease as well as the increase in required capital for illiquid investments, but we did feel that it was important to fund the Netherlands to support its illiquid asset strategy, and importantly to start to paying dividends as quickly as possible. We also funded it fully, so that it could absorb these changes in the UFR going forward.

So, given where we expect them to sit within the capital management zones that you're in, it should be able to pay €100 million dividend in the first half of 2017 over the 2017 performance year, but they will need to work through their normal governance. After that, if they can execute their strategy and with dividend subject to market circumstances while adhering to their capital management policy, we would expect them to pay a normal pattern of interim and final dividends.

A - Alexander Rijn Wynaendts {BIO 1821092 <GO>}

Let me take the second question, Robin. I think we have been extremely consistent in saying that we're reviewing our portfolio on an ongoing basis. And clearly, you know how long it's taken us to execute on the BOLI/COLI and restructured settlement deal. These portfolio changes that we have recently announced, we were actually pleased that we are able to do them in a way that we are clearly showing that we are not leaving value on the table, we have real focus on achieving the right value. And from a timing point of view, it was clearly fortunate that we were able to announce it just before or even on the day of this important result.

So this process will be ongoing, and I think we've been very clear in saying that we look at all our businesses. And if they don't fit our strategic objectives, we will take action. And also, if we see that we are not able to achieve scale, we will also act on it and we'll continue to do so. And that means an ongoing process.

I also want to remind you that it's not only been about selling activities, we've also acquired pension business in the U.S. with Mercer expanding our franchise. As you know, we have done a significant move in the UK with Cofunds, where we are leveraging our platform and adding customers, and you will continue to see these kind of activities going forward.

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

And so, thank you, maybe coming back on the first question, do you actually expect the €1.4 billion of normalized capital generation to be remitted to the holding or do you expect a lower number in 2018?

A - Matthew J. Rider {BIO 20002664 <GO>}

We have to recognize that the normalized capital generation is more of a longer or, let's say, medium-term thing and that we are having to absorb the UFR impact in 2018 as well as the increase in required capital for the illiquid investments strategy. And that's highlighted in sort of the notes on slide 17.

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

Okay. But you're not willing to give any guidance there?

A - Matthew J. Rider {BIO 20002664 <GO>}

I think slide 17 gives the guidance that we'd like to give.

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

Okay.

Operator

Thank you. Our next question comes from the line Nadine van der Meulen of Morgan Stanley. Please go ahead.

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

Yes. Good morning. Thank you very much for taking my questions. First question I have, the planned €100 million dividends upstream from the Netherlands, why are you doing this if you are at the same time increasing your debt by €500 million? I believe that's a one year facility, whereas you have to pay that back, why not first pay the debt back or raise that (35:25) debt. It sounds a little bit like you're funding one thing with the other.

Then, the second question is perhaps on the new money yield for Aegon versus the back book yield in the U.S., if you could let us know what those are and how is this developed and what your expectation is there? Thank you very much.

A - Matthew J. Rider {BIO 20002664 <GO>}

Thanks, Nadine. Yes, in terms of the €100 million dividend out of the Netherlands, like I said before, we felt that it was important that they start to resume paying dividends and to act like a normal insurance company taking normal risk, paying normal dividend, and this is part of a hygiene factor frankly.

With respect to the €500 million debt issuance, this is more to actually fund the entire amount of capital injection with cash as of September 30, so we don't have to keep talking about Dutch capitalization for the next three quarters. So, we just wipe it

completely off the table. But the €100 million is a hygiene factor and I would stress that that would be evaluated using their normal governance, under normal market circumstances, we would expect it to come, but they have to work through their governance as well.

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

Thank you, that's very clear.

A - Matthew J. Rider {BIO 20002664 <GO>}

I'm sorry. Your second question for new money yields, the new money yields in the U.S. for the second quarter were 3.5%. Now, this is down from 4.35% in the first quarter, but this is a consequence of just adding additional treasuries to manage interest rate risk. The third quarter outlook - I mean just what we're seeing so far is about 4.1%. Book yields are down about 0.1% down to 4.6% as a consequence of COLI/BOLI and payout annuity transaction.

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

Thank you very much.

Operator

Our next question comes from the line of William Hawkins of KBW. Please go ahead.

Q - William Hawkins {BIO 1822411 <GO>}

Hello, gentlemen. Thank you very much. Appreciate the hard work you guys have done year-to-date. Could you help me a bit with slide 21? The capital generation outlook, you've given 2018 normalized, could you just help us be clear about what is the expected in 2018 relative to the €1.4 billion, because you've been very clear that the €300 million for the Netherlands could be €50 million (37:53) because of the issues you talked about. I'm just trying to get clear for the UK and the Americas, can we hang our hats on those normalized being the same as expected, should we make similar adjustments?

And then secondly, that €1.4 billion by 2020, to pick a number, you've been very clear that the figure should grow, you've been clear that the Netherlands could be at €325 million. Could you try and give us an indication of the growth potential in the other areas? I mean, you threw out for example \$300 million of cost saving mostly in Americas, but I'd be surprised if you wanted to add that to the €850 million. So, if you could just give us an indication of how that figure could grow, that would be helpful. Thank you.

A - Matthew J. Rider {BIO 20002664 <GO>}

Thank you, William. So, I think you have it exactly right. So, we have €1.4 billion in normalized capital generation and in terms of expected capital generation, (38:46) for the UFR change, as well as the additional required capital for the illiquid assets in the Netherlands and then you come to what our expectation is. Of course, and you see it every quarter, there's going to be market movements. But that's basically the capital generation going forward.

Q - William Hawkins {BIO 1822411 <GO>}

So (39:05) want to adjust?

A - Alexander Rijn Wynaendts {BIO 1821092 <GO>}

No. Let me add on your second point, Will, that in the U.S., yes, you are right to identify cost savings that will have a positive effect on the cash flows. I also would like to remind the growth, we are growing our fee-based businesses in the U.S.,

and that means that we are effectively moving towards more capital light business that should also support cash flows.

In the UK, we have the integration of Cofunds. That is going to be a significant boost. And what you see there is that, not only we're growing our business but we're also having very good retention actually on the Cofunds funds, better retention than we originally thought. And I am also pleased to mention here that the Asia capital generation, as you will have noticed, has had a significant turn into positive. By looking at the management actions we could take on the balance sheet of, in particular, our high network business to Bermuda and Hong Kong and Singapore business, and by also taking actions on the way we price and the way we design our products in that area, that has turned into effectively saying that we're moving from a negative capital generation to positive capital generation, and that is going to continue going forward.

Furthermore, I've been clear in the previous question that we continue to look at those businesses that meet our requirements. And we have a number of businesses that have had negative capital generation, one of them we announced to sell this morning. And all of that should - by stopping the negatives, that will also lead to a positive on the - from the €1.4 billion. I'm not going to give you exact numbers, but I think all these elements should give you more than enough comfort.

Q - William Hawkins {BIO 1822411 <GO>}

Thanks, gentlemen. Thank you.

Operator

Thank you. Our next question comes from the line of Ashik Musaddi of JPMorgan. Please go ahead.

Q - Ashik Musaddi {BIO 15847584 <GO>}

Yeah. Hi. Good morning everyone. This is Ashik Musaddi. Just two to three questions. First of all, Alex, as you flagged about Asia, your capital generation which was negative is now kind of zero, I mean all positive. So first of all, what is driving that? Is it your - the way you're thinking about that Business, i.e. let's not invest and waste money in Asia, or is this some structural change that is happening which is improving the capital generation? The reason why I'm asking this is, I mean, if I look at your earnings profile from Asia, it's around €25 million, which is like 1% of the group. And if you're not injecting any capital in Asia,

probably is it worth really thinking about that business from a disposal perspective because, as you always mention, that if it's not scale, it's not for you. So, how should we think about your Asian operations?

The second thing is your capital generation in UK is going up pretty much, €25 million to €100 million. Now, that's again a big number for a platform business. So, how should we think about that capital generation? How much of that is earnings-related? How much of that is capital release-related? So, how much do you have confidence in that €100 million?

And thirdly is, is your updated numbers adjusted for the recent currency moves, which is the euro has moved quite a bit towards the U.S. dollar, et cetera. So, any thoughts on that would be really helpful. And thank you, thanks for all the hard work you've done over the past six months, thank you.

A - Alexander Rijn Wynaendts {BIO 1821092 <GO>}

Thank you for asking the question on Asia. I think we have taken quite a number of steps in Asia. First of all, we announced last year that we have put our affinity business in runoff. Now, putting our affinity business in runoff effectively meant that we went from a capital utilizer to a capital generator, and it's quite a pattern of runoff in our annuity business in Asia.

We've come to the conclusion in line, by the way, with the decisions we've taken in the U.S., in the UK, that the affinity business is not a business we believe we want to be in for the long term. We do not believe that's strategically important for us nor is it really attractive from a customer value for our customers. So, that's step one. The big change is really on our High Net Worth individual business, the Bermuda business, is we have seen that by taking a number of actions, ALM driven, redesigning our products, we have been able actually to free up capital and I think we shared that with you in the previous quarter, and that has been translated in the dividend of \$200 million.

We also continue to grow our business, so we've maintained more than enough capital in that business to fund itself the growth of the business. So, when you look at the business in Asia, you should be looking at a number of specific businesses that we actually see growing successfully and the High Net Worth individual business is growing successfully and is well funded to effectively fund its own growth. But because of the changes we've made, we need less capital.

In the UK, yes, you point to the significant improvement. We have been very clear about the steps that we are taking and taking out the expenses after the Cofunds acquisition will lead to a structural improvement of our cash flows to over £100 million. And I actually believe that, with the markets being positive, the growth which we're seeing, retention levels in our Cofunds business that are actually better than we could have expected, that actually - that number can still fairly grow.

Now to think about it, for a platform business, cash flows actually are very similar to net earnings. I do not have any more like a run off book debt is running off capital, and therefore, you could really say the two are the same. Also, I want to point here is that not

only we're improving our cash flows, but we are also compensating the fact that we have lost €25 million of cash flows related to the annuity book which we have disposed.

And finally on the U.S. dollar, as you know, we have I think a very clear and a consistent strategy. We match our assets and liabilities in each of the countries we operate, so assets and liabilities in the U.S. are matched, assets and liabilities in the UK are matched, and same in other countries, and we leave the translation risk from a currency point of view effectively open. So the earnings are in the translated up the rate that is the rate of the market, but it is only a translation risk of earnings and the repeat here, from balance sheet point of view, our assets and liabilities are well matched currency by currency.

Q - Ashik Musaddi {BIO 15847584 <GO>}

That's very clear. Thank you.

Operator

Thank you. Our next question comes from the line of Mark Cathcart of Jefferies. Please go ahead.

Q - Mark David Cathcart {BIO 19783252 <GO>}

Hello. Taking Aegon hygiene to new levels, do you think there's an argument that Aegon continues to restructure but at a much more significant level? In other words, you go on longer lines of (46:13) might do with some sort of U.S. quote. I guess my question is, given the outcome at the holding company over the past few years, what is it that you do for the U.S. operations that they couldn't actually do for themselves? I'm just trying to work out what is the advantage to the European shareholder of having the majority of dividends coming through in dollars? I just wondered what your thoughts are on that, please.

A - Alexander Rijn Wynaendts {BIO 1821092 <GO>}

Mark, first of all, I appreciate you recognize the hard work, which we have been doing in restructuring the company. And as you know, this has taken some time, we have to take into account market conditions, we have to ensure that we look for companies or parties that take over our businesses that we believe are better fitting somewhere else. We need to ensure our customers and our employees really very important find a new home and I think we have been able to find quite significant new homes for these companies.

The second thing you're asking me is more explicitly about the U.S. I can only remind you that U.S. is a significant part of our business. It has been a key contributor, as you point out, to the success of Aegon and I really expect this to be the case for the future.

Q - Mark David Cathcart {BIO 19783252 <GO>}

So you don't think that there's an argument for more efficient shareholder structure for Aegon with a separate U.S. quote? You don't believe in that argument at all?

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A - Alexander Rijn Wynaendts {BIO 1821092 <GO>}

I am just repeating what I said - I am just repeating that the U.S. is a significant part of our business, key contributor in dividends and cash flows. But I also would like to say that with the steps we have now been taking, Aegon in Netherlands will be, and again, a normal contributor of dividends. The UK will be a contributor and as you all just have heard, even we have had a significant dividend from the Asia. So, it is important that we indeed have a balanced portfolio of which the U.S. because of the nature of the market and our presence will continue to remain an important part.

Q - Mark David Cathcart {BIO 19783252 <GO>}

Yes. So my second question, you mentioned about the balanced portfolio. Your aim when you first became CEO was to have 50% of earnings actually coming from outside of the U.S. You didn't particularly like the dependency on the U.S. What has changed since for you not to be pushing for less dependency on the U.S.? I mean, do you think that's efficient for the shareholder to have 70% or even 90% of the dividend stream in U.S. dollars?

A - Alexander Rijn Wynaendts {BIO 1821092 <GO>}

As I just said and mentioned, and Matt also explained, going forward there will be much better balance from where we're going to get our dividends. I mentioned the Netherlands will be paying a dividend going forward. The UK had paid a dividend in Asia, so the balance actually has improved. And what is important for us is to have a company that is well-balanced, but also to recognize that the U.S. is today, and will continue to remain, the largest market in the world and we are very pleased with the very strong presence we have in the UK, and the U.S., and the fact that they performed very well.

Q - Mark David Cathcart {BIO 19783252 <GO>}

So, my third question is you can say categorically that you're not considering in any shape or form a potential U.S. quote for your U.S. business?

A - Alexander Rijn Wynaendts {BIO 1821092 <GO>}

Mark, I don't think I need to repeat my answer. Thank you.

Q - Mark David Cathcart {BIO 19783252 <GO>}

Thank you. Thank you.

Operator

Thank you. Our next question comes from the line of Andy Hughes of Macquarie. Please go ahead.

Q - Andy Hughes {BIO 15036395 <GO>}

Hi, guys. A couple of questions if I could. The first one is on the cost savings. So, just to be clear that I can understand how much of the cost savings are in the 2018 numbers and

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how much is kind of still to come through in terms of maybe on top of that, especially in the Netherlands, because I remember you have the risk margin effect on the expense inflation coming through. So, I thought any kind of cost savings you put in the Netherlands would be material for the capital generation.

I just want to check your comments on the Americas cash generation where you're saying cash generation in the Americas not really going to be from runoff businesses, it's going to be from organic and growing businesses. Are you, kind of, saying that the €850 million from the Americas you expect to grow over time, as the fee businesses grow, or is there kind of two books in there, one that's running off, and one that's growing? Thanks.

A - Matthew J. Rider {BIO 20002664 <GO>}

So, on the first one, on the cost savings especially in the Netherlands, we'd expect the run rate savings to come through by the end of 2018. With respect to cash generation, I think this has been really a highlight of the Americas business. I mean, to see so much of it coming from businesses that we're currently active in, rather than run-off businesses, I think is an extremely healthy thing. And as long as we continue to grow our presence in fee-based businesses, capital light businesses, and those types of things, I think that we could grow that capital generation modestly in the future. Definitely, the cost savings that you mentioned earlier are contributing to cash flows in 2018 now.

Q - Andy Hughes {BIO 15036395 <GO>}

Okay. And another one-off benefit that came through thereafter like for something in Netherlands, you might have a capitalization effect in that year, and then they drop off. And can I just ask a question about the Americas, how much is - of the €850 million, how much is roughly run-off and how much is ongoing? Is most of it ongoing and growing, or is it sort of into the relative mix, please? Thanks.

A - Matthew J. Rider {BIO 20002664 <GO>}

Yes, I mean very little of it is from closed blocks. I mean the COLI/BOLI payout annuity transaction that we did raised something on the order of €14 billion of liabilities and there was some capital generation that was coming through on that one. But for the vast majority now, it's just part of the normal operations, open businesses, ones that we're currently active in. So I think that one is actually pretty encouraging.

Q - Andy Hughes {BIO 15036395 <GO>}

Yes. And just a quick question on Netherlands, I forgot to ask actually, the €100 million liquidity (52:27) asset strain, that's quite a lot of money. Roughly, how much illiquid assets does that equate to and what kind of return on capital do you get on the €100 million because I'm guessing it must be quite a lot of illiquid assets that you're buying or quite a high yield because otherwise you wouldn't bother and you'd just run it for cash in the short term. Could you just clarify what exactly...

A - Matthew J. Rider {BIO 20002664 <GO>}

Yes, certainly. It's a giant balance sheet, so when you want to make portfolio restructurings, they have to be in magnitude. So the illiquid strategy is going to be on the order of €3 billion to €4 billion over the next couple of years. But in terms of, let's say a return on capital, we think this is a pretty good tradeoff. We would expect something on the order of perhaps even 15%, something like that. So, it's actually, this is one that's a good trade-off.

Q - Andy Hughes {BIO 15036395 <GO>}

Thank you very much.

Operator

Thank you. Our next question comes from the line of Steven Haywood of HSBC. Please go ahead. Your line is open.

Q - Steven Haywood {BIO 15743259 <GO>}

Good morning. Just following-up on that, the illiquid investments, you say it leads to €50 million increase in your capital generation. I assume that's already in your normalized capital generation plan. So, without this investment, illiquid investments, the Dutch business would have been a zero capital generative business in the next couple of years. And then, if you look at the group normalized business capital generation for the next couple of years, that comes down to around €850 million. So, that is just covering your dividend and your holding company expenses for the next couple of years, what additional flexibility do you have over the next couple of years with your cash roll forward here?

And then, secondly, on your Dutch dividends, you say you're going to resume a normal pattern of interim and final dividend in the Netherlands. Considering the last few years have been not really normal, what would a normal level of dividend be and what is the normal pattern? Please can you go into more detail here?

And then, finally I think you mentioned that you said that Aegon Leven, the Dutch life business has a target range of 145% to 175%. Can you confirm this or did I get this from (54:52)? Thank you very much.

A - Matthew J. Rider {BIO 20002664 <GO>}

So, maybe I'll take the last one first. So, I can confirm the 145% to 175% and I think you didn't take it out of scenario I remarked out it in the presentation. So, maybe on the illiquid investments, yes, we expect that the illiquid investments will return about €50 million in additional capital or in capital generation over the coming years. But it's important to reflect that the capital generation in 2018 and 2019 also reflects the fact that we're having to put up additional capital for them.

So, you can't really say, if we didn't do the illiquids, then there would be zero. If we didn't do the illiquids, we wouldn't have the strain either. So, I think you have to take that into account.

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In terms of the group normalized capital generation, I think that importantly here, we wanted over the next several years to grow the Netherlands to a point where it could remit reasonably significant dividends. And yes, you're absolutely right that there has been, over the past several years, it's been a pattern of non-normal market circumstances and whatsoever. But that's exactly the reason why we increased the target level of capitalization so that we could absorb some of these shocks while continuing to pay a normal dividend. And that is a critical element to the new capital management policy.

We want to capitalize them at a level where they can continue to pay dividends in normal market circumstances. And even when there are shocks, we don't force them to derisk in order to increase their capitalization. Putting them at a higher flying level is critically important to this strategy.

Q - Steven Haywood {BIO 15743259 <GO>}

Okay. Thanks very much.

Operator

Thank you. Our next question comes from the line of Bart Horsten, Kempen & Company. Please go ahead.

Q - Bart Horsten {BIO 2390919 <GO>}

Yes, good morning. Thank you for taking my questions as well. I have a follow-up question on capital generation in the Netherlands. Just if I understand it correctly, in the table on slide 17, you deduct €150 million for the lowering of UFR by 15 basis points. Do I understand it correctly that if you would deduct this - take the impact of the UFR lowering through your Solvency II ratio, your capital generation would then increase by €150 million, or am I misunderstanding something, and what would then happen if the actual UFR would go down to the 3.7 (57:27) target?

My second question is on your capital return strategy. You said that in the period 2016 to 2018, you will return €2.1 billion and that you're on track. With your revised outlook on free capital generation and free cash flow generation, is it fair to assume that beyond that you will also expect to increase that capital return target?

And lastly, coming back on the reinvestment yields, you reported quite a significant drop, and if I translate that and I thought you earlier said you have reinvestment portfolio of around \$6 billion annually, that could impact your free cash flow from the U.S. by approximately €50 million to €100 million on an annual basis. Is that already included in your forecasted free capital generation going forward? Thank you.

A - Matthew J. Rider {BIO 20002664 <GO>}

So, on the UFR, you have it correct in that the 15 basis-point reduction in each year as we go down to €365 million is the €150 million reduction in cash flow generation. If we went all the way down to €365 million initially, it would have an impact of - it's basically linear

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take three to four times of €150 million, and that would be the impact immediately on capital. But, if you went immediately down to €365 million, it doesn't mean that cash flow generation goes up by €150 million a year. It's actually spread out over a longer period of time than that.

So, I think it's important that, as you start to think about - the way that, let's say the way that we defined normalized capital generation, it's important that you should haircut one or the other, either capital generation or the normalized free cash flow. So, only do it one time, reduce it by €150 million for the UFR decrease and by €100 million for the illiquid stream.

Q - Bart Horsten {BIO 2390919 <GO>}

Okay. Thank you.

A - Alexander Rijn Wynaendts {BIO 1821092 <GO>}

And I'll take your question on the €2.1 billion by 2018. Appreciate your question, what we'll do after 2018 and obviously you have the right to ask that based on the outlook which we're providing. But I really want to say here, let's first deliver on 2018. It's a commitment we want to deliver on, we'll see thereafter.

A - Matthew J. Rider {BIO 20002664 <GO>}

And then your last one, with respect to the reinvestment yield, I think this was a bit of an odd quarter. I mean, really it was a quarter marked by significant investments in U.S. treasuries to manage more interest rate or interest rate risk going forward. But we're already seeing new money yields for the third quarter up to 4.1%. So, this is not a material thing. This is just the normal course of business, managing a portfolio prudently and making sure that we have interest rate risk managed well.

Q - Bart Horsten {BIO 2390919 <GO>}

Okay. Thanks very much.

Operator

Thank you. Our next question comes from the line of Matthias de Wit of KBC Securities. Please go ahead.

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

Yes. Good morning and thanks for taking my questions. Just on the Dutch capital generation, you were previously guiding for €200 million to €250 million. You raised this to €300 million for 2018. Just wonder what's driving that €50 million to €100 million increase in 2018. I understand that the derisking will help, but presumably not immediately, so any additional color would be helpful in that respect.

And then, just secondly on the Dutch business, the capital generation as well on the amortization of that UFR benefits, it's a large negative component of €200 million. I guess

it will go down firstly because of the cut in the UFR, but secondly because of the amortization of that benefit over time because I guess you do not write that much new business subject to the UFR. So, could you say anything on how you would expect that to evolve in years ahead, please? Thank you.

A - Matthew J. Rider {BIO 20002664 <GO>}

On the first one, with respect to the Dutch capital generation, yes, we had previously guided for a lower number, but I would say there are quite a number of moving parts here. So, on one side, we've sold UMG that had a small amount of capital generation, that gets deducted off. We fine-tuned a lot of our thinking around capital generation.

You can imagine as we've gone through this portfolio rebalancing, we've taken a sharper pen to the way that we analyze the stuff. But importantly, the illiquid strategy has that - an amount of capital generation going forward. So, this is a bit resetting the bar in line with a new portfolio and so you can take our guidance as read here.

With respect to the amortization of the UFR, I think maybe just on one point, we have a normal UFR amortization and it's about €200 million a year, and then we have the special one-off €150 million for the coming, let's say, three to four years, and it's - when the UFR goes down, it means that ultimately capital generation will go up. But maybe detailed questions on this when you could refer to IR.

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

Yes, okay. That would be helpful. If I could just follow up the results in that Dutch capital generation and SCR release on a regular basis of €100 million, is that expected to continue for many years or is that just linked to individual life run-off which will maybe continue for a few more years and then wear off? Anything you can say on that?

A - Matthew J. Rider {BIO 20002664 <GO>}

Just that it would be continuing to come off in the sort of medium term.

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

Okay. Thank you.

Operator

Our next question comes from the line of Albert Ploegh from ING. Please go ahead. Your line is open.

Q - Albert Ploegh {BIO 3151309 <GO>}

Yes. Good morning, all. Thank you also for taking my questions. The first question I have is, given the disposal so far done and all the other management actions as well, can you help us also a little bit on the underlying earnings before tax for what is more or less the normalized impacts from all of these actions?

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And the second question, I still have - I'm sorry to come back to that slide 17 again on the capital generation and I've taken notes of your remark on the flow and stock and not to penalize you twice for the UFR, et cetera. But I would like to understand a little bit better your thinking between let's say the UFR drag and let's say the target range of the 150% to 190%. So, if I look at let's say the flow on the chart, the €50 million probably for 2018 and 2019 at that same kind of level, if I'm not correct your stock for the UFR as well. But that still means, if you're going to pay out let's say a meaningful dividend, you're Solvency II ratio in the end will go down.

So, let's say if we're three years from here in 2020, with the UFR at 3.65%, Yes, are you then basically still wanting to be in the middle of the target range or is then happy to be operating at the low end of that 150% to 190% range to understand that a bit better. Thank you.

A - Matthew J. Rider {BIO 20002664 <GO>}

Albert, thank you for your questions. I think maybe on the first one, with respect to the earnings before tax, UMG was contributing about €20 million and Ireland was effectively nil. So this is not -- these are not material things for the underlying earnings.

With respect to the Dutch capital, yes so in terms of our - in terms of the way that we think about the capital generation capability going forward, we do of course factor in what the, let's say, the normal UFR drag is going to be and then we're also taking into account, let's say, the special nature of the reduction in the UFR in the coming three years.

Now as we take a look at it going forward and again under kind of current market circumstances, and this is quite an important one, we would expect that the Netherlands could pay a normal dividend and stay within its target zone. That's in effect why we've capitalized them at this particular level. But markets can change a course and they will evaluate dividend payment by dividend payment, their ability to do so based on everything that they see in their balance sheet and the markets, and in accordance with their capital management policy.

Q - Albert Ploegh {BIO 3151309 <GO>}

Okay. Thank you.

Operator

Thank you. Our next question comes from the line of Farquhar Murray from Autonomous. Please go ahead.

Q - Farquhar C. Murray {BIO 15345435 <GO>}

Good morning, gentlemen, and congratulations. It must have been a lot of work. And a couple of questions, if I may. Firstly on capital generation, I think I'll have to come back to slide 21 and on the U.S., could you just explain how the \$1 billion from the U.S. is unchanged given that you've done disposals over the period, and that presumably in the background,

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the fixed annuity book has been running off for a quite long period of time, which I presume would it be supporting cash as well.

And then, on the Netherlands, I know you kind of suggest that you just fine-tuned the numbers. But, as far as I can see, we've gone from €225 million to €300 million. And I think it would be legitimate to get just a little bit more detail on what's driving that, and in particular, how much of the \$50 million from the illiquid investment strategy is phasing through there?

And then, also on the Netherlands, you mentioned a kind of risk profile enhancement, which seems to involve some hedging. Is the cost of that hedging also being factored into the €300 million, just a point of detail.

And then secondly, on leverage, the 29.4% is unlikely to change near-term given you are now refinancing the senior. That keeps you kind of relatively high within the leverage target, which I presume is unchanged at 26% to 30%. Is there a timeframe on which you'd like to get deeper into that target range given that or certainly on most other capital metrics, now you are extreme - really quite comfortable? Thanks.

A - Alexander Rijn Wynaendts {BIO 1821092 <GO>}

I could you say maybe quickly on the first one, Farquhar, the €1 billion is a number that included a very small element from BOLI/COLI. I think we shared with you \$30 million impact. In the meantime, of course a lot of (1:08:24) are being taken in cost, which more than offset the decline. So, the difference is more a difference related to the currency when you translate it back into euros.

Matt, would you like to?

A - Matthew J. Rider {BIO 20002664 <GO>}

Yes. So maybe on the Netherlands capital generation again, I think you have it exactly right. So, let's say that the illiquid strategy will add €50 million, and the rest of it is frankly properly recognizing the way that the runoff or let's say the back book is running off together with other modeling improvements that have allowed us to be able to track this a bit more closely. So that - I think that's all I can really say on that one.

You have mentioned the cost of hedging, is that factored in? Yes, absolutely, that is factored in.

And with respect to leverage, I think as Alex had said in his presentation, we'll continue to work that leverage number down over time. But even with this - so we'll refinance the senior. But also we're going to be issuing €500 million to be able to satisfy our obligation and inject capital into Aegon Leven. But that's going to be only one - it's going to be only one year senior and would expect to still remain below our - the top end of our range of 30%. But I would expect to work that down over time.

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Q - Farquhar C. Murray {BIO 15345435 <GO>}

Just a quick question then on Dutch number actually. I mean, are you saying the full €50 million per annum is effectively in there for 2018 then? And why is it coming through so quickly, particularly given that you seem to be then suggesting the strain of €100 million per annum for the next three years?

A - Matthew J. Rider {BIO 20002664 <GO>}

Let's say that the €50 million is not in there for all of 2018. And the reason is that it does take time to put these assets on our books. So it's really after we have the assets in place that will improve the capital generation. But importantly, there is a strain for the illiquid assets program in 2018 and 2019. And of course these are rounded numbers. So, yeah, I'll just leave it there.

Q - Farquhar C. Murray {BIO 15345435 <GO>}

But then if there is only a small contribution in 2018 from the illiquid asset program, again, where is the bulk of the €75 million coming from?

A - Matthew J. Rider {BIO 20002664 <GO>}

I'm not sure I understand the question well.

Q - Farquhar C. Murray {BIO 15345435 <GO>}

Well, we go from €225 million to €300 million, so it's a €75 million increase. Let's say the €50 million is phased in over three years, so that's a relatively small number. It's more than say €20 million -- €50 million coming through from somewhere else in 2018 and it's just a question of where is that coming from?

A - Matthew J. Rider {BIO 20002664 <GO>}

Yes. I think we can give you more detail on this later. But it's really a bit of a methodology change and there is -- we've got more insight and more granularity into our projection of cash flows going forward. But I think we can provide you more detail offline.

Q - Farquhar C. Murray {BIO 15345435 <GO>}

Okay. Thanks very much.

Operator

Our next question comes from the line of Arjan van Veen of UBS. Please go ahead. Your line is open.

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

Thank you. Couple of questions if I may. Can I ask one more follow-up question, apologies, this in on the Netherlands, the guidance you give around capital generation. So, the €325 million in 2020, if I understand your answer right now includes the €50 million

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fully for illiquid assets. My question is the reduction to the UFR down to 3.65%, which obviously has - you indicated what the drag is as you move down. But now you said then the future cash flow (01:12:08) will go up, so my question is the €325 million, does that include the benefit of the reduced UFR because obviously you drag in the future post that date is going to be lower?

And then secondly, just to reiterate, you've done a lot in a very short space of time. And I'm impressed with what you've done in terms of filling that hole in the Netherlands and fixing the balance sheet. A lot of issues obviously could have been done earlier as well, and maybe some more, as you indicated before, things you can do in the future to improve it further.

When I look and read, the same thing with the guidance, with some of your assumptions, you still tend to be a little bit on the aggressive side. You assume interest rates going up. You assume equity market returns of 7% to 8%. You're showing capital generation that hasn't yet materialized. So, I'm just curious in terms of going forward, will you look to continue doing this and then try and move to some guidance number that's kind of more stable over time because now in the space of 12 months we've seen your cap gen numbers change 3 or 4 times.

So, ideally, obviously, I don't want to take away from the positive things you've done, but I just want to - how you think about going forward and try to get to a status quo that is more sustainable, is more stable over time and that you don't - you can sort of hit every period and get that confidence in that. Probably, it's for a long answer, but hopefully that's clear.

A - Matthew J. Rider {BIO 20002664 <GO>}

So, with respect to the first one on the guidance for the capital generation in the Netherlands, you talk about 2020, yes, the €325 million does include the contribution from the illiquid assets. And at that point in time, of course, the additional strain from putting those assets on the books is gone and that's why it all comes through in that. That's included.

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

So, the question was specifically on the €325 million, does it include the lower UFR, because they were issuing that therefore the drag of UFR haven't gone down to 3.65%?

A - Matthew J. Rider {BIO 20002664 <GO>}

Yes. That was your second one. So, yes.

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

Sorry, yes.

A - Matthew J. Rider {BIO 20002664 <GO>}

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No. No. That's all right. Yes, it does include that one. So, that's fully baked in. And in terms of – and by the way, thank you. We have done quite a few changes to the balance sheet. We do make assumptions going forward on interest rates and on equity market movements fully in line with peers. But I'd like to think that we can get into a little bit more stable period.

And frankly, we refine our techniques for being able to estimate this stuff going forward, especially in a Solvency II environment that – we always have to remember, it's a principles-based framework and we're still trying to, and I think the industry as well as regulators are still trying to work out the exact application of this stuff.

So, we have to work through this, but it's actually quite comforting that we've been able to close a lot of these methodological issues with DNB, not to say that there couldn't be more. We have EIOPA reviews coming in 2018 and 2020. So, there will be bumps in the road.

But I would like to get into a position where our capital generation can become a little bit more stable and we can communicate that more effectively, of course. But, we need to get into a pattern of, let's say, under-promising and over-delivering.

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

Yeah. Okay, great. Thanks, Matt.

Operator

Thank you. And we will now take our final question from Benoît Pétrarque of Kepler Cheuvreux. Please go ahead. Your line is open.

Q - Benoît Pétrarque

Yes. Good morning, guys. Just two questions on my side. The first one is just on the assumptions, are you planning any review in the third quarter and could you share something with us on that at this stage?

And the last one will be on the capital generation. So, if I (1:16:05) €1.4 billion net of all the incurred cost, I get to roughly 14 percentage point of Solvency II capital generation organic. Obviously, you will pay dividends so that figure will come down. The UFR drag is not that huge at group level. But you have 185%, you might get close to 190% maybe at the year-end and normal market circumstances.

So, next year, we might get above the 190%. So, what do you think about kind of the 190% figure? Do you want to stay a couple of quarters above 190% before taking actions there or do you think about opportunities above 190%? Thank you.

A - Matthew J. Rider {BIO 20002664 <GO>}

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So, maybe on the first one I think everyone knows we do our normal assumption review in the third quarter, and so the results will come out in 3Q and that's all I can really say on that one.

A - Alexander Rijn Wynaendts {BIO 1821092 <GO>}

Yes. You want me to say something on the Solvency II ratio, Benoît. I appreciate you are looking forward indeed. We would end up close to the higher end of the range. We have a range of 150% to 200% but I think in this environment, being at the upper end of the range is certainly not negative. And as I said earlier, we have committed to our €2.1 billion return to shareholders by 2018, and we'll review obviously thereafter if situations change and then they require a different outcome.

Q - Benoît Pétrarque

Okay. Thank you. Bye-bye.

A - Matthew J. Rider {BIO 20002664 <GO>}

Thank you.

Operator

Thank you. I would like now to turn the call back to our speakers for any additional or closing remarks.

A - Alexander Rijn Wynaendts {BIO 1821092 <GO>}

Well, thanks a lot everybody for tuning in. With that said, we had a long one than usual. So, thank you and have a great day. Bye-bye.

Operator

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

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