Q3 2019 Earnings Call

Company Participants

- Cristiano Borean, Group Chief Financial Officer
- Frederic de Courtois, General Manager
- Giulia Raffo, Head of Investor & Rating Agency Relations

Other Participants

- Ashik Musaddi, Analyst
- Elena Perini, Analyst
- Farooq Hanif, Analyst
- James Shuck, Analyst
- Niccolo Dalla Palma, Analyst
- Nick Holmes, Analyst
- Peter Eliot, Analyst

Presentation

Operator

Good afternoon. This is the Chorus Call conference operator. Welcome and thank you for joining the Generali 2019 Nine Months Results Conference Call. (Operator Instructions)

At this time, I would like to turn the conference over to Ms. Giulia Raffo, Head of Investor & Rating Agency Relations. Please go ahead, madam.

Giulia Raffo {BIO 21037091 <GO>}

Thank you very much. Good morning everyone, and welcome to Generali nine months 2019 results conference call. I'm here with our General Manager, Frederic de Courtois and with our Group CFO, Cristiano Borean. Without further introduction, we would like to open the Q&A session. Thank you very much.

Questions And Answers

Operator

(Operator Instructions) The first question is from Peter Eliot with Kepler Cheuvreux. Please go ahead.

Q - Peter Eliot {BIO 7556214 <GO>}

Thank you very much. My first question was just the usual ones. I'm trying to get just a little bit more detail behind the numbers if possible. And I was wondering if, as usual, you could give us the split of run-off gains and expense ratio within the combined ratio and also if you could spell out the moving parts of the Solvency walk in Q3.

And then secondly, similar two asked one of your competitors this morning, but just wondering if you could share any thoughts that you have on the impact of EIOPA's review. I mean, it looks to me like you could see quite a material benefit under some of its proposals for changing the VA beyond just the country, VA proposals, but interested to hear your thoughts on the matter. Thank you.

A - Cristiano Borean {BIO 15246531 <GO>}

Hi, Peter. So, split of expense ratio, you have a movement of the expense ratio which is on a nine months -- over nine months increasing 0.4%, which is mainly the effect of an increasing of cost acquisition, 0.6% because of the expenses of acquisition of the non-motor business which we are steering to grow for and a reduction of 0.2% in the administration cost, thanks to our tight cost control. On the movement of the third quarter Solvency, I would first would like to comment, but basically, you have mainly 4 percentage points of capital generation, and these are -- in the holding part. And these are counterbalanced by 4 percentage point of capital movement, which includes also the effect of our liability management exercise we did, as you know, by -- in the end of September and we account for already in this presentation. There are something like 3 percentage point of market variances and another 2 points of other truly due to the 2% or 4% [ph].

Q - Peter Eliot {BIO 7556214 <GO>}

Okay. That's good. If it's not being cheeky, would it be possible to spit out the market variances in terms of interest rates and BTP? And also I was wondering, if we could have the run-off gains within the combined ratio. Thank you.

A - Frederic de Courtois {BIO 16976110 <GO>}

Okay. Okay. So, Peter, this is Frederic. I complete on the loss ratio and the combined. So as mentioned by Cristiano, our combined -- so, the improvement of our combined by 0.3 points is explained by the deterioration of the expense ratio by 0.4 points and an improvement of the loss ratio by 0.7 points. Out of the minus 0.7 points of the loss ratio, we have less run-off, so by 0.6 points, we have a slight deterioration of cat by 0.3 points, and we have a significant improvement of the current year attritional loss by 1.6 points, which is I think the interesting trend because this is a trend that we already had over last year and that we still have over this year and which is probably linked to our strong technical excellence initiatives.

So the -- we see a strong decrease of our attritional currency loss ratio. Before giving the word to Cristiano on the Solvency again, let me comment on the impact from EIOPA. So you know that, first, we had this draft from EIOPA. They are two big topics I would say. The first one is the topic of the last liquid points. Very difficult to know at this stage, but my only comment is that due to our geographical mix and our business mix, we are much less impacted by this topic compared to our peers. And the second big topic is obviously the volatility adjustment, but as you know, we have no clear proposal on the table, so we are still very much at the stage of a lot of various scenarios. So, I wouldn't comment on fees at this stage. Cristiano, on the Solvency?

A - Cristiano Borean {BIO 15246531 <GO>}

Yes. To complete, Peter, let's say that the net effect between the decrease of the government spread, especially BTP, and the decrease of the interest rate is a net 2 percentage point decrease. My comment would like to be to you to focus more on the fact that the BTP tightening was less pronounced in the 15-year bucket than in the 10-year bucket and this clearly has, when you evaluate, an impact, which is exactly the opposite if you look at the 15-year swap movement on the flattening part of the curve. So, you have also this, let's say, non-linear parallel effect in your understanding of estimation.

Q - Peter Eliot {BIO 7556214 <GO>}

That's great. I hope you don't mind me asking a very quick follow-up on that, Cristiano, because obviously the sensitivities you give, it's a parallel shift, and we can do the work very, very thoroughly or we can take a point estimate. It sounds like you're saying 15 years. It's probably the best point to use if we want to have sort of quick and dirty method. Would that be about right?

A - Cristiano Borean {BIO 15246531 <GO>}

Given the structure of our liabilities in life, it is more consistent to focus on there.

Q - Peter Eliot {BIO 7556214 <GO>}

Yeah, great. Thank you both very much.

Operator

The next question is from Farooq Hanif with Credit Suisse. Please go ahead.

Q - Farooq Hanif {BIO 4780978 <GO>}

Hi, there. Thank you very much. Just quickly on new -- life new business mix. I mean the margin decline is quite low in US profit. I was just wondering whether you're seeing a further increase in protection and your linked business and whether you can comment on that. And secondly, clearly, you could see a material decline in investment yield now particularly in Italy in your P&C business. Is there some easy metric we can think of in terms of the basis point decline per year roughly to model that? Thank you.

A - Frederic de Courtois {BIO 16976110 <GO>}

Hi, Farooq. So, on the -- yes, you can see it on the NBV. So the NBV margin is resisting well which is due to a very good increase on protection, better third quarter on unit-linked, and the fact that we continue to roll out the strategy that we have already explained on the fact that our -- especially in Italy, our general account are now lighter and lighter because we've moved to maturity guarantees. Then, if you ask me why do we have a significant increase on protection, my only good answer is that this is really our strategy to develop protection in other countries, so mainly Europe and Asia. And that -- the fact that we have proprietary channels, helps us on this because they are well aligned with the company's strategy.

Q - Farooq Hanif {BIO 4780978 <GO>}

Can I just ask quickly on protection, if I may? When you say protection, is the majority of this business a rider, is it mortality, or is there quite a lot of health?

A - Frederic de Courtois {BIO 16976110 <GO>}

So in -- as you know, the business in Asia is mainly about riders, and the business in Europe is, as a majority stand-alone business. You have also riders but the majority is stand-alone business.

Q - Farooq Hanif {BIO 4780978 <GO>}

Okay, thank you.

Operator

The next question is from Nick Holmes with Societe Generale. Please go ahead.

Q - Nick Holmes {BIO 3387435 <GO>}

Oh, hi there. Thanks very much. Just one question. Just wanted to ask if you can give us an update on pricing in the Italian motor market. Are you seeing price stabilization do you think?

A - Frederic de Courtois {BIO 16976110 <GO>}

Sorry, I need first to answer, Farooq, which I don't know why the operator skipped the answer. So the reinvestment yield in P&C. First, let me say and repeat what we said last time, the amount of money to be reinvested in P&C is very limited in the next two [ph] years coming from the structure of our collection and the structure of our fixed income portfolio. And this is visible also in the third quarter, where there was a very small amount of reinvestment to be down, one third compared to last year, if you have to keep in mind this. So the strategy is to keep a reinvestment yield which is sufficiently in line with some drops going forward of some tens of bps, but you should not expect a huge effect due to the fact that the portfolio to be reinvested is very small.

Q - Farooq Hanif {BIO 4780978 <GO>}

Thank you, Fred. Very kind. Thank you.

Operator

The next question is from Nick Holmes with Societe Generale. Please go ahead.

Q - Nick Holmes {BIO 3387435 <GO>}

Oh, hi, there. Yeah. Thanks very much. Just one question. I wondered could you update us on pricing in the Italian motor market? Just wondered if you think finally we're getting to price stabilization.

A - Frederic de Courtois {BIO 16976110 <GO>}

So, Italian motor market's combined ratio is continuing to improve. As far as prices are concerned, I would say stabilization, may be, slightly up in a market which is still competitive, but the fact that -- again, that we have rolled out or our technical excellence initiatives have led to better combined ratio on the motor. So no -- on the trend -- on the prices, no big changes compared to what we have discussed during the last period, so stable to slightly up.

Q - Nick Holmes {BIO 3387435 <GO>}

That's great. And can you share the combined ratio with us again for Italian motor?

A - Frederic de Courtois {BIO 16976110 <GO>}

Nick, sorry, we don't share this information for the quarter. We'll discuss at year end.

Q - Nick Holmes {BIO 3387435 <GO>}

Okay. Yeah. Sure. Sure. No problem. Thank you very much.

Operator

The next question is from Ashik Musaddi with JPMorgan. Please go ahead.

Q - Ashik Musaddi {BIO 15847584 <GO>}

Hi. Good afternoon everyone. Just a few questions. First of all is around the number, there is some consolidation number in the P&L in operating profit, that improved materially year-on-year. So what's going there? Any thoughts on that? Secondly is, can you walk us through the operating profit to the group net profit number, just what are the key elements there? Any thoughts on that?

And thirdly, if I understand correctly, you did a bit of re-risking of your assets in third quarter. As a result, there was a bit of a drag on solvency ratio. What was that re-risking, in which particular asset class? Any thoughts on that would be great. Thank you.

A - Cristiano Borean {BIO 15246531 <GO>}

Hi, Ashik. So, let's start with consolidation adjustment. First of all, in the quarter, you have two effects. One is related to the IFRS 5 companies like in Generali Leben, which last year were put in this category where there was some interrelation among the company and the group which were netting out. And now, we will not have this effect of consolidation adjustment, the negative part going forward and this will be stabilized with the year end. And this is, in a certain sense, recurring because it will not be there. Then there is a one-off effect of a realization of an intra-group bond losses which has been consolidated out positively on the other side, but this effect is not an effect, which is recurring. So on the -- about EUR30 million difference between third quarter 2018 and third quarter 2019 of consolidation adjustment, you have about half of this coming from the recurring and half coming from this effect.

Second point, regarding the walk from operating to net what are the key element? Well, first of all, in the effect of investment non-operating result, there are still some impairments of around EUR200 million before taxes, which is consistent to what I told you last time of our rules of once impaired, always impaired and the 12-months rule which is applied under our IFRS accounting rules. Then, we have an improvement on the non-operating of the expenses, because of the interest rate debt where you (inaudible) slightly more than EUR30 million improvement.

And then we have, basically, the same level of -- in absolute number on taxes, which brings you -- taking into account the discontinued operation of EUR475 million coming from mainly the capital gain from the sale of Generali Belgium for EUR128 million and the gain coming from the sale of Generali Leben for EUR352 million brings you basically there apart for the result of the previous Generali Leben. And then on the minorities, you get the EUR200 million minorities. These are the major drivers for the operating to effect.

Then I would like to recall that within the non-operating investment result, when you go on the final net result, you have to account the EUR188 million of liability management, which we communicated also in the press release and it is accounted in the non-operating investment result. Hope I gave you clarity on this point.

Q - Ashik Musaddi {BIO 15847584 <GO>}

Yeah. It's very clear.

A - Cristiano Borean {BIO 15246531 <GO>}

On the re-risking in our asset, first of all, the re-risking is completely consistent with our Generali 2021 strategy in the investment, which brings us the increase in the real asset like private debt, private equity, infrastructure. What is important to be understood, it is clearly that depending on the level of interest rate as of today, the capital intensity of this investment is different, so it's higher. And the impact on the Solvency was in the order of 1 percentage point of Solvency for the quarter.

Q - Ashik Musaddi {BIO 15847584 <GO>}

That's very clear. Thank you. Thanks for the detailed explanation.

Operator

The next question is from Niccolo Dalla Palma with Exane BNP Paribas. Please go ahead.

Q - Niccolo Dalla Palma {BIO 16052945 <GO>}

Hi. Good afternoon everyone. I have one question on the Life New business mainly where you mentioned the futures of new products, the sort of recalibration of financial guarantees, and you gave just now the example of the at-maturity guarantees. Is there any other important changes you are making? I think you have been vocal in France about the changes. Is there any practical examples that you can give us of significant changes to products across the business maybe also in Germany? Thank you.

A - Frederic de Courtois {BIO 16976110 <GO>}

Hi, Niccolo. This is Frederic. So, yes, you are right. We've been very vocal in France and I think we've been right to do this. And by the way we've been followed by the market. So we are in France. Of course, like, every other market we're strongly developing protection, but the big change will be on the savings part.

So, we are much -- even more -- much more focused than before on unit-linked. And we will be much more focused than before on the euro croissance. You know that the euro croissance is the equivalent of what I call the maturity guarantee in Italy. So in euro croissance, you have -- you also have a maturity guarantee. You also have the possibility to guarantee less than 100%, so 80% or 90%. And you know that the French government has -- or is currently simplifying the euro croissance, which will probably help to boost the volumes in 2020. So, euro croissance is and will probably be a good alternative in France.

Saying this, we are also doing all what we can to disincentivize general account in France. We recognize that the general account will remain in our product range, but we also recognize that the -- what was paid by the markets on the general account product was not sustainable. So, we will decrease the payout on general accounts and we are obviously ready to have net outflows in general accounts. So, we are clearly focused on margins on this.

A - Cristiano Borean {BIO 15246531 <GO>}

Sorry. It is Cristiano. So, just to follow-up on the previous answer to clarify the EUR188 million of net result impact of liability management is net result. So, after-tax. The pretax impact was EUR245 million, just to have everybody on the same page.

A - Frederic de Courtois {BIO 16976110 <GO>}

And I may complement my answer to Niccolo because I realized that you were also asking about Germany, but Germany is not really an issue for us. Not only on the in-force, as you know, after the sale of Generali Leben, but also because our new business is extremely strongly focused on unit-linked and protection. So usually, what we sell in Germany are bundled products with various guarantees. And the general account part is extremely small, and most of the annuities are unit-linked and protection. So, we don't see an incentive to have strong changes on this and I would say, unlike the market, because the market is still very much focused on general account in Germany.

Operator

The next question is from Elena Perini with Banca IMI. Please go ahead.

Q - Elena Perini {BIO 4202240 <GO>}

Yes. Good afternoon. I've got only one question and it is about your growth. You still have more than EUR3 billion to be potentially used for acquisitions. And in particular, you stated to be interested in P&C and asset management. Can we expect something new after Portugal on this side? Are you working on this? And do you have any updates? Thank you very much.

A - Frederic de Courtois {BIO 16976110 <GO>}

Thank you, Elena. This is Frederic. What I can tell you on this is that our strategy is unchanged. So we are still -- we still have money to be reinvested if there are good opportunities. We -- as you said we're interested in P&C asset management also in protection and health. And again, we need to be very disciplined. I mean, we are aware that we are probably at the end of a cycle, so we are aware that the opportunities are not cheap. So, we need to be even more disciplined than before on the prices and conditions.

Q - Elena Perini {BIO 4202240 <GO>}

Okay. Thank you.

Operator

The next question is from James Shuck with Citi. Please go ahead.

Q - James Shuck {BIO 3680082 <GO>}

Hello. Good afternoon everybody. So, I'm going to try and ask this question, but I'm not sure what kind of answer I'm going to get, but I'll give it a go. We might well be seeing the nuance of the various cross-shareholdings in Italy. There's a few things happening in terms of stakes at various companies changing and some of the families changing their exposures in certain areas. To the extent you can comment on that, I'd welcome any comments that you might be able to give in terms of how you see that evolving over the medium term. And so, a semi-linked question, if capital wasn't an issue for you i.e. the EUR3 billion you got available for acquisitions, if that was suddenly a much bigger number, how do you think you could accelerate your expansion in Europe? Thank you.

A - Frederic de Courtois {BIO 16976110 <GO>}

Hi, James. First, sorry for this, but I will disappoint you on your first question. I will not comment on the cross-shareholding in Italy. And we, as you know, that we have the rule to never comment on our shareholders. So, I have no specific -- have no specific comment on this.

Then on acquisitions, so yes, we've talked about EUR3 billion to EUR4 billion. We -- to complement the answer I've given before, we especially like acquisitions with synergies. So, we have a specific focus on Europe. Not only on Europe. You know that we have -- we are in a limited number of markets in Asia and Latin America. We like also the Assistance business for instance, but -- so, if we are going to buy something in Europe, I cannot answer and I don't know, but we like Europe. We are the market leader in Europe and we like synergies, which we have in Europe.

Q - James Shuck {BIO 3680082 <GO>}

I guess -- I'd take the point on the cross-shareholdings, but I thought I'd try. But I mean just in Europe, I mean, are you seeing assets come to market at the moment? Are the mutuals and things looking at the demutualizing? Are there companies looking to sell off parts of their businesses? I guess if EUR3 billion -- if there's an opportunity that came along that was more opportunistic and you wanted to do more than EUR3 billion, would you consider that?

A - Frederic de Courtois {BIO 16976110 <GO>}

So first, we believe that there will be opportunities because we have 4,000 insurers in Europe and we believe that some of them will be heavily impacted by interest rates. So, we believe that there will be a trend of consolidation. Then, I'm not sure to have understood your question about demutualization. I don't know what you are referring to.

Q - James Shuck {BIO 3680082 <GO>}

Just mutual companies with -- coming under Solvency stress and business models that don't work in the digital age may be looking to sell off parts of their businesses.

A - Frederic de Courtois {BIO 16976110 <GO>}

So, again we will see. They are good demutualizing. This is -- it maybe an opportunity, but more globally, again I think that and we see that some of the insurance companies in Europe mutuals or not, will be heavily impacted by the low interest rate. And yes, it may be lead to opportunity.

Q - James Shuck {BIO 3680082 <GO>}

Yeah. Okay. Thank you very much.

Operator

(Operator Instructions). Ms. Raffo, gentlemen, there are no more questions registered at this time.

A - Giulia Raffo {BIO 21037091 <GO>}

Thank you very much. If that is the case, I believe we can conclude our conference call. As always, the IR team will be at your disposal for any follow-up question that you might have. And as far as the activities are concerned, we will be having our next conference call in March 2020 for our full year results. Thank you very much. Have a good day. Bye. Bye-bye.

Operator

Ladies and gentlemen, thank you for joining. The conference is now over. You may disconnect your telephones.