Q1 2018 Earnings Call

Company Participants

- Andrea Novelli, Head of BancoPosta and Chairman, BancoPosta Fondi S.p.a SGR
- Massimo Rosini, Director Mail, Logistics and Communication Services
- Matteo Del Fante, Chief Executive Officer & Managing Director
- Roberto Giacchi, Chief Financial Officer

Other Participants

- Anna Maria Benassi, Analyst
- Ashik Musaddi, Analyst
- Elena Perini, Analyst
- Fabrizio Bernardi, Analyst
- Gianluca Ferrari, Analyst
- Giovanni Razzoli, Analyst
- Matija Gergolet, Analyst

MANAGEMENT DISCUSSION SECTION

Operator

Good day, and welcome to the Poste Italiane 2018 First Quarter Results Conference Call. Today's conference is being recorded.

At this time, I would like to turn the conference over to Mr. Matteo Del Fante, CEO. Please go ahead, sir.

Matteo Del Fante {BIO 6237992 <GO>}

Thank you. Good afternoon, ladies and gentlemen. We're pleased to present Poste Italiane First Quarter 2018 Results as well as an update on Deliver 2022. As presented at our Capital Markets Day in February, we are undertaking the Deliver 2022, a group-wide transformation program with a focus on Poste Italiane people and system for the benefit of our customers. As you will see today, we're already on track with our financial targets and KPIs, underpinned by the renewed focus on operational performance.

We closed the first quarter with a net profit of €485 million, up by a strong 38%. Some of the key initiative related to the execution of Deliver 2022 have already been launched and we will share some of the major developments with you today. We'd also provide additional details on our increased focus on commercial distribution across our network, which we will have an impact in the coming few quarters. We will also outline our efforts in maintaining cross business, cost control which is already delivering a cost base in line with our five-year target.

Let's first move to slide number 4 for an overview of the financial results for the first quarter. The first quarter results demonstrate that we are on the right track with our Deliver 2022 plan. Revenue reached almost €2.9 billion, an increase of 1.8%. This was mainly thanks to a renewed focus on postal savings under the new CDP agreement and remuneration scheme. EBIT was €703 million, underpinned by our cost discipline efforts. As a result, our EBIT margin increased to 24.4%, up by almost 6 percentage points year on year, resulting in a net profit of €485 million, up by a sound 38.2% year on year.

We have also included, for your information, EBIT, excluding capital gains, which demonstrates the underlying improvement in our operational performance. Earnings per share reached €0.37, up €0.10 versus last year.

On slide 5, we see that revenues in the first quarter increased by 1.8% year on year to €2.884 billion. The revenue mix across our business segments is in line with our expectations and guidance within the Deliver 2022 strategic plan. Mail, Parcel & Distribution is down by only 1.8%, with passive revenue up, mitigating mail revenue, which are actually declining at a slower pace. Financial Services improved by 3.9%, thanks to a renewed focus on postal savings under the improved remuneration agreement reached with CDP. There is more to come in terms of product distribution in 2018 in this space.

Payments, Mobile & Digital posted a healthy revenue increase of 10%, with positive trend across all commercial TPIs. Insurance Services proved to be resilient, supported by P&C and pension plan contribution and we expect non-life revenue to continue to gradually increase. All of these translates into a stronger growth in operating profitability shown on slide number 6.

EBIT rose significantly, up 33.7% year-on-year. Thanks to a strong focus on efficiency, especially in Mail, Parcel and Distribution. Please bear in mind that Mail, Parcel and Distribution revenue in the first quarter benefited from most of the capital gains booked in 2018. On the cost side also, early retirement charges will be booked towards year end.

Financial Services improved by 25% year-on-year, after outperforming revenue trends. Payments, Mobile and Digital shows a positive trend with EBIT up by 3.6% year-on-year, supported by all business lines as we will see in more detail later on. EBIT for Insurance Services remain resilient and we'll go into the segment in more detail later.

Slide number 6 summarizes our progress to-date on our Deliver 2022 targets. We're committed to providing regular updates on our five-year plan. We're pleased with the immediate actions that are delivering changes across each business division. Specifically, in Mail, Parcel & Distribution, our strategic focus is on rolling out the new joint mail and parcel delivery model, with a new approach based on population and volume density, which includes afternoon and weekend deliveries. We also invest in new technology to create a fully integrated mail and parcel network. We have already launched the new joint delivery model and have initiated a phased rollout across Italy and we have streamlined our organizational structure, reducing territories and operating areas from nine to six.

Mail, Parcel & Distribution is gradually improving, with €3.5 billion revenue target for 2018 and an improved operating profitability. The focus on Payment, Mobile & Digital segment is to capitalize on opportunity arising from the convergence in the sector, while also supporting a group-wide Digital division. We will consolidate our leadership in payment system, including expanding our acquired business and in Mobile, thanks to innovative new offers. We have really obtained attained Bank of Italy authorization for our payment institution and we are on track for the formal launch in the second half of 2018. This will be key to reaffirm our undisputed leadership in Italian digital ecosystem.

Payment, Mobile & Digital is growing at a sustained pace, aiming to reach an EBIT of about €0.2 billion in 2018.

In Financial Services, we will capitalize on growing Italian household wealth, while capturing additional opportunities, thanks to our market-leading physical and digital distribution networks to drive growth and serve customers in the best possible way.

So far in 2018, we have fully implemented the new CDP agreement with an attractive new offering and new commercial initiatives. We have also booked the capital gains for 2018 in the first quarter and also secured most of the capital gains, which we will book in 2019. This gives us a clear visibility. And impacting both our Payment, Mobile and Digital and Financial Services segments, we have signed a distribution agreement with Banca Intesa.

In the Financial Services, Total Financial Assets are increasing at a rate of 3%, in line with our target. The goal is a net profit of €0.7 billion for 2018. In Insurance Services, we will retain our leadership position in life and develop our non-life offer, providing our customer with the best products. We're also launching a selection process in order to choose the best potential partner in motors insurance and new initiatives are underway to complete the range of our products in non-life, in line with our plan.

Our Insurance business is expected to maintain its market leadership, but with resilient revenue and net profit in 2018 compared to last year. Across our Payment, Financial and Insurance activities, we have already begun the implementation of a smart distribution model, balancing white label and in-house products to optimize capital and gradually develop the internal knowhow in Financial, Insurance and Payments.

On the next two slides, I want to focus on two key areas of progress related to Deliver 2022. On slide number 8, let's first look at two developments in relation to our Mail, Parcel and Distribution segment. The first and most important is the implementation of the new joint delivery model. As you remember, this model is based on applying three different approaches based on the distinctive characteristics of each area, mainly in terms of job density and competition level. The new joint delivery model will improve service level in order to meet the needs of e-commerce consumers; two, provide increased flexibility through afternoon and weekend deliveries; and number three, reduce costs.

During 2018, we will reorganize more than 300 delivery centers out of a total of 800 requiring reorganization. This process began on April 16 and already 71 delivery centers have been rolled out on the new model. More than 500 municipalities in Italy are already working under the new joint delivery model. As a result, efficiency and flexibility is already improving in line with our target. Execution is on track.

We have also reduced the number of operating regions as anticipated from nine to six across region. As a result, 3,000 FTEs are gradually being redeployed to commercial frontline activities to support our distribution efforts.

Let's move to slide number 9 on the distribution agreement with Intesa. Poste Italiane, most trusted and effective distribution business and unlocking the power of our network is a key component of Deliver 2022. In April, as you know, we signed a three-year non-exclusive agreement with Intesa Sanpaolo for the reciprocal distribution of selected products and services. There are three area of focus and I will briefly share the key details and strategy behind the agreement.

Number one, we will distribute Intesa mortgages and loans through our postal office network. This will be white-label products underwritten by Intesa, with upfront fees for Poste Italiane. This is in line with our strategy to expand our product offer to meet customer needs without increasing our risk profile. Number two, in Payments, Intesa will accept traditional Bollettino Payment Slips and allow the top-up of PostePay prepaid cards in their 20,000 points of sales across the Banca 5 network. As a result, we will be able to better manage the transition from Bollettino to digital payments, while also leveraging on third-party networks to consolidate our leadership with PostePay. And third, we will distribute asset management products without any exclusivity or target in terms of minimum volumes. We will widen our product range, in line with our strategy to have a controlled open platform to better serve our customer and our sales teams will benefit from training and commercial support to strengthen our financial advisory capabilities. We began to distribute the first fund in April, a simple and competitive product, which has already proven to be successful with net inflows exceeding €100 million during the first week.

I would like now to hand over to the head of our business unit and to our CFO, who will explain these trends in more details. As stated in our Capital Markets Day in February, we have a strong leadership team, committed to making Poste Italiane a great success. You will hear more from our business leader on these calls going forward. Today, you will hear Massimo Rosini, Head of Mail and Parcel; and Andrea Novelli, COO of BancoPosta, who will share more detail on the results of Financial Services. Payments, Mobile and Digital highlights will be covered by our CFO, Roberto Giacchi as Marco Siracusano unfortunately cannot be here with us today.

And as per our Capital Markets Day, Roberto will also cover Insurance Services and other group topics.

Over to you, Massimo please.

Massimo Rosini {BIO 20101636 <GO>}

Thank you, Matteo and good afternoon, everybody. In Mail, Parcels and Distribution, our efforts to refocus this segment, as presented within the Deliver 2022 plan, have already begun and you are seeing some of the key trends as well as the impact show through in these results. Segment revenue decreased by only 1.8% year on year. We have had a strong performance in Mail revenue, down only 2% or €14 million. Parcel revenue increased slightly, recovering from an industrial action that affected our Express's full-year SDA, which negatively impacted the fourth quarter 2017. This result is in line with our expectation. B2C revenues are up 18% and we confirm our targets for the full-year 2018. Also intercompany revenue were up 3% or €36 million, thanks to the growth in other segments revenue.

This positive revenue trend, combined with a strong cost discipline, allowed us to post an impressive €263 million EBIT, up nearly 95% year-on-year. The first quarter, as usual, includes the positive impact of capital gains, while early retiring incentives show later in the fourth quarter. Considering all of this, at the moment, we forecast a full-year result in line with targets, with a significant improvement compared to 2017.

Let's move to slide 12. Here you can see volumes and price trends for Mail and Parcels. Mail volume decreased by only 3%, which positively exceeded expectations. Additionally, the decrease is mainly related to lower margin products such as direct marketing. Mail volumes are also positively impacted by the significant increase of packets and small parcels related to e-commerce transaction coming from abroad that are distributed through our postal network.

The 5.4% register in parcel volumes in the first quarter 2018 will therefore actually be 11.3% including this packet. Average prices increased by about 3%, thanks to positive volume mix effect. At the moment, we confirm our 2018 target for Mail revenue, because we believe that the trend improvement recorded in this quarter has yet to be confirmed in the coming months. Parcel volumes increased by 5.4%, boosted by positive e-commerce developments. Average parcel prices were down about 4%, reflecting the changing volume mix from C2C, B2B to B2C.

Thank you for your attention. I will be available for any questions during the Q&A part of this call.

Let me now hand over to Andrea Novelli.

Andrea Novelli {BIO 15185958 <GO>}

Thank you, Massimo, and let's start from slide 13, with our segments' key financials. Here we show our Financial Services revenue, including net capital gains, rather than gross capital gains as shown on slide 6.

Revenue increased by 2.2% in the first quarter 2018, reaching €1,494 million, mainly thanks to the revamp of postal savings under the new remuneration agreement in place since January. Postal savings are key for Poste and will support the profitability of our Financial Services segment, while also allowing us to attract new resources and to engage in strong and trusted relationship with our customers, thus enabling cross-selling.

Third-party distribution revenue was impacted by two items. First, accounting changes introduced in 2018, which require us to report a revenue net of the fees paid back to the originating bank (00:20:37) back loans. And second, the impact of the disposal of Banca del Mezzogiorno - MCC, which record in August 2017. Utilizing these two items, as we show later, third-party distribution revenue increased by 12% in the period.

Interest income maintained a highly resilient trend and assets under management are showing a positive growth trend, with revenue relying more on asset management fees rather than upfront fees. Thanks to our systems and our people, we are now poised to develop on our asset management business to best serve all our customers. The launch of the new mutual fund back in April that Matteo Del mentioned earlier is a good example of our development.

EBIT and net profit growth outperformed the revenue trend just described, supported also by reduction in provisions.

Let's now look more in detail at the evolution of Total Financial Assets on slide 14. Total Financial Assets levels confirm a solid positive trend over time and show an increase of 3.3% in the first quarter 2018 compared to the previous year and in line with Deliver 2022 projections, with a €17 billion increase in assets.

We booked strong net inflows of €4.4 billion, driven by life insurance, deposits and mutual funds. Overall net inflows increased by over €0.2 billion year-over-year, while retail new inflows increased by €0.5 billion, confirming our ability to attract new resources, also thanks to the new postal savings products. As a result, postal saving's negative net inflows significantly improved to minus €2.6 billion, thanks to new commercial initiatives, while maintaining positive inflows for all other products. Net inflows in insurance were equal to 3.1 billion, of which more than €200 million coming from unit-linked and multi-asset Class III products. And mutual funds posted positive net inflows above €100 million.

Let's see these components more in detail over the next slides. On slide 15, we have the distribution of TFAs in the first quarter of 2018 by customer segment, based on wealth and related financial needs, adjusting our Deliver 2022 plan.

The growth of €8 billion on TFA is distributed across almost all customer segments, with the concentration in private and affluent. Thanks to our marketing approach aimed to increase our share of the assets with a stable number of clients. The total number of retail customers increased from 34.4 million at the end of 2017 to 34.5 million at the end of the first quarter 2018.

Slide 16 focuses on postal savings, but we can already see early results of the new remuneration scheme agreed with CDP. The average stock remained broadly stable year-on-year; thanks to the interest accrual on postal bonds mitigating the negative flows.

Negative net sales came to €2.6 billion in the first quarter, strongly improving versus the previous year and we expect a stronger performance in the second half, given traditional positive seasonality. It is in line with our guidance of progressively improving negativity net inflows, keeping an average of minus €4 billion between 2018 and 2020, allowing us to enhance (25:02) our remuneration.

In the first quarter, we launched the three new products with CDP, all with very attractive yields and different maturity options for our customer's financial need. As a result, fees from postal savings came to €450 million in the first quarter, delivering an increase of 27% year-on-year.

Let's move to slide 17. Average current accounts reached €57.8 billion in the first quarter of 2018, up by 5.9%, mainly thanks to corporate and public administration customers. Interest income from the (25:53) portfolio in which we must invest deposits was €361 million, broadly stable year-over-year, thanks to higher volumes offsetting lower accounts.

We realized the expected capital gains for 2018 and we secured most of the capital gains that we planned to book in 2019. Notwithstanding that, unrealized gains at the end of March increase to €2.8 billion, improving mostly thanks to the reduction of the B2B bond spread (26:29). In terms of sensitivity to interest rates, a parallel increase in the yield curve of 10 basis points results in less than €10 million interest income on a yearly basis, while the sensitivity to the (26:46) gains. With plus 10 basis points of spread, (26:48) gains decreased by about €550 million.

Moving to slide 18, here we focus on asset management and loan and mortgage distribution. In the first quarter of 2018, we registered positive net inflows for €322 million in mutual funds, Class III multi asset and unit-linked insurance products.

During the period, we also completed the deployment of MiFID II guided advisory platform in all post offices and the assessment of our salespeople. The vast majority of our staffs are now MiFID II compliant, while the small reminder will work under supervision until qualification. We therefore expect to see a positive impact of this development as the year progresses.

Assets under management increased reaching €9.3 billion including multi asset Class III and unit-linked insurance products, with a change of mix from bonds and cash towards other asset classes with a higher share of equity.

Moving to loans and mortgages, in the first quarter of 2018, (28:16) continue to increase. Volumes increased 2% year-on-year, leading to higher revenue by 12%, as you can see underlying adjusted revenue. The 2% increase in volumes is the result of high growth in personnel and salary backed loans, while on mortgages, we expect a meaningful ramp up in the second half of the year, also thanks to the new agreement with Intesa.

As I said earlier, stated numbers are not meaningful due to a change in accounting principles as of this year and for the disposal of the BdM-MCC in August, 2017. You can also find further detail in the appendix of this presentation.

That's all from me. Thank you for your attention. Let me hand over to the CFO, Roberto Giacchi to talk about Payments, Mobile & Digital, Insurance Services and other group topics.

Roberto Giacchi {BIO 20101579 <GO>}

Thank you, Andrea. I will briefly take you through the highlights for the Payments Mobile & Digital segment, where Poste Italiane benefits from clear readership in a fast-growing market. Revenue increased by 10% in the first quarter of 2018 compared to 2017, supported by all business lines, leading to an operating profit of €57 million, up by 3.6% year-on-year.

In card payments, we have increased revenue by 20% year-on-year, supported by an increased stock of PostePay cards and higher transactions, both in physical and digital channels.

In other payments, revenue amounted to €32 million, up by 3%, thanks to positive seasonality in utility bills. In telecom, we have registered revenues of €52 million, increasing by 4% compared to last year, as we continued to grow, thanks to our new product sales, both mobile and fixed.

Let's move to slide 20 to have a closer look at the drivers underlying this business. In card payments, we reached 18.4 million PostePay prepaid cards, increasing 12.6% year-over-year. Poste Italiane carried out some €270 million payments card transaction, increasing by 24.8% year-on-year.

In the fast-growing environment of e-commerce, we reached almost €50 million transaction, increasing by 25.2% year-on-year. In telecoms, we sold about 300,000 new lines, mobile and fixed, increasing by nearly 1% year-on-year. Finally, the success of our digital e-wallets is confirmed, reaching €2 million in the first quarter.

Let's move to slide 21. The continued increase in user accessing our digital properties shown on this slide confirms our leadership in the digital ecosystem in Italy. For mobile apps, we had reached 16.5 million downloads, up 47% year-on-year. Online registered users increased at a pace of 20%, reaching 15.6 million at the end of March. We have also seen a very solid growth in the number of electronic identification system released, reaching 2 million identities at the end of the first quarter, up 70%.

On the right side of the slide, you can see the synergies between our physical and digital channels. Daily online user reached 1.4 million, approaching the number of physical visitors to our post office of 1.5 million. This translate into a strong growth of online transactions increasing by 20% year-on-year, and into a strong growth of track and trace searches mainly related to the delivery of parcel increasing by 24% year-on-year. This is only the beginning of the story.

As Matteo mentioned, we have now obtained the necessity authorization from the Bank of Italy to set up our payment institution, which we expect to be fully operational by the last quarter of 2018.

Let's now move to the insurance business on slide 22. All in all, insurance revenues was resilient despite lower gross written premiums with an ongoing balance of the insurance offering. In particular, life insurance related revenue decreased 5% year-on-year, while Private Pension Plan related revenue increased 77% and P&C was up 19%. EBIT is almost in line with last year at €144 million and also net profits remains resilient. In line with Deliver 2022, we confirm that full-year 2018 results will be broadly stable compared year-on-year.

Let's move to slide 23, gross written premiums. Here we can see that as announced, a gradual rebalance of our insurance business is taking place. Gross written premiums of life products are down by 11% year-on-year, with a steady increase in unit linked and multi-asset premiums.

Gross written premiums for Private Pension Plans increased by 6% to €272 million, while our P&C business increased by 21% to €48 million, supported by all business lines, welfare, personal, property and payment. In P&C, we had experienced not only a strong performance in premium growth, but also a combined ratio level of 51.1%, mirroring the strong relationship with our customer.

Looking at gross written premiums as a whole, the trend is in line with our expectation for the full-year 2018 where we expect a reduction by about €3 billion compared to 2017.

Moving to slide 24, technical reserves increased versus full year 2017 by €4.6 billion or 3.7%. In particular, net premiums and accrued interest increased the stock by €5.7 billion, run-off decreased the stock by €2.2 billion and capital gains contributes to an increase of €1 billion. The evolution of our investment portfolio is in line with the new strategic asset allocation, that foresees a gradual increase in multi-asset funds and in alternative investments and consequently a reduction in bonds. The minimum return guaranteed to our customers has been reduced by 2 basis point in comparison with full year 2017, mirroring the gradual runoff of this type of policies. Please bear in mind that even this current level of minimal return guarantee is below our competitors, we expect

(37:04) improvement due to the increasing weight of new business. Class 1 return was down due to a persisting low interest rate environment, but we are in line with our target.

Slide 25 gives a comprehensive picture of regulatory requirements for the insurance business. Poste Italiane solvency ratio is up to 284% from 279% at year-end 2017. Own funds increased, thanks to the growth of business and the higher risk-free rate in a context of lower duration on assets than liabilities. The increasing capital requirements results from higher lapse risk, mitigated by higher interest rate and lower spreads. The sensitivities on the bottom right part of the chart confirms the resilience of our solvency ratio (38:11).

That's all on our business segments breakdown. Let's now move to group cost on slide 26. Here, you can see the results of our focus on cost discipline. All ordinary items were down. HR cost amounted to €1,430 million in the first quarter, down by 3.4% or €50 million compared to the same period of 2017. The weight of HR cost of revenue came down to 50% in the first quarter 2018 from 52% one year before. On HR cost, please remember that we expect to book the majority of early retirement incentives in the fourth quarter of 2018. Non-HR operating cost were also down 9.2% year-on-year.

In particular, cost of goods and services are down by 5%, other costs are down by 38%, depreciation and amortization decreased, but are expected to remain broadly stable in 2018 versus 2017. The weight of non HR operating cost of revenue came down to 26% in the first quarter 2018 from 29% one year before.

Please note that there are some non-recurring cost in the first quarter 2017 that we need to consider when looking at the yearly trends. The deconsolidation of MCC during 2017 for $10 million, charge for early redemption on distributed loans which are now deducted from revenue since 2018 for $7 million, provision related to real estate funds for $6 million. Excluding these non-recurring items impacting the first quarter 2017, non-HR operating cost decreased by 7% year-on-year. Overall, the first quarter cost base is in line with our targets for 2018.

On slide 27, we had outlined the positive HR cost trend as well as provided additional details on average head count levels. We have reduced the total head count year-on-year by 2,200 FTEs, despite flexible hirings of 3,000 FTEs. Let me highlight that we can rely now on about 8,400 temporary FTEs on average, which can enable further efficiencies going forward, as the joint delivery model is rolled out and head count requirements decreased.

Labor cost per FTE stood at €42,000, broadly in line with year-end projection and down year-on-year, mainly thanks to one-day paid national holiday less in the first quarter 2018, the release of provision previously accrued, and the deconsolidation effect of BdM-MCC.

Finally, slide 27 shows that the industrial net cash position stood at €385 million at the end of March 2018, affected by a seasonal trend, which also occurred last year. The operating activities increased the cash position by €279 million compared to the end of 2017. The change in working capital resulted in lower cash of about €700 million, due to the payment of personal early retirement incentive, the cash out of the 14 months' salary installment paid in March, the one-off payment related to the renewal of labor contract.

Capital expenditure absorbed €46 million, with investments due to ramp up over the next quarter as Deliver 2022 moves forward. Overall, our financial position is strong, confirming our ability to generate positive cash flow, after taking account into account

our needs from operation.

That is all on my side. Let me now hand over back to Matteo for some closing remarks. Thank you.

Matteo Del Fante {BIO 6237992 <GO>}

Thank you to my team. Before taking your question, let me briefly reiterate some key points. Poste Italiane achieved strong results in the first quarter. Revenue increased by 1.8% year-on-year, while EBIT was up by a much stronger 33.7%. This performance was underpinned by renewed commercial progress which you will see ramping up in 2018, as well as an ongoing focus on cost discipline that is already positively impacting our bottom line.

Deliver 2022, our group-wide transformation program based on (44:15) targets and clear KPIs is moving ahead. This has just been one quarter in our five-year journey to 2022 and all businesses segments are fully focused on the effective execution of the plan. We will continue to provide progress updates on a quarterly basis.

Thank you very much for your attention. We're now ready to answer your questions.

Q&A

Operator

Thank you. We will now take our first question from Fabrizio Bernardi from Fidentiis. Please go ahead. Your line is open.

Q - Fabrizio Bernardi {BIO 3565544 <GO>}

Hi, everybody. I've got three questions on the cost base, if I can. I would like you to focus on the trend of the (45:14) which had a great trend in this quarter. In particular, I would like to understand if we can consider this improvement as recurring. More specifically, if I consider the, let's say, the EBIT margin of 29% of the M&P division versus the 15% one year ago, as a new sort of that base case for the division. Obviously, apart from the earlier retirement cost usually booked in the last quarter of the year?

Also if you can give us a little color on D&A mainly obviously in the M&P division, where they were down more or less €10 million, which seems a small amount, but on a full-year basis would be great. And then a curiosity, if I can, would you remind me what happened to HR cost in the banking division? There is a sharp drop. But if I'm not mistaken the same drop was visible already in the last quarter of 2017? Thank you.

A - Matteo Del Fante {BIO 6237992 <GO>}

Thank you for your questions. I'll start with the D&A. Yeah, the €10 million lower CapEx is under scrutiny and control. But there are no worry, and I will not consider the exercise of taking the €10 million and making it €40 million decrease in CapEx in 2018. So we are targeting our CapEx for year-end in line with the plan. On cost, maybe Roberto, you want to follow-up.

A - Roberto Giacchi {BIO 20101579 <GO>}

Yes. Thank you. As we see, at this stage, we are confirming the target for 2018 that we deliver within the Capital Markets Day. More precisely, we can consider the efficiencies that we had reached in this quarter all consolidated, and when I say consolidated, I mean that only a small part of these efficiencies are related to the shift of some costs to the next quarter. But we cannot say that this kind of efficiencies will be repeated in the next quarter.

On depreciation and amortization, Matteo already answered. Then, if I may, I would ask you to repeat your last question on banking HR costs.

Q - Fabrizio Bernardi {BIO 3565544 <GO>}

Yeah. If I look at the presentation, one of the last two slides where you put the P&L of financial services, I read that personal expenses were €30 million in 2017 and €21 million in first quarter 2018, so it's a drop of €9 million, minus 30%. I checked the fourth quarter of 2017 and HR personal expenses were already down materially. So, I would like you to remind me what happened to the Financial services division in terms of HR cost, because minus 30% is a record I guess?

A - Roberto Giacchi {BIO 20101579 <GO>}

Yes. Thank you for your question.

Q - Fabrizio Bernardi {BIO 3565544 <GO>}

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A - Roberto Giacchi {BIO 20101579 <GO>}

Yes. As we said before, in the first quarter of 2017, we have – or we still have on our numbers the BdM-MCC legal entity. Yeah. So we had deconsolidated the revenues and cost, so that deduction is mainly related to the consolidation of BdM-MCC.

Q - Fabrizio Bernardi {BIO 3565544 <GO>}

Okay. Thanks.

Operator

We will now take our next question from Gianluca Ferrari from Mediobanca. Please go ahead.

Q - Gianluca Ferrari {BIO 15042989 <GO>}

Yes. Hi. Good afternoon, everybody. I have three questions. The first one is on the 2% decline in retail deposits. I was wondering why you had this small reduction, given that your retail deposits were up quite substantially last year.

Second is on the buyback, when you intend to start it? And I know you have an authorization to complete it by 18 months, but I was wondering if you plan to complete it by end of this year. Third and final question is, if you can give us a sense of the rebates that you will get from Intesa on the mortgages? Thank you.

A - Roberto Giacchi {BIO 20101579 <GO>}

Okay. On the buyback, we're not yet authorized. There is the General Assembly on the 29 of May, then we have 18 months. But I want to be clear with investors, no decision has been taken by the board. And so the board has allowed us this flexibility for the future, but there is no commitment to proceed with the buyback and no specific decision has been taken.

The third question was on rebates which is I think easy, because we don't disclose it. And more specifically, on the first question, 2% decrease in retail deposits, I think Andrea can talk about it.

A - Andrea Novelli {BIO 15185958 <GO>}

Yes, thank you Matteo. If you look on the same slide at the corporate and other component, in that part, that is actually growing. You have also the deposits coming from the PostePay part of our business. So if you take into account the total retail component, summing up the current accounts and the PostePay accounts, that component is actually growing and not declining.

Q - Gianluca Ferrari {BIO 15042989 <GO>}

Okay. Thank you.

Operator

We will now take our next question from Kunal Zaveri from JPMorgan. Please.

Q - Ashik Musaddi {BIO 15847584 <GO>}

Hello. Hi, this is Ashik here and I'm using Kunal's line from JPMorgan. Just a few questions I have is, one is can you give us some color about what's happening with the non-life distribution. Where are we on the process? When shall we expect clarity on non-life distribution? So that would be the first one.

The second question is, with respect to mail and parcels business, now, the volume of mail business declined only by 3% in the quarter. And if I understand correctly, this used to be around, say, 7% to 9% (53:10). So what's driving such a low drop in mail business in the quarter? And is it fair to say that this would be the new normal, i.e., it will decline, but at a slower pace?

And the third question is, you mentioned that you have logged in some capital gains for next year, now what does that mean? I mean, is it still part of unrealized gains or is it already taken out of unrealized gains? So a bit of clarity on - if you can give on that capital gains for 2019, which you mentioned you have taken some forward contracts, any clarity on that would be great? Thank you.

A - Matteo Del Fante {BIO 6237992 <GO>}

Thank you for questions. Non-life distribution is in motor, specifically partner or partners that we are going to select and the process is ongoing. In terms of mail and parcel - sorry, please.

Q - Ashik Musaddi {BIO 15847584 <GO>}

No, I was just saying, is there any particular criteria that you are looking for like, okay, this must be my upfront payment I should be expecting, this must be the commission? Any sort of criterias you have in mind to select a partner that you can disclose or is it just a bit too early to disclose that? Thank you.

A - Matteo Del Fante {BIO 6237992 <GO>}

Yeah, yeah. I mean first of all let me remind that in terms of Deliver 2022, this was an activity plan towards the last two years of the plan. So we are anticipating potentially the process and there are no meaningful revenues embedded in the plan for this distribution agreement. In terms of criteria, there are two main criteria, if I want to summarize. The service that we get from the partners on the overall product and specifically the claims management is going to be fully analyzed, because we want to give to our customer the best possible product.

And the second is competition in pricing of the product, because if Poste enters such a market, the natural expectation from our clients would be for us not only to offer a very good product and our reputation is extremely important and the trust that our clients have with Poste is extremely important. But our clients would expect also to have a competitive product in terms of pricing.

So, there is quality and price, and obviously, fees consideration for us, but this is not the main criteria, because with the number of clients and the opportunity that we have ahead of us, it's not a matter of maximizing the upfront fees in the first few months or years, but it's a matter of building a stable presence into a new segment.

And your last - your second question on mail and parcel is, unfortunately, we cannot consider, I believe, the minus 2%/3% on mail as the new normal, as you hinted. We believe that we have to be more conservative. There have been some one-off revenues that have been booked in the first quarter. (57:41) our focus on commercial activities in this space is increasing.

The third question on capital gains of 2019 is straightforward. The €2.8 billion unrealized in the portfolio today is a number that has to be considered after having already closed all the capital gains we needed for 2018 and a meaningful part of the 2019. We don't disclose at the moment the 2019 total amount, but we have started when the spread was interesting and low to realize the gains, so that we would have the opportunity in a more volatile environment with wider spreads to reinvest in a more benign and rich yield and spread environment.

Q - Ashik Musaddi {BIO 15847584 <GO>}

Sorry, just to confirm. So you mentioned €2.8 billion is after 2018 and after meaningful part of 2019?

A - Matteo Del Fante {BIO 6237992 <GO>}

No, sorry, only 2018.

Q - Ashik Musaddi {BIO 15847584 <GO>}

Okay. And 2019, which you have already secured will have to go out from this number?

A - Matteo Del Fante {BIO 6237992 <GO>}

Yes.

Q - Ashik Musaddi {BIO 15847584 <GO>}

Okay, clear. Thank you.

Operator

We will now take our next question from Giovanni Razzoli from Equita. Please go ahead.

Q - Giovanni Razzoli {BIO 7269718 <GO>}

Good afternoon to everybody. I've a couple of questions. The first one is on the very good results in my view on the mail and parcels and distribution division. I was wondering whether you can provide us an update of the (59:55) that you have started, if I'm not mistaken, at the beginning of the year, if you do plan to enlarge this project to other areas. And to what extent this can contribute to accelerate the revenues of the B2C segment?

The second question is actually a clarification on the EBIT of the mail and parcel, distribution. Honestly, I didn't get why you provide an adjusted EBIT figure of minus €43 million, excluding the capital gains. If you – I mean, it's my mistake, I don't understand this. So if you can just give us an idea? And shall we consider this as a rate going forward, excluding the extraordinary cost for (01:00:52) that you expect to book in the Q4?

And the very last question, a clarification on what's the sensitivity of the capital gains of the (01:01:03) portfolio. You said you have sensitivity of minus, if I'm not mistaken, €550 million to 10 basis points in the sovereign spreads. I was wondering whether this understanding is correct. Thank you.

A - Matteo Del Fante {BIO 6237992 <GO>}

Okay. We're working very hard in terms of the joint delivery model on one side, which is the last mile, which is basically increasing the number of parcels that our lettermen deliver. And this is going relatively smoothly. As I said, we have implemented already 71 delivery centers since mid-April and already 500 new municipalities in Italy are experiencing the new delivery model.

On the back of it, if I understood correctly the question, we are optimizing the backbone and the network and direct injection is being implemented everywhere we can in terms of shortening the number of touches, the number of work that needs to be done for the parcel to get to the delivery center. And that's part of the reorganization of our backbone logistic infrastructure and clearly covers also our Express Courier SpA.

In terms of the second question, why do we show the EBIT adjusted, I'll let the CFO.

A - Roberto Giacchi {BIO 20101579 <GO>}

Thank you, Matteo. As we see, we had booked both in the first quarter 2017 and in the first quarter 2018 capital gains. Capital gains are plus for something like 80% to the mail, parcel & distribution segment as commission for sales of product. So if we do not consider this part of the commission, like if we do not have done the capital gains, the underlying EBIT would have moved, would have passed from minus €186 million to minus €43 million. That's the underlying EBIT without the capital gain effect. And I would take also the question on sensitivity. With 10 basis points rate increase, our realized capital gain would decrease by about €550 million.

Q - Giovanni Razzoli {BIO 7269718 <GO>}

Thank you.

Operator

We will now take our next question from Anna Benassi from Kepler. Please go ahead.

Q - Anna Maria Benassi {BIO 1557710 <GO>}

Yes. Good afternoon. I have three questions. The first question relate to the unit-linked business is a small portion of your Insurance business, but is the most – the fast growing segment and we hear about the Supreme Court, Corte Costituzionale, having taken a view on that. We hear the association of insurers, but can you give us an idea of what you expect to happen in coming months in terms of the regulator, the authority could change some of these products and how do you expect to react to that?

My second question relates to SIA. We have understood that the CEO has resigned. And as far as we understand, he was in favor of the IPO of the company. You are a shareholder of the company and the fit between the SIA business and your business could be perfect. Do you believe that something could move in terms of changing the shareholder base of the company?

And my last question relates to your several comments about (01:05:56) Q1 results, both in terms of EBIT and net profit, but it's very clear to us for what capital gains and restructuring charges are concerned, that is typical between the third quarter and the last quarter. But looking today that the cost performance for the efficiency and also better growth in certain division and they're on top of the Intesa agreement in the second half of the year, don't you think that we can consider your comments as conservative just because we are only in May and not in September? Thank you.

A - Matteo Del Fante {BIO 6237992 <GO>}

I wanted to interrupt you because the line was really, really bad and it was difficult for us to hear. We missed basically the first question. We understood that the second question was about Corte Costituzionale and with the new ruling on the unit link. Not much to say that first of all, we are the company which is the least exposed to the matter because we have always sold Class 1 products. As you have seen in the data, we're starting to increase our penetration of Class 3. But we believe that the insurance component of unit link is there by law, by contract and this will be clarified down the road. We're not worried; we're not changing our business and marketing strategy. I captured the word SIA and shareholders in your third question. So I assume you were referring to our participation in SIA, which is the process payment company controlled by CDP and to a lower extent ourselves, with 15%. We're working with SIA on many industrial developments to support our business. The business is changing from an operating level very fast and the fact that we can be supported into the new developments, into the new products, into the new integration from the excellence that the market recognizes to SIA is clearly positive for us. In terms of shareholders, there is nothing on the table. And I have to apologize, but it was very difficult to understand your last question. Maybe you were saying something like given this very strong Q1 on costs, and to some extent on revenues, aren't you too conservative towards your year-end targets? Can you say yes or no? So maybe we lost the line?

Operator

Pardon the interruption, the line has disconnected. We will now take our next question from Matija Gergolet from Goldman Sachs. Please go ahead.

Q - Matija Gergolet {BIO 3561672 <GO>}

Yes, hello, good afternoon and first of all congratulations on the results, which I think were better than most of us expected. I have three topics if I can, we can elaborate a bit on. First is on capital gains. I find it very interesting that you are saying that you have already locked in some forward capital gains for 2019; you have almost €3 billion of accumulated capital gains. Can you help us a little bit to understand how you're thinking about, say, forward sales to log in more capital gains for the coming years? Because it seems that you had almost a bit of a play on the spread, right, 50 basis points of spreads is basically €3 billion of capital gains. Why not just realizing now a good chunk of those spreads and thus securing sort of €100 million of capital gains all the way through 2022, are you thinking about this? That's the first question.

A - Matteo Del Fante {BIO 6237992 <GO>}

Yeah. That's a good question. Sensitivity is really extremely big, because at the end of the day, 10 basis points of spread are something that can happen over one or two weeks. The way we look at it is combining our capital gains needs for the plan and you remember from Deliver 2022 that the needs we have in the plan are decreasing more or less, call it a €100 million per year decrease. We want to be, at the end of the plan, in 2022, with an EBIT without capital gains, but we need to balance our capital gains in the plan with our interest margin in the plan. And if you have the time to go back to Section 5 of our Deliver 2022 plan and specifically on page 13, 1-3, of Section 5, we were showing exactly the balancing effect of the two elements.

So when rates are going lower, we clearly have a benefit in terms of higher potential capital gains, but we suffer on the interest margin, so we run and what we stated in Deliver 2022 is that all assumptions and all simulation and all the stress scenarios were performed with a static management approach, but we're showing, I believe, already in the first quarter that we're not static. And when the market allows us to bring home and anticipate some capital gains because the spread is on the tight end of the range, we bring it home. That means that basically, should there be a widening of the spread, we will have liquidity and opportunity to invest more. Should there be additional tightening that is putting pressure on our interest margin, we will be able to sell more and get what we need to deliver the plan.

Q - Matija Gergolet {BIO 3561672 <GO>}

Okay. Okay. Understood.

A - Matteo Del Fante {BIO 6237992 <GO>}

It has not gone unnoticed when we presented the plan that we did it with a spread of 130 (01:14:03). And if you sum up the capital gain needs that we have put in the plan decreasing, you always get, for the time being at a total value, which is significantly lower than what we have in the portfolio. And nobody has asked us what we would do with the rest, but we have it. Okay.

Q - Matija Gergolet {BIO 3561672 <GO>}

Okay. Got it. Thank you. It's very clear. Secondly, on the costs, so slides 26 and 27, I think now, I find this (01:14:45) cost reduction almost a bit surprising. Now, I think the CFO mentioned that in the wage costs, there was also say a one day of national holiday is not paid this year on some provision reversal. Could you just quantify that please, because 3.4% lower employee costs, I don't think has been achieved at any point in time, in the last three, four years, but the number of FTE reduction is more or less in line with recent history?

A - Roberto Giacchi {BIO 20101579 <GO>}

Yes. The one day less paid national holiday has a value of €12 million that was accounted in the first quarter 2017. And the effect of the provisions that we did in the first quarter of 2017 to take into account the renewal of the labor contracts had a value, would reduce net in the value, the labor cost for full-time equivalent from – for this value, this value would be reduced from €0.431 million as stated in the chart to €0.426 million (01:16:13). These are euros annualized labor cost for FTE.

Q - Matija Gergolet {BIO 3561672 <GO>}

Got it. And sorry, just now on the cost side, what are the expected wages for wage increases for this year, is that like a premium in Q2, you mentioned this; what should we say assume for the rest of the year to say wage increases?

A - Roberto Giacchi {BIO 20101579 <GO>}

Yeah. We can assume the same value that we stated in the Deliver 2022 plan. We think we are in line with that value.

Q - Matija Gergolet {BIO 3561672 <GO>}

Okay. And just last topic quickly. So you mentioned on Mail volume declines and (01:16:52) Q1 is good, but it almost seems that you don't want to increase the guidance for that division, because you say that you want to see these trends from our international e-commerce inbound or say e-commerce going via mail have to be confirmed? What exactly do you need to have confirmed at the end of the day, basically to have more confidence that there is a change in trend in Mail, perhaps driven by more Mail going through more – so e-commerce going through Mail? We're hearing the same thing from pretty much all the other postal companies, so there is now more and more e-commerce packages going through the Mail. So what's your view there?

A - Roberto Giacchi {BIO 20101579 <GO>}

Yeah. The trend of international package markets going through the Mail channel, I agree with you, is there is not a lot we need to wait to see it confirmed. If anything, probably it will increase, but it's probably not only that. First quarter of the year, there were some additional mailing due to regulatory aspects that we need to verify whether it will be replicated towards the end of the year. In the first month of the year, for regulatory purposes, all financial institution need to restate conditions. And that has been, in our opinion, particularly strong this year and we're not sure that this will be sustained. So that's the reason why we are not ready to change our view towards year-end volumes and guidance.

Q - Matija Gergolet {BIO 3561672 <GO>}

Okay. Thank you very much, very clear. Thank you for the time.

A - Matteo Del Fante {BIO 6237992 <GO>}

Thank you.

Operator

We will now take our next question from Elena Perini from Banca IMI. Please go ahead.

Q - Elena Perini {BIO 4202240 <GO>}

Thank you, and good afternoon. I have two questions left. The first one is again on the Mail and Parcel business. If I understood correctly, you had not recorded any one-offs in terms of costs in this first quarter, but you have recorded some one-offs on revenue side. Could you please make some sort of a recap on this please? And the second question is on the Insurance business. Because if I look at your Excel file, Excel database, I see that Financial and Insurance activities suffer from a strong decline in this quarter compared to the first quarter of 2017. In particular, we have €429 million versus €982 million last year. If I look at page 14 of your press release, I see that this comes from both income and expenses. Could you please elaborate a bit more on this please? Thank you.

A - Matteo Del Fante {BIO 6237992 <GO>}

Okay, I will ask the CFO to take the first question. Please Roberto.

A - Roberto Giacchi {BIO 20101579 <GO>}

Yes. Thank you, Matteo. As we see, the non-recurring items that we have recorded on this quarter or last quarter, Q1 quarter in 2017 versus the first quarter 2018 are the one that I mentioned on slide – I give the number – on slide 26. Those are the non-recurring items. The figures for Mail and Parcel so are consistent in terms of revenues and in terms of cost quarter versus quarter. The only adjustment that we did is we take into consideration the capital gain effect and to show you the underlying EBIT of the segment without the capital gains.

Q - Elena Perini {BIO 4202240 <GO>}

Okay.

A - Roberto Giacchi {BIO 20101579 <GO>}

On the second question, I'm not sure I understood it, but if I try to answer anyway. When you say that on page 14 of our press release, you see a decrease in revenues or income from the insurance activities, I believe the answer was in the presentation related to the financial, the insurance sector where we actually sold in the first quarter less Class I premium that we sold in the first quarter of 2017. This is absolutely in line with the plan because there is a rebalancing exercise taking place with our clients that in the first quarter of 2017, we're not able to buy postal savings products because basically the offering was not there. So as we anticipated in Deliver 2022, the new offering of postal savings plan is creating with (01:23:27) clients in the interest and under the choice of clients, a gradual rebalancing away from Class I products and that is clearly an impact on the specific insurance premium. But all in all, the segment has provided stable margins and revenues.

Q - Elena Perini {BIO 4202240 <GO>}

Okay. Thank you.

Operator

I would now like to hand the call back to Matteo Del Fante for any additional or closing remarks.

A - Matteo Del Fante {BIO 6237992 <GO>}

There are no additional remarks on our side and we're on the road to see more clients and we thank everybody for the attention and the time you spend on Poste. Thank you.

Operator

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