Q3 2017 Earnings Call

FINAL

Bloomberg Transcript

Company Participants

- Delfin Rueda Arroyo, Chief Financial Officer & Member-Management Board
- Eilard Friese, Chief Executive Officer and Chairman

Other Participants

- Albert Ploegh, Analyst
- Bart Jooris, Analyst
- Cor Kluis, Analyst
- Farooq Hanif, Analyst
- Michael van Wegen, Analyst
- Nadine van der Meulen, Analyst
- Robin van den Broek, Analyst
- Steven Haywood, Analyst
- William Hawkins, Analyst

MANAGEMENT DISCUSSION SECTION

Operator

Good morning, ladies and gentlemen. This is the operator speaking. Welcome to NN Group's Analyst Conference Call on its Third Quarter 2017 Results. The telephone lines will be in listen-only mode during the company's presentation. The lines will then be opened for a question-and-answer session.

Before handing this conference call over to Mr. Lard Friese, Chief Executive Officer of NN Group, let me first give the following statement on behalf of the company. Today's comments may include forward-looking statements such as statements regarding future developments in NN Group's business, expectations for its future financial performance and any statement not involving historical fact. Actual results may differ materially from those projected in any forward-looking statement. Any forward-looking statements speak only as of the date they are made and NN Group assumes no obligation to publicly update or revise any forward-looking statements, whether as a result of new information or for any other reason. Furthermore, nothing in today's comments constitutes an offer to sell or solicitation of an offer to buy any securities.

Good morning, Mr. Friese, Over to you.

Eilard Friese

Yes. Good morning. Good morning, everyone, and welcome to our conference call to discuss NN Group's results for the third quarter of 2017. I will kick off today's presentation by looking at the highlights of the third quarter results, as well as our progress on the integration and commercial developments in the past quarter. Delfin Rueda, our Chief Financial Officer, will then take you through the details of the financial results and will talk to you through the capital position and free cash flow. I will conclude the presentation with a short wrap-up, after which we will open the call for Q&A. Jan-Hendrik Erasmus, our Chief Risk Officer, is also with us today to answer your questions.

So, let's go to slide number 3. We are pleased to report another strong set of results for NN Group for the third quarter of 2017. This is the second quarter in which the results of Delta Lloyd have been included in our company's overall performance after completing the acquisition in April this year. The operating result of the ongoing business was higher year-on-year, again, driven by higher results at most segments, the contribution of the Delta Lloyd businesses of €51 million, and a total of €32 million of non-recurring benefits in the segment Other. This was partly offset by an unfavorable claims experience in the individual disability portfolio at Netherlands Non-life.

Commercial momentum was also strong. Total new sales of our insurance businesses were up 33% at constant currencies, compared with the third quarter a year ago, driven by higher sales at Netherlands Life, Insurance Europe, and Japan Life, as well as the inclusion of the Delta Lloyd businesses. Higher life sales were reported across the Insurance Europe region; and, in Japan, we saw higher sales of new COLI products launched this year and sales through the Sumitomo partnership, which started in April of this year.

Our balance sheet remains robust with a strong Solvency II ratio for NN Group of 204% at the end of the third quarter, up from 196% at the end of the second quarter. Our strong cash capital position of €1.8 billion allows us to redeem the €575 million senior notes, which mature tomorrow, without the need for refinancing.

Taking this redemption, together with the transaction that we concluded with Fonds NutsOHRA in April, we have reduced notional debt by about €1 billion since the announcement of the Delta Lloyd acquisition, bringing the financial leverage to 28.1% on a pro forma basis.

Let's turn to slide number 4, we are making good progress with the integration of Delta Lloyd and NN in the Netherlands and Belgium, supported by the agreements reached with the Dutch trade unions and Works Councils. The timelines for integration differ for each business unit, with the integration of some smaller teams already complete and other departments in progress. We've also made a start to rebrand Delta Lloyd to the NN brand, including rebranding the Delta Lloyd offices and selected products.

At the same time, we never lose sight of our customers, and our aim is to provide them with excellent products and services through multi-access distribution channels. For example, we introduced a new pension product in Turkey in response to new legislation under which all employees under the age of 45 will be enrolled in a new compulsory pension scheme to be managed by a pension company selected by the employer. Our new product has captured around 7% market share.

In our international businesses, we continue to strengthen our distribution. For example, the recent renewal of our bancassurance agreement with Pireaus Bank in Greece. Innovation at NN is about increasing customer satisfaction, flawless and intuitive interaction, and about efficiency at the same time. NN International Insurance has developed the tool to support sales agents in their daily activities. The Smart Agent Mobile App, which is currently being piloted in Greece, is integrated with NN systems and allows agents to easily connect with customers and prospects.

To round off, our bank activities continue to grow their mortgage business, with the mortgage portfolio increasing to €17.8 billion at the end of the third quarter. To support this growth and its ongoing funding needs, NN Bank successfully completed its inaugural conditional pass-through covered bond transaction in October raising €500 million from institutional investors.

Let's move to slide number 5, we continue to focus on improving efficiency across the organization. And in particular at the business units where we expect the integration of Delta Lloyd to create cost synergies. Compared with the full year 2016 expense base for the units in scope, we have reduced cost by a total amount of €86 million in the first nine months of 2017. Please note that the expense reduction will not always be linear and that at some units we may sometimes see expense increases to support growth, such as the asset management business and the bank.

We are holding a Capital Markets Day in two weeks' time on the 30th of November at which we will give strategic update of the combined group, including the announcement of our new cost reduction target and the measures we are taking to achieve it.

Let's turn to slide number 6, where I will hand over to – or 7, where I will hand over to Delfin Rueda.

Delfin Rueda Arroyo {BIO 7032761 <GO>}

Thank you, Lard, and good morning, everyone. Let me start with the third quarter consolidated results. NN Group reported an operating result of the ongoing business of €431 million in the third quarter of 2017, up 35% on the same quarter last year. This was driven by higher results at most segments, the inclusion of Delta Lloyd, as well as some non-recurring benefits in the segment Other.

On the other hand, the results of our Non-life unit were lower due to a negative claims experience in the Disability & Accident business. The net result for the third quarter was €734 million. This reflects the higher operating result, as well as higher non-operating items, mainly capital gains from the sale of sovereign bonds. This was partly offset by higher special items and the amortization of acquisition intangibles.

Moving on to slide 8, I would now like to take you through the third quarter performance of each individual segment. Let me start with the third quarter operating result of Netherlands Life, which increased to €215 million supported by an inclusion of Delta Lloyd, a higher technical margin and lower administrative expenses.

Fees and premium-based revenues continue to trend lower. Please note that the technical margin this quarter includes €12 million of nonrecurring benefits and positive experience variances related to mortality results.

The operating result of Netherlands Non-life decreased to €1 million, which includes a negative contribution of Delta Lloyd. As we've also seen in the past, the results of D&A can be volatile. And this quarter, we're impacted by a negative claims experience in individual disability.

The results of Property & Casualty improved compared with the third quarter last year, thanks in part to better underwriting performance in motor and the miscellaneous portfolio, partially offset by large claims in the Delta Lloyd Fire portfolio.

All together, the combined ratio for the segment Netherlands Non-life increased to 102.5% from 97.9% in the third quarter of 2016. The operating result of Insurance Europe increased to €77 million, reflecting higher fees and premium-based revenues, partly offset by higher administrative expenses. The current quarter also includes the contribution of Delta Lloyd Belgium and €5 million of nonrecurring benefits.

The operating result of Japan Life increased 48% on the third quarter last year, excluding currency effects. This increase reflects higher fees and premium-based revenues and improvements in both the technical margin and investment margin, partially offset by higher expenses to support the business growth. The increase in the operating result of asset management is explained by higher fees, partly offset by higher expenses, and includes a positive contribution of Delta Lloyd.

Total assets under management decreased from the end of the second quarter by €1 billion to €244 billion, as positive market performance and a net inflow of third-party assets were more than offset by net outflows of proprietary assets.

The components of the segment Other are the holding result, the reinsurance business, the bank and other results. The improved results of this segment in the third quarter were supported by a higher operating result at the banking business as well as €32 million of both nonrecurring benefits at the reinsurance business and a provision release related to a legacy entity.

On the next slide, I would like to take you through the free cash flow generation of NN Group in the quarter. As you can see, on slide 9, the holding company cash capital increased to €1.8 billion at the end of the third quarter. The free cash flow in the third quarter was €268 million, for the most part explained by €332 million of dividends received from subsidiaries. As usual, details of the dividend upstream by segment can be found in the appendix to this presentation. The capital flows to shareholders were €209 million, representing the cash part of the 2017 interim dividend for shares repurchased in the third quarter.

Let's move to slide 10 on the evolution in NN Group's solvency ratio. In the third quarter, NN Group's solvency ratio increased to 204%. This was explained to the greatest extent by the operating return, which added 6 percentage points to the ratio, including a contribution from Delta Lloyd of approximately €60 million to Own Funds and a small release of the solvency capital requirement. The market variances, which added 2 percentage points, reflect the tightening of credit spreads, mainly on Dutch and French sovereign bonds, as well as positive revaluations of equity and real estate investments. Let me remind you that the 2017 interim dividend was already deducted from the Solvency II ratio at the end of the second quarter, which is why you don't see any capital flows in the movement graph.

To finalize my presentation today, let's turn now to slide 11. As Lard already said, given our strong cash capital position, we will repay the €575 million of senior notes that mature tomorrow without the need for refinancing.

On this final slide, you can see the impact of the repayment on cash capital and financial leverage on a pro forma basis. The pro forma cash capital position in the holding company will decrease to €1.2 billion at the end of the third quarter, which is well within our target range of €0.5 billion to €1.5 billion. The pro forma financial leverage ratio will decrease to 28.1% which is a comfortable level that give us additional financial flexibility.

And with that, I pass you back to Lard for the wrap up.

Eilard Friese

Yeah. Thanks, Delfin. Today, we have presented NN Group's results for the third quarter of 2017, and I am pleased with a strong operating performance, including the contribution of the Delta Lloyd businesses. Most segments posted improved results. However, unfavorable claims experience in D&A led to a lower result of the Non-life business. We continue to focus on increasing efficiency, and we have achieved a further €64 million of cost savings in the third quarter. We've also kept up commercial momentum with higher sales at our insurance businesses.

Our balance sheet remained strong with a Solvency II ratio of 204%, and a cash capital position of €1.8 billion or €1.2 billion after repayment of the senior notes tomorrow. We are making good progress on the integration of NN and Delta Lloyd in the Netherlands and Belgium. But obviously, there is still a lot of work to do. We're also working hard to further improve the performance of the businesses of the combined group. We will give a full update on all our plans and targets at our Capital Markets Day on the 30th of November. A lot is changing within our organization. But throughout all of this, our employees remain committed every day to delivering an excellent customer service.

I will now open the call for your questions.

Q&A

Operator

Thank you, Mr. Friese. Go ahead, please. The first question is from Mr. Cor Kluis, ABN AMRO. Go ahead, please.

Q - Cor Kluis {BIO 3515446 <GO>}

Good morning. Cor Kluis, ABN. A couple of questions. First of all, about the Non-life business, especially the disability, individual disability line, where the ratios were been favorable in NN and both Delta Lloyd. Could you elaborate a little bit on what's exactly going on over there? And will this continue, or is this a onetime item?

And the other question is about related to that Non-life Delta Lloyd. Apart from disability, also in P&C, there were a few large claims where just the individual files which were in the media, it was quite high this quarter, most especially at Delta Lloyd.

And my other question is about Life Netherlands. The fee and premium line that was €103 million this quarter, previous quarter was €127 million, especially because we tried to find a run rate, of course, including Delta Lloyd. Could you explain what's the right figure? Is the €127 million a good one or the €103 million this quarter or is there a one-off in those lines?

And my last question is about the Delta Lloyd's earnings. Basically, I think pre-tax earnings was €51 million, after tax €38 million, but the Own Funds generation is €60 million. So, could you explain the difference between the IFRS result and the €60 million Own Funds generation in Solvency II framework? Those were my questions.

A - Eilard Friese

Yeah. Thanks, Cor, for your questions. We're going to take them one by one. Let me start with Non-life. Non-life indeed had a weak Q3. But I think it's important to understand the components because unlike previous quarters, this was driven by the volatility in the individual D&A portfolio, while in fact, the Property & Casualty business improved.

The Property & Casualty combined ratio improved versus the same period of last year from 106% combined ratio to 100.8% combined ratio. I think it's important to note, in fact, if you look at Property & Casualty, this is one of our best - it's our best P&L quarter for the past six quarters since the first quarter of 2016. Still not where we need it to be obviously, but it's definitely a trend that I'd like to underscore here.

The other piece is the individual disability, which was the main theme for this quarter. And then, I will get to the Delta Lloyd big fires in the fire book. The results were impacted negatively by individual disability, and that was mainly on the NN portfolio where we experienced higher claims and lower levels of reintegration. Note, however, that in the same period last year, benefited from positive experience on this portfolio, if you compare the quarters.

Now, as you know, that structurally this disability business has performed very well. And we monitor the claims development closely. Now, the most recent experience we have, of course, is the month of October and we did not see the elevated claims experience that was observed in the third quarter. We have a number of measures in place, and we'll continue to take new measures in the areas of expense reduction and underwriting improvements to improve the Non-life business structurally further. When it comes to the large fires indeed, we saw large fires in the fire book of Delta Lloyd specifically in this quarter, which contributed to the overall result as well.

By the way, just maybe a final remark on the Capital Markets Day two weeks from now, we obviously will expand on the improvement program that we have for the Non-life business moving forward. With that, can I hand over to you, Delfin, for the life questions and the Delta Lloyd earnings, yeah.

A - Delfin Rueda Arroyo {BIO 7032761 <GO>}

Good. Thank you, Cor. Indeed, as you compare the fees and premium-based revenues for Netherlands Life with the second quarter, you see a decrease. Maybe just as a reminder, for the second quarter we flagged some non-recurring and seasonal items at Delta Lloyd which, part of that were impacting the fees and premium-based revenues. So there is also some seasonal effects here, but we have not flagged anything, especially our one-offs for this quarter. But please take into account the seasonality that is embedded in this line.

In terms of your last question on the difference between IFRS and Own Funds generation. Well, we know, I mean, among other things, one significant item of difference is the investment margin. As under IFRS, you will only see what is basically the market yield which there is quarter per quarter will be varying a bit versus the Own Funds generation. Also, keep in mind that the capital generation includes the Solvency, the SCR release which does not exist under IFRS.

Q - Cor Kluis {BIO 3515446 <GO>}

Okay. Very clear. Thank you.

Operator

The next question is from Mr. Robin van den Broek, Mediobanca. Go ahead, please.

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

Yes. Good morning, everybody. My first question is the Delta Lloyd Life Solvency II ratio. I was wondering if you could give any indication of progression there. Also, in connection with the Dutch Central Bank remarks that you have to look at Solvency II ratios ex-UFR, ex-VA, in order to look at the dividend potential. And I was wondering if the Dutch Central Bank is willing to look through basically also with the legal merger in mind when it comes to free cash flow given the fact that you've guided for €100 million to €150 million of free cash flow for initial year of Delta Lloyd. So that's the first question.

And the second question relates to the sizable gains you've made on government bond selling. I was wondering if you could disclose the size of the underlying asset that has been sold and what the rerisking potential could be for that? Yeah. Those are my questions.

A - Eilard Friese

Yes, Robin. I'll hand over to Delfin in a minute. When it comes to the DNB remark, the DNB remark was more to ensure that – they call the industry to ensure that they look at all elements of capital generation. And, obviously, it is something that we always do. So Delfin, over to you for the questions.

A - Delfin Rueda Arroyo {BIO 7032761 <GO>}

Yes. Thank you, Robin. Indeed, the Solvency II ratio of Delta Lloyd Life has had a very good progression, moving from 139% to 149%. This is driven by both strong operating return, as well as the positive impact of the markets, especially the decrease on the spreads in government bonds, as well as some positive revaluations on equity and real estate. And I think that I won't add anything else to what Lard has said in relationship to your comment on DNB. There is only one regulatory regime that we follow. And, of course, the unbundling of the UFR, as expected, is being reported on a quarter-per-quarter basis.

In terms of government bonds, we sold approximately €1.4 billion of government bonds. And basically that was very much related to the amount of credit spread locks that we entered into in the previous quarters. And as this was for our sale of the bonds and then it has been materialized this quarter. In terms of the reinvestments, it's very much going into mortgages, some loans and some real estate.

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

Okay. Thank you very much.

Operator

The next question is from Mr. Steven Haywood, HSBC. Go ahead please.

Q - Steven Haywood {BIO 15743259 <GO>}

Thank you. Good morning, everyone. I see that you've gone quite well ahead of sort of expectations in terms of your cost savings in the third quarter. Could you tell us now sort of where these cost savings came from in the third quarter, mainly which business? And it seems that you're now down to around €200 million level of cost savings remaining. But I guess, that target is now up for a new target with the Capital Markets Day coming in. Well, I'd just like to know where the main cost savings were made in the third quarter.

And then, second question, in your Solvency II capital generation, could you just explain to me on a technicality why holding expenses are included in your operating return? The debt costs are included in your Other bucket, compare this to your IFRS operating result. Thank you.

A - Eilard Friese

Yes, Steven. Hi. So, let me talk first about the cost saves. As you know, we have guided that at the time of announcing the transaction that we believe that by 2020, we would be able to extract another €150 million of cost reductions on top of the existing programs that both companies have running. So, don't forget that both companies had existing programs running.

We have also said that we believe that 50% of the additional cost saving would come from Life and Non-life, 30% from bank and asset management, and 20% of holding. Now, what you see is that the result that you see coming through in the first nine months and also in this quarter is the combination of work that is being done in both companies on existing programs that they have plus some components that are the start of an integration process where we for instance has stopped some projects that we don't believe that under the combination are necessary to do. So, this is the combination of that.

We will expand indeed more at the Capital Markets Day on the integration plans that we have for the various businesses. And obviously, we will also express the combination of this €150 million on top of the existing cost plans of both companies into one target as the addressable cost base has different units and scope than for instance NN had in the past; now they also include for instance the banks, the asset manager, et cetera.

So, with that, I'm handing over to you, Delfin, for the capital generation.

A - Delfin Rueda Arroyo {BIO 7032761 <GO>}

Yes. Thank you, Steven. Indeed, holding expenses including also the interest on the non-qualifying debt is included as part of the operating capital generation or operating return bucket. We do show the cost of the hybrid debt as part of the segment Other. Technically speaking, as you know, the qualifying debt which is the part that is included within the bucket Other is Solvency II capital. So technically speaking, you could also see it as a retribution or a capital flow to shareholders. That's why we do include it in Other. But that is the distinction. Maybe as a reminder, as you know the amount of the cost of hybrid that comes through Solvency II is approximately €40 million per quarter in the bucket as Other. And the cost of the debt coming through the operating expenses is much lower, as you know, around €2.5 million per quarter because this is only the after-tax market yield of the senior debt.

Q - Steven Haywood {BIO 15743259 <GO>}

Okay. Thank you very much.

Operator

The next question is from Ms. Nadine van der Meulen, Morgan Stanley. Go ahead, please.

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

Yes. Hi. Good morning, everyone. Thank you for taking my questions. I was looking to your operational capital generation and it looked quite high, if I take the 6%, I get to €460 million, in the second quarter that was €410 million. The €410 million also included Delta Lloyd of around €50 million. Can you talk about what was driving that uplift and perhaps also give an indication of what you consider normalized annual number, let's say, pre the additional uplift expected from Delta Lloyd? And perhaps in that line you can also talk a little bit about how much of that is coming from the closed blocks runoff in the Netherlands and Japan?

And then the second question was what was the value of new business in Life and how do you see that develop? Thank you so much.

A - Eilard Friese

Yes. Thank you, Nadine. Delfin, would you be so kind?

A - Delfin Rueda Arroyo {BIO 7032761 <GO>}

Yes. Thanks, Nadine. Well, the operating capital generation includes approximately €0.3 billion of Own Funds. And as you said, it includes a contribution from Delta Lloyd of around €60 million.

Also, we have some release of the solvency capital requirement, somehow below €100 million in the quarter, and that explains the 6 percentage points contribution to the Solvency II ratio in the quarter.

There is nothing special to mention on the quarter except that, if I may say, every quarter is special in some sense. So this quarter, of course, it shows negative experience variance or contribution from the Non-life business because it has bad result and it also reflects the positive contribution coming from Japan also from our asset management business and the pension funds. So, all that contributed to the approximately €0.3 billion of Own Funds.

Your question about how to normalize, as you know, Nadine, my resistance in order to provide you a normalized level, but we have seen already for a few quarters some stability around this level of operating return contribution. But we will always have some deviation coming from the respective contribution, from investment spreads, as well as what is the experience variance occurring both for the Solvency II entities, as well as the non-Solvency II entities there.

In terms of how much comes from closed books, I think, is more reflected obviously in the evolution of the SCR, which tends to decrease over time with the run-off of the portfolio.

A - Eilard Friese

Yeah. Nadine, there's also the value of new business. And well, we report value of new business, as you may know, twice a year, at the half year and at the full year. And you saw at the half year a marked growth in the value new business. In this quarter, you see an additional constant currency growth of APE of about 30%, 33%. And what I can say is that you can see the similar progression that you saw of the business being profitable that we sell, the similar progression, it has happened this quarter on VNB.

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

Thank you very much.

Operator

The next question is from Mr. Farooq Hanif, Credit Suisse. Go ahead please, sir.

Q - Farooq Hanif {BIO 4780978 <GO>}

Hi. Thank you very much for the opportunity to ask questions. In terms of the operational capital generation, can you just confirm that you just said that the experience variance was, overall in that number, negative this quarter? And if you took out the €60 million of Own Funds generation from Delta Lloyd, would it still be €0.3 billion movement in group Own Funds?

Secondly, I noticed there was some big outflows in Netherlands Life, which I guess is the thing that's contributing to the outflows for asset management. But just wondered if that was a normal kind of maturity or is there anything special to mention there?

And lastly, on the Non-life business, and the Individual Life segment in particular, but also D&A. Last year in the third quarter you had, I think, roughly 88%, 89% combined ratio. I'm just kind of wondering where in your mind do you think this business should be into the profitability, so, is it below-90s%, sub-90%, what would you see as a kind of good acceptable level of combined ratio for the D&A business? Thank you.

A - Eilard Friese

Yes. So, thanks, Farooq. So, Delfin, why don't you take the first one and I'll take the other two. Thank you.

A - Delfin Rueda Arroyo {BIO 7032761 <GO>}

Yes. Farooq, the experience variance, I only refer it to a contribution from the Non-life business. But, overall, the experience variance for the Solvency II entities was positive in the quarter. Also, we had significant contribution from the asset management, Japan Life, and the pension funds.

Another element that impacts every quarter the evolution of the operating capital generation is, of course, the release of the UFR that, as interest rates, has gone up somehow has had also a positive impact this quarter, if you were to compare it with previous quarters.

And to your second question, yes, if you were to reduce the Delta Lloyd contribution, it will also still be on the €0.3 billion.

A - Eilard Friese

Yes. Farooq, on the outflows, indeed nothing special. The net outflows were in the proprietary book. It's a combination of two things. Of course, we have the runoff of the variable annuity book in Japan which is part of that. But also it mainly regard the sale of the government bonds on behalf of NN Life. So that's nothing particular there.

When it comes to Non-life and D&A, as I said and I don't know whether you were on the call at that point, individual D&A saw volatility this quarter. Obviously, we're monitoring that. But in the most recent experience that we have, which is only the month of October, we did not see those elevated levels. The business in the past has, yeah, always hovered around the low-90s to 95% combined ratio, the D&A business. So it's been a good business over the last years as you know.

Q - Farooq Hanif {BIO 4780978 <GO>}

Thank you very much.

Operator

The next question is from Mr. William Hawkins, KBW. Go ahead, please.

Q - William Hawkins {BIO 1822411 <GO>}

Hello. Thank you very much. I guess it's mandatory to ask about capital generation. The €60 million Delta Lloyd Own Funds contribution, how much of that is coming from the life business? I'm assuming that given you had losses in Non-life, it could even be more than €60 million coming out of Life. But then again, asset management may have been strong. So how much of the Delta Lloyd results is coming from the life side of their business?

And then, secondly, can you just remind me where you feel comfortable with regards to leverage? You said the 28% I think is the figure that you're kind of comfortable with. But just directionally, should we be assuming that structurally you still want to get the leverage ratio down, or given in the past I know you've mentioned even 30% is comfortable. In theory, would you be happy with the leverage going up again? I'm just not quite sure about how important that figure is. Thank you.

A - Eilard Friese

Yeah. Thanks, Will. Delfin, I'm handing over to you.

A - Delfin Rueda Arroyo {BIO 7032761 <GO>}

Yes. Thank you, William. In terms of capital generation coming from Delta Lloyd, yes, the majority of it is coming from the life business. In terms of leverage, I mean, leverage is only one element among the full picture of looking at the financial flexibility of the group. So it's the Solvency, it's the cash capital at holding and then the leverage. We have said that we are at a very comfortable level, and this is covered by around 12 times fixed charge coverage ratio, so that the coverage of the debt is not an issue. The rating is not an issue. So we feel comfortable with that.

In terms of going forward, as you can see, the next natural point in order to reduce the level of leverage will be in 2020, and that will be with the reduction of €300 million senior debt that will be maturing then. And, obviously, we have financial flexibility not only in senior debt, but we also have approximately €800 million of unused hybrid capacity between restricted Tier 1 and Tier 2. But you only borrow when you need the proceeds. And our level of cash capital, excluding the €575 million that we will be repaying tomorrow is around €1.2 billion. So certainly liquidity is not an issue.

Q - William Hawkins {BIO 1822411 <GO>}

Right. Just on your helpful answer to my first question. Given your answer, presumably it's still very clearly the case that that capital generation is not fungible to the center. And given the position of Delta Lloyd Life, it's not going to be fungible to the center for quite a long time. Do we have any visibility on when it may become fungible to the center?

A - Delfin Rueda Arroyo {BIO 7032761 <GO>}

I think you're not right on this. So the capital generation of Delta Lloyd Life is fungible. The other thing is what level of Solvency capital you want to keep in any of the legal entities. But by all means, that capital is part of our eligible Own Funds and is certainly fungible to the holding company. So in terms of our dividend policy, we will determine at which point of time is advisable to pay dividends from any of our subsidiaries including Delta Lloyd Life. But certainly that capital is fungible.

Q - William Hawkins {BIO 1822411 <GO>}

Thank you.

Operator

The next question is from Mr. Michael van Wegen, Bank of America Merrill Lynch. Go ahead, please.

Q - Michael van Wegen {BIO 6435238 <GO>}

Yeah. Hi, there. Morning. One quick question on your investment margin in the Netherlands or in Dutch Life business. Essentially, Q3 shows an investment margin that is pretty similar to Q3 last year, difference being that it now includes Delta Lloyd. Can you explain why Q3 2017 is relatively weak underlying? You've been trading some of your bonds. I don't know whether that has temporarily pressured the investment income or whether there's something else going on. Thank you.

A - Eilard Friese

Yes, Michael. Thank you very much. Delfin?

A - Delfin Rueda Arroyo {BIO 7032761 <GO>}

Yes. Thank you, Michael. We always see some volatility from one quarter to another in terms of the investment margin. Basically, you can see also the impact. Keep in mind that this is the last 12 months, so that also includes the deviation from the amount of dividends and private equity that comes through. And no doubt, in terms of our IFRS investment margin, it is under pressure and that's not new. We have flagged it, as you know, also from the past because every time that we do replace a bond with a high book yield, even if we replace it with an investment that provides a higher market yield, that increase our Solvency II capital generation, but still put a pressure on our IFRS investment margin.

Q - Michael van Wegen {BIO 6435238 <GO>}

So, in your view, in your absolute amount, rather than looking at the yield, the net yield that you're getting, the absolute amount, you think there's nothing special in there. And essentially, you see an acceleration in the pressure from low interest rates because, H1, you weren't seeing that much pressure versus what's coming now through underlying adjusted for the Delta Lloyd contribution.

A - Delfin Rueda Arroyo {BIO 7032761 <GO>}

Yeah, but also, when you compare it with the third quarter of last year, I think it's important to remember that through the inclusion of Delta Lloyd, all the assets were value as of the 1st of April at market value. And as a consequence, in terms of the yield that comes from these assets, it's only the market yield at that point of time. So, in relationship to the book yield that NN Group had before the acquisition of Delta Lloyd, that explains the very significant decrease on the investment margin.

Q - Michael van Wegen {BIO 6435238 <GO>}

Okay. Thank you.

Operator

The next question is from Mr. Bart Jooris of Petercam. Go ahead, please.

Q - Bart Jooris {BIO 3470300 <GO>}

Yes. Hi. Most of my questions have been answered. Just one small question for a moment, if I may. You received around €290 million for the sale of the Unilever preference shares. Could you explain me what your plans are regarding reinvestment?

A - Eilard Friese

Yes. Hello, Bart. Thank you for your question. Look, this is just part of our overall book. We have a very large proprietary book that we hold. This is just part of it. So it's part of the reinvestment program that we have in various asset classes.

Q - Bart Jooris {BIO 3470300 <GO>}

Okay.

Operator

The next question is from Mr. Albert Ploegh, ING. Go ahead, please.

Q - Albert Ploegh {BIO 3151309 <GO>}

Yes. Thank you for taking my question. The following question on the repayment of the debt in the holding cash buffer now roughly at €1.2 billion. How much or how relevant is the holding cash buffer basically in relation to your LACDT? So much how credit do you get from the holdco cash from the Dutch Central Bank? It would be helpful to have some color around that. Thank you.

A - Eilard Friese

Yeah. Thank you, Albert. Delfin?

A - Delfin Rueda Arroyo {BIO 7032761 <GO>}

Thank you, Albert. Well, there is not too much of direct relationship between the holding cash and the LACDT. The LACDT is basically what is the amount of taxes that you would be able to recover after stress shock. And of course, the holding cash does provide only – basically does not provide any investment yield, and as a consequence is not having any particular impact. It does however, help in order to support the recapitalization or the fact of not requiring basically, external funding in case of a stress for the subsidiary. So it's important that level of holding cash in order to be a support of the Solvency of the – any of the legal entities after shock. So, on that sense it's important, but not in terms of the revenue generation.

Q - Albert Ploegh {BIO 3151309 <GO>}

Okay. Thank you.

Operator

And the next question is from Mr. Steven Haywood, HSBC. Go ahead, please.

Q - Steven Haywood {BIO 15743259 <GO>}

Hello again. A couple of questions. On your announcement of merging Bidco into NN Group NV, can you just confirm this is the first legal entity merger that you're doing? Does it bring any benefits, or is it just a simplification? And if possible, how many legal entity mergers will you be doing in the future?

And then, another question on your unit-linked issue. Is there a timeline for this appeal going forward? What's the next sort of step, and is there any other updates you can give here? Thank you.

A - Eilard Friese

Yes. Let me talk about unit-linked first, Steven. So, on the unit-linked file, it's still progressing. As you know, in the third quarter, there were a number of things happened. For instance, a collective case against us in front of the judge in or the court in Rotterdam that basically ruled in our favor. The other side has lodged appeal. It's very difficult to say how long that is going to take but usually these processes take a lot of time. I think that's what you need to take into account here.

So, therefore we're just observing the various cases and proceedings individual and collective that are going through the entire industry, and that will take quite a long time, I think, to arrive to a more clear path. And with that, I hand over to Delfin for the other questions.

A - Delfin Rueda Arroyo {BIO 7032761 <GO>}

Yes. Thanks, Steven. Indeed, as you know, the Delta Lloyd NV merger with Bidco on 1st of June this year. And then, now, this is the next natural step in order to simplify our legal structure, so we will merge Bidco with NN Group. That has no implication whatsoever in terms of our Solvency or IFRS. So, it's purely an elimination of an intermediary holding.

In terms of the legal entity mergers that we plan to do, it certainly are related to our asset management companies, the banks, the life companies in the Netherlands, as well as in Belgium, and the non-life companies. So, this will follow different timings and patterns, but this will be also the next natural step in order to simplify the legal structure. And in terms of the benefit of some of these mergers, is very much more important movement to the partial internal model than the legal entity itself.

Q - Steven Haywood {BIO 15743259 <GO>}

Okay. Thanks very much.

Operator

There are no further questions. Mr. Friese, back to you, please.

A - Eilard Friese

Yes. Thank you, operator. Thank you, all, for being available on this call and for your questions. Before we end the call, let me just round off by saying that I'm pleased with the progress we are making to integrate Delta Lloyd into NN Group. I see employees from both companies working together and committed to making a success of the combined business.

There's still a lot of work to do to complete the integration and to further improve the performance of our businesses. We look forward to providing a full update of our strategy and targets for the combined group at our Capital Markets Day on the 30th of November, and I hope to see many of you there. I wish you a very pleasant day. And thank you very much.

Operator

Ladies and gentlemen, this concludes the NN Group's analyst conference call. Thank you for attending. You may now disconnect your line. Have a nice day.