S1 2019 Earnings Call

Company Participants

- Fernando Mata Verdejo, Director and Chief Financial Officer
- Jose Luis Jimenez Guajardo-Fajardo, Chief Investment Officer
- Natalia Nunez Arana, Capital Markets and Investor Relations Director

Presentation

Natalia Nunez Arana {BIO 19480994 <GO>}

Good afternoon, and welcome to MAPFRE's results presentation for the first half of 2019. This is Natalia Nunez, Head of Investor Relations. First of all, I would like to give a warm welcome to our CFO, Fernando Mata. As in various quarters, he will take us through the main year-to-date figures and trends. And it is also a pleasure to have here with us today, Jose Luis Jimenez, our Chief Investment Officer, to discuss our investment portfolio and answer all the questions you may have regarding this topic.

Allow me to remind you that you can send questions to the Investor Relation e-mail address, and we will try to answer them during the Q&A session, if time permits. If there are any pending issues after that, the IR team will be delighted to attend them.

And now let me hand the call over to Fernando.

Fernando Mata Verdejo {BIO 19676348 <GO>}

Thank you, Natalia. Hello, everyone. Welcome to the presentation of our half year results. As always, it is a pleasure to be here with you. We are now six months into our three-year strategic plan. And as you can see, the numbers are very positive, fruit of the transformation that we are implementing and align with this strategic plan.

Looking at the key figures for the quarter, revenue is up almost 7%, mainly due to the rise in premiums and higher financial income, stemming from the rally in financial markets. Overall, premiums are up nearly 5% with similar growth rates in Life and Non-Life. Constant exchange rates, there is little variation. Our combined ratio has improved 150 basis points and it's now under our target of 96%. The net result of almost EUR375 million has fallen 2.9%, mainly as a result of lower financial gains, together with weaker performance in Life that we will cover later. Shareholders' equity is up 10.6%, mainly as a result of the fall in interest rates as well as currency appreciation. The ROE, excluding the 2018 goodwill write-downs, will have been almost 8%. And the Solvency II ratio stood at around 189% at the close of March, the first quarter, quite stable compared to the previous period.

On the next slide, we'll take a look at the key figures by unit. On the right side, you can see the KPIs by region and business unit. Regarding attributable result, I would like to highlight, first, Iberia continues to be the largest profit contributor with close to EUR232 million net result, and solid underlying performance, especially in Non-Life. Second, there were strong improvements in Brazil, up EUR19 million and in North America, up EUR41 million, resulting from improved underlying performance as well as an absence of negative extraordinary items.

Third, LATAM North and South were also strong contributors to results, which is reflected in the low and improving combined ratios. Fourth, MAPFRE RE, which comprises traditional reinsurance and the Global Risks business contributed EUR85 million, despite a large industrial claim and the impact of the drought in Brazil. Lastly, Eurasia and ASISTENCIA continued facing profitability challenges in Turkey and the United Kingdom, respectively. We expect this trend to change over the coming quarters.

In ASISTENCIA, the majority of countries are making profit, and the losses are concentrated in the UK Travel Assistant business, where measures are already being taken. Regarding premiums, growth is very strong in Iberia and LATAM North, the latter fueled by a large multi-year contract, we will comment on later. In addition, appreciation of the US dollar and some Latin American currencies have also supported premium growth, while the Brazilian real is still a drag on premiums, but to a much lesser extent, than last year.

On Slide 4, we will look at the adjusted attributable result. I will comment on the extraordinary drivers of the result. As a reminder, last year, the US was impacted by a severe winter weather. It didn't happen fortunately this year. There were a few large claims affecting MAPFRE RE that we will discuss later, but they have not been considered extraordinary. The reorganization of our US operations has had a positive net impact of EUR4.5 million in 2019, driven by a net financial gain from an investment portfolio existing at the time of the Commerce acquisition, which was partially offset by operational restructuring costs. Realized financial gains decreased by almost EUR23 million in our actively managed portfolio, and the transaction made were exclusively in equity.

Despite the current rally in bond markets, we didn't realize gains in this period to protect our content euro. And regarding real estate, we have not completed any transactions despite having some units available for sale. The adjusted attributable result, excluding all these impacts, is down by around EUR11 million, largely driven by the fall in the Life result, which we will discuss on the next slide. Iberia is performing well, maintaining the same positive trend. As you well know, in Spain, we are expecting a new regulation, updating life actuary table for longevity by year-end.

And as we did with Baremo, we have been gradually preprovisioning for this effect over the last few quarters, starting last year. At the end of June, we have already expensed over 80% of the cost based on our estimate of EUR56 million before taxes and minorities. The fall in Brazil is explained by the non-recurring reversal of a provision in 2018 in the Bancassurance channel, which had a EUR109 million positive impact on the gross results, and EUR50 million after-tax and minorities. There has also been an increase in acquisition expenses this year in the Bancassurance channel in order to boost sales. The fall in LATAM

North is due to higher claims and large corporate life protection policies in Mexico. In LATAM South, there were negative adjustments in Colombia, affecting annuity runoff portfolios as a result of updating long-term financial assumptions, as well as a lower extraordinary results compared to same period last year.

And finally, MAPFRE RE realized gains are slightly down, and there has also been a negative impact from some analytic contracts in Latin America. Please turn to the next slide. On the left, you can see the breakdown of the capital structure with amounting to EUR13.2 billion. Our credit metrics remain quite strong. We leverage around 23%, affected by acquisitions, financing as well as transitory funding of subsidiaries. Leverage should go back down to target levels over the course of the year.

Interest coverage is around 20x earnings before interest and tax. And on the next slide, we'll take a look at our equity position. Shareholders' equity is up 10.6% over EUR8.8 billion. The main reasons behind these improvements are: first, EUR707 million increase of unrealized gains on assets held-for-sale portfolio, net of shadow accounting. The change is based on the strong fall in interest rates in Europe; second, the appreciation of all main currencies with the exception of the Turkish lira, which has had a EUR50 million positive impact during the year. And finally, the decrease of EUR262 million, corresponds to the dividend paid in June.

I will now hand the floor over to Jose Luis, and we will take a look at the investment portfolio.

Jose Luis Jimenez Guajardo-Fajardo

Okay. Thank you, Fernando, and good afternoon to everyone. On this slide, I think it's No.8, you can see on the right-hand side, the assets under management, which are up by 7.8%, driven by: first, improvements in the financial markets after the important correction at the end of 2018; second, FX; and third, the consolidation in March of bancassurance operations; and fourth and last, the value of real estate increased due to the application of IFRS 16, which was already reflected in the first quarter of the year. The background of the investment portfolio is on the left. Asset allocation has been relatively stable through the year and exposure to government on corporate debt remains mostly unchanged.

The largest exposure correspond to Spanish sovereign debt with EUR18 billion and Italian debt with EUR2.7 billion. As we have mentioned in the past, the majority of this investment are in immunized portfolios. Our cash position is up to EUR2.4 billion and include short-term investment and temporary cash balances. Exposure to equity in mutual fund has gone up slightly, thanks to the positive recovery in the financial markets. The strong rally in the financial markets is also reflected in our assets under management, which are up nearly 8% year-on-year.

On the bottom right-hand on the slide, you can see the unrealized gains on our actively managed portfolios in MAPFRE RE and Iberia. At the end of June, there were over 42 million from equity and mutual funds and EUR324 million from fixed income investments. On the next slide, we will look at our actively managed investment portfolios. First, I would like to comment on our actively managed portfolios. Yields are still quite high, around 2% in Non-Life and 3.7% in Life, well above market yields. Nevertheless, the downward trend continued deteriorating our financial income.

We partially neutralized this effort by a slight increase in duration and allocating part of reinvestment to alternative assets. Something that we plan to increase in the future. Duration has gone down as we sold global risk asset portfolio last year, as part of the business reorganization and proceeds has been gradually reinvested through the year. Realized gains in the euro area reached nearly EUR50 million during the first half of the year, over EUR30 million less than the previous one.

Asset sales continue to be selective as we expect the positive trends in markets to continue, and we prefer to protect the recurring deal of our fixed income portfolio. Analyzing the recurring financial income in Non-Life, we can see that geographic diversification is playing an important role. Duration increases has contributed to enhance our fixed income portfolio yield, especially in Latin America. In Brazil, market deals has begun to increase and our accounting deal is even slightly up since the start of the year.

In the Rest of Latin America, we are actually seeing an increase in portfolio deals over 50 basis points. In North America, the accounting deal has been stable since the start of the year, around 3%, despite the strong fall in rates. And duration is around five years, which offer us some protection with the recent fall in yields. In Eurasia, we have seen a very limited decrease, around 10 basis points.

And now I will hand over to Fernando again.

Fernando Mata Verdejo {BIO 19676348 <GO>}

Thank you, Jose Luis. Welcome from Fernando speech. Please turn to the next slide, where we will begin a breakdown by business, starting with Iberia. In Spain, premium performance has been excellent. We are outperforming the market in our main line of business, both in Life and Non-Life. In Motor, premiums are up 2.3%, with positive developments, both in retail and in fleets.

General P&C growth was mostly driven by homeowners and condominiums, helping to offset the fall in commercial lines. Sales campaigns in both agent and bancassurance channels drove the Life business. It is also important to keep in mind that we rolled a large group policy in the first Q for EUR45 million in the bancassurance channel. Motor results and combined ratio. Motor maintained an excellent ratio in a very competitive market environment. We've seen pricing playing claims costs, 13 property damage, mainly and a slightly rise in frequency trends in full coverage products but both in line with our expectations. In General P&C, we have seen a nearly 3 percentage points improvement, thanks to Homeowners, Condominiums and General Liability segments.

The improved result in Portugal with a strong reduction in the combined ratio is also worth highlighting. Let's take a look now at Brazil. Premiums grew almost 2% over 5.6% growth in local currency, especially in the Life protection, Agricultural and Motor segments. There was a fall in Motor premiums as a result of selective underwriting guidelines. The activity will result amounting to almost EUR49 million, up nearly EUR19 million compared to last year. The largest profit contributor was General P&C, driven by improved underlying technical performance, now that the operations are fully normalized.

Losses in Motor are slightly down with 7 percentage point reduction in combined ratio, thanks to stricter claims management and new pricing tools. Overall, the new business model has greater technical control and discipline, and we are not on track to meet our 105% Motor combined ratio target for year-end. Financial income is up, mainly in the Life business due to opportunistic realized gains mainly during the first quarter as well as resilient portfolio deals. Regarding Life protection, variation were discussed at the beginning of this presentation.

Finally, the negative impact of the depreciation in the Brazilian real and average exchange rates has been less than previous quarters. In LATAM North, I would first like to highlight the extraordinary combined ratio, which stands at 93.1%, with a more positive currency scenario. Excluding the multi-year PEMEX policy. Mexico has strong premium growth of almost 15% in the Motor, Health and Life segments. Motor combined ratio went down over 7 percentage points to below 94%, thanks to tariff and risk solution measures. General insurance has also seen an improvement in results. Regarding Central America, part of my experience, an increase in the loss ratio in motor, General P&C and that particular line of business.

But the new appointed seat, CEO, started last year is implementing technical measures, including tariff increases to correct this trend. Honduras continues to have excellent recurring results with the combined ratio below 86%, while El Salvador is also performing well. Dominican Republic saw a strong local currency growth in premiums and receiving combined ratio under 87%. Please turn to next slide. We see LATAM South with an extraordinary combined ratio standing at 95.7%. With the exception of the Argentine peso, there were already strong local currency trends across the region and tailwinds from currencies.

In parallel, premiums were up 8.6% in local currency, with a strong technical performance, reducing the combined ratio by 3 percentage points, driven by Motor and Health and Accident. In Colombia, there was a reduction in the combined ratio set -- by offset by negative adjustments in the annuity runoff portfolios. As a result of the -- of updating long-term financial assumptions, mainly the minimum weight already discussed in previous presentations. Financial performance improved, mainly as a result of the increase of the market value of the trade-in portfolio.

Chile saw local currency growth of 16%. There was a higher combined ratio in Motor as well as an uptick in General P&C due to stands in the central region of the country, offset by strong improvements in health and accident. Argentina saw a decline in premiums, driven by currency depreciation. There was also an increase in the combined ratio. In general, P&C And motor. Let's move to North America. The appreciation of the average dollar exchange rate has positively impacted both premiums and results. Premiums are down almost 8.5% in local currency as a result of the exit from five states in 2018, as well as from underwriting measures.

Underlying results have improved in the US, especially in Personal Motor, with a 3 point -- 3 point improvement in combined ratio. We are reducing our exposure in those areas where we aren't profitable. We have a stopped commercial line renewals this quarter, the second quarter, in all states but Massachusetts. And we are also working on improving client segmentation in several regions, including California, to attract and retain the clients we truly want. Outside of the Northeast, in Western region, states like Washington and Oregon have improved significantly, as you can see on this chart. Results are also benefiting from lower weather-related losses as well as the exit of the five states last year already discussed.

As I said, 2019 results are also a benefit forming a EUR4.5 million net positive adjustment, which comprises, first, EUR19.2 million net financial income arising from equities and high-yield bonds that existed before MAPFRE's acquisitions of Commerce. We saw equities for a gain, while we booked a provision for the bonds. Second, up EUR14.7 million extraordinary expense related to business restructuring. Half of this amount corresponds to the write-off of assets, including accounts receivable as well as layoffs, we were the consequence of our exit plan. The other half corresponds to a provision. It's a general provision to cover any potential runoff from Commercial Lines outside in Massachusetts that we stopped renewals.

Finally, positive premiums and profitability trends continue in Puerto Rico after the two hurricanes that hit the island a couple of years ago. Please turn to next slide. In Germany, premium trends continue to be positive with an improving attributable result and resilient combined ratio. In Turkey, first of all, average exchange rates for the lira are down 22%, and premium growth in local currency was up around 10%, as we continue reducing our MTPL exposures. The attributable loss reached EUR3 million at June compared to a nearly EUR9 million net profit last year.

The loss is mainly due to MAPFRE's participation in the high-risk MTPL pool, which had a negative impact of EUR4.6 million. This bullish compulsory, our losses are allocated in proportion to the entities and market shares. Italy experienced strong premium performance, driven by the dealership channel and a strong improvement in the combined ratio, down 4 percentage points. As we announced last quarter, we are working on the process of transforming our Italian entity into a VERTI Spain brand under EU regulations. The transformation will allow us to optimize capital and reduce cost. So far, we're happy, the plan is moving forward according to schedule.

Please turn to next slide, to the next slide to discuss MAPFRE RE. Premiums are benefiting from currency movements, especially the US dollar. MAPFRE RE has an excellent combined ratio of 94.5%. It is up on the year as a result of, first, a large industrial claim that we already commented in the first quarter amounting to almost EUR20 million, of which 12 million comes from GLOBAL RISKS. Second, the loss from the Brazilian drought amounting to nearly EUR12 million pretax net of reinsurance.

And last, net earned premiums, which are down, resulting from a different distribution of earned premium accruals with more weight in the second half of the year, the impact will be neutral for the full year. The Life business is down year-on-year, mainly due to some annuity contracts in Latin America affected by the update on long-term financial assumptions, which we already explained in the earlier slides for that business. And finally, financial gains are down EUR4 million to EUR14.8 million. Please move to the next page, Solvency II figures as of March 31 continue to reaffirm MAPFRE's solvency position. The 189% Solvency II ratio is based on a high-quality capital structure of EUR8.8 billion in eligible own funds.

Of which, 87% is Tier 1 capital and the remaining 13% in Tier 2. The ratio in March is quite similar to the year-end, but even so, on the right, you have a breakdown of the variation of the different components of our eligible own funds or some more detailed information regarding these solvency figures can be found in our financial report. Also you can find the information for embedded value for 2018 in our new Financial Documentation Center on our website. Please turn to the next slide, for closing remarks. We are clearly seeing a turnaround in both the US and Brazil. We expect the improvements to gain momentum throughout the year.

And both operations are on the right path to meet our targets. In Iberia, both premium and profitability performance have been excellent and are in line with our expectations, even in a very competitive market environment. MAPFRE RE has had resilient results, and we've continued to be an important contributor to our earnings. Growth trends are good in LATAM North and South and profitability trends continue to improve with combined ratios consistently below 96% Regarding Turkey, we're careful in monitoring profitability, but our outlook for the second half of the year is slightly better. MAPFRE continues to boast an excellent financial position. We expect leverage and solvency ratios to convert to target. All in all, we consider the first half results to be a very good start to meet the group objectives set in the new strategic plan.

And now I will hand the call back to Natalia to begin the Q&A session.

Questions And Answers

A - Natalia Nunez Arana {BIO 19480994 <GO>}

Okay. Thank you very much, Fernando. So we are going to start now with the Q&A and with the questions we have received from you. We are trying to group them by topics. We will do our best. Okay, the first topic is about Brazil. Ivan Bokhmat, Barclays; Andrew Sinclair, Bank of America; (inaudible) BBVA; Michael Huttner, JPMorgan; and Sofia at Caxiabank have the following question. Brazil already performs at a low combined ratio of 91.6%, considerably below the 96% hurdle outlined in the strategy. What went better than your assumptions here? And what level should we consider sustainable for 2019, 2020?

A - Fernando Mata Verdejo {BIO 19676348 <GO>}

Yes, thank you, everybody. First of all, this is the first half of the year over three years that the plan, I mean, it's too early to reach a general conclusion. I mean, we're happy, as I said, both Brazil and also USA will discuss later, for sure. I think there will be questions coming, and we're very happy with Brazil. And also, as a reminder, the targets we set are for a medium and long-term basis. The Non-Life combined ratio should be in 2021, lower than 96%. And for Motor, the combined ratio last year was more or less 115. And what I said in different presentations is the underlying should be between 110, 111, more or less. Target for 2019 is 105%; for 2020, 103; and for 2021 is 100, 1 percentage point improvement from expenses, and the rest is reduction of loss ratio. What we're doing? We're more focused on medium and long-term results rather than on a quarterly result, which could be affected by also the transitory efforts. But the targets for 2019 remains at 105%.

A - Natalia Nunez Arana {BIO 19480994 <GO>}

Okay. Thank you very much. Next question from Andrew Sinclair is, why were minority interests so high for Brazil, in Q2 even better P&C profitability, where you have greater ownership and lower life profitability?

A - Fernando Mata Verdejo {BIO 19676348 <GO>}

Yes, auto is where we have the greatest share, it's 100% MAPFRE. The bancassurance channel with the -- joint venture with the JV we have with Banco do Brazil also includes Agro insurance, which is not like where we have a 25% share. Plus, if you recall in the first quarter of the year, Agro was affected by a drought in Brazil. By the way, the same drought that is affected MAPFRE RE during the second quarter. I mean, this is basically the explanation for the question.

A - Natalia Nunez Arana {BIO 19480994 <GO>}

Okay, thank you. Also, Andrew Sinclair has the following question. Should the new lower level of expenses for Brazil P&C in (inaudible) be seen as a reasonable rate?

A - Fernando Mata Verdejo {BIO 19676348 <GO>}

Yes. Thank you, Andy. We're work in reducing cost in Brazil. As you see, the low ratio, I mean, is fine in majority of the Latin America countries, but the spend ratio is pretty high. And it's mainly due to the acquisition expenses that in Latin America are consistently higher than in Europe in already mature countries like the US. We're doing a lot of things. And -- but as I said before, I mean, we are focused on the medium and long term, and we're looking forward to next quarters. We are still working on reducing expenses, but it is still too early to reach a conclusion.

A - Natalia Nunez Arana {BIO 19480994 <GO>}

Okay, great. Now we are moving to balance sheet and investment portfolio. Ivan Bokhmat at Barclays has the following question. 2Q19 realized gains continue to track below last year's result and below full year indication of a stable result. Could you share your views on the tactical asset allocation and timing for portfolio sales, particularly considering a strong increase in unrealized gains?

A - Fernando Mata Verdejo {BIO 19676348 <GO>}

Yes. Yes, you're right, Ivan. We're below, let's say, our '18 realized gains. But let's say that the -- no, MAPFRE, I mean, the entire sector and the entire financial institution, we were navigating choppy waters during the first half of the year. I wouldn't say that I am 100% happy. I mean, I will rather see -- we'll be happier, I mean, looking at numbers higher. But the reality, we should be quite satisfied according to the current scenario that we realize almost 35 million in financial gains, mainly in equity. We are confident, I mean, that we could achieve for the entire year, I mean, the same level of realized gains that we achieved last year.

I mean, our balance sheet has enough volume of unrealized gains, particularly in equity. I mean, to meet the targets or meet the average. And also, on real estate, as I said, during the press presentation, we have over, I guess, four, five relevant units in the market currently we have for sale. We haven't agreed any transactions so far, but there are good opportunities, and one is in Spain, another in Europe and there are two, three relevant and one as well in Latin America. All in all, we, at the current situation, we're confident enough that we will achieve. If there is no extraordinary events that we cannot anticipate at the moment what we do not expect, that we will able to achieve the similar level of realized gains that we did last year.

But by the way, I mean, we're talking about the number, because it's more or less is EUR100 million, comprising both real estate and financial investment. And I said as well, the fixed income portfolio remains untouched. We want to protect our recurring financial income from fixed income. I mean, the curve is down quite clearly. And we want to protect our investment portfolio, which, by the way, we consider it quite privileged. I don't know if you want to add, Jose Luis, but this is more or less, I mean, the overview regarding capital gains.

A - Jose Luis Jimenez Guajardo-Fajardo

Absolutely. Well, I think we are on the same page. And we have probably lower equity capital gains, but it depends on the markets. So probably, right now we are in much better position and we hope this trend will continue from now till the end of the year. But on the fees income side, we prefer to keep what we have on our booking yields, because probably, we see that we have a low interest rate scenario for longer. So the low for longer is our main case.

A - Natalia Nunez Arana {BIO 19480994 <GO>}

Okay. Thank you, Jose Luis. I guess, that this one is also for you. Ivan Bokhmat at Barclays and Farquhar Murray at Autonomous have both asked about the drivers of the increase in duration to eight years in the (inaudible) managed non-life portfolio.

A - Jose Luis Jimenez Guajardo-Fajardo

Basically, I would say this is due to current market conditions, we decided to increase slightly the duration. And so far, I think it was the right decision. But those of you will be in mind that we have the barrier business in the Non-Life portfolio, which is, roughly speaking, less than 20% of the total portfolio on the physical side. So we increase from time to time, the duration on the burial portfolio, this is slightly the total ratio.

A - Natalia Nunez Arana {BIO 19480994 <GO>}

Thank you very much, Jose Luis. Next one is what guidance can you give for investment income in each of your key regions, given recent bond yield moves? Would also like to know what your investment strategy is, given the low interest rate outlook for Europe and Brazil.

A - Fernando Mata Verdejo {BIO 19676348 <GO>}

Yes. I'll go for the first one. Sorry about that, but we don't give any guidance regarding future expectations on our financial returns. Sorry about that. Second question is for you, Jose?

A - Jose Luis Jimenez Guajardo-Fajardo

Yes. So how we are going to deal with the low interest rate environment in Europe and in Brazil. Well, I would say, in Europe, we are really active in doing a lot of the income operations. As I said before, our basis scenario is low for longer. And probably, we will continue to see a low interest rate for at least one or two years more. So we try to keep us from and before. We try to keep the high-yield that we have in most of our securities on the portfolio. But on the other hand, we are starting to diversify.

We also pointed out on Investor Day, there are different drivers. One is the fee-based business, when we expect, as I said before, 8% growth on the asset management side, I think this is good business, as they happen as well with Life on the unlined. So the fee-based business we continue to grow. And on the other hand, we are starting to diversify more and more our investment portfolio to alternative. Because, probably, this is a thing that we have to do, we have a low exposure, broadly speaking, 0.6, and this is due to grow in the coming years. So we have a margin (inaudible) to fight in this low interest rate environment.

A - Natalia Nunez Arana {BIO 19480994 <GO>}

Talking about alternative assets, also Rahul Parekh from JPMorgan wants to know if there are any specific targets for alternative assets.

A - Jose Luis Jimenez Guajardo-Fajardo

Well, in terms of the philosophy, I would say, we are extremely prudent and cautious in the way we manage money. So most of it will go to real estate. You probably know that we have launched several funds with different partners and co-investment philosophy. We will continue with that trend. So far, I would say, it's a good, there has worked extremely well, and we will continue with that. On the other hand, we will do a little bit on private equity and private debt.

But mostly, it would be real estate. It's a kind of one proxy. And probably, this is a way to continue with another EUR400 million has been approved by the board. So in this scenario, we will move from zero two years ago to 1 billion in the coming years. And this is a source to increase deal in one hand. And in the other hand, to try to diversify more our assets within the portfolio.

A - Natalia Nunez Arana {BIO 19480994 <GO>}

Okay. Thank you very much, Jose Luis. Now we are moving to North America. Andrew Sinclair, Merrill Lynch has this question. After a positive technical result in Q1, what led to a negative technical result in Q2, which tends to be a lighter quarter?

A - Fernando Mata Verdejo {BIO 19676348 <GO>}

Yes, Andrew, thank you. Your question, I mean, is quickly and basically, the answer is the restructuring cost that we have accrued in the second quarter in MAPFRE USA. As a result, half of the cost of our exiting states and also the general provision of amounting approximately EUR8 million after-tax to cover any potential runoff from the commercial lines outside of Massachusetts that we stopped renewals in the second quarter. So both the both FX are a relevant impact in our combined ratio. And I estimate, yes, the -- right now, in a percentage point per now for North America, roughly talking.

A - Natalia Nunez Arana {BIO 19480994 <GO>}

Next question is about Solvency II. Farquhar Murray at Autonomous would like to know the following regarding solvency. Interest rates were down in Q1 '19, and I will have expected that to support the Solvency II ratio. Please, could you explain the flat outcome? And looking into second quarter of '19, is it fair to assume that tighter Spanish spreads will have been supported to the ratio?

A - Fernando Mata Verdejo {BIO 19676348 <GO>}

Yes, fortunately, I mean, there is a sort of symmetry in the effect of lower interest rates, and that is affecting both. I mean, the eligible capital. And also, I mean, we have more net equity under IFRS. But we have as well a change in the value of both and the increase in interest rates in the first quarter, and it is one of the main drivers is like 7.4 percentage points uplift in net equity. But there is also are reflected in the liability side with more or less 5% decrease in the other changes in the sustainabilities. Due, obviously, to lower discount rates that we applied to estimate the liabilities.

Also the improvement in the Spanish service in the second quarter of the year, we supported -- will be supportive to the ratio. But again, the solvency ratio is made up of several moving parts. I mean, not only the Spanish service. As a conclusion, we have a very strong solvency position, as you have seen over the last few years, and we tend to move in the upper part of our target range. And we have buffers, such as the model and also if the profits for life with the not accounted for yet. And also additional buffers that we needed. We put in the formula.

A - Natalia Nunez Arana {BIO 19480994 <GO>}

Okay. Thank you, Fernando. I guess, it also answers the question coming from Sofia Barallat that it was regarding solvency, could you elaborate on the changes in this country during first Q? And should we expect more impact of this chart during the second quarter or third quarter, given recent yields evolution.

A - Fernando Mata Verdejo {BIO 19676348 <GO>}

Well, if there is any change in the third quarter, we expect a smart symmetric effects in both in IFRS and also in the best estimate of liabilities. So we do not expect any relevant change in our Solvency II ratio for the remaining part of the year.

A - Natalia Nunez Arana {BIO 19480994 <GO>}

Okay. Now we have questions regarding MAPFRE RE. Ivan Bokhmat of Barclays and Michael Huttner of JPMorgan about the Life results for MAPFRE RE which was affected by negative annuity contracts in Latin America. Can you provide a more -- a bit more details. Is that group or several business? Will there be any recurring impact looking forward?

A - Fernando Mata Verdejo {BIO 19676348 <GO>}

Yes. Thank you, Ivan and Michael, and you're right. I mean, we've seen, let's say, a temporary lack of profitability in Life, both in the RE business and also in the insurance. In our case of direct, which is Colombia, let's say, sort of structural, there is a lack of matching between assets and liabilities. In case of reinsurance, the decrease in the profitability in Latin America is domino effect, but there is still a decrease in profitability in Europe, which is not that big, but the main effect is in Colombia, which is external business and then coming from MAPFRE subsidiary and also in Peru. I do not expect those efforts to be recurring and hope the Life business to come back to healthy levels, probably at the end of this year.

A - Natalia Nunez Arana {BIO 19480994 <GO>}

Great. Thank you. And with regard to reinsurance and GLOBAL RISKS, of BBVA would like us to provide a breakdown, the one-off issues -- of the one-off issues in the quarter. Are there signs of deterioration overall?

A - Fernando Mata Verdejo {BIO 19676348 <GO>}

Yes, first, I mean, the global reasons, I mean, is pretty competitive and globally. I mean, it's not affecting MAPFRE exclusively, I mean, it's affecting the entire globe. And the first half of performance of our reinsurance business, in general, has been excellent. Results were affected by lower level of realized gains and that we expect to catch up in the second part of the year. And also a large industrial claim that we already reported in the first quarter.

In Asia, it was a fire in our plant, a power plant and affecting both GLOBAL RISKS and also the national reinsurance business. Also in the second quarter, we had the Brazilian drought that impacted our insurance second quarter results and our direct business first quarter results in Brazil. The following live business, I already discussed, I guess, is the, you already know, is the application of one conservative longer hypothesis on life annuity contracts in LatAm. Basically, it's the difference between inflation rates and also the minimum wage.

A - Natalia Nunez Arana {BIO 19480994 <GO>}

Okay. Thank you. Next set of questions are regarding Iberia business. Ivan Bokhmat of Barclays, Michael Huttner of JPMorgan, of BBVA, and Sofia Barallat have the following question regarding the worsening of Iberia combined ratio. What were the drivers for that? How does this affect your outlook for the year?

A - Fernando Mata Verdejo {BIO 19676348 <GO>}

Yes. And let's say that the -- where Materis reporting in Iberia regarding Life is something that we expected. And also we discussed in previous presentation. Automobile combined ratio was extremely low. I mean, it was something that we knew some quarters ago that it wasn't sustainable in the long run. And let's say that the current combined ratio in Iberia, I mean, is in line with our expectation, should be between 92% and 94%. This is a long run sustainable combined ratio.

And also, in the past, what we had is a pretty high combined ratio in Homeowners, Condominiums and also in third particular interparty in General P&C. And what we've seen is, during this first half of the year is an increase in motor combined ratio and a relevant reduction in other lines business, particularly in Homeowners is a reduction of 2 point -- it's 25 percentage points and in Homeowners, is from the numbers over here, is last year was 95, currently it's 92.6%.

In Condominium we're seeing higher, the reductions from 94.3 is to 89 lower than 90. And in general, third party liability, the reduction is quite significant as well from 95 combined ratio last year to 83, so there is significant reductions that help MAPFRE to offset a slight increase in automobile combined ratio. Regarding the outlook, we should expect the three relevant lines to be in this level. I mean, a combined ratio for Condominiums and Homeowner as being lower than 95. And as I said, for Motor, in a range between 92 and 94.

A - Natalia Nunez Arana {BIO 19480994 <GO>}

Thank you very much, Fernando. Also, Paco Riquel at Paz Ojeda at Sabadell asked about the updating of mortality tables. (inaudible) potential new provisioning needs for up to EUR2 billion in the Spanish insurance sector, resulting from the update in the life expectancy payrolls. Can you please comment on this? And if we should expect any impact at all from MAPFRE.

A - Fernando Mata Verdejo {BIO 19676348 <GO>}

This is a question that arose at the press presentation, we've had a couple of hours ago, and we discussed, I'm more than happy, I mean, just to comment with you our view. I do know MAPFRE is actively participating in at a technical level in the meanings conversation between UNESPA, which is the Spanish National Association of Insurance and TDS, which is the (inaudible) the supervisory body. We feel that the proposals made by UNESPA, together with what it was based on our report made by one, the largest insurer, and I'm not going to say the name now.

And it's a solid starting point, but will be -- my view is that our view is that we should be quite careful to avoid unnecessary adjustments, unnecessary buffers since the insurance company in Spain and in the globe. We got buffers everywhere. I mean, in the balance sheet, in Solvency II, but -- and also in the actuarial longevity tables. Even when we did at the press presentation, we disclosed the numbers that we have our best estimation of the impact on Life provisions, currently, it's EUR56 million before taxes and minorities without any buffer. And so far, as of June, we booked like 82%, I think -- I don't remember if I said 82 or 83 but more or less, 83 of this effect is already expensed and booked in our financial statements as of June.

For MAPFRE, this is an ongoing process. It's business as usual. We've done -- we're doing with this update of the longevity actuarial tables is to anticipate our financial statements to the new regulation. And since many, many quarters ago, we started provisioning leaded by lender, because we consider that the, I mean, it's fair, it's the normal thing. I mean, just to have your provision according to the most recent biometrical assumptions. I don't know what they do in the rest of the sector for MAPFRE, we're very prudent. The same we did for the Baremo some years ago, we're doing with the actuarial tables. That's may be on -- this is our opinion that we disclosed in the press presentation.

A - Natalia Nunez Arana {BIO 19480994 <GO>}

Thank you, Fernando. A second question from Paco Riquel, again. Can you update on any potential interest that you may have regarding Gaza?

A - Fernando Mata Verdejo {BIO 19676348 <GO>}

I'm going to repeat the same I said at the press presentation. We didn't get any answer from the letter sent by MAPFRE. And I said that the press presentation for the first quarter, this process for MAPFRE. No additional comment, please.

A - Jose Luis Jimenez Guajardo-Fajardo

Okay. Thank you. Andrew Sinclair from Bank of America Merrill Lynch asks about Iberia P&C. Was there anything exceptional or oneoff losses or reserve releases during the second quarter that we should be aware of?

A - Fernando Mata Verdejo {BIO 19676348 <GO>}

No, there's nothing insignificant. The sufficiency we're holding now and in our P&C in June is quite similar to last year. There is no relevant changes, and the minor genes, perhaps in some line of business or reclassification between the lines. But overall, there is no change on the level of sufficiency.

A - Natalia Nunez Arana {BIO 19480994 <GO>}

Okay. Thank you. Now the next question is regarding ASISTENCIA. Rahul Parekh from JPMorgan with the following question. He just wanted to understand the development of MAPFRE ASISTENCIA in first half 2019 versus first half 2018.

A - Fernando Mata Verdejo {BIO 19676348 <GO>}

Yes. No, you didn't miss anything. And the only thing I discussed is that the net loss of the MAPFRE ASISTENCIA is practically equal to the losses coming from the UK, which is travel assistance. Fortunately, I mean, all the changes implemented in this unit are giving fruit and the majority of the countries are in breakeven or even giving us more profit. And also, we haven't found the right button to fix the UK business and travel assistance. We have a full dedicated team. I know that you get the right answers and is the only unit in country that is still in the write-up. That's it.

A - Natalia Nunez Arana {BIO 19480994 <GO>}

Okay. Thank you very much. Next question is regarding Brazil. Michael Huttner at JPMorgan has the following question. On Slide 4 of the presentation, for first half 2018, comparative you did not adjust for Brazil Life accounting oneoff gain? Why not?

A - Fernando Mata Verdejo {BIO 19676348 <GO>}

Yes, we didn't -- we didn't adjust for last at year, the presentation, but we discussed at that point, we -- even we gave you the information in order to do your own estimation of the adjusted net result. Some of you analyst investor want to do in your own adjusted net result. Obviously, last year, they were both affects Life and Non-Life and ultra effect but we consider it's clear, I mean, just to put the net adjustment result as we did -- as we've done during this quarter.

A - Natalia Nunez Arana {BIO 19480994 <GO>}

Again, there is one more question from Paz Ojeda of Banco Sabadell regarding Brazil. What are the drivers in order to reach ROE target of 12%?

A - Fernando Mata Verdejo {BIO 19676348 <GO>}

The main driver should be an improvement in net income. That is quite clear. I mean, it has been a good start for the 3-year strategic plan. And we expect, I said as well as the press presentation, we expect good news to come for the remaining quarters from Brazil. The team is working together, I mean, with the same level of commitment. And once that the operation is fully normalized.

There is one leadership only, particularly in Non-Life business that last year was, let's say, a shared decision between managers from the Bank of the Brazil and also from MAPFRE, now it's completely different. And let's say that the outlook, our view is much better. So let's say that the main improvement will come from net income, which would -- we shouldn't expect any relevant change on the equity base on the capital base in Brazil.

A - Natalia Nunez Arana {BIO 19480994 <GO>}

Okay. Thank you. Next question is regarding investment, Paco Riquel at Atlanta has another question regarding this. The interest rate cycle has turned for the worse. Can you comment what assumptions had you consider in your strategic plan how could it impact your financial income? Any new mitigating measure that you may consider okay.

A - Jose Luis Jimenez Guajardo-Fajardo

Thanks, Paco. As you say, unfortunate, we had already contemplated the falling interest rates and assumptions of our strategic plan. We hope for the best, but we plan for the worst. And also, as Fernando has said several times, we are putting more focus on the technical side, rather on the investment side. It is true that in terms of the mitigation measures. We had the alternative diversification with the first 400 million and now another 400 in a very cautious way, as I say before, in partnerships with our big players, and we expect to get something between 4% and 8% in this type of asset class.

The other mitigating measure is to try to grow even more on the asset management side or what you call the fee-based business, which basically is about mutual funds, pension funds, unit links, which is an area where we are really, really committed to grow in the coming quarters and years. And also, it is true that the low interest rate is not good news in US and in Europe. But on the other hand, you also should bear in mind that this is extremely good news for emerging markets, where we have, I would say, our highest pusher. So they continue low, probably the economic activity in these markets will continue rising as well.

A - Fernando Mata Verdejo {BIO 19676348 <GO>}

If I may add something, Paco. I mean, we are not concerned regarding the fall of interest rates. We're really concerned with the improvement we can apply in our operations in order to reduce our combined ratio. And unfortunately, I mean, we're reporting from the majority of the countries, particularly in LatAm is relevant reductions in combined ratio. And yes, the reduction in Mexico in automobile or just the combined ratio we reported in Central America. And also in Colombia, in Peru. I mean, just, this reduction is big enough, able to offset any reduction in yield. So we had to focus on what we can change in our operations rather than external factors affecting financial markets.

A - Natalia Nunez Arana {BIO 19480994 <GO>}

Okay. Thank you, Fernando. Now we have a question regarding North America. (inaudible) asks, can you update on the US restructuring plan? And whether you are considering to exit from further states?

A - Jose Luis Jimenez Guajardo-Fajardo

Yes, In that case, there is no really on fact there is a press release, but what we've done is to renewals for commercial lines, both order and also for property in all the states but Massachusetts. It's like a -- it's a relevant reduction. Let me tell you that the last year, it was like a USD 44 million of commercial Lines outside Massachusetts. And this is basically the first business plan that we are implemented. Other states, we said at the Investor Day that, if any, we will unveil at the summer. I don't see -- I mean, that we will leave any additional step in the short run, where we had to focus is and the cancellation of the non-renewal of the commercial lines and trying to reduce our expenses in order to get a lower combined ratio.

A - Natalia Nunez Arana {BIO 19480994 <GO>}

Okay. Thank you. Thank you. And now also, regarding North America. (inaudible) from BBVA asks what are your expectations in the financial results in this unit?

A - Jose Luis Jimenez Guajardo-Fajardo

I think in terms of the investment portfolio. In the US, I think, is quite a strong portfolio quite solvent. I think the fees income part of the portfolio is great, with a 5-year duration. So we will keep -- we will try to keep the deal as much as possible. But on the other hand, we have started as well to diversify the portfolio. So we haven't started to do in more alternative because we have a lot of the space with most levels is traditional securities. And I think this year, we started to increase our alternatives. So we are looking for, for next Wednesday and see what the effect has to say. But we think that the portfolio is well prepared for lower interest rates in the coming years.

A - Natalia Nunez Arana {BIO 19480994 <GO>}

Okay. Thank you very much Jose Luis. Last question from BBVA, I think we have already answered, is regarding the Life business. The profit performance of the unit in the quarter, we have already mentioned about Brazil, Brazil performance. And the increase in provisions, we have mentioned several times that you cannot consider separately provisions and financial income. So you can look to both together in order to now to see what's the evolution of the trend in the Life business. So provisions, plus financial income, you need finance planes, we are open to later on?

A - Fernando Mata Verdejo {BIO 19676348 <GO>}

Yes, for just a very short comment. I mean, the main change in life was the was due to the cancellation of the provision in Brazil last year. Life results are quite stable, and particularly in Spain, and you just see the numbers are quite positive, quite stable. And even the update of the actuarial tables. I mean, we haven't seen a change in the profit contribution from MAPFRE. So let's say that the we're quite happy. I mean, the level of Life contribution in terms of profit is very good. And also Malta is performing very well. And the only variation could affect MAPFRE from small countries on a small operations, particularly in LATAM, smaller, smaller than Spain. Sorry.

A - Natalia Nunez Arana {BIO 19480994 <GO>}

Thank you, Fernando. That's all from the Q&A. So I guess, this is the end.

A - Fernando Mata Verdejo {BIO 19676348 <GO>}

Okay. Thank you, everybody, and thank you for -- I mean, it has been a long presentation. A lot of the speech was, I think it was the longest. Hopefully, I mean, the -- I guess, that this provision will help you, I mean, to understand, so you better understand our business, and we wish you -- all of you a great summer. And I guess I see you for the presentation for the third quarterly results. Bye-bye.

A - Natalia Nunez Arana {BIO 19480994 <GO>}

Thank you. Bye.