S1 2018 Earnings Call

Company Participants

- Chris Figee, CFO
- Jos Baeten, CEO
- Michel Hulters, Investor Relations

Other Participants

- Albert Ploegh, Analyst
- Andrew Baker, Analyst
- Ashik Musaddi, Analyst
- Cor Kluis, Analyst
- Farooq Hanif, Analyst
- Matthias De Wit, Analyst
- Robin van den Broek, Analyst

Presentation

Operator

Good day, and welcome to the Investor Call Interim Results ASR H1 2018 Conference Call. Today's conference is being recorded. At this time, I would like to turn the conference over to Michel Hulters. Please go ahead sir.

Michel Hulters {BIO 19111905 <GO>}

Thank you, Operator. Good morning, ladies and gentlemen, welcome to the ASR conference call on our first half year result. On the call with me today are Jos Baeten our CEO, Chris Figee the CFO. And Jos will kick-off as customary with an overview, the highlights of our financial results and will discuss the business performance. Chris will then delve into the developments of our capital and solvency position and after that we'll open up for Q&A. We've got schedule till 12'o' clock and as usual, please review at a time that's convenient for you the disclaimer that we have in the back of the presentation on any forward-looking statements and the disclaimer.

So, having said that, Jos, the floor is yours.

Jos Baeten {BIO 2036695 <GO>}

Thanks, Michel and good morning everyone. Good to have you all here. Thank you for joining us on this call. Ladies and gentlemen, as you have seen from our this morning published numbers, we realized very strong results in the first half of this year, and we continued to deliver solid performance.

I believe we are well on track to meet or even exceed all of the medium term targets for 2018. And without further ado, let's turn to the highlights and those are on slide two. As you may see at this dashboard, it shows our performance over the first half of 2018 and it has been solid on every key metric. Operating result amounted to 382 million almost at the same level as the already very strong result of last year, which we already knew was going to be a tough to compare with due to the exceptional favorable claims experienced last year while in January this year, we suffered from a severe storm that impacted our non-life results with 31 million, 3-1.

Underlying our non-life performance continues to be very strong and each of the other segments reported higher results in the first half this year, reflecting higher investment margin and good momentum in the fee-based business segments. Our business yielded an operating return of 14.7 on an annualized basis, well over our target of up to 12%. Overall, I believe this is an outstanding achievement. Combined ratio of ASR stood at 97.1 just above our target of 97. The 97.1 include the impact of the storm, which is 2.1 percentage points, and furthermore, the inclusion of the Generali Nederland portfolio with a combined ratio of 101.4 in the first half of 2018 which had an impact of roughly 0.5 percentage point on the combined ratio. We remain as you know sharply focused on cost levels and are pleased with our achievements. Our operating expenses headline figure increased with 60 million to 299 and it was due to the inclusion of the EUR22 million of operating expenses from Generali.

Adjusting for additional cost base of Generali Nederland our operating expenses decreased by 3.2% over the first half year, mainly driven by expense savings within the Life segment for EUR8 million. Our Solvency II ratio remained very robust, still based on the standard formula at 194 after the interim dividend that will be paid in September. So basically, we have been able to keep our Solvency II ratio pretty stable while absorbing the impact from the Generali transaction for 9 points, organic capital generation amounted to EUR179 million adding 5 points to the solvency and there are some other moving parts that Chris will provide further detail later on in this presentation.

Quality of our capital remains high with unrestricted Tier 1 capital alone representing 151 of the Solvency II, and then there is still plenty headroom to maneuver. In total we have the possibility to issue almost 1.6 billion of hybrid capital within the Solvency II framework. Our strong solvency position enables us to remain entrepreneurial as we have always set everything above 160 allows us to be entrepreneurial and to pursue profitable growth, which we have proven to do so with for example the acquisition of Generali Nederland last year.

Speaking about Generali, as you may recall from the call, which we hosted in June, this is progressing very well. Generali Nederland contributed to the operating result for already 8 million in the first half of this year. As announced last February, we introduced an interim dividend of 40% of last year's dividend. This amounts to EUR92 million of interim dividend or EUR0.65 per share together with the full-year dividend already paid, we will distribute in total EUR321.5 million to shareholders this year.

Let's now turn to our business portfolio and talk about the developments there, that's on slide three. Starting with our solid back books in box B. In the first quarter of 2018, we finished the migration of two individual Life books towards the software as a software -- sorry towards the software as a service platform, making the cost more variable in order to keep cost in line with the decline of the book. Migration of those two books were completed with a total of roughly 215,000 policies. Like I mentioned earlier, strict cost control is key and in the Life segments this lead to a decline of EUR8 million of operating expenses.

This is due a decline of 5 million within the individual Life business driven by the system rationalization and a decline of 3 million within our pension business. In the top left, in box A, are our businesses that provide opportunity of growing cash flows. In funeral, we successfully migrated to first portfolio of Generali Nederland to the ASR funeral platform. The migration of 363,000 policies was finished on the 1st of July. In P&C organic growth was driven by inflow in the broker channel as well as price increases in the motor segment. Within disability, we launched two new products, the so-called Langer Mee disability insurance in June of 2018.

This is the disability product aimed at the blue collar group to offer an affordable disability product for this class with a kept payment for the insurer in case of disability. Initial market response was very positive and already in the first few weeks, more than 100 -- we could welcome more than 100 new customers in this product. Within pensions, we see good momentum in the DC area as employers decided to move to the so called WerknemersPensioen. This half year, we have reached the milestone of 50,000 active participants and almost reached 3,000 employers who have opted for a contract with this product. Currently over 600 million of assets under management are in this product group and this is going to grow on a year on year basis.

In asset management, there are also very good developments to mention. We see that investors appreciate the recently launched ESG funds and we saw already an inflow of over 0.5 billion. Also the mortgage fund proved successful with new inflows of 700 million and mortgage fund today has now reached over EUR1 billion of assets under management. Within the real estate funds, we see continued interest from investors over there. This half year we have a withdrawal request from an investor that we were able to provide liquidity for that investor and actually realize more inflow than outflow.

Let's now move to slide four, as this slide shows momentum in our operating result remained high in the first half of 2018. Despite the severe January storm, we managed to almost equal last year's result. Higher results from Life plus 26 million bank and asset management plus 6 million distribution and services plus 2 million and the holding and other plus 3 almost offset the decline in non-life. We are confident with our performance but would urge some caution and not automatically multiply by two when projecting for full year because as you know, typically we see in the first half year seasonality mainly driven by the investment margin, because most dividends are in the first half. For instance half-year too dividend could be roughly 30 million lower than the first half year's dividend. Let's have a closer look at our business segments.

Starting at slide five with non-life. In this segment, we still see a very strong performance, despite the storms in January, we managed to keep our combined ratio at 100% sharp. The disability combined ratio improved even further from already very strong levels. Our gross written premium increased by 16.5 mainly driven by the inclusion of Generali Nederland, excluding Generali Nederland, the gross written premium increased with 4.5. So organic growth over the first half year again was very high with 4.5.

All of our business lines showed an increase of the gross written premium driven by new sales and in some areas with price increases within the existing portfolio. We still see good opportunities to grow organically in the non-life segment. Combined ratio as said was 97.1 in the first half and slightly above our target of 97. The storm in January had an impact on the combined of 2.1 percentage points and the inclusion of the Generali Nederland portfolio had an impact of 0.5 percentage point.

When adjusting for those two events, a normalized score of the portfolio is below 96, meaning that we have a very profitable underlying combined ratio at this moment. As the health business is a more regulated also from a margin and profitability point of view. We also look at a non-life combined ratio, excluding health and consisting of only P&C and disability. On this basis, the combined ratio of ASR would be 96.7. The combined ratio of P&C and disability excluding Generali Nederland would be 96.0. So all in all, a very solid combined ratio in the non-life area.

In the breakdown of the combined ratio, you can see a pickup in the claims as an effect of the storm of January this year. We had roughly 12,000 claims only due to this storm. The increase in the commission ratio is mainly a consequence of the inclusion of the Generali Nederland portfolio. This portfolio comprised mostly P&C projects, which in general come at a higher commission ratio. Therefore the uptick in the commission ratio is a reflection of the change in the distribution mix. If we were to look at the combined ratios for each of the different business lines, you can see good momentum in the disability portfolio. Last year we saw unfavorable claims development in the absenteeism portfolio, though we took measures of the result -- we took measures over there and resulting in margin expansions within this portfolio.

Let's now have a look at slide six, the Life segment. In Life, we saw a strong increase of operating result of 8.3 towards EUR340 million. This increase was mainly driven by an increase of the investment margin of 27 million. The increase of investment margin was driven by a number of factors. First of all, our direct investment income benefited from the re-risking we have done of the last year of the investment portfolio, for instance, we received 10 million more -- EUR10 million more dividends. Furthermore, as the individual Life book runs off, the results show a decline of required interest, which is positive for the investment margin as investment income remains relatively stable.

Generali Nederland had a contribution of 8 million mainly within the investment margin. We see most of the increase of the Life result as sustainable for the coming years. Please bear in mind that H1 is typically supported by dividends as I just have mentioned. Furthermore, we are pleased with the inflow, which we see in the so-called WerknemersPensioen. Currently 82% of the new business APE is for the new DC solution, which is very positive development, because it's all recurring premiums. The gross written premium of the Life segment increased towards EUR885 million, due to the increase of capital light gross written premium within pensions and the contribution of EUR54 of Generali Nederland. This positive development was slightly offset by experienced higher lapses in the individual Life portfolio.

Let's now turn to the other segments of ASR, which are gaining traction and that's on slide seven. Operating result of the bank and asset management showed a strong increase to 11 million. This was written by the launch of the mortgage fund and ESG funds which resulted in additional fee income from third parties for the asset manager and higher fee income from the real estate funds. Furthermore, the operating result of the bank increased mainly due to lower cost.

Operating result of the distribution and services segment increased with 20% to 12 million. This was driven by a strong contribution from Dutch ID and the contribution from the Generali Nederland distribution companies like ANAC which contributed almost EUR1 million. Holding results were slightly better. This was mainly driven by lower net current service cost due to our own pension scheme for amount of 1 million and lower incidental cost compared to last year.

Now let's move to slide eight to measure our performance against our targets. As said in my introduction, our performance has been strong on all key metrics in the first half of 2018. We've been able to keep our business momentum at a high level and our performance is better than our medium term targets. As you may know, 2018 is the final year of the medium-term target and will -- and we will present a new medium-term target at a Capital Markets Day in October this year.

Having said this, I would like to hand over to Chris for further details on our capital and solvency. Chris the floor is yours.

Chris Figee {BIO 18815839 <GO>}

Very good. Thank you very much Jos. Ladies and gentlemen please turn to page 10 where we start to talk about our solvency. Firstly, apologies for my voice. Fortunately, our solvency is better than my voice, still better than the other way around. But my voice keeps cracking out from time to time. So, bear with me.

Page 10 shows our book values, IFRS equities and Solvency II owned funds. And we see continued growth in book value is something we like. In the long run we appreciate that, the book values of our company whether measured from an IFRS perspective or a Solvency II perspective continue to grow. Grow slightly less than last year, grows on 1% to 2% mark year-on-year. Due to the fact in the first half year, we tend to pay our dividends. We acquired Generali in this first half year. And as you understand in financial markets, the valuation, the unrealized capital gains were bit less than last year. But in spite of dividends in the Generali acquisition, we continued to grow our book value. Interesting to note that the owned funds of our Group, including hybrids touched the 7 billion. That's not a specific goal itself, but it's fun to see that we've met 7 billion just before we paid interims. And the unrestricted Tier 1 level is on 5.4 billion.

Just a bit of background to our solvency levels. Then turn to page number 11 please on our solvency level. Solvency II 194% as per the standard formula. After payment of interim dividends, before interim dividend at 196. So business wise effectively our solvency stayed stable from the year end last year 196 to 30th of June this year of 196. And you take out the interim dividend, you get to 194. In the appendix E, you'll find more data and more intelligence on the development of the required capital. At this point safe to say that we feel strong and comfortable with the level and quality of solvency. Tier 1 is about 78% of our capital, the Tier 1 ratio alone would be 151%, and Tier 2 and Tier 3 headroom is 750 million, actually an increase from Q4 last year. ASR does not use Tier 3 capital, we do not have the DTA. We still have a net DTL position on our books.

LAC DT is stable 74 and our market risk is at 43%, leaving some room to re-risk our business. And it's fair to presume that depending on markets in H2 of this year, we will spend some of our capital on re-risking our business. So we feel that the strength have not widened to and around where they become attractive again. The equity market is stable, so expect -- but view some of that market risk will typically into support our earnings, not the entire 7%, but some point or so that we will spend on market risk.

So as far as we can see a solvency good from a level perspective and good from a quality perspective. Please move to page 12, on capital accretion. We continue to amass capital -- page 12 show the breakdown of the sources and uses of capital generating an accretion of 331 million or about 9% to 10% of our required capital. Then after repayment of 92 million of interim dividend, we get to the retention of capital of about 239 million or at 6% of our capital base. So 6% retention or 9% net accretion. That actually is the increase in the fungible and upstreamable and investable capital that we have. And as you are aware, we have a very strong and consistent capital spend framework, but at 240 million gives additional flexibility for our Group to invest.

Page number 13 is our alternative view or the most common view these days on capital generation. It's a solvency ratio movement. Let me give you some further details on this. On this page, you can see how we spent 9 percentage points on Generali acquisition from 196 to 187. So that actually is the base, you could use to start with to assess how our solvency moved through year. And we moved to 187 to 197, which is again the 9% to 10%, capital accretion that I explained in the previous page. In this page we have an operating capital accretion of 179 million or organic capital generation of 179 million. Slightly less than last year, but if you appreciate the fact that we this year had a significant store as well to absorb, the underlying capital generating ability of the Group actually gone up. I just explained the storm charge in H1 was 31 million in January, secondly, there was some water damage in May, last year we had no large claims in Q1.

So effectively, and our property and casualty business on a like-for-like basis we generated less capital last year, fully understandable it's a comparison thing large claims or it's a storm thing. If you adjust for the storm, you can actually see that the underlying organic capital generation is up. And if you dive deep into the sources of that increase of the structural improvement in capital generation, it is with a lower UFR unwind, which effectively counter by slightly higher hybrid cost, but it's higher excess spreads is lower cost and higher returns in our disability business.

So all in all, we feel comfortable with the organic capital generation 179 million, but structurally elevated versus last year. And also of course Generali starts to contribute to that level. Think about the 5 million to 7 million of cap gen, structural cap generation of the Generali business adds to this number.

And if you look at our OCC over the quarters, there's not much point in (inaudible) quarterly OCC, but in Q2 this year Q2 '18 versus Q2 '17, we already have 9 million higher OCC in the quarter, which confirms in a quarter where there is no storm and in normal claims pattern, this Group generates more capital than it is last year.

Finally to preempt any questions that are no doubt coming towards us, if we were to align the investment spread to the actual market rates, so instead of using our long-term investment assumption to market rate, the OCC would increase by about 7 million, so we aligned fixed income spreads, we aligned the VA, we add about 7 million and if we were to put our equity and fixed income with -- actually in real estate return let's say 7%, you could add another 60 million to the organic replicable capital generation. Now, again, that's not our policy but just for your perusal for your background, aligning to fixed income market rates at 7, aligning to 7% as an example for equities in real estate, (inaudible) 60 million. But that's for you to assess how you use it.

Overall we see 10% solvency accretion, out of which is 5% is organic, 3% paid out in dividends ending up with a virtually stable solvency ratio in spite of the acquisition of Generali, in spite of the lowering of the UFR. From our perspective tantamount to the ability of ASR to continue to amass capital.

Move to page 14 please, if you wish sensitivity of our ratio to the UFR. You can see the stock of our solvency with various UFR levels, the flow, the addition of our lower UFR unwind and the amount of owned funds, at this point in time the UFR is 4.05, we expect it to be dropping by 15 basis points a year. So by the year 2021 as far as you can see today, you're expected to drop to 3.6% at least according to the current market information. Roughly every 15 basis points drop of UFR cost us 3.5%, 3.6% of solvency, but adds about 5 million of lower UFR unwind per year. That was also the case in this year, this was the actual development in the UFR contribution and the UFR unwind. So we're 183%. We are very well able to absorb any lowering of the UFR if they come due.

Furthermore, please note the solvency at the UFR of 2.4, you may be aware of our more economic view of the UFR where we say that, economically speaking, you would like the UFR to reflect your investment income and use that as a more economically consistent solvency metric. The economic UFR will increase from 2.2 to 2.4, reflecting a higher investment income also in line with the IFRS results and operating result just reported in Life. I think the investment income is structurally higher than where it used to be adding 20 basis points to that long-term more economic view of our, which gives a Solvency II ratio at UFR of 2.4 of the 154% safely in north of 100 -- safely north of our risk-appetite 120.

And finally, if you were to calculate the Solvency ex-UFR and ex-VA, depending how you deal with tiering think about the number around 110%, 125% in terms of solvency ex-UFR, ex-VA. So, (inaudible) the impact of LPD [ph] measures on our solvency is very, very manageable and very, very well under control.

Moving then to page 15, which is our strong balance sheet. Balance sheet strong with ample financial flexibility. You can see again our solvency composition of 194%. Financial flexibility, again, there is no DTA, we only have a DTL on our balance sheet. Headroom has increased, so we can actually -- we have that sufficient financial flexibility, if you wanted to further strengthen our capital base.

Financial leverage is at 25%. I think if you did on a more like-for-like basis compared to industry norms and use it just for the share of accounting reserve that are not reflected in our book equity a more comparable number would be around low 20s. So both from a Solvency II perspective, as an IFRS perspective, this Group has financial, financial flexibility. Just confirm the interest cover, which is still at 12 times on basis of IFRS. If you had an high operating result, interest cover it would be 9.4 versus 10.2 last year.

So again, way we take the IFRS perspective or you take the operating results perspective, interest cover is stable to strong. A strong balance sheet with ample financial flexibility. And last but not least, our solvency and cash position, all in cash at the first half year is 229 million. Just to reiterate our holding cash policy, we do not strive, we do not strive to maximize cash at the holding. We believe for a company as ASR, one jurisdiction, one management team, one regulator, the cash is best placed at the operating entities. That is just the way we do things around here and the way we continue to do things around here.

So we were holding cash to cover, holding cost to cover hybrid cost and to cover dividends, not too much optimize a cash flow as a whole, we believe it's best served in the business where it supports our customers, where it yields an income. Holding cash at the Group 229 actually comparable to last year with 201, so up 28 from last year. 195 remittances, little details, little note here, the 195 is a net remittance, actually the gross remittance to the Group was 246. So, the upstream is 246 million out of our entity to the group, injected 51 million back into the Generali entities just after the acquisition, you know, to fund some re-risking of the Generali business, which gives the I95. So 246 was the upstream out of the traditional ASR businesses, which is equal, roughly equal to the 253 we up-streamed last year, we just injected cash back to the Generali, and when the Generali entities merged back into ASR Life and ASR P&C that cash showed up back into the ASR Life business. So it was small kind of, circa [ph] amount of cash to support the timely re-risking of the Generali balance sheet.

And again remittances exceeds our operating capital generation around 70% of the net operating profit. And finally, all our entities this year will contribute cash at holding, not just Life and P&C, but also for example, the asset manager, also for example distribution businesses are able and will be able to upstream cash. So in terms of cash, holding cash, we hope cash to support the operating businesses. And for that we keep the cash in the holdings or in the operating entities.

With that, I get you back to Jos, who is going to wrap up.

Jos Baeten {BIO 2036695 <GO>}

Thank you, Chris. And as said, to wrap up this call, I would like to conclude that we are very pleased with the strong set of results. We were able to match our records of operating result in the first half of 2017 despite the severe impact of the storm in January. Our businesses are all very well performing and that enables us to remain entrepreneurial. We have shown that we put our excess capital to work.

We are pleased with the progress of the integration of Generali Nederland, but also with its contribution to the operating result and the OCC of ASR. Before we open for Q&A, may I remind you of our Capital Markets Day, which will be hosted on the 10th of October, where we will provide a full update on -- of the strategy and the fresh new set of medium-term targets.

And with that, I would like to conclude this presentation and we are very happy to take any question that you might have.

Questions And Answers

Operator

Thank you. (Operator Instructions) We can now take our first question from Cor Kluis from ABN Bank. Please go ahead.

Q - Cor Kluis {BIO 3515446 <GO>}

Good morning. Cor Kluis, ABN AMRO, I have a couple of questions. First of all, about the (inaudible) Solvency II. Could you elaborate a little bit more on the category markets and operational developments, which is minus 53 million, and that includes of course the UFR effect of minus 93 million that which are the components are in that category? And related to that also the re-risking, what could be the effect of the -- on the solvency ratio of the re-risking in the second half of the year. And of course related to that the P&L effect of that, how much could it finance the profit, the profit stream. And as we are already in at the end of almost the end of the second month of the third quarter, could you give us a date on the Solvency II ratio developments in the third quarter especially given what's going on in the macro-environment. And the last question is about the bank and asset manager, which had quite strong results in the first half. Is this kind of a run-rate or was there something one-off in -- that's all my questions.

A - Chris Figee {BIO 18815839 <GO>}

Great, good Cor. Chris here. Thanks for your questions. I'll take them all for one by one. On the book, on market development, indeed it was minus 53. I mean, key driver of course was the UFR decline. Had it not been for the UFR decline, this thing would have been roughly 50 million positive. And the rest is really a collection of different bits and pieces, some pluses, some minuses.

On the positive side, you have an increase in the VA, that supports this bucket. We have some positive revaluations in real-estate especially. On the neutral to slightly negative side, we had impacts on equities in the first half year and to some, but lesser extent credit spreads widened. There were some tailwind from rate developments, especially on our DBO owned pension plan according to very specific IAS 19 modelling. And then there were modelling and assumptions changes in the Life best estimates. We increased our lapse rate assumption when we just talked about the Life business, we see a structurally elevated level of unnatural lapses, which has to do with a deleveraging cycle that's going through our country, clients are paying down their mortgages, lapsing policies.

It's slightly less than what it used to be last year, but we think the last level in Life is structurally elevated. We reflected that in our best estimates. And finally we made some modelling changes in our disability business and here it gets a bit tricky and a bit geeky. But for example, claims handling costs used to be classified as claims costs, we moved from claims to expenses and when you expense them, you had a capital charge for expense risk and NPV of the duration of the disability book is a bit higher. So we reserved more capital due to the reclassification of claims handling costs, which (inaudible), so nothing changed in the business. It just that charge for it goes up. By the way we got it pretty prudently, if you would go further that means the reclassification of expenses would also actually lead to a lower modelling of lapses, which should lead to a small release of lapse risk, which we haven't yet put through.

So in summary, a bunch of I'll say a very nitty-gritty almost geeky changes in modelling where we've taken a prudent approach. And that together drove a minus 90 -- minus 53, but again if it had not been for the UFR decline, it would have been 50 million plus.

On your second question, on the re-risking, I think it depends a bit on the market, when we commenced this year, we had a re-risking ambition. During the first half, we paused it, if you look at the developments in market, spreads that were widening, there's no point in re-risking while the markets are very jittery. Today with spreads widening, we think we can continue again. Think about up to five points of solvency. It depends a bit on how the market develops, but think of up to five solvency points that we can spend, we will continue on real estate. We're very comfortable on our real estate business. We'll continue on mortgages, I think we will pick up the tab again on credits where spreads have widened and there will be some room to buy an equity -- buy equities.

I think the return on solvency capital is today around 12% after diversification is our estimate since we got the direct yields that we're going to make on these investments after diversifications on this 5%. We think we can make 12% return on capital, which will again, gradually feed in, so that's not immediately it will feed in, if you reinvest the cash and it will gradually start to contribute to earnings. But at times the order of magnitude that we are looking at. Solvency II during the quarter is positive. Market was a little bit volatile. The VA widened a bit year-to-date. I think the VA is now around 12-ish point. So from where we are today, which is the 29th of August, solvency of the Group has probably moved up a few points.

But again, that's really the weekly lay of the land, the formal numbers I think will be done on a quarterly basis. But when I look at our weekly monitor, it shows a supportive development. And finally on the asset manager, indeed we're proud with a significant increase in earnings, significant increase in fee-based earnings. What I like a lot is that, both the asset manager and distribution business together are fee-based earnings are now at 23 million earnings. So they are on track to contribute for the full year at least one point of solvency, which is where we wanted, actually we'd like it to go further, but the fee-based earnings adds one point of solvency during the year from an OCC perspective.

I wouldn't double the number, I would be careful just to take, full year is twice half year. But we'll continue to see some growth in the asset management earnings.

Q - Cor Kluis {BIO 3515446 <GO>}

Okay. Helpful. And the 12% return coming back on your re-risking, you said around 20 million or something in extra profit stream pre-tax.

A - Jos Baeten {BIO 2036695 <GO>}

No, it's 75 million of required capital right, so that if you think about the current solvency is 194 which means 75 million required capital is about up to 5% of ratio impact. So again that 12% on the required capital is more like 10 million to 15 million.

Q - Cor Kluis {BIO 3515446 <GO>}

Okay. Okay. Useful.

A - Jos Baeten {BIO 2036695 <GO>}

It is also a numerator and denominator effect. If you spend 5% on the denominator, the total ratio you need to multiply by the ratio itself. So 5% is after the multiplication effect.

Q - Cor Kluis {BIO 3515446 <GO>}

Okay. Very clear. Thank you.

Operator

Thank you. Next question comes from Albert Ploegh from ING. Please go ahead.

Q - Albert Ploegh {BIO 3151309 <GO>}

Yes, good morning. Thank you for taking my questions. I have basically three. One is on the Life earnings, which it really were quite strong. In your opening remarks, you already mentioned and also couple of time not to double for the full year. I recognize the impact of the extra dividends in the first half, but adjusted for the different effects, can you then underlying basis say okay, the second half could then mirror the first half adjusted for the difference. So that's question one.

On the non-life premiums, which stripping out the acquisition impacts were still up I think around 4.5% organically, quite a strong performance. So I guess you clearly owning market share. I know in the past you alluded that you want to remain very disciplined in underwriting, but yet the low combined ratio give you some leeway to become also bit more aggressive on the market share. Is this basically a reflection of that and should we expect this to continue going forward as well?

And then the final question is a bit more related on accounting on IFRS 9 and 17. Competitor for yours disclosed that you made quite some upfront investment costs already for the implementation. Yeah, is there anything in the results of ASR already and what are your thoughts on the potential impact of IFRS 17? Thank you.

A - Jos Baeten {BIO 2036695 <GO>}

Thank you, Albert. I'll take the first two. Chris will answer the last one. On the Life earnings, yes, it's right that we said you shouldn't double it, and your assumption that if you take out the dividends and could you double it then, the answer is, yes. So, the assumption made by you that would be a fair way of looking at the Life earnings. And on your non-life, question the 4.5 percentage points of growth. We are very happy with that indeed. We however did not change our way of looking to risk. We still are running the Company value over volume. But within that, we have identified market parts where we are able to grow our business especially in packages, in individual packages for families. There we have seen significant growth and that is all within the strict criteria of accepting risks. And for example, in Q2, our combined ratio was at 96, which is below target. It's better than target, so we haven't changed our philosophy. And yes, we are growing in market share, but not at the price of getting sloppy on how we look at risk.

A - Chris Figee {BIO 18815839 <GO>}

Okay, Albert on your question on IFRS 9, IFRS 17, to be honest Albert, the mood in this Group is very cheerful this morning. But now as you're mentioning IFRS 9, and 17 it's darkening a bit, you know, we're repeating our (inaudible). In the first half year we spent about 3 million on IFRS 9, IFRS 17. So, it actually is a costly project. I think we're going to set this on 3 million, I think the second half we'll spend probably at least another three, probably more 5 million in the second half of the year. We'll try to keep our costs as low as possible, be as constrained as possible, that's kind of the realistic perspective on this.

Q - Albert Ploegh {BIO 3151309 <GO>}

Okay. And any thoughts on, let's say, actual implications of IFRS 17 or 9?

A - Jos Baeten {BIO 2036695 <GO>}

Again, many. Early days, I think we'll spend some time on this in our Capital Markets Day in October. Perhaps not then to the full extent because if we're all trying to read tea leaves here (Technical Difficulty) IFRS 9, IFRS 17 we postponed one year over two years. I mean, our honest perspective is, I wouldn't mind a small postponement, but not a lot. I mean, if we have to go through it rather close our eyes and work our way through it and just not continue to postpone it.

So one year would be good, more than two -- if you actually postpone it by more than two years, you'll find that the cumulative cost will go up, the more you take, the more you spend. But again, in the CMD we'll talk about, more about IFRS 17. We can give some first color on what it means, but it depends also a bit on what we get and what we learn on the timing from paper [ph].

Q - Albert Ploegh {BIO 3151309 <GO>}

Okay, thank you. Thank you very much.

Operator

Next question comes from Matthias De Wit from Kempen. Please go ahead.

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

Hi, good morning and thank you for taking the questions. The first one is on the Life business. You referred to the decline due to the acceleration of lapses linked to the mortgage prepayments. Just wonder if you could expand a bit on this. So, what are, for example, the like-for-like decline in reserves or number of policies. And is there any risk around that this could accelerate going forward to a level, for example, where it becomes more difficult to cover the costs? And then just linked to that, I remember you updated us once on the unit cost assumptions in the best estimate liability. Can you update us on these in light of everything what's happening in the Life business?

And then just secondly on the non-life business, can you provide the breakdown of the organic growth in the premiums to tweak pricing and volume, and is there anything you can say in general on the pricing environment you're currently observing in the non-life business? Thanks.

A - Chris Figee {BIO 18815839 <GO>}

All right. Matthias, on Life, the unexpected lapses, and the unexpected lapses were up. We said to ourselves, we think the book growth -- when we IPO-ed our business, we said our book will decline in terms of premiums, in terms of policies by about 9 to 10 -- 9 point a year on average. I think if we compare to our premium levels today, as to the IPO, which is now two years back, our premium level is about 5% less than what we expected at IPO, which is two years down the road. So actual expiration of Life polices were -- in terms of premium levels of 5% more than what we expected. So the unexpected lapses think about another two percentage points in a number of policies on number of premium level on an annual basis.

I'll give you some color on the order of magnitude. Now in terms of competent nuances, actually this level, the unexpected lapses peaked -- appeared to peak in Q3-Q4 last year. If we look at the unnatural lapses, the Q3, Q4 last year that really are high. Also in our mortgage business, we saw an increase then in mortgage redemption, since then, so today H1 '18 versus H2 '17, the unexpected lapses have dropped back by another 20 point -- 20%. Mortgage redemption has also dropped by another 7%.

So in the last two years, two percentage more decline in our premium levels per annum that we expected because of unexpected lapses, it's probably structurally at an elevated level, but calming down a bit after last year's deleveraging way, that's kind of second bumping.

Second observation is, this effect -- premiums effect number of policies, it effects much less our reserve base. So the reserve base in our Life entity declined by 2.5 percentage points a year. So you get to see lapses in terms of number of policies and lapses in terms of number of clients, but much smaller impact when it comes to the total reserve base, in terms of total asset base, which in the long run will have the consequence that our Life business becomes much more investment business. You can see a shift at the investment contribution to our Life earnings will gradually grow, the contribution from technical results will gradually fade away as the book declines. In the last half year, we have been able to keep the technical result stable, so components vary, but you have mortality and cost result were virtually unchanged for the last year. But in the longer term expected to decline -- expect the investment results to keep up for longer. So that's kind of some point on lapses.

Secondly on unit costs. So, the unit costs on Life has gone up a tiny bit, the cost per policy, simply because of this lapsing effect, we are reducing cost in the Life business, but when there is a peak lapse event, you can't just cut your cost as quickly as that. So our cost initiatives will continue to feed through. I would expect us to take additional cost initiatives in the coming years, that's something we're contemplating. We're moving as fast when it comes to the migration of policies. And then the integration of Generali for example at scale will ultimately lead to further improvement in the cost per policy.

So we're responding to this by cutting costs faster in the migration and doing scale deals like Generali where you take out much more cost. So the average cost policy goes down. When it comes to the unit cost assumption, our best estimates, we feel very comfortable that the assumptions in the best estimate today we can and will meet. So there is lowering lapses, we've had some -- has been reflected in our liabilities, but it's more on a best estimate side than in the cost element. So, and then when it comes to unit cost on best estimates, we feel comfortable in that area. Hope that answers your -- it's a lengthy answer, but it gives you some color on the lapse development.

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

Yeah. (Multiple Speakers) yeah, sorry, can I just very briefly follow up regarding, I know, correctly, you were assuming rising unit cost assumptions for both funeral, individual Life, and group Life, is that still the case or?

A - Chris Figee {BIO 18815839 <GO>}

Yeah up to a certain -- not eternally up to -- there some reason. So you can't -- in 2014 you defined all the cost on one policy. So there's gradual increase up to a certain point mitigated by long-term some varialization. But our cost assumptions in our best estimate, I would not see them as very aggressive in light of the book development.

A - Jos Baeten {BIO 2036695 <GO>}

On your last question, on Life, organic growth it was on average 4.5, all three businesses were able to meet that number. In P&C, it was mainly pure organic growth, roughly 4% out of the 4.5 was organic growth and 0.5% was due to price increases especially in car insurance. In the disability business, the pricing in the individual area remained stable. And out of the total growth of 4.5 disability, roughly 3% is due to a better market position and 2.5% is due to price increases especially in absenteeism that we have done over last year. And in health, there we also have seen some growth, there the total growth is due to premium increases that we did last year.

And on your second part of the question, pricing conditions in the market, we still see the continued hardening of prices, especially in P&C, the storm over the first -- in the first quarter has helped to stop thinking about lowering prices in the markets. So we think that is still a favorable development going forward. Same in disability, there is currently not a lot of downward pressure on the price level, so that's also good. And health we will have to see in the last quarter because health insurance, as you may know, Matthias, in the Netherlands is only a December a product where people can -- can make a new choice for their insurance company. So general pricing conditions still favorable in terms of better margins going forward.

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

Okay, very clear. Thanks a lot.

Operator

(Operator Instructions) Next question is from Farooq Hanif from Credit Suisse. Please go ahead.

Q - Farooq Hanif {BIO 4780978 <GO>}

Hi there guys, thank you very much. Could you comment again on your plans for internal model. I know it's a pain to do it. And you've talked about in the past, but it seems to me that, as you think about growing inorganically and given EIOPA et cetera, et cetera, it seems to be something that probably has gone up your agenda. So could you comment on operations for that. And on the debt capacity, is your kind of capacity numbers that you gave on slide 15, do they also work on a kind of rating agency framework, where you look at financial leverage and interest coverage ratio. So do you think you could raise that much debt and remain within tolerable levels? Thank you.

A - Chris Figee {BIO 18815839 <GO>}

Okay, hey Farooq it's Chris. On the internal model, couple of perspectives. As -- if you look at our solvency level today, standard formula, there is no immediate need or immediate benefit to go to an internal model. As you will say, we could report a higher number, but that would materially change the business. We of course continue to look at the EIOPA rules and regulations. I think, the recent consultation paper that they published is reasonable, although version 0.1 did get us -- the version 0.1 of the consolidation (inaudible) in December last year had some very inappropriate ideas on how to calculate solvency for a Dutch insurance company, luckily they didn't make that a final report. So the final report gives a solvency number that we still see as reasonably appropriate.

We are, of course, always on the look out for what it would mean and could mean, if you would move to an internal model. We've done some sketches and done some calculations on what it could mean, and what it would require. We need to be vigilant in understanding that today, the same people that would build the internal model would also be the same people that would built IFRS 17. So, you think very carefully about capacity planning where you could do in parallel.

And finally, when it comes to M&A, I can't imagine cases where internal model might very well, work very well in an inorganic growth situation. But that depends, of course on that very situation. So in summary, Farooq, not much news to add, there is no immediate obstacle to building an internal model. We need to be careful on capacity planning, I can see the uplift in the numbers from doing internal model. But we have to find a meaningful way to then use the proceeds from that model.

And it depends on how the external market develops and depends a bit on how EIOPA develops. When it comes to debt capacity, I go to slide 15. You asked question about the rating agencies and how they look at stuff. I think from a rating agency perspective, we of course would have room to lever the business. I think the capital redundancy from an S&P perspective, we're at a AAA level, whatever that could mean, but basically we're at AAA level. I think the formal upper limit for leverage in an S&P environment is 40%. And interest cover is between 4 times to 7 times. So with the current level we could actually add more debt within the current rating band. I think within the current rating band, I would think that we'll be pretty strong in the similar rating band that we have. But again, it also depends, what do you do with the debt. If you just raise money just for the heck of it, I don't think S&P will see the humour of that. If you take debt to make a meaningful acquisition, make an investment, you know, put the money to work, it could make sense.

So I think, at today's rate and today's balance sheet there is no constraints from either our own balance sheet or rating agency perspective.

Q - Farooq Hanif {BIO 4780978 <GO>}

Can I just come back on one thing, sorry, this is actually a third question. But just on the great development that you've had in bank and asset management and all of the fee-based businesses. What is your ability to grow further inorganically there. I mean, it seem the payback from what you've been doing has been great. So is that something that you are -- is constantly on the radar as well still?

A - Chris Figee {BIO 18815839 <GO>}

So Farooq maybe one more comment on your -- on the pieces on debt. It's not that we're just now about to got to massively do debt finance acquisitions, but we have the headroom to do it. It would also dependent on what you're actually doing with it. If you have a business -- suppose if you were to acquire a business completely debt free, it would make sense to buy the leverage, if you were to buy a business already has significant debt on the balance sheet, we definitely need to take into account in the funding mix. But I think what we have today is flexibility for multiple perspectives to optimize financing and then you have to take into account what you should do with the money.

When it comes to the asset manager, we're very pleased with the fee-based income, it's both in the real estate business and in the capital markets business where the fee has grown up. We've -- today we're looking at mostly organic growth opportunities, we are not at this point looking at massive inorganic opportunity in the asset management space. I think most asset management are fairly expensive and or not for sale. But if you bump into a more niche play or where you can continue on our buy and build strategy, yes, we definitely look at it.

So if you look at what we've done, we bought a small LDI specialist. We bought a specialist in (inaudible) for government institutions. We have invested money in buying a portfolio, warehousing then turning into a fund. Thinking more about those buy and build type of initiatives rather than pursuing a big standalone asset manger at current valuations.

Q - Farooq Hanif {BIO 4780978 <GO>}

Okay. Thank you very much. Thank you.

Operator

Next question comes from Robin van den Broek from Mediobanca. Please go ahead.

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

Yes. Good morning, everybody. Thank you for taking my questions. Sorry to going back on the bank asset management and distribution services. But last year you seemed to show quite a bit of seasonality on H2 versus H1. So I appreciate the comment you made before, but can you may explain why that seasonality is there just to give a little bit more of understanding what kind of number we should add to the second half of the year.

And the second question is on the economic UFR spreads and yields have moved up and down quite a bit over the last few years. And this is the first time you've basically changed your economic UFR. So just wondering why now and how often are you planning on doing this?

Third question is on M&A, I guess I won't ask too much about fees out specifically. But I was more wondering from an operational and financing point of view, I mean, you've been talking about M&A for quite a while, there's still lots of opportunity in the funeral market. And then in the non-life and in the Life market. So just wondering how would you prioritize M&A from an operational perspective, from a financing perspective, if you could elaborate on that a little bit that would be very, very handy. Thank you.

With operationally, I mean, basically integrating the asset, is it a binding constraint that you can only do one or can you do more at the same time basically.

A - Chris Figee {BIO 18815839 <GO>}

On the seasonality I'll pick -- I'll tell you a bit on the seasonality of the asset manager, Jos will take distribution business. On the asset manager, in principle, it's not that much seasonal, it depends on how your assets under management develop.

So I think, you see continued earnings growth in H2. I just wouldn't double it, simply because if you look at the pipeline of assets under management discussions we have, there are a number of significant potential assignments out there, but they need to fall, right, they need to close. And of course, the summer periods, you get new inflows in the months up to May and June then July and August is very few new managers [ph] are being assigned. So you have always this seasonality when money comes in. So there will be growth in the asset management fees, it's just not something you double because it depends on actually how the pattern of new inflows actually evolves.

A - Jos Baeten {BIO 2036695 <GO>}

And in distribution, distribution is commission business, for us the inflow is -- are commissions earned by the distribution company. And there it fully depends on how a portfolio looks like. If you, for example, have a portfolio only existing out of car insurance, and they came in constantly over a year, then there will not be a lot of seasonality. But traditionally, the first quarter and the last quarter, you see more commissions in distribution companies and in the second and in the third quarter, the level of commission is lower because people tend to go on vacation don't buy insurance. So it's fully depending on the portfolio of the distribution company. If (inaudible) for example is more in the P&C business, that's more through the year a consistent picture both our Group is more in disability and there it is more loaded in first quarter and last quarter.

That to the seasonality on distribution. Chris, on the economic UFR?

A - Chris Figee {BIO 18815839 <GO>}

Well, the economic -- the setting and determination of the economic UFR is actually quite an elaborate process. It's not that there two guys in a room (inaudible) let's take a number. We look at the actual returns we make on the investment portfolio and then we run an extensive monte carlo simulation. If we value our liabilities with this new UFR and we run 10,000 risk and return scenarios around it, what are -- and we just continue our policy, distribution policy that we have to date, what are the odds of us at some point missing our solvency level. So you stress it, you monte carlo simulate it with the UFR of 2.4 and then re-assess the annual and the underscoring probability.

That's how we do in the first quarter every year. So it's quite an elaborate process, it takes time. So we do it once a year, mostly around the end of the first quarter when the full year results are done, when the strategic asset allocation review has been done. That program is underway and implementing and that's when we do the annual economic UFR reassessment. So it's an annual thing done around March-April.

A - Jos Baeten {BIO 2036695 <GO>}

And on your last question, the M&A flexibility from a more operational point of view, I think Chris already elaborated a little bit on the room to maneuver that we do have financially it's depending on how the balance sheet of the company looks like, whether it is fully loaded with debt or not. Operationally, it depends on the type of business you acquire, for example, we already integrated the funeral portfolio of Generali. So, if we could do a funeral transaction tomorrow, the team in Enskede [ph] is ready to integrate such a portfolio because they are already done with the integration of all the funeral portfolios we acquired recently.

In non-life, we are in the middle of the integration of the portfolio of Generali, that should be done somewhere over the first quarter. So, that wouldn't withhold us from looking seriously at potential non-life portfolios. Same for disability.

In Life, it's more a matter of building a queue to integrate, to bring of portfolios to our software as a service platform. So that wouldn't withhold us from buying businesses if and when we could do a very good and responsible transaction. So in general, there is no operational reason for us at the moment for not looking at potential transactions in the area of the insurance business. Same for distribution, distribution companies are not integrated into ASR, we leave them alone and entrepreneurial so that wouldn't withhold us in that area. So in general, Robin, if and when there would be an opportunity, there wouldn't be a lot of operational reasons not to look at it. Having said that, let's assume there starts a process tomorrow, it normally takes three to four months to get a signature, then you need two to four months to close a transaction. So any integration would start as from mid next year.

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

Okay, that's very helpful. Maybe Chris one follow-up on the economic UFR. I mean, I guess it's some sort of game between stock and flow, but is there any implication connected to the fact that you've raised it on how you look at M&A as well or is it irrelevant?

A - Chris Figee {BIO 18815839 <GO>}

No, it's not linked to M&A, it's more -- it gives you more feeling our -- well, in essence, it gives you some feeling on our capital capacity right. If the UFR move from 2.2 to 2.4 from our perspective, we believe that if you compare that number 154 to say 120, there is a good 30 percentage points of capital that is actually, you know, not immediately needed to run the business. From that perspective, it gives you more feeling on our capital strength and on our investment thought.

But it's less, it's not so much -- it's not given by (Technical Difficulty) we did it once a year, we run the numbers, we tested and out comes the economic UFR and this which then drives, and gives you feeling of our distribution or investment capacity. It's not -- but it's not that mean, it's that comes first and how we spend it comes later, it's not that the spending plan comes first and then (inaudible) how we're going to make up UFR that fits this plan. That's not the way we work.

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

That's very clear. Thanks.

Operator

Next question comes from Andrew Baker from Citi. Please go ahead.

Q - Andrew Baker {BIO 20402705 <GO>}

Hi, thank you for taking my questions. Just two questions please. First is on the individual Life systems. I know you converted two in this period to the software as a service platform. Can you just remind me how many are left in the queue and what the approximate timing and size of these conversions are? And if there's any reason to believe that cost savings associated with the two systems in this period would be materially higher or lower versus the other systems in the queue?

And then secondly, you touched on the EIOPA changes or proposed changes for the standard formula briefly. You are in a position where you are able to give any potential impacts to your ratio at this point? Thank you.

A - Jos Baeten {BIO 2036695 <GO>}

On the individual Life systems, the software as a service system, Andrew, is a system which we don't own. So we only pay the variable cost per policy. There are two in the queue currently, one of that is a portfolio of our own and the other one is the Generali portfolio. And they should both be done before the end of next year and then we might be able to shut down some of the existing systems where -- which are all based on fixed cost and that would be a next jump in lowering the cost in our Life business. But that's all projected in our targets to lower the cost according to the less -- the decrease of the portfolio. So that's already in the plan, those lower costs.

A - Chris Figee {BIO 18815839 <GO>}

Yeah, on the EIOPA review of the standard formula, Andrew. If you go through the entire report, which I hope you do not do, but if you were to do it, (Technical Difficulty) we could be affected or it could impact us, which is the capital charge for rate risk, which is government guaranteed mortgages and which is LAC DT. On rate risk, that could be a small negative for us, the existing standard model does not allow for negative rates and the new model actually does allow for negative rates, which makes all the sense in the world. That will feature in over time, there will be a small negative, in the past six months, we actually did tighten our rate exposure a bit, we reduced our interest rate exposure. So the impact of this change is a function on your interest rate exposure, anyway, how much you're lower or negative rate assumption could affect you, it's going to be a small negative, but not, not a huge amount because through rate management you can actually manage a lot of this.

Secondly, the new EIOPA regulation do actually recognize government guaranteed elements in mortgages, that will reduce the counterparty default element of your mortgage book, that's a small positive. And finally, there is a LAC DT, to-date our LAC DT does not require any future fiscal profits to substantiate our LAC DT. Our LAC DT is fully build up, current year profits and DTLs (inaudible) of the risk margin. So pure future profit are not in there. And the way I interpret the EIOPA documentation is, that actually there is some more room to include future profits under certain conditions as substantiation for your LAC DT, so it could give some upside to your LAC DT, if you were to use that component as well to substantiate and underpin your LAC DT assumption.

To-date, we haven't done that yet. The net of all those three components, I would guess it's a neutral, possibly a small positive, depending on how far you want to go in your LAC DT assumption. So far we've been quite conservative on LAC DT and our -- the way we substantiated. So, depending on how far you want to stretch yourself in that field, it's a neutral to possibly a small positive given the fact that the tightening of our interest rate hedge. And if you reduce (Technical Difficulty) small rate shock.

Q - Andrew Baker {BIO 20402705 <GO>}

Very clear. Thank you.

Operator

Last question comes from Ashik Musaddi from JPMorgan. Please go ahead.

Q - Ashik Musaddi {BIO 15847584 <GO>}

Hi, good morning, Baeten and Chris. I have three questions, if I may. So first of all, I mean, if I read the press release and your presentation, it looks like you're talking about re-risking your assets versus full year '17. But then if I look at one of the slides, which is where you had shown the market move -- the SCR movement, slide number 26. So that says that market risk is going down by 63 million in the SCR, so, you re-risked your assets, you have acquired Generali's asset portfolio, so that should have bought some market risk. But as this slide shows, market risk has gone down. So what am I missing because this slide shows that spread risk has actually decreased whereas you have moved more into corporate bonds.

So that's one question. The second question is, I may have misheard it, but you mentioned that your Solvency II ex-UFR is 154 and if we ex-out VA, it's somewhere in 110% and 125%. So that looks like your VA benefit is north of 30 points, that number doesn't sound -- doesn't make a lot of sense to me, because if I look at your sensitivity, you have always given that one point VA is equal to one point of solvency. VA at the moment is like 10, 12 points. So is that understanding correct or I misheard something when you mentioned ex-UFR ex-VA number.

And the third thing is, can we get some clarity as to your IFRS numbers and Solvency II capital generation is diverging a bit. For past two years as well and this half as well your Solvency II capital generation dropped by 7% year-on-year whereas your IFRS earnings was only down 1%. And in past two years as well that similar trend has been visible 2017 versus 2015. So, any thoughts on these three questions would be very helpful. Thanks.

A - Chris Figee {BIO 18815839 <GO>}

Yeah, Ashik, it's Chris, I think you referred to page 26, in these you can see our market risk down by 63. That market risk reduction actually is a result of various moving parts. In the first half year, real-estate risk was up a tiny bit, equities is virtually stable in a portfolio, spread risk was down slightly not because we declined our corporate bond portfolio, but we shortened the duration of our corporate bonds. So, (inaudible) was down. So, it was the duration of credit spreads rather than credit spread as such. But the main driver of the reduction in market risk was a limitation on the rate exposure on rate risk because we felt that actually the expected return on an open interest rate position is very small and given today's rate and market environment, we felt it was again not very useful to run some rate risk. So we have to reduce our rate risk, that interest rate risk component that was the key driver behind market risk.

If you net for that, market risk would actually have gone up during the first half. And so, the re-risking we're proposing to date will be as of (Technical Difficulty) solvency for today. So in the first half, market risk X rates went up tiny bit. It was net negative due to interest rate risk charge. And (Technical Difficulty) will go up again. But that will be of a classical (inaudible) credit equity and some on mortgages.

Q - Ashik Musaddi {BIO 15847584 <GO>}

Sorry, just a follow-up on that, I mean, sorry, just a follow up on that, you're mentioning that you're shortening the duration of credit and you are taking hedges on interest rate. So how does that stack up with your duration matching or cash flow matching year-on-year. Is that not getting changed because it's, I mean, I think, last year as well, you mentioned that you have shortened the duration of your sovereign bonds. So if you keep on shortening your duration, does that match with your cash flow profile or duration?

A - Chris Figee {BIO 18815839 <GO>}

No, because we also have a significant derivatives program. So, the interest rate management is a function of corporate bond, swaps and swaption. So it's a mix of the thing that works. So we've tightened the interest rate risk on a total holistic basis in that we shortened corporate credit to some extent, we swapped some traditional (inaudible) even for Italian government bonds post the spread widening. And we -- and there's a swap at swaptions portfolio that is still the rounding to make sure the total interest rate risk is where it is. But we felt at this point, in the first half year, that was more basically, slightly less duration credit plus more elongated swaps than the other way around.

Q - Ashik Musaddi {BIO 15847584 <GO>}

Okay.

A - Chris Figee {BIO 18815839 <GO>}

And on the UFR, you've slightly misunderstood me. Our apologies for that. I think the solvency of UFR of 2.4 is 154 right. That is it's not UFR of zero, but UFR of 2.4 is 154. Our VA effect is around 10, where one point of VA is one point solvency effect. So if you were look at our solvency ex-VA, you would move from 194 to 180, 184. The solvency ex-VA and ex-UFR is 113 to 127 to be very precise, depending a bit on whether you -- if you take a simple UFR out, you get to 127, if you (inaudible) also take a hit for less tiering risk. If the UFR would be taken out completely, you would have a tiering issue like most of us have today. If you adjust for the tiering, you move to 113. So to recap, solvency 194, solvency ex-VA 184, ex-VA ex-UFR 127. And if we then take the harshest view on tiering, assuming that there would be mechanical consequences for tiering, I get to 113. So and with the UFR of 2.4, is 154%.

Q - Ashik Musaddi {BIO 15847584 <GO>}

Yeah. Got it. That's clear. Thank you.

Operator

That concludes the question --

A - Jos Baeten {BIO 2036695 <GO>}

And the third question on IFRS.

A - Chris Figee {BIO 18815839 <GO>}

Sorry, Ashik on your third question, I think there are various parts. I think that gap between (inaudible) on operating result and solvency cap generation is practical [ph] shadow accounting. Shadow accounting results do contribute to operating result or the release of the capital gains reserve, thus contribute to the operating result, but does not contribute to our solvency. And a cap gen release was effectively stable versus down 6 million in the first half year, effectively stable.

When it comes to headline IFRS numbers, I think therefore we move more in sync, there you see slightly less capital gains than we had last year and a good contribution to the Generali social plan cost just on the reorganization of Generali.

Q - Ashik Musaddi {BIO 15847584 <GO>}

Okay. That's very clear. Thank you.

Operator

Thank you. That concludes today's questions. I will now turn back to the host for any additional or closing remarks.

A - Jos Baeten {BIO 2036695 <GO>}

Well, thank you. Hopefully this call was helpful to answer all your questions. We were happy to do so. We look forward to meet you all at our Capital Markets Day at the 7th of October. And in the meantime, we continue to deliver on our medium term targets and we are confident that we will be able to continue to deliver in a way as we have done it until today. So thank you all and I wish you all a very good day.

Operator

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