Q1 2018 Sales and Revenue Call - Activity Indicators

Company Participants

- Andrew Wallace-Barnett, Head-Investor Relations
- Gérald Harlin, Group Deputy Chief Executive Officer and Group Chief Financial Officer

Other Participants

- Andrew J. Crean, Analyst
- Andrew Sinclair, Analyst
- Colm Kelly, Analyst
- Farooq Hanif, Analyst
- James A. Shuck, Analyst
- Johnny Vo, Analyst
- Mark Cathcart, Analyst
- Michael Huttner, Analyst
- Nick Holmes, Analyst
- Oliver Steel, Analyst
- Peter D. Eliot, Analyst
- Pierre Chedeville, Analyst

MANAGEMENT DISCUSSION SECTION

Andrew Wallace-Barnett {BIO 18671460 <GO>}

Okay. Good morning, everybody. This is Andrew. Welcome to the AXA Conference Call on our Activity Indicators for the First Quarter of 2018. I'm pleased to welcome Gérald Harlin, Deputy CEO and Group CFO of AXA, who will be taking you through the highlights of the first quarter, and be very happy afterwards to take your questions.

Gérald, I hand over to you.

Gérald Harlin

Thank you, Andrew. So, hello and good morning to all. Thanks a lot for joining this call. AXA has delivered strong operating performance in the first quarter of 2018. We are growing out of line with total gross revenues growing by 2% at the group level. Our APE was up 5% and our NBV was also up 5%.

This overall growth was supported by a continued focus towards our preferred segment, Health revenues were up 7%, with growth in all geographies. Protection APE was up 9% and P&C Commercial lines revenues were up 2%. We also reported a Solvency II increase of 16 points from full-year 2017 to 221%.

Let me now take you into the details of each of our geographies and starting first with AXA France. AXA France had an excellent first quarter with revenues increasing by 8%. APE was up 20% from higher sales across product lines with particularly strong growth in Health, plus 39%, coming from growth in both Individual and International Group business.

Protection was up 11% from strong sales in Group Protection business and Unit-Linked plus 7%. The Unit-Linked share of Individual Savings business was 43% as compared to French market at 33%. In P&C, we saw growth in Commercial lines, but continue to face tough market competition in personal lines, particularly in Motor.

In Europe now, total revenues grew by 1% as we continue to see the successful business repositioning towards better segments. APE in Europe increased by 9% with strong growth in Protection plus 17% and Unit-Linked 32%. The Protection APE in Europe growth was mainly driven by higher sales of semi-autonomous solution in Switzerland, in line with our strategy. With the transformation of our inforce book announced last month, we will become the largest provider of semi-autonomous solution for SMEs in Switzerland.

Unit-Linked APE growth in Europe was driven by Italy following a continued recovery in AXA MPS and strong sales in agency channel and by Spain due to the repositioning away from G/A Savings towards Unit-Linked. P&C revenues in Europe increased by 2% and Health revenues increased by 3%.

Moving now to Asia, we continued our focus on improving businesses in China moving away from short-term single premium products and towards regular premium, represented in a 45% decline in APE for China contributing significantly to the overall increase in NBV margin for Asia increasing 4 points to 62%. Indeed, the NBV margin in China went up from 27% to 56%.

In Japan, APE grow by 4%, driven by the launch of the new Protection product. And in the rest of Asia, APE was 7% with growth in all country. The Philippines and Indonesia were up 37% and 9%, respectively, driven by growth in Protection. Thailand was up 6% from a higher Unit-Linked sales and Hong Kong was up 3%, with the successful launch of the new G/A Savings product and higher Health sales.

In the U.S., Life & Savings APE was up 3% from higher Mutual Funds advisory sales, partly offset by non-repeat of the 1Q 2017 strong sales of non-GMxB Variable Annuity in anticipation of the implementation of the U.S. Department of Labor rule. APE revenues were up by 13%, with higher average AUM, mainly due to positive market developments in 2017 and improved business mix.

In International, revenues were up 3%, mainly driven by a good performance in Health, especially in Mexico. In AXA IM, revenues were up 1%, linked to higher average assets under management. We also had strong net inflows in our AXA IM Asian JVs and third-party clients amounting to €7 billion.

Now, moving on to Solvency II ratio which, as I mentioned earlier, was up 16 points. This increase was driven by three main factors: strong operating return net of accrued dividends; second, a €2 billion Tier 2 debt issuance in March to finance part of the XL acquisition, plus 7 points, and last, management action to reduce equity market risk around 8 points. This is partly offset by EIOPA changes in UFR and on the reference portfolio weights for the volatility adjuster. At 221%, the group is in a very strong position.

So, to conclude, a strong quarter with top-line growth for group, an excellent quarter in France, continued growth and shift in business mix in Europe and in Asia and net inflows in AXA IM, all this with a very strong capital position and Solvency II ratio at 221%.

So, I'm now ready to take your question.

Q&A

Operator

Ladies and gentlemen, we're entering the question-and-answer session. We have a first question from Mr. Peter Eliot from Kepler Cheuvreux. Sir, please go ahead.

Q - Peter D. Eliot {BIO 7556214 <GO>}

Thank you very much. I had two questions on the Solvency, please. I guess the first one the ratio came in quite a distance ahead of all of our expectations. So, I was wondering if you could just talk us through the drivers, quantify the drivers in a bit more detail. And you gave the 7 points from the debt issuance and the 8 points from the de-risking, but I was wondering if you could quantify the other moving parts, in particular, the operating profit. And I mean given that you've guided for 3 percentage points on the UFR drag I'm guessing that was maybe a bit lighter and maybe we can expect a lower drag in future years as well.

Secondly, at the full year results, you indicated that there was a link between the position you were within your Solvency target range and the position you were in the payout ratio range. I'm just wondering if you can comment on whether there's any reasons behind the recent jump in Solvency ratio or, indeed, the announcement to the XL Group acquisition which might change our perception of that link. Thank you very much.

A - Gérald Harlin

Okay, Peter. So, first of all, so let me go through the 16-point increase in Solvency II ratio. So, first, we have a strong operating return. You remember that we told you that we were expecting between 15 and 20 points. And here, obviously, we are at the high end of the range, at 20% equivalent. So, that's on a yearly basis. Second, the €2 billion Tier 2 debt issuance. You notice that on the 5 of March when we announced the XL acquisition, we said that we would raise €3 billion of Tier 2 debt. We did already €2 billion under excellent conditions because we did it at 3.25% pre-tax which means that the cost post-tax will be 2% only. Then we have some management action to reduce our equity rates, which led to 8-point positive impact.

Maybe a few words about this. You know that we constantly seek to optimize the return on SCR. So, indeed, we reduced our exposure to equitable derivatives by purchasing put options. We captured the benefit from the relatively low level of volatility while we retain the upward equity movement. So, that's mainly the reason why we did it. And, as you know, we have 44% of equity exposure, which is roughly €22 billion, and we did it on roughly 20% of our portfolio. So, that answer your first question.

The second is the Solvency target range. So, it's quite obvious that we are at the top end of the target range, but you can imagine that the acquisition of XL will put us back, I would say, comfortably within the 190% to 200%. So, I'm quite comfortable to say that we will be within this range. Whether it change something on the payout ratio, there is no direct link with our payout ratio but I remind you that our payout ratio will move from 48% to 49% this year. And we are not at the tip of the range because the range still remains between 45% and 55%.

Q - Peter D. Eliot {BIO 7556214 <GO>}

Thanks so much. Maybe just to come back quickly on the first question, I was just wondering if you could comment on that the UFR drag in particular and what we should expect going forward. And also the 20 points you mentioned, I mean, I'm just assuming that translates into 2.5 points of net for the quarter.

A - Gérald Harlin

Yes, agreed. That's roughly 2.5% net. About UFR, we have a reduction of 15 basis points, which means that we are moving to 4% or 5%. And the UFR represents roughly minus 2 points in term of Solvency. And you know also that we have the recurrent portfolio. You know that the recurrent portfolio – that is used in order to calculate the volatility adjuster. It's on a recurring basis it's reviewed and we had a negative impact of minus 3 points.

Q - Peter D. Eliot {BIO 7556214 <GO>}

Okay. Thank you very much.

Operator

Okay. Next question from Farooq Hanif from Credit Suisse. Sir, please go ahead.

Q - Farooq Hanif {BIO 4780978 <GO>}

Hi, there. Good morning. I just want to go back to your comment about being comfortable about the 190% to 200% range post the XL deal. So, when you first set that target, presumably you didn't know what the impact of equity hedging would be. So, you're 8 points better on that basis following the hedging. So, when you say comfortably, does that really imply that you're bullish about the range? That's my sort of questions to your comment. Second point is, are there any major earnings implications of the equity de-risking that you've done? And third question is – actually, I forgot the third question, just those two. Thanks.

A - Gérald Harlin

Okay. So, Farooq, about your first question, you know that taking into – first of all, it's a measure that has been taken – this hedging has been taken just in line with the present market condition. So, first of all, we consider that whatever happen, it's sound capital management. At the time we announced the deal, at the beginning of March, we knew that we would make some equity hedges because it made a lot of sense in term of capital management.

So, you cannot consider that it's 8 points on top. And so, you can expect, we will be within the range, 190% to 200%, which is a quite sound range, meaning that I remind you that, at the end of 2016, we were at 197%. So, that means that we remain – at the very strong we will remain with this transaction. And taking into account the IPO of the U.S. business, we will be at a very strong Solvency level.

You said the question about the impact of this hedging on earnings. I just would like to remind you that we ended up 2017 with a quite strong level of equity and realized gains because we were at a level of €2.5 billion, so meaning that – and that's also the reason why it made a lot of sense to move in this direction because for a limited cost, again, it's an excellent return on capital.

So, no problem because you know that we are realizing some capital gains. I don't expect that realization of capital gains will be lower due to this hedging, not at all. And so, that's why, again, it's a good use of good management of capital.

Q - Farooq Hanif {BIO 4780978 <GO>}

Okay. Thank you very much.

Operator

Okay. Next question from Andrew Sinclair from Bank of America Merrill Lynch. Sir, go ahead.

Q - Andrew Sinclair {BIO 17749036 <GO>}

Thanks. Morning, everyone. Just wondering if you could give us – I just have three questions. Firstly, Asia sales look maybe a little bit weaker than expected this quarter. Hong Kong Protection sales, in particular, down 25% year-on-year, seemed a little bit disappointing, just wonder if you can let us know what's happened here.

Secondly, I just wonder if you could give us an update on thoughts on recent DOL development which looked somewhat more positive for the industry. And thirdly, just wondered if you're able to give any commentary on XL's results. In particular, the shift in portfolio mix, increased use of over (00:16:19) reinsurance on XL's reinsurance segment is not kind of in line of what AXA is proposing to do going forwards. Thanks.

A - Gérald Harlin

Okay. So, what I can say about Hong Kong, so that means that as far as Hong Kong, as you can see in the document in the Appendix, APE in Hong Kong grew by 3%. So, we had the plus 15% in Health which is quite good, and we did it mostly on group contract which is absolutely in line with our strategy. At the same time, in Protection, we had some declines that – no specific worry on this time. So, that means that we have the business mix where we did more – less Protection, more Health this quarter. By definition, it has an impact on the NBV margin, but at the same time, I should remind you that we still have a very solid and high NBV margin at 44% in Hong Kong.

So, it's quite obvious that we have a competitive market over there. But you remember that we have to do the right balance to strike the right balance between volume and profitability. We had a very strong profitability at level around 60% up to now and especially last year. We are back at the level of 40%, 44% which we consider this good and which allows us to be positive and you can expect us to still remain in positive territory in Hong Kong this year. So, that's for your first question.

About the second one, about DOL. So, I believe that if I could say the situation in the U.S., that we have an APE growth of 3%, but still the APE growth would have been higher if the reference wouldn't be Q1. Last year, why? Because in Q1 last year, it was just before the DOL and, at that time, we had strong sales in anticipation for DOL. So, that means – and to answer more precisely your question, so that means that the underlying trend is above 3%, which is good.

And second, it means that, indeed, the DOL impacts are quite good with the reference events, which means that the DOL impact will be much weaker than what we could fear some time ago. About XL and XL's...

Q - Andrew Sinclair {BIO 17749036 <GO>}

Sorry, Gérald, just before you move on, I was more looking for a commentary on the announcements over the last few weeks from regulators and government in the U.S. suggesting maybe DOL was being rolled back to some extent. I just wondered if you could give any thoughts on that.

A - Gérald Harlin

Well, I believe that I cannot be more precise. It's a good decision. It's should be a good outcome. But I don't want to anticipate it. That's only my point. So, yes, it's good. So, it's upside for us. But how far it will translate, how quickly it will translate into our figures, I cannot be more precise. That's the limit. But, yes, it goes in the right direction. But I don't want to oversell it, and that's why let's wait. But it's good for the U.S. business. And at the time we do the IPO, it's a good news.

Q - Andrew Sinclair {BIO 17749036 <GO>}

Sure.

A - Gérald Harlin

Okay. So, about XL. So, I would say that XL, first of all, I would like to say that we are legally constrained in what we can publicly discuss about XL. You know that you can refer to their press release and their earnings deck. What I can tell you is that they published solid Q1 results, and they were in line with their expectations. So, I would say no surprise. What I could say that top line, top line grew at constant FX by 4%, which is a good news.

It's partly supported – and this is important. It's partly supported by an increase in both insurance and reinsurance, plus 3.3% increase in rates in insurance, plus 4.3% increase in rates in reinsurance. I just would like to add one technical point. So, the effect of price increase on earnings could not be visible in Q1. Why? Because you know that the earnings are coming from earned premium. And so, that means that it will take time before this rate increase will flow into the earnings, but that's a good news.

Second, I could say that the management of XL is taking some strategic initiatives to shift the portfolio mix toward lower volatility and then move to higher-cap protection. This was absolutely in line with what they announced. And I would say that, just to conclude that – from their press release, significant improvement. You saw a significant improvement in the operating net income in Q1. And, again, it was in line with the management expectation. So that's what I can tell you, so it's no surprise, I would say.

Q - Andrew Sinclair {BIO 17749036 <GO>}

Thanks,

Operator

Okay. Next question from Mr. Nick Holmes from Société Générale. Sir, please go ahead.

Q - Nick Holmes {BIO 3387435 <GO>}

Hi there. Thank you very much. Just one question. I wondered how concerned are you about the French banks saying that they want to write more P&C business in France. Is this much of a threat? Thank you.

A - Gérald Harlin

Hello, Nick. Good morning. So, I would say that it's not new. So, we have a quite competitive environment, and you can see it in the press release. In Motor in France, we had some positive price increases. Nevertheless, in Personal Motor, we were at minus 4%. So, yes, there is a competitive environment. I believe and I don't expect that we will stay at such a level of minus 4% and we are taking some measures in order – and it's not a decrease in our profitability. It's more segmentation, some incentive that could be given to the sales force, which means that we can expect to have an improvement in the course of the year.

But, nevertheless, it's obvious (00:24:04) we have more competition in France. At the same time I remind you that we have a strong and a good and sound profitability throughout P&C in France whatever the products, including Motor and Individual Motor, which means that – and which is not the case of the whole market. I remind you that the whole market is far above 100 (00:24:28), which is not our case. So, nevertheless, in the end, I'm quite happy and proud with the global group plus 2% revenue, which means that we can be extremely profitable going on improving our profitability while growing the top line.

Q - Nick Holmes {BIO 3387435 <GO>}

That's very clear. Thank you very much.

Operator

Thank you. So, next question from Oliver Steel from Deutsche Bank. Sir, please go ahead.

Q - Oliver Steel {BIO 6068696 <GO>}

Morning. Thank you for taking the call. I have three questions. The first is just coming back to the equity hedging. I mean, you said that it was a reaction to present market conditions. How long is the hedging actually in place for? And perhaps linked to that, you could give us the new equity sensitivity both upwards and downwards on your Solvency.

Secondly, I mean you produced some extremely good growth numbers in the French Life & Savings business and Health. How much of that – I mean that feels as if it's a bit of a sea change relative to – I mean even some pretty good numbers last year. I'm just wondering how sustainable those sort of growth numbers are.

And then, the third question because I didn't talk to you at the time. You released or you're going to release something like €2.5 billion of capital, I think, from the Swiss Life business. But I think you've also released an equivalent amount of reserves and I'm just wondering what the net Solvency effect will be from that at the group level.

A - Gérald Harlin

Okay. Good morning, Oliver. So, first, how long – your first question is the equity hedging, how long. So, what we did is we did it quite long, two years, equity hedging. Why two years? Because in order to benefit from the Solvency, we should have quite some visibility and we should have at least a one year visibility in order to have the full benefit in term of Solvency.

So, to make it clear, it's more rational to do long-term hedging. What's the new equity sensitivity? We can calculate it. I'd give you just a quick guideline. As I told you, we hedge 20% and it's 20% which had been hedged at – so that means that you could imagine that, more or less, you can reduce by 20% the sensitivity, so maybe slightly higher, but that's what you can keep as a good guideline.

The French – your second question was about the French Life & Savings. So, yes, we had a very good start with some contracts and some good contracts – international contracts in Health. It's a good start. We still are expecting to have a strong growth this year in France. Nevertheless, I just noticed – and sorry to make this digression, Oliver, but I just wanted to highlight one point. On the APE side, we are posting plus 5%, okay? But look at China, if I exclude China, we would have been at plus 8%, which confirms this very strong start and the strong expectation. And it's not a new strong start. We hope that this year will be good in term of Life growth.

As far as Swiss business is concerned, yes, that's what we announced. And we announced on April 10 that we would release CHF 2.5 billion of capital over three years. And this is linked to the Swiss Solvency test. So, it means that the Swiss Solvency test, as you know, is much tougher than the Solvency II test, which means that the global group Solvency in term of Solvency II might be 1%, something like this. So, it will be much smaller. But in term of capital and cash, we'll effectively – we'll collect and it will be good for the remittance ratio. We get CHF 2.5 billion which will be upstreamed to the holding company.

Q - Oliver Steel {BIO 6068696 <GO>}

Okay. Thank you very much.

Operator

Next question from Andrew Crean from Autonomous. Sir, go ahead.

Q - Andrew J. Crean {BIO 16513202 <GO>}

Good morning, Gérald. A couple of questions and a request. Just going back on the de-risking, do you intend to do more than 20% of the XL portfolio at some point in time? And after two years, I assume you would intend to reload.

Then secondly, on the Personal Lines pricing. I see just over a year ago, Personal Lines rates were rising about 4% and now rising about only 1%. Do you think that has implications for your profitability? I.e., do you hope to maintain average claims growing by only 1%?

And then a request. Given the multi-actions you've taken both in XL and the IPO of the U.S. business, would you, at some point in time, be able to give us a sort of pro forma balance sheet, so that we can work out the tangible equity moves and the impact on debt guarantees (00:30:39)? It's quite difficult to do from the outside.

A - Gérald Harlin

Okay. Andrew, let's start with the de-risking. So, do we have an intention to do more? Not today. So, that means that we consider that it's a good level, and we presently don't have our intention. It doesn't mean that we could not change our minds, because it depends, of course, on the economic condition. It depends also on the cost of volatility, as you can imagine.

Your question, which is good, do you intend to reload at the end of the two years? It will depend on the equity markets. But, roughly speaking, what guided me in this decision was just to say that we had the strong growth of the equity market over the last years and it was a way to secure part of the capital gains while being extremely effective in term of capital management. But that's an old (31:55) pricing. Again, I see your point. And does it mean that we will reduce our profitability? No. It's not our intention and that's the reason why we were in France to – when we were at minus 4% in term of top line for Individual Motor at the beginning of the year.

We don't intend to reduce our profitability. And we don't believe because you know what – I remind you that we have some objectives in term of – at the end of our plan in term of combined ratio to be between 94% and 95% and we stick to it. So, we could, from time to time, adjust the top line because we have to keep a certain level of profitability. But the price increases is not the only driver because we have also the claims management and we have also fraud and all different drivers that we can use in order fighting fraud, leakage and so on that we can use in order to keep a strong profitability, so, no worry on that side.

Your last question, first of all, I just would like to because I take this opportunity. You all read that we intend to launch a Mandatory Exchangeable. That was what we announced last week. And this Mandatory Exchangeable, some of you believe that it would be considered as a debt. Indeed, it's a bit technical, but the net present value of the future interest rates that will be paid will be considered as a debt, but the principal will be in minority interest. And that's (00:33:53) because it's mandatory. So, it's not convertible at the option of the holder. It's mandatory redeemable bond, redeemable into share, into AXA equitable holding share. So that's the first point.

Second point, at what time we will – I believe that we will wait. Let's wait for the events next week. We should have the pricing of the IPO. But as soon as feasible, of course, we will update you with some elements, so that you could have a sound view of our balance sheet and of our debt gearing. So, it will be an update of what we presented on the 5 of March.

Q - Andrew J. Crean {BIO 16513202 <GO>}

Gérald, one follow-up question. Is the mandatory convertible part of your €3 billion of debt financing? So the XL...

A - Gérald Harlin

No.

Q - Andrew J. Crean {BIO 16513202 <GO>}

It's not, so there's another €1 billion or so to write (00:35:00)?

A - Gérald Harlin

No. It's not part of it. It's not part of it. But I would like just to tell you that, first of all, the mandatory is a way to reach alternative investors, long-term investors. So, it's one - it's technical. It's the product which is on top of the traditional IPO. But, again, it won't replace the €2 billion, just keep it in €1 billion of this €3 billion debt. For the time being, it's not planned like this.

Q - Andrew J. Crean {BIO 16513202 <GO>}

Thank you.

Operator

Perfect. So, next question from Michael Huttner from JPMorgan. Sir, please go ahead.

Q - Michael Huttner {BIO 1556863 <GO>}

Fantastic. Thank you so much and thanks for the guidance on the operating profit contribution to Solvency. Just going back to the Solvency, my math is probably really wrong, but the figures you've given, 7 points from the debt, 8 points from the hedging, so that's 15. Then, there's a couple of - one, there's a minus 3 and a minus 2 linked to the UFR and the change in volatility adjuster and plus 2 or something from the operating profit contribution. So, that gives me a figure of 12 and you actually improved by 16. So, just wondered maybe you can talk about the other bits. That would be lovely.

And then, I think, the opening question alluded to that and you kind of alluded to that, but I just wondered if you maybe can give a bit more color. So, on the Swiss announcement, you said that the kind of profit impact in the first half of about €400 million. Is that also the gain that you've made on the hedges which will come through, and the gain on the hedges, will they come through in the underlying, in adjusted or in net profit?

And then the final question and - you probably think I don't know anything of it. That's probably true. But your Solvency, so you include the U.S. under equivalents. Once you've sold a portion of the U.S., does that reduce the Solvency requirements and the Solvency numbers in the U.S. pro rata, or do you have to - nothing change until you actually reduce to below 50%? Thank you.

A - Gérald Harlin

I'll start - hello, Michael. I'll start with the last question first. Yes. It will be pro rata. So, that means that it will be pro rata depending on the percentage that will be sold. About the Solvency, which is your first question, so I said that, in fact, we have three main elements. We have the operational return, operating return, which is a bit more than 2%. Then we have the sub-debt, 7%, and then we have different elements plus which is the hedges that we discussed just before.

And we have plus and minuses which, as a whole, makes that - this block represent 7%. So, the management actions, I would say, correspond to plus 8%. And then we have some negatives, but also, we have some small positives coming from various elements. And very often, we are dealing with elements that could be extremely small and will be some small positives. Next is the - your second question was?

Q - Michael Huttner {BIO 1556863 <GO>}

So, my second question was fishing really. You said €400 million is the cost of the Swiss thing in terms of net earnings, and I was wondering the gain you've made on the hedges, where will it appear in the profit and loss, which level of earnings? And is it roughly equivalent to this €400 million?

A - Gérald Harlin

I'm sorry. I don't understand your question. So...

Q - Michael Huttner {BIO 1556863 <GO>}

Okay. So, let me – so, you've hedged 20% of your equity portfolios. So – and equities in Q1 went down, so you've made a profit. And my question is where does the profit appear? And in size, is it roughly of the same order of magnitude as the €400 million cost of the Swiss thing?

A - Gérald Harlin

Okay. So, wait – so long as you buy a put, that it add to value of this put which is the increase, so that's the mark-to-market of your put. This mark-to-market will flow in net income. And at the time you will realize it if the option in the money. You will leave some intrinsic value, and this intrinsic value should flow into the adjusted earnings. That's the way it will work. I hope I'm clear. Tell me if I'm not, and...

Q - Michael Huttner {BIO 1556863 <GO>}

Yeah, yeah. No, the accounting is clear. But you made the profit in Q1 – and, I mean, I'm sorry. Where will it come?

A - Gérald Harlin

No, I don't publish – let's be clear. We don't publish our earnings in Q1.

Q - Michael Huttner {BIO 1556863 <GO>}

No.

A - Gérald Harlin

So, it's two ways, there are plus and minuses. So you have – but anyway, again, you can get expect it to have a – to get it in your earnings net income at the end of H1. So, we'll re-discuss it at the end of H1.

Q - Michael Huttner {BIO 1556863 <GO>}

Lovely. Thank you very much. Thank you.

A - Gérald Harlin

Okay.

Operator

So, next question from James Shuck from Citi. Please go ahead.

Q - James A. Shuck {BIO 3680082 <GO>}

Good morning. Thank you for taking my questions. Three for me this morning, please. Firstly, returning to the XL earnings that were reported yesterday, I can appreciate you can't really comment on the direction of travel and you're kind of legally impeded on saying some things but I'm just struggling a little bit with the ROE of XL. It's a 9% ROE based on a 95% combined ratio.

There's a reasonably high level of debt gearing in that company and there's also quite a high level of investment risk. And the 95% combined ratio from what we've seen from the earnings, any improvement in the underlying is actually being offset by a reduction in the volatility. So, could you just clarify for me how you actually see that ROE improving and why you're confident it will?

Secondly, a kind of more general question. Looking at your Life sales in Europe, you seemed to be controlling those very nicely. You've seen a decent growth in the Protection side and in the Health side, particularly in Europe. I'm just wondering about how reliant that distribution is on commissions, in particular, because we have the Insurance Distribution Directive that goes live in October. And I'm just interested to know how that will play out amongst your tight Asian network.

Final question just around the Solvency II ratio. Kind of return a little bit to Michael's point, let me try not add up all the numbers and what kind - exactly what's changed in in the quarter. I mean, you say that the 4 points is kind of unexplained differences due to small positives kind of being cumulative, but that's bigger than your operating earnings in the period. So, a little bit more color around actually what changed in that Q1. And then, looking forward over the rest of the year, can you anticipate any modeling changes, management actions or any impact from any changes around the calibrations on that Solvency II ratio? Thank you very much.

A - Gérald Harlin

Okay. So, starting first with your question, first of all, about XL, the ROE - so you can notice that the ROE that they published was above 9%, I believe, and that's why I said no surprise because it's quite in line with what they expected. I remember that when I presented in March, beginning of March this acquisition, we said that we should be close to 10%. And I said no surprise because, indeed, they're at the right level, at the level of profitability that, indeed, they were expecting.

About the investment, and when I stopped because I'll go beyond what I'm allowed and then try to tell you but, in investment, I recommend you to go through the disclosures because, honestly, their investment portfolio is extremely safe. And I'm quite relaxed on that side and I don't consider at all that their portfolio is aggressive at all.

On you second question, which is, if I'm right, your question about the Insurance Distribution Directive. And we are ready for this. That means that it's something that we're anticipating and we don't have any specific fee on that side and we don't expect that there will be any decline in our sales following the implementation.

Your last question, so we'll start from 205%. Starting from Solvency position at 205%, we have an operating return with a rounding. It's plus 3 because, as I said before, it's 2.5. So we have the debt, the €2 billion of debt that we issued. So that's plus 7. And then we have the hedge which is plus 8. And then we have UFR plus VA which represents minus 2.

Indeed, I was wrong when I said - answering a previous question, I said minus 2 for UFR and reference portfolio minus 3. It's not additive. I'm very sorry for this. So we are between minus 2 and minus 3 for the combined effect of these two. Sorry for that. So that's why you had - I introduced a bit of confusion. And so, if you can, 3 plus 7 plus 8 minus 2, you are at 221%. I hope that it's clear now.

Q - James A. Shuck {BIO 3680082 <GO>}

Okay. And I guess that why is the UFR impact so much less than the previous guidance, I suppose, would be the question from that.

A - Gérald Harlin

No, no. I maintain that we are - the combined effect should be minus 3, so that's a - no, no. That's in line with what we - this is the calculation and this was where we end up.

Q - James A. Shuck {BIO 3680082 <GO>}

What would be the annual drag from the UFR going forward, please?

A - Gérald Harlin

But the UFR – so long as you have the impact on the UFR, it's a one shot. So that means that it will be exactly the same for the whole year because you have a minus – so long as you have an effect, an impact, which is an impact, which has been taken, 15 basis points in the first quarter. So, net effect will be the year after. It won't be this year. So, it will be exactly same.

A - Andrew Wallace-Barnett {BIO 18671460 <GO>}

Yeah. I think, James, we can take that offline with you. I suspect that probably the UFR estimates that you guys have been doing is probably quite accurate. I think it's the reference portfolio that's a bit harder to model. And we'll try and see if there's something we can give to everybody to help that to be easier to estimate in the future. And, of course, reference portfolio is something that changes annually.

A - Gérald Harlin

Anyway, as explained by Andrew, so that in that we want to be absolutely transparent on this. And if you need any more guidance or explanation, don't have any feel, we'll give it.

Q - James A. Shuck {BIO 3680082 <GO>}

Sure. Okay. And just to be clear, are there any foreseeable modeling changes or management actions, et cetera, for the rest of the year?

A - Gérald Harlin

No. For the time being, I don't expect such type of actions.

Q - James A. Shuck {BIO 3680082 <GO>}

Wonderful. Thank you very much.

A - Gérald Harlin

Okay. Thank you.

Operator

Next question from Colm Kelly from UBS. Please go ahead.

Q - Colm Kelly {BIO 19140684 <GO>}

Thank you. Just one question on your business margin. So, the new business volume margin was flat year-on-year 1Q, and it's lower than the full year despite the continuation of the business mix shift. So, at full year, I know you were confident around the progression of that margin and the scope for that to continue to grow. So is the impact we're seeing in 1Q just a bit of short-term seasonality or is there anything within that number that would indicate that the margin expansion is largely complete going forward? And then the reason I ask is obviously the margin expansion has been key to the new business value growth to-date and that's obviously key to maintaining future cash flow growth for that Life business. So it's quite an important to understand where the driver of that is going to be going forward. Thank you.

A - Gérald Harlin

Okay. So, first, we are at 42% which is extremely strong. And when you compare ourselves with our peers, first of all, I would like to say that we are far above our peers in term of profitability. Of course, it depends on the business mix. You can notice that there are plus and minuses, as I mentioned. Roughly, we are flat in France. I don't expect that France will move a lot.

In Europe, we could have some improvement coming progressively from Switzerland because the fact that we will move to a semi-autonomous means that, normally speaking, we should have an increase in the NBV margin in Switzerland. In Italy, you noticed that we benefited from a strong recovery. And so long as we are growing quite fast in Unit Linked, maybe we could have a slight improvement on that side. So, on Europe, I would say maybe it could go on slightly increasing.

In Asia, I would be cautious. In Asia, I would be cautious because we're already at 58%. In China, we are above 50%, meaning that we will stay most probably at the same level. In Japan, we are around 100%. We can expect to stay at this level. When you are at 100%, it's difficult to do better. And in Hong Kong, we are at 44%. So, it's a balance between growth and profitability that I explained before. So, I believe that we will stay much more at 45% around than 60% like last year.

In the other high potential, we are at still 49%. So, we should stay there. Maybe we could slightly improve, but that can slip (00:51:42). As far as the U.S. is concerned, we are around 20% – we were at 23%, 22% flat and we can expect to remain flat. So, I don't expect to make it short. I don't expect we will keep a strong level of NBV margin. We have some elements that could let us believe that we could have some improvement. But I believe that it should be marginal because we reached a level of profitability which is extremely strong. And as you can imagine, we will try to grow the top line based on this high level of profitability.

Q - Colm Kelly {BIO 19140684 <GO>}

Okay. That's clear. Thank you.

Operator

So next question from Johnny Vo from Goldman Sachs. Please go ahead.

Q - Johnny Vo {BIO 5509843 <GO>}

Yeah. Thank you very much. Just, guys, just in terms of the hedge, where in the group have you purchased the put options? Is it in the holding company? And where is the shareholder-exposed equity in the group, in which entities is it in? Also, the strike of the puts, have you bought at the money or out of the money and how far out of the money? And, finally, what is the premium cost for that put option? Thank you.

A - Gérald Harlin

Okay. So, it's very precise. Hello, Johnny.

Q - Johnny Vo {BIO 5509843 <GO>}

Yeah. Hi.

A - Gérald Harlin

First, about the hedge, it's in the holding company. Second, the strike, we bought 10% out of the money option. Third question, what's the premium. So, premium is roughly 5% pre-tax for a two years' option.

Q - Johnny Vo {BIO 5509843 <GO>}

Okay. So, therefore, if the hedge is in the holding company, I guess, it changes. Because you released capital, it doesn't change the remittance profile of your subsidiaries though because each subsidiary...

A - Gérald Harlin

No. Sorry. I see your point. But I would say that I remind you that the companies we see are quite strong. France, for example, has a strong equity exposure in P&C, just like it would be in the holding company. So, that means that it won't change the remittance ratio of the companies. The only point is it's easier to manage from a practical point of view, because when you have such type of hedges, you have to manage the collateral and so on, and it's easier to do it in the holding company.

Q - Johnny Vo {BIO 5509843 <GO>}

Yeah.

A - Gérald Harlin

No more reason than this one.

Q - Johnny Vo {BIO 5509843 <GO>}

Okay. That's very clear. Thank you.

Operator

So, next question from Mr. Michael Huttner from JPMorgan. Sir, please go ahead.

Q - Michael Huttner {BIO 1556863 <GO>}

This is a slightly strange question. So, one of your European competitors with a very large U.S. variable annuity business, they have, obviously, hedges for that variable annuity business, which means that when equity markets go up, the hedges lose value and that eats into their reserves, which means that, at some stage, the reserve becomes zero and then it becomes a problem. Is there anything like that in your business model?

A - Gérald Harlin

Relative to the U.S., yes, we have – I remind you that we are in a situation today where most of the equity in the U.S. are hedged and where we keep an open position on the interest rates, which is relatively good position. Why? Because interest rates are going up so – and they went up, so I'm quite happy to have this underlying position.

As far as the RBC in the U.S., we have an excellent RBC position, so that we are above 600%. So I don't have any such fear even if there would be bigger moves on the equity market. So, honestly, I don't have such type of fear. You'll remember that when I presented the plan, it was in November, I said that we would be at least at 500%. We are far above this level, meaning that we have a significant buffer.

Q - Michael Huttner {BIO 1556863 <GO>}

Excellent. Thank you. Well done. Thank you very much.

Operator

We don't have any question for the moment. We have a new question from Mr. Pierre Chedeville from Credit Suisse CIC (sic) CM-CIC Market Solutions. Sir, please go ahead.

Q - Pierre Chedeville {BIO 15076220 <GO>}

Yes. Good morning. I have two quick question. The first question is that I recently read that, in Italy, the fact that MPS belongs to a public sector, it could be prohibited to sell insurance products and the IVASS which is the supervisor in Italy considers it as an anomaly so far. So, what is your view regarding this potential evolution of the regulation that could impede your strong recovery in Italy through the MPS?

And my second question is how do you see the evolution of the P&C business in France considering the stronger and stronger competition from the banking sector? What, in your view, are the measures that you can take to fight against this new competition and I would see much more aggressive competition in the P&C, not Life, which is a not competition, I would say, but in the P&C business more specifically? Thank you.

A - Gérald Harlin

Okay. Relative to your first question, so that's about the MPS. Remind you that we renewed our bank insurance agreement with the MPS for 10 more years. Second, it's a significant – it's a 50%/50% partnership, meaning that we participate to the recovery of the bank, which means that it's a strong contributor to the earnings of the bank. And so it's the direct interest of the bank to go on selling it. I remind you at the same time that the shareholder being the state it's the interest of the state to keep this bank insurance business because it will be part of the recovery of the bank. So, I have no specific feel on that side. And you noticed again that I remind you we are very proud to announce that our Unit-Linked business in term of APE grew by 42% in the first quarter which highlights the strong recovery in the market.

About the P&C business, I believe that it's by different measures. So it's more by segmentation, by favoring some cross-sell, for example, that we have some possibility to grow more the top line of our P&C business in France. But, again, Personal Non-Motor, we're at zero. We can expect to recover with more household insurance. And on Personal Motor, as I said, answering your previous question, I believe that minus 4% is very low and that we will do better in the rest of the year. So, we will have different measures but – which are traditional incentives that are given to the networks and some incentive also to sell some combined product and to cross-sell products between Motor and Non-Motor.

Q - Pierre Chedeville {BIO 15076220 <GO>}

Okay. Thank you.

Operator

Okay. So, next question from Mark Cathcart from Jefferies. Sir, please go ahead.

Q - Mark Cathcart {BIO 19783252 <GO>}

Yeah. Hi. It's Mark Cathcart from Jefferies. I think you mentioned that post XL, your gearing ratio will be somewhere between 31% and 32%. If I take the convertible that you're raising of €750 million, that's worth about 1 point on that debt ratio. So, can you confirm that the debt ratio guidance is still within that 31% to 32% range, but likely at 32% because of the convertible or is there any risk that it could go above 32%? Thank you.

A - Gérald Harlin

All I consider is that we have no risks to go above this level. Second, Mark, I confirm that this mandatory convertible will not be part – only a small part of it will be considered as debt. A great majority will be considered as a minority interest. And, again, it's not a debt. It would be a debt. It would be up to the holder to decide whether they will convert or not. So long as it's a mandatory, it means that whatever happens, after a while, you will convert this debt into equity. So, that's quite logical that it's not considered as a debt. And so that's the point. So, no, to make it clear, I have no fear that we would go above the guidance that we gave you so, no, not at all, not at all.

Q - Mark Cathcart {BIO 19783252 <GO>}

Okay. Thank you.

A - Andrew Wallace-Barnett {BIO 18671460 <GO>}

Mark, the NBV is roughly neutral for the gearing ratio.

Q - Mark Cathcart {BIO 19783252 <GO>}

Okay. Thank you.

Operator

Okay. Next question from Michael Huttner from JPMorgan. Sir, please go ahead.

Q - Michael Huttner {BIO 1556863 <GO>}

Sorry, last question. In Germany, you had this lovely growth in Personal Motor and Personal Non-Motor of 3% and 4%. Is this mainly price or is this mainly volume, please? And just to gain a feel for where pricing is moving, I guess, – because you said pricing in France up 1%, and I just wondered in Germany.

A - Gérald Harlin

Okay. Maybe we can go to page 14, Michael, of the press release and you will see that on Personal lines, we had 1.2% price increase which is more or less in line with our own expectation. So, if your question is, do you still expect to have such type of price increase? Yes, I believe that for Motor, it's a maximum. For other lines, we have much more flexibility. But, again, I repeat what I said. And again, I'm not at all worried by the global effect on our P&C business. I repeat what I've said. But in France, yes, we have a situation where the Individual Motor business is under pressure from other competitive pressure and coming mostly from the bank insurance but also from the mutuals.

I remind you and I repeat that the average combined ratio in France should be at 105%. So, it's a point. About Germany, the price average price effect in Personal lines for Germany is 2.4%. So we think there are other countries where we keep a stronger price effect, and at that same time in Germany, we have a volume effect of plus 1%. So, in Switzerland, we have a volume effect of plus 1%. So, Spain, 1%; Italy, 1.1%. So, we have a specific test in France, but then Italy, in most of the other countries, it's not only driven by the price effect. It's also the volume effect, which is positive.

Q - Michael Huttner {BIO 1556863 <GO>}

Oh. That's a brilliant answer. Thank you so much. Thank you.

Operator

So, next question from Andrew Sinclair from Bank of America Merrill Lynch. Sir, please go ahead.

Q - Andrew Sinclair {BIO 17749036 <GO>}

Sorry. Just one final question from me. Just wondering if you could confirm for the mandatory convertible, what are the terms under which AXA can compel conversion prior to maturity of the bond? Thanks.

A - Gérald Harlin

Okay. Of course, Andrew, I cannot answer your questions because it's a point that I cannot disclose for the time being. And what I could say is that you can see and the best way for you is to look at the other mandatory convertibles that have been issued and you will see what are the common financial features, so that you will see how it works but it's not very complex. It's a mandatory convertible. At the end, it's just a loan. And after you have a mandatory conversion. At this mandatory conversion you have a flexibility in the number of share that you give because if there is a price appreciation, then the holder will get less shares because there is a value appreciation.

So, in other terms, it's just like you would buy a call option, something like this. And it's - but honestly, my advice would be for you to go through documentation of other type of mandatory like this. It's extremely simple. The fact that it interest investors that when you are long-term investors, when you are sure that you will stay a long period of time, it could be interesting because, of course, in exchange for this option, you have a higher return and you have a coupon which is higher.

Q - Andrew Sinclair {BIO 17749036 <GO>}

Okay. So, just fairly standard terms that's got. Thanks.

Operator

We don't have any more questions. We don't have any more question. Back to you for the conclusion, sir.

A - Gérald Harlin

Okay. So, I thank you a lot for this call. So, I was happy to have this exchange with you and speak to you soon. Thank you.

A - Andrew Wallace-Barnett {BIO 18671460 <GO>}

Have a good day.

A - Gérald Harlin

Have a good day. Bye-bye.
