

Q3 2017 Earnings Call

Company Participants

- Alexander Rijn Wynaendts, Chief Executive Officer, Chairman-Executive & Management Board
- Matthew J. Rider, Chief Financial Officer & Member-Executive & Management Board
- Willem van den Berg, Head-Investor Relations

Other Participants

- Albert Ploegh, Analyst
- Andy Hughes, Analyst
- Arjan van Veen, Analyst
- Ashik Musaddi, Analyst
- Bart Horsten, Analyst
- Benoît Pétrarque, Analyst
- Farooq Hanif, Analyst
- Farquhar C. Murray, Analyst
- Gordon Aitken, Analyst
- Mark David Cathcart, Analyst
- Nadine van der Meulen, Analyst
- Robin van den Broek, Analyst

MANAGEMENT DISCUSSION SECTION

Operator

Good day, ladies and gentlemen, and welcome to the Aegon 3Q 2017 Results Conference Call. Today's conference is being recorded. At this time, I would like to turn the conference over to Willem van den Berg, Head of Investor Relations. Please go ahead, sir.

Willem van den Berg {BIO 15203834 <GO>}

Thank you, Barbara. Good morning, everyone, and thank you for joining this conference call on Aegon's third quarter 2017 results. We will keep today's presentation short, leaving plenty of time to address all your questions. We would appreciate it if you take a moment to look and to review our disclaimer on forward-looking statements, which you can find in the back of our presentation.

Our CEO, Alex Wynaendts, will first provide an overview of our third quarter results and will then be joined by CFO, Matt Rider, to answer your questions.

I'll now hand it over to Alex.

Alexander Rijn Wynaendts {BIO 1821092 <GO>}

Thank you, Willem, and good morning, everyone, and thank you, all, for your continued interest in Aegon, and of course also for joining us today for today's earning call. So, let me begin by providing you with an overview of this quarter's key developments.

I'm pleased with the clear improvement in our operating results, with underlying earnings increasing 20% to €556 million, driven by improved claims experience, by increased fee revenue resulting from favorable equity markets and lower expenses in our U.S. business. As a result of our strong underlying earnings, our group return on equity increased by 120 basis points to 8.9%.

Net income was also strong this quarter, even though it was impacted by assumption changes and model updates. Our Solvency II ratio increased to 195%, which is at the upper-end of our target range of 150% to 200% for the group. This increase was mainly the result of strong capital generation this quarter, which amounted to €324 million, excluding €485 million of market impacts and one-time items.

And finally, sales were very strong year-over-year, rising by more than 50% to €4.5 billion. This increase is mainly a reflection of our continued success of strategic shift to fee-based businesses, in particular, our UK platform and our asset management business.

Let's now take a closer look at our underlying earnings for the quarter in the next slide. I am very pleased that our underlying earnings are up for the fifth consecutive quarter. This reflect growth across our businesses, expense savings and management actions. During the third quarter, we saw significantly improved claims experience in our life and health businesses in the U.S. compared with the same quarter last year. This improvement is a result of the management actions we have taken to improve profitability as part of our five-part plan.

Another main driver for increased earnings is the continued success or execution of our expense reduction program and I will elaborate further on this program in a moment on the following slides. Also earnings from our fee-based business continued to perform well as higher account balances benefited from new business and higher equity markets. U.S. interest rates increased, but still remain below our long-term assumption for reinvestment yields. The improvement in reinvestment yields resulted in a €10 million positive effect compared with last year.

As I mentioned on the previous slide, we continue to make good progress on our group expense savings program. So far, we have achieved run rate expense savings of €170 million across the group, of which €130 million are from the U.S., €30 million from the Netherlands and the remainder from the holding.

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We continue to work hard on implementing further expense savings in our business units. The plans we are putting in place gives us the confidence that we are well on track to reach our target of €350 million by the end of 2018. These savings are resulting in higher returns, while they're also enabling us to invest in the growth of our business.

I would now like to turn to slide 5, which shows the development of our net income. As you can see, net income was strong, amounting to €469 million for the quarter, driven by both solid underlying and non-underlying results. The latter was mainly driven by strong gains on fair value items and by higher realized gains on investments. Fair value gains of €159 million were mainly the result of positive real estate's revaluations in both the U.S. and Netherlands and of hedging gains in the U.S. The hedging gains reflect changes that we've made to our U.S. macro equity hedge program in the past few quarters.

This program is in place to protect our capital position against falling equity markets, and given current market conditions, we have switched to a 100% option-based program and, as a result, significantly lowered the quarterly run rate cost of the program from \$60 million to \$45 million in the base case scenario, while leaving open the upside in case equity markets further rise. More details can be found on slide 21 in the back of this presentation.

Realized gains amounted €135 million, and these were primarily related to the share of equity investments in the U.S. Finally, other charges amounted to a loss of €233 million, which was mainly resulting from assumption change and model updates, which I would like to take you through on the following slides.

Bloomberg Transcript

As you know, we review our assumptions every year in the third quarter, and we run an ongoing model enhancement and validation program throughout the company. This quarter, assumption change and model updates result in a one-time charge of €198 million. This charge was mainly driven by the completion of the conversion of our largest block of universal life business in the U.S. to a new, more dynamic model. This conversion led to a one-time IFRS charge of €252 million, while it had limited impact on the capital position and has no impact on earnings going forward. We have transitioned from modeling policyholder behavior and other assumptions on the cohort basis to a policy-by-policy basis, thereby significantly improving the granularity of our modeling.

The completion of this model conversion effectively concludes the first phase of our model enhancement and validation program covering all high-impact models identified when the program started in 2014. Our assumption changes and model updates in the U.S. netted to €52 million. These charges are one-time in nature and will have no material recurring impact to underlying earnings and to capital generation going forward.

In Europe, the combined impact of assumption changes and model updates was positive totaling €125 million. These were mostly related to the Netherlands where there was a release of a guaranteed provision as there was excess prudence in our reserves. The remaining other charges were primarily driven by impairment of intangibles related to the announced sale of Aegon Ireland. The sale is in line with our strategic objective to

optimize our portfolio, and the impairment is part of the book loss we guided for when we announced the transaction.

Let's now turn to slide 7 where you can see the breakdown of our very strong deposits. In the third quarter, gross deposits continued to be strong across all our businesses, increasing significantly to a record €41 billion. Our UK platform performed very well over the quarter, with institution sales totaling nearly €5 billion. But I want to remind you here that these institution sales are often large in size and can fluctuate quarter-to-quarter.

Higher gross deposits of close to €23 billion in our asset management business were mainly the result of a large mandate won by a partner, La Banque Postale Asset Management, by inflows in the Americas and by the inclusion of the first inflows from Stap, the Dutch general pension fund initiated by Aegon.

You may recall Stap was the first fund of its kind and makes it possible to combine a financial administration of multiple pension plans for multiple employees. Stap currently manages over €2 billion. What's more, Stap enables smaller pension schemes to benefit from the economies of scale and also to comply with complex pension regulations. And its fiduciary management is carried out by a subsidiary of Aegon Asset Management.

We will provide more details on Stap and other opportunities that we see in the Dutch market on December 1 where we'll be hosting a strategy update for analysts and investors at our offices in The Hague. The Dutch management team will provide you there with further insights into the prospects of our business in the Netherlands.

Let me now turn to the next slide where I'll take you through our life and health sales for the quarter. I'm on slide 8. New life sales declined by 8% to €202 million. The U.S. term and indexed universal life sales were down compared with the same quarter last year, and this decline was due to our continued focus on profitability in markets with increased competition.

Lower sales in Europe were mainly the result of our exit from the UK annuity market, and reflect a strategic shift to fee-based businesses. New premiums for accident and health sales decreased by 17% as product exists and lower supplemental health sales in United States more than offset higher travel sales.

As announced at last year's Analyst & Investor Day in New York, we will exit the Affinity, Direct TV and Direct Mail distribution channels as these channels and associated products do not fit strategically within our wealth and health strategy. And for this reason, we expect travel sales to reduce significantly as of the first quarter of 2018.

Let me now turn to the excess capital position of the holding on the next slide. As announced during our second quarter results call, we have injected €1 billion of capital into the Netherlands. This injection temporarily decreased our excess capital position at the holding to €0.9 billion, which is just below our target range of €1 billion to €1.5 billion.

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During the third quarter, excess capital at the holding was supported by regular dividends from our units of close to €400 million from our U.S. and asset management operations. The redemption of €500 million senior unsecured notes last July was offset by the issuance of a one-year senior note of the same amount in August. Notes were issued at a negative yield of 16 basis points, and this enabled us to inject the €1 billion in the Netherlands already in September.

Last month, the UK upstreamed £131 million as part of the special £150 million dividend following the sale of the annuity book. The UK dividend and the proceeds from the sale of the majority of our U.S. run-off business will more than offset expected cash flows - outflows from holding expenses and the share buyback to neutralize the dilutive effect of the 2016 final and 2017 interim stock dividends. As a result, we expect our excess capital position at the end of the year to be in the upper end of our target range as we indicated at the time of our second quarter results.

I would now like to focus on our group capital position on the next slide. Our Solvency II ratio increased 10 percentage points to 195%. The strong increase is attributable to capital generation from the operating units. Excluding market impacts and one-time items of €485 million, capital generation amounted to €324 million. One-time items mainly related to model change in Netherlands and the UK, with all major changes having been approved by the College of Supervisors. These model changes have a limited impact on capital generation going forward.

The completion of the Legal & General Part VII transfer related to the divestment of the UK annuity book led to an increase of 2% for the group. These positives more than offset the interim 2017 dividend, which was announced in August.

And lastly, I would like to highlight that, as a result of both the capital injection to the Netherlands and model enhancements, the Dutch Solvency II ratio improved to around 190%. The UK ratio improved to around 200%, where the U.S. RBC ratio stood with continued strong level of approximately 445%. And this means that the capital ratios for all our main operating units are at the upper end of their respective target ranges.

So, let me now conclude. This was clearly a strong quarter from an earnings and a capital perspective, but it was also one in which we made a series of significant steps forward in execution of our strategy. In all our markets, we're delivering on our commitments as a result of the management actions we've taken. We have addressed the underperformance of our U.S. life and health business and put both our Dutch and UK businesses back in a position to resume dividend payments to the holding.

We also continued to see business growth in our main markets as the strategic investments into new platforms are gaining traction. So, overall, I am pleased with how we are successfully changing the profile of the company to position us strongly for future growth, and this gives me every confidence that we are taking the right steps to achieve our ambitions.

Matt and I are now ready to take your questions. Thank you.

Q&A

Operator

Okay. Thank you. We will take our first question today from Benoît Pétrarque from Kepler. Please go ahead.

Q - Benoît Pétrarque

Yes. Good morning. It's Benoît from Kepler Cheuvreux. Three questions on my side. The first one will be on the Dutch business. I know you have a strategic update on the 1st of December. But could you kind of update us on your view on the consolidation of the Dutch live market. There have been some rumors in the market recently. I know you don't comment on the rumors, but what is your ambition on this market. You have not been very active until now. So, could you update us briefly on that?

Also second question on the Dutch ratio, which is clearly, well, up 15 percentage point, I think, Q-on-Q. Could you clarify a bit the move has been over the quarter, break down between organic capital generation, impact of model updates and also impact of the market in the quarter?

And then just finally, sorry to stay on the Dutch side, but the release of the guarantee provision in the Netherlands. Could you just clarify what has been the driver of this change? I think you referred to excess prudence, but just wanted to know a bit more about the driver of the release? Thank you very much.

A - Alexander Rijn Wynaendts {BIO 1821092 <GO>}

Good morning, Benoît. Let me take the first question and I'll pass it for the second and third one to Matt.

Benoît, as you know, we've been very consistent saying that, our focus - our strategic focus in the Netherlands is on organic growth, and we're saying this because we have a very strong position in the key market in which we want to operate. As a particular, the markets of pension, work site, helping people securing a financial future. And that strong position effectively already gives us a very broader market position. I think we've mentioned that and you'll get much more color when you see the whole management team later here in The Hague. Out of every two Dutch households, one is a customer, a pension customer of the Netherlands.

The second thing I want to say on this subject is that the new government that has just been installed right now is also taking measures that will very much support the business areas in which we're in, an effective support then by accelerating the shift of responsibility to individuals. Whereas you know, Netherlands in the past pension provision was very much something, which was done by employer, by the government. More and more we see a shift to individual responsibility.

Effectively, the government has now also announced measures to facilitate the creation of individual pension products and is exactly the area where Aegon has been focusing on for quite some time. So, we feel very comfortable that we have there a strong position. But again, I'm sure our management team will do a much better job than I do right now, ensuring how well we are positioned in that area with our defined benefit plans, with our DC plans, but also would stop where we are - we were the first one to come into market and we also are now market leading in providing that offer.

Matt, you want to take the two other questions, please?

A - Matthew J. Rider {BIO 20002664 <GO>}

Yes. On the group solvency ratio, you did see the strong improvement in the ratio from 185% in the second quarter to 195%. I think the presentation does a pretty good job of laying it out, but you think of it as 4 percentage points coming from normalized capital generation. That would be the total capital generation excluding one-time items and market impacts, and then you have 6 percentage points coming from one-time items and market impacts including model changes, and this actually bears quite a lot on the Solvency II ratio for the Dutch business, especially as there were some changes to our internal model that were recently approved by our College of Supervisors. So, that had a good impact on the Dutch ratio.

And then importantly, we were able to complete the L&G Part VII transfers that were related to the previous sale of the UK annuity block. And because we were released from some contingent capital risk, we were able to add 2 points to our solvency, and add those numbers up and then take away the interim dividend; the interim dividend was about 3%, and then you get to about 10.

Now for the Dutch ratio, Alex mentioned that we had improved it to around 190% for the quarter. This reflects those model changes but also importantly the injection of the €1 billion dividend into the business. I would also mention that the UMG transaction is just recently completed, so that is not yet been incorporated into that figure.

Q - Benoît Pétrarque

And on the release of the guarantees in the Netherlands?

A - Matthew J. Rider {BIO 20002664 <GO>}

Yeah. So, that was - the number that we referred to related to - mainly it's an IFRS change or was in fact a small solvency position change in that one too, but this just relates mainly to mortality updates.

Q - Benoît Pétrarque

Yeah. Great. Thank you.

Operator

Thank you. Our next question today comes from Farquhar Murray from Autonomous. Please go ahead.

Q - Farquhar C. Murray {BIO 15345435 <GO>}

Good morning, gentlemen. Just two questions, if I may. Firstly, going back actually probably to slide 10. Please, could you just decompose the fall of €0.7 billion in the SCR ideally obviously between the UK and the Netherlands?

And then secondly, the slide indicates the model changes have a limited impact on capital generation in the near term, which is obviously helpful. And this is probably nitpicking, but can you just double-check whether there's anymore material impacts longer term, and in particular, are there any changes in the decomposition of capital generation between the geographies? I think you've indicated the U.S. doesn't really change, so I presume nothing is really changing, okay.

A - Matthew J. Rider {BIO 20002664 <GO>}

Maybe to talk about the SCR reduction. So, we had about €700 million reduction in SCR in the quarter. Part of it is related to just revised modeling of currency risk and related diversification at the group level that has no impact on capital generation. But also, I think, importantly for our internal model improvements that have been recently improved in the Netherlands primarily, we revised our method for doing credit risk shock for non-safe haven sovereigns, and that's basically it.

Q - Farquhar C. Murray {BIO 15345435 <GO>}

And how much was that?

A - Matthew J. Rider {BIO 20002664 <GO>}

I don't have the breakdown, but I'm sure that we can get it to you. As for the model changes - I'm sorry, the balance of the question?

Q - Farquhar C. Murray {BIO 15345435 <GO>}

You just said that that has a limited impact (23:19) The model changes for the quarter mainly related to - basically the impact comes to reserve increases. So, we would not expect that this would have any kind of an earnings impact in the short term, and in fact in the longer term, it actually reduces what would have otherwise been a drag on earnings. So - but that's in the very long term. These are long duration contracts.

Okay. So that's positive very further out?

A - Matthew J. Rider {BIO 20002664 <GO>}

Yes.

Q - Farquhar C. Murray {BIO 15345435 <GO>}

Okay.

Operator

Thank you. Our next question today comes from Farooq Hanif from Credit Suisse.

Q - Farooq Hanif {BIO 4780978 <GO>}

Hi there. Thank you very much. Three questions, if I may. First one, do you have any other sort of modeling improvements that you think you can – that you'd like to put through in the Netherlands particularly? So I'm thinking sort of further refinement to the internal model, and that's obviously on top of the disposal gain that you're going to get. That's question one.

Question two, are you – I get that you don't really want to participate in consolidation in the Netherlands, but are you seeing any positive impacts from the consolidation that's happened elsewhere in terms of profitability? So are there any early signs that that could help you?

And the last question is, you referred to reinvestment yields improving, but could you just update us on the current U.S. ALM gap. The typical question you get when – if yields remain where they were – where they are, sorry, what implications that might have on earnings and capital generation? Thank you very much.

A - Alexander Rijn Wynaendts {BIO 1821092 <GO>}

Farooq, let me take your second question, and Matt can take the first one on the impact of model improvements on our Solvency II position in Netherlands and provide you with the investment yields. I think we've been clear, and I've just stated in one of the previous questions that, for the Netherlands, with the position that we have in that segment of the market, which we believe is a segment of the market where we see really the future growth very much driven by the shift of responsibility to individuals, the need for people to save more for the future, people living longer and being less dependent on governments or employers, then that trend is really the area we want to be. But we have a market share, as you know, above 30%. I just mentioned that, out of every two Dutch households, one is a customer of us, so there is no need for us there to be bigger.

In terms of other areas, I want to remind you maybe our Cofunds and Mercer acquisitions explain here that we were not so much acquiring companies and taking costs out, the objective really of these transactions was to acquire customers. And let me take you to Cofunds, for example. We have a state-of-the-art, recognized, as you know, by the place in the UK market platform capability. That is by the way very scalable. So, for us, it's all about trying to get as much as customers on that platform as we can with as low as possible in acquisition cost.

So, the Cofunds acquisition was effectively moving 900,000 customers for which we paid £150 million, which effectively is – or £140 million to be exact. Effective means that we acquire the customers for £150 per customer. That's another way of looking at it. If you

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look at acquisition of the Mercer pension plan, it is very much similar. And we will continue to be looking at where we can leverage very specific technology that we have in place that is scalable by attracting customers on our technology.

And what we expect going forward is that, since we have invested in specific areas of technology, the 401(k) business in the U.S. I think you're well aware of that. The UK, I just mentioned, we will continue to look at ways of bringing customers to our platform, and this is a more effective and a cheaper way, I can assure you, than go in a market and go and chase 900,000 customers.

So you see more of that happening because we also see that the skill means that those players that are smaller or mid-size will just not be able to play the game, so we see more opportunities in that area going forward. Matt?

A - Matthew J. Rider {BIO 20002664 <GO>}

Maybe with respect to the modeling improvements, so we've just had what we call IMAB 2 (27:40). So, this is major model improvements that have been submitted to DNB and have been approved by the College of Supervisors. I would expect that we will continue to basically improve our modeling. But I would not anticipate any major model submissions to DNB in the very near future.

With respect to your question on U.S. reinvestment yields, currently where new money yields are at about 4.05% for the quarter. And that is below our long-term expectation. But we would think that has a quite limited impact on near-term capital generation.

Q - Farooq Hanif {BIO 4780978 <GO>}

Thank you very much.

Operator

Thank you. Our next question comes from Nadine van der Meulen from Morgan Stanley. Please go ahead.

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

Yes. Good morning, and thank you for taking my questions. The first question is on the holding excess capital position. You've upswinged quite a significant dividend out of the U.S. in the third quarter. What should we expect for the full year or in Q4 in this light? Is it just that you brought that forward?

And then second question is, on the assumption changes and the model updates, a one-time charge as you put it of the €198 million, do you mean to say that we should not expect any further charges from model updates? Or if there are, what region we could expect because this is an ongoing thing? And then I suppose, lastly, in the U.S. life sales, they were down in new business margin, which was also a bit a lower. Could you talk

about sort of the main drivers and how would you think about the outlook for the profitability here on new business? Thank you.

A - Alexander Rijn Wynaendts {BIO 1821092 <GO>}

Let me maybe take you to questions two and three, and then Matt will take your first question on the movement of excess capital position to the holding. I think it's good to remind everybody in the context. As you know, we've announced at the end of 2014 that we were undergoing a very thorough model validation, model review process of all the high-impact models. And I think, we've been very clear that this model, which is related to the universal life policies in the U.S., was kind of the last of the large models, and that we said we would do and make all the efforts to ensure that we could get this model validation concluded by the third quarter, so we can bring it all together with model validation in the Netherlands and assumption changes.

So, yes, in the U.S., it has led to a charge. I'd like to point out that in the Netherlands, actually it has led to a gain. So, this model change is for high-impact models not effectively concluded. It doesn't mean that we will not continue to do model refinements and model changes for the rest of our business. Actually, in fact, we have done and performed quite a number of what we call medium impact and low model changes and updates in the course of all the quarters. But, as these low and medium impact also suggests, the impacts are very small and have been quite limited, and have actually also offset each other. So, we do not expect to see significant impacts going forward now that we have effectively concluded this high-impact model.

Also, I want to make sure that you see that the IFRS loss here of the U.S. model was more than offset by share value gains in the U.S., was also offset by fair value gains and gains we've made, real estate and other positions, and has had limited impact on our capital position and no impact on our ongoing capital generation, no impact on ongoing earnings impact. So, it really is an IFRS impact here.

In terms of life sales, as you know, the market is competitive in the U.S. Interest rates clearly coming down have only made that worse. We have a clear strategy and maintain a discipline in pricing.

So, what we are looking at is where - in which parts of the market can we continue to sell and grow our business, and particularly indexed universal - indexed-linked universal life is an area where we have significant market share and where we have been able to kind of effectively reduce the decline in sales. So I'm positive there because we've also made changes. With the improvement in interest rates, it will make it easier for us to see our sales going up there.

But it fits all in the strategic shift that we've mentioned many times is that more and more of our business is going to fee business; more and more business is going to deposits, pension business, asset management, mutual funds in particular in line with the shift, as I said earlier, of responsibility to individuals. So, that's why you see - you will continue to see more of the growth of our business.

So, Matt, do you want to take the first question?

A - Matthew J. Rider {BIO 20002664 <GO>}

Yeah. On the excess cash on the holding, you've seen that at the end of the third quarter we're standing at about €900 million, which is slightly below our target area of €1 billion to €1.5 billion. Now, I'll tell you that that was corrected just a few days after the end of the quarter when we received the special dividend from the UK in the amount of £131 million. And then, for the rest of the year, as Alex said in his opening remarks, we would expect to be at the top end of the range in part from additional dividends from the UK but mainly from dividends that we would expect from the U.S. following the close of the BOLI/COLI transaction.

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

Sorry. Can you say it again? So, at the end of the year, you expect to be at the top of range including the special dividends from the UK?

A - Matthew J. Rider {BIO 20002664 <GO>}

Yes.

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

Okay. Thank you very much, all. Thank you.

Operator

Thank you. Our next question comes from Mark Cathcart from Jefferies. Please go ahead.

Q - Mark David Cathcart {BIO 19783252 <GO>}

Yeah. Hi. Congratulations, Alex, on what I thought was a really good underlying set of numbers. And having followed the stock for many years, it's the most cheerful up-sell, I think, since the 1990s. I think things are really heading in the right direction. So, on that basis, can you give some sort of indication on how much further you believe you can get costs down across the group? You must walk around the Aegon offices thinking that there's more costs that can be cut and more efficiencies. And the second point is, because you're moving towards the high end of your capital range within holding by the end of this year and with nice capital generation repaired (34:45) across the group, where do you think you're going to be most keen to put that capital to work, say, over the next 12 to 24 months?

A - Alexander Rijn Wynaendts {BIO 1821092 <GO>}

Mark, thank you for your very kind words. That is appreciated. You have followed us indeed for a long time, and I can tell you that I am also – and I had made it hopefully clear in my introduction speech – pleased to see that we have strong earnings, strong capital generation, but also strong growth because a strong growth is what is going to define the

future of a company, that is going to create the cash flows of the company going forward and, of course, paying the dividends.

So in terms of expenses, we have in place a plan that we've communicated a number of times to effectively generate €350 million of expenses between 2016, 2017 and 2018. So by the end of 2018, we have committed to reduce expenses further from the €170 million that I announced we have now achieved at the third quarter to €350 million. So there still is another €180 million to go.

Now, as you will appreciate, I cannot be more precise in saying exactly what plans will be announced, when and where, but what I have said in my speech and I can reiterate, we have very clear plans to achieve that additional €180 million of cost reductions, in particular in our large businesses where the impact will be most, but in all of our businesses, we are looking at ways to being more efficient. That efficiency is absolutely required not only because we need to get the returns to the level where we need to get them, but also because we need to create the room to invest in the future. We need to have a more lean, efficient, technology-driven organization that not only serves the customers in the more efficient way, but serves also our customers in a cheaper way and in a way our customers are demanding for. So the plans are in place. They will be communicated in the due time. And I can assure you, we are working very hard, and I feel confident that we will achieve the €350 million upfront cost reductions.

Now, in terms of the capital position, we've given and set ourselves a clear target and a priority, that is to return €2.1 billion to our shareholders over the three-year period. Still, we have achieved a significant amount of that, but the capital that has been generated will be returned to shareholders for us to meet our target of €2.1 billion. Thank you.

Q - Mark David Cathcart {BIO 19783252 <GO>}

So - Yeah. Yeah. Okay. So you can't say geographic arenas where you may be looking to make fresh investment. You've mentioned about Asia being a real critical component of your earnings going forward.

A - Alexander Rijn Wynaendts {BIO 1821092 <GO>}

Well, in all our countries, we continue to grow, and I hope you see, Mark, that with the sales we're showing is that we're not holding back on growing our business. Obviously, we want to do that in an efficient way. We want to make sure we make our returns. And we will continue to commit capital to those businesses that not only generate our returns, but also fit strategically where we want to grow.

On Asia (38:07), just to take that point, as we shared with you also previously that instead of having a capital drain of €100 million, which was kind of the old position, we have, as a result of management actions and decisions we have taken, been more efficient, shutting down certain businesses, taking expenses down, actually turned it around where Asia is effectively a small capital generator.

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We also mentioned that in Asia, we're not going to chase growth in the, I would say, traditional way where you would build up agencies which require very significant amount of upfront capital. Now, we are looking at modern ways - new ways where we can deploy the skills we have and technology we have to enter the market digitally which, as you know, will have much less of capital requirements because upfront expenses and particular acquisition expenses, like such as commissions, will not be the case here. So there's no reason to believe that that will require a significant capital investment. It's a very different business model.

Q - Mark David Cathcart {BIO 19783252 <GO>}

Okay. Thanks, Alex. Thank you.

A - Alexander Rijn Wynaendts {BIO 1821092 <GO>}

Thanks.

Operator

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

Q - Albert Ploegh {BIO 3151309 <GO>}

Yes. Good morning, all. Thank you for taking my questions. The first one is on the illiquid investment program in Holland. Can you update us what has been done in Q3 and what are the plans for the remainder of the year, and what type of assets being bought? And the second question is again coming back to slide 10 with some explanation on the development of the SCR. I noticed that the own funds went down, I know of the different impact what has also been (39:51) generate. So, yeah, what happened basically on the own funds development during the quarter in relation to the potentially model changes also on the group level there?

And the final questions on the macro sensitivities on the Solvency II ratio. I know it's only disclosed two times a year, but given the model changes in the changes in the hedging (40:16) sensitivities in the midyear still felt (40:18) or have you been positioned more to, let's say, rising interest rates or rising equity markets compared to the first half? Thank you.

A - Matthew J. Rider {BIO 20002664 <GO>}

On the first point, I think the illiquid strategy, I think it's a little bit slower than we had expected, several hundred million but no more than that. We would expect this to accelerate during the backend of this year and going into 2018. With respect to the SCR and the own funds, so you rightfully point out that own funds reduced by about €300 million and that related to the dividend and that balance of it is, yeah, it's market movements and obviously the normalized capital generation comes through. I think the big story in the Solvency ratio is the reduction in SCR and the major model improvements had a major impact there with 6 percentage points. And, yeah, for the rest of it, we just have to recognize that our position for own funds going forward is we recognize that this

is an important valuation metric, and that we are committed to growing our own funds in the future.

With respect to the sensitivities on the macro hedging, I think we're just going to update that in due course at the end of the fourth quarter.

Q - Albert Ploegh {BIO 3151309 <GO>}

Okay. Thank you.

Operator

Thank you. Our next question comes from Bart Horsten from Kempen. Please go ahead.

Q - Bart Horsten {BIO 2390919 <GO>}

Yes. Good morning. Thanks for taking my questions. Well, first on the Solvency II position and at the half year numbers, you gave us more guidance on your group capital zones. And well, from the positive development we've seen, you're now already close to your opportunity bucket in this capital zone. And I was wondering could you please remind us what this would mean if you would go above the 200% level and what we can expect there.

Secondly, you had very impressive growth - deposit growth. Unfortunately, still the lapses from the Mercer account made that you come out with a net decline. I was wondering we know about the decline at the Mercer, but what's the absolute amount you still expect to lapse at the Mercer so that we can see some net growth going forward?

And my final question relates to your decision to stop publishing quarterly results. I was wondering what's the reasoning behind that. And well, that's the question. Thank you.

A - Matthew J. Rider {BIO 20002664 <GO>}

With respect to the Solvency II position, yeah, the top end of the range is 200%. We're approaching that now. Technically, that puts us - if we get above that level, then it puts us into what we call the opportunity zone. Opportunity does not mean immediate deployment. So we will take the opportunities as they come and decide what we want to do with the excess capital once we get over that level.

With respect to the gross deposits, yes, you're right in saying that it was a fantastic growth deposit quarter. But obviously on the net side, we lost about \$13.6 billion in assets related to the Mercer outflows. We would expect something on that order to occur again in the fourth quarter. And then after that, it should be - that should be done.

Now with respect to publishing semiannual results and moving away from quarterly results, I think basically all European insurers or most of them have recognized that this is an extremely long-term business, and certainly our investors and other stakeholders are long term in nature. So we think that we can do a better job in giving you more

substantive information on a semiannual basis, not have to deal with such quarterly fluctuations. And in the meantime, we can take the time that we will save to actually improve running the businesses. And I think that's an important thing going forward.

Q - Bart Horsten {BIO 2390919 <GO>}

So you will also (44:51).

A - Alexander Rijn Wynaendts {BIO 1821092 <GO>}

But it's for sure...

Q - Bart Horsten {BIO 2390919 <GO>}

Sorry.

A - Alexander Rijn Wynaendts {BIO 1821092 <GO>}

I just want to say it's for sure not the reasons that we don't enjoy having these calls. Matt, don't we?

Q - Bart Horsten {BIO 2390919 <GO>}

But you're also not planning to give trading updates on high-level developments in term of group solvency or other items?

A - Alexander Rijn Wynaendts {BIO 1821092 <GO>}

No. No.

Q - Bart Horsten {BIO 2390919 <GO>}

No. Okay. Thank you.

Operator

Thank you. Our next question comes from Arjan van Veen from UBS.

Q - Arjan van Veen {BIO 5197778 <GO>}

Thank you, gentlemen. Most of my questions have been answered. Just two follow-ups, firstly on cost savings. You highlighted you're halfway into that program, and you're confident in terms of achieving your target. I just wanted to just follow up in terms of how it's flowing through the P&L. I assume there's a bit of a lag, so just a bit of color around how it then flows through and how we should think about the underlying earnings with those things coming through.

And the second question was on the U.S. tax reform. Given the proposals have now been put out, can you give us a bit of a color how that impacts your business, i.e., where are

your effective tax rates today, whether that improves, and also the impact on any deferred tax assets you may have on the balance sheet in the U.S. business. Thank you.

A - Alexander Rijn Wynaendts {BIO 1821092 <GO>}

Yeah. As I said, we are halfway what I think is a very ambitious cost reduction program, €170 million out of €350 million. We have also now – and we made good progress in defining and setting the plans for the remaining €180 million, of which of course a big part is in the U.S. As you know, we have €300 million of cost reductions for the U.S. What I can say on how they will flow through earnings is that we expect that the remaining part of the cost reduction, particularly those in the U.S., will, for a big part, flow back through earnings. So you'll see them coming through to earnings and that will support obviously not only earnings, but also our targets in terms of return on equity.

Now, on the...

Q - Arjan van Veen {BIO 5197778 <GO>}

Is it fair to say that the amounts you've achieved today, they are not fully sort of flowing through? That's one of my questions.

A - Alexander Rijn Wynaendts {BIO 1821092 <GO>}

It's fair to say that the amount – I think it's fair to say that the amount that we have seen today is probably for flowing through earnings for around half of it. I think that's fair assessment. And then the remaining, as I said, we expect a bigger part, clearly a bigger part to flow through earnings. We'll provide you, obviously, with more updates when we come with plans and when we announce them also to the market, but as you can imagine, we got to deal with this first internally before we deal with that externally.

Q - Arjan van Veen {BIO 5197778 <GO>}

Yeah.

A - Alexander Rijn Wynaendts {BIO 1821092 <GO>}

In terms of taxes, unfortunately – I wish I could say more, and I also wish we would know more. It is a very fluid situation. Yes, there's been a headline proposal for a tax reduction in corporate tax rate, which, as I think we will all agree, is a positive. It's a positive for the economy, therefore it's a positive for our business. It's going to be meaning, less taxes on our earnings, less taxes on our cash flows. But what we're also seeing is that there's a lot of discussion back and forth about how these tax cuts are going to be financed, and to what extent the insurance industry is going to be impacted from that. It's way too early now to give you any impression. It is a very fluid situation, which we're following very closely.

I can also say that not only are we following very closely, but the CEO of our U.S. business, Mark Mullin, is the Chairman of ACLI, so he's directly involved. It is important for us as it is important for the whole sector, but with the situation right now, there's absolutely nothing more we can say other than that lower corporate tax is a positive, and we need to make

sure that the way that it gets financed is not going to impact our industry. That's really where we are today.

Q - Arjan van Veen {BIO 5197778 <GO>}

Is it possible to give us some indication where the effective tax rate is because just looking historically it does bounce around a bit from the U.S. business?

A - Alexander Rijn Wynaendts {BIO 1821092 <GO>}

Yeah. I think that's a good point. The effective tax rate effectively is 27%. So, what you see in many cases when taxes are coming down, and by the way, the same applies to the Netherlands, they take the headline number down, but they take away deductions. So, ultimately, it's very important to see what all the rules are and exactly how they get applied to understand what the impact is because even from 35% to 27%, as you see, there is already quite a big gap because we are running now at 27% roughly.

Q - Arjan van Veen {BIO 5197778 <GO>}

Yeah. Fair point. Thank you, Alex.

Operator

Thank you. Our next question comes from Gordon Aitken from RBC. Please go ahead.

Q - Gordon Aitken {BIO 3846728 <GO>}

Yeah. Thanks very much. Three questions, please. First, on the UK platform business. I mean these flows are good and the annuity assets are now in excess of £110 billion. But pension's earnings were just £8 million in the quarter. Is this the run rate or whether one-off effect in that number?

And second question on the Dutch market, and obviously you've been looking at assumptions. But can you talk a bit about mortality assumptions you're using and is there potential gains to come there still from moving to a new table due to the slowdown in life expectancy improvements that we've seen in the last few years?

And the final question is on the Dutch and defined benefit pensions book. It's obviously a spread business and you've been talking about you move away from spread. And what proportion of the Dutch reserves at the moment are spread or defined benefit? And could you offload that book and would you want to offload that book? Thank you.

A - Alexander Rijn Wynaendts {BIO 1821092 <GO>}

Yeah. On the platform, Gordon, yes, we are making, I think, really good progress with the platform in terms of getting close. Equally importantly, we're also making good progress of moving our Cofunds customers onto our platform. As you can imagine, that is kind of a big exercise. I think it's important that you look at close into the platform in a positive sense, but also looking at the fact that we've seen outflows being very limited. Actually, where - on the Mercer deal, we were expecting outflows and anticipated them. We see in

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the Mercer deal more outflows than we are anticipating. Here, with Cofunds, it's been the other way around. I think the customers (51:03) the customers are very pleased with what they're getting from us, from Aegon. We are definitely seeing less outflows.

Yeah, in term of the splits between what is, we call, pension and life, I'll refer you back to IR (51:17), but I think that you can say that the earnings, which we have shown in the third quarter, are a pretty good indicator of what we would expect the run rate going forward. But you should also take into account that we also announced that the integration of Cofunds on to our platform is going to yield additional cost savings.

So, the run rate will start increasing when these cost savings all are being realized over the course of 2018. And the amount, which we put in the presentation when we did the acquisition of Cofunds, shared with you, was around £60 million and we're still committed to deliver on that £60 million.

On UK, yes, I think you were talking about improvements in mortality, people living this long. That is in particular a positive impact for annuity business rather than it has an impact on business we have, because, as you know, we have actually disposed of our annuity business. By the way...

Q - Gordon Aitken {BIO 3846728 <GO>}

No, the question was about the Dutch market.

A - Alexander Rijn Wynaendts {BIO 1821092 <GO>}

Oh, the Dutch market, in the Netherlands?

Q - Gordon Aitken {BIO 3846728 <GO>}

Yes.

A - Alexander Rijn Wynaendts {BIO 1821092 <GO>}

So, in the Netherlands, we've seen improvement. I think what we see is too early now to say there is a reversal of a trend. Yes, we have seen an improvement. We had apparently some colder winters. We had more flu than usual. I mean, this is the kind of explanations I'm getting and these explanations are in my view too early to say there's a reversal of a trend. But it's clear that we have, indeed, effectively had benefit from, call it, improved longevity. In other words, people living a little bit less longer than we were anticipated. But I would caution really on trying to get a sense that this is a longer-term trend. It's too early to say that. In any case, we have build up the right reserves.

And I think your final question was about where is earnings coming? In the Netherlands, the biggest part of earnings is, indeed, still coming from our defined benefit books. That is by far the biggest part. We are seeing there the positive impact of what you just mentioned, some improvement indeed in the longevity, people living less longer.

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We have a significant book that is going to run off over time and actually, we haven't had many new customers and buyouts on our book, particularly with very low interest rates makes it very challenging to make that an attractive proposition, but I also like to point that, for us, it's important to not only have this book that is a very positive book that's running off, it's that we are building the capabilities for the future and that is our defined contribution business. You'll hear more about that when you get the presentation. Hopefully you'll be here in The Hague to hear from my Dutch colleagues. The DC business, the hybrid Stap, we talked about that earlier where we provide the administration for smaller pension funds, again, a fee business.

So, we are really moving, trying to not only protect the spread business, which we have built over the time, but very - also much focus on building the fee business in the pension business, which we believe is going to be the future, in particular, was mentioned earlier, with the Dutch government, we have a new Dutch government that has announced a number of steps in changing the pension world from what we would call average premiums in the pensions toward individual premiums.

They have also now agreed that individuals can set up an individual pension products, which will be managed individually, very much in line what you see in the UK. So, this clearly is a trend of accelerating now and the government has taken steps that will make you accelerate even further the shift towards DC from DB, but also the individualization, meaning that people will have themselves take more responsibility. They will have to take, first of all, make choices. They will have to be educated and they will have to take decisions as to how they will manage the pension products and in particular how they will do the drawdowns. That is really the sweet spot of our strategy here in the Netherlands, but again, as I said earlier, I hope you will be here in The Hague to hear from them.

Q - Gordon Aitken {BIO 3846728 <GO>}

I mean just to follow up on that. I mean, you sold your spread business in the UK. I mean, there was buyers for that business and more than one. I mean, would you sell your spread business in the Dutch market? Is it because there's no buyers or is there another reason you like that business?

A - Alexander Rijn Wynaendts {BIO 1821092 <GO>}

Well, I would say that in the UK, we were pleased to sell our annuity business, spread business. We were pleased also with the price we got for it. I would say there are buyers, but I think that the universe as buyers is probably smaller than everybody believes it is. And, therefore, seeing in the Netherlands at this point in time, we have not really seen buyers in this universe. And again, we're always looking at the best way of allocating our capital. If there would be options effectively to offload some of it and create capital synergies, we should reconsider that, but I can tell you at this point in time, I have not seen anything viable that we should be looking at.

Not surprised, because effectively in our pension business, you get underwriting risk, you get market risk and we took about quite significant exposures, which we haven't seen in any other place at this point in time being interested (56:34).

Q - Gordon Aitken {BIO 3846728 <GO>}

Great. Thank you.

A - Alexander Rijn Wynaendts {BIO 1821092 <GO>}

Thanks.

Operator

Thank you. Our next question today comes from Andy Hughes, Macquarie. Please go ahead.

Q - Andy Hughes {BIO 15036395 <GO>}

Hi. Thanks very much. On the €2.1 billion by the end of 2018, I think that's more than €900 million supposed to return to (56:56) shareholders. I'm just wondering, does that mean you're expecting €900 million to be upstreamed to the holding company between now and the end of 2018?

And given the way in which the operating earnings appears to be developing, are you sort of thinking more about increasing the kind of base dividend level as a way of returning that or is it going to be mainly through some sort of capital return? And then, are you planning further disposals to get to that or does that come in entirely organic?

And I think the final question is, on the half year, you obviously put in the higher cash flow target for 2018. Looking at particularly the market movements and increase in fee income, which should be recurring I guess, depending where some of the (57:45) markets going forward, is it fair to say that you are ahead of where you thought you would be on that target so far? Thank you.

A - Alexander Rijn Wynaendts {BIO 1821092 <GO>}

So, Andy, thanks for your question. The €2.1 billion is a commitment and a target we have set. We will take our dividend in – I would say, the final dividend in 2017 entering for (58:13) 2018 to the level that is required to bring it to the €2.1 billion. I think it is very easy to calculate it back. That is very much supported by flows, which we are getting from our business units. Because you know in the U.S., we have a capital generation of \$1 billion, of which 90% has been upstreamed and with an excellent record for which we are very pleased.

The Netherlands, we've also guided you on our dividend. We've mentioned there would be €100 million interim dividend, the first half of 2018. The UK now that we have addressed, I would say, the sale of the annuity book, and we are integrating Cofunds with our platform, we expect actually, with the level of solvency, which we are at and I guided you to the 200% level to effectively upstream most, if not all, of the cash that's being generated. So, there's around £100 million as you know. And for the rest, we've been quite consistent of upstreaming dividends from asset management of around £100 million (59:15). The rest of Europe has been around €5 million (59:18).

And in Asia, while we used to be consuming capital at the tune of €100 million (59:23) a year, we actually had a one-off dividend and we are now capital generative. So, if you add it all up, you, I think, will see very easily that the flows that we are expecting from our units will more than cover what is needed for the dividend and will also actually increase the buffer we have at the holding, and therefore, increase the flexibility we have.

Now, we have given you an indication of our cash flow targets for 2018. These are supported, as you rightly point out, by good market conditions, more fees, but also, are supported by the management actions we're taking to take our expenses down, because they will not only flow on earnings, but they will, of course, also flow into the capital generation. But I think it's now about delivering on 2018. And yes, I hope we can over deliver. Thank you.

Q - Andy Hughes {BIO 15036395 <GO>}

Okay. Thanks so much.

Operator

Thank you. Our next question comes from Robin van den Broek from Mediobanca. Please go ahead.

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

Yes. Good morning, gentlemen. We just like to circle back to the tax reform in the U.S., because you've mentioned an effective tax rate of 27%. But I think for your required capital, you're using a 35% tax rate. And I would say that also assuming the DTA write-offs that's connected to a potential tax cut, you could see a hit to your RBC ratio between 75 and 100 percentage points, which is also consistent with what two peers in the U.S. have indicated as a potential hit. So, the number you recognize (01:01:01) first of all.

And secondly, do you think the NAIC will provide any tools to navigate through this potential hit for the industry?

And thirdly, what could the Dutch Central Bank do? You've just been through a process where the calibration of the RBC ratio basically has been changed. I was wondering how did that process exactly look like and how difficult was it to get approval for Dutch Central Bank to revise that?

And how does all of these feed into your - you're close to your opportunity buckets of 200%, is there any buffer you want to keep with regard to this potential capital distortion coming from the U.S.? Thank you.

A - Alexander Rijn Wynaendts {BIO 1821092 <GO>}

I think maybe the first point is a tax bill does not a law make (01:02:01). So, we are still early stages here with respect to even looking at what the proposed bill might be, how that is going to be treated. So, you mentioned quite a number of effective tax rates and

DTA write-offs and implications for the RBC ratio, but I think it's a bit too early to comment on that kind of thing.

One thing I would say, and we've commented on this before, that if there was a change to the DTAs and in fact, RBC ratios came down, I think the first reaction would be – in the U.S. life industry would be sort of a rebasing of what is acceptable capital for U.S. life insurance companies. So, that would be the first point.

The NAIC ultimately may make changes to required capital in response to that, but again that's sort of a second-order effect and we wouldn't comment on it. At this point, we don't think that there would be any – we're not holding any extra buffers for tax reform changes nor would we expect to see any changes in dividend repatriations from the U.S. or what we give to our shareholders.

In terms of the calibration that we did with DNB, I think that what we had shown at the time was that we basically looked at European peers and how their conversion was coming in the Solvency II. And they were quite interested and understanding how other European regulators were treating it. So, we did a kind of a balanced approach. The idea was level playing field.

Now, one thing we did agree with them is to the extent that there are substantial changes to, let's say, the structure of U.S. risk-based capital, then we would go back and then we would re-discuss what the appropriate effect on our own conversion would be. And I think that should be about it. Thanks.

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

Okay. Thank you for that commentary.

Operator

Thank you. Our final question today comes from Ashik Musaddi from JPMorgan.

Q - Ashik Musaddi {BIO 15847584 <GO>}

Yeah. Hi. Good morning, Alex. Good morning, Matt. Just couple of questions I have. One is, I mean, it looks like your solvency ratio is 195% on the top end of the range. So, would you say that the capital debate is now more or less over and if couple of quarters you can stay there, this would not become an issue at least in your internal discussions, et cetera, so we move away from capital debate. Will that be a fair expectation?

Second thing is can you just remind us about capital generation and how much will that capital generation convert into cash? I mean, the numbers keep on changing, so just a reminder would be great as to what is the conversion from that.

And thirdly, can you give us some color about what is your hedging policy at the moment for the Dutch business? I remember you had Solvency II ratio-based hedging rather than

cash flow hedging. So, if you can remind on that, the only thing I'm trying to look for is if interest rates were to rise here in Europe, will that feed through in your capital benefit or not, i.e. if your Solvency II based hedge rising interest rate is a very good news? So, any color on these three questions would be great. Thank you.

A - Alexander Rijn Wynaendts {BIO 1821092 <GO>}

Ashik, I think that you say it rightly. The capital debate is over. With 190% in the Netherlands, the capital debate is certainly over and behind us. This was our objective in Q2. I think we wanted to make that very clear. Matt and I, to the regulator, to all our stakeholders internally, externally, including you of course saying that discussion on the capital is a distraction from where we need to focus our efforts in growing our business and serving our customers. So, to me, the debate is over and I also expect it to remain over for the foreseeable future.

Now, on capital generation, I thought I had just expressed it earlier is you're well aware of the numbers, I'll repeat it very quickly then if you want. We said \$1 billion capital generation in dollars from the U.S., \$900 million upstream. From the Netherlands, we've mentioned €100 million interim dividend. The UK we said the cash flow of around €100 million should be entirely (01:06:19) tangible, and therefore, sent to the holding.

And the other asset management and rest of Europe are unchanged at effectively dividends in holding of respectively €150 million. And the difference being that we are not anymore expecting to put amounts of capital in our Asian business, where the minus €100 million a year, which as you know, we had kind of indicated a year ago, has turned into a slight positive actually as a result of the management actions we are taking. So, I think that picture hopefully is clear.

Now, in terms of hedging, you're right, we do hedge our capital position in the Netherlands interest rate from a Solvency II point of view, but you never hedge all the impacts. The secondary order (01:07:06) impacts that you don't hedge, there is the risk margin that you don't hedge. So, the answer is that when rates, and hopefully rates will start moving up in Europe, you will see a very clear benefit in both our capital generation and in the level of capital.

Capital generation becomes a drag in relation to the UFR is going to reduce and the Solvency II capital, because we are not entirely hedged on the Solvency II base, but we only hedge our capital. And therefore, big parts are not hedged. It will also mean that there is a positive sensitivity to interest rates. So, let's hope for these interest rates to move up.

Q - Ashik Musaddi {BIO 15847584 <GO>}

That's very clear. Thanks a lot, Alex, and well done today.

A - Alexander Rijn Wynaendts {BIO 1821092 <GO>}

Thank you. This was the last question. Thank you for, again, your interest in the company. I really hope to see you next time in our offices here in The Hague when we'll have the

Dutch management, because I can tell you that there's very exciting story to tell about the opportunities we have here in the Dutch business, the pension business and the steps we are taking here to really also work on innovation. That's going to be big part of the presentation.

So, I look forward to seeing you there in The Hague and take care for today.

Operator

Thank you. That will conclude today's conference call. Thank you for your participation. You may now disconnect.

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