

Mapfre, S.A. BME:MAP

FQ2 2017 Earnings Call Transcripts

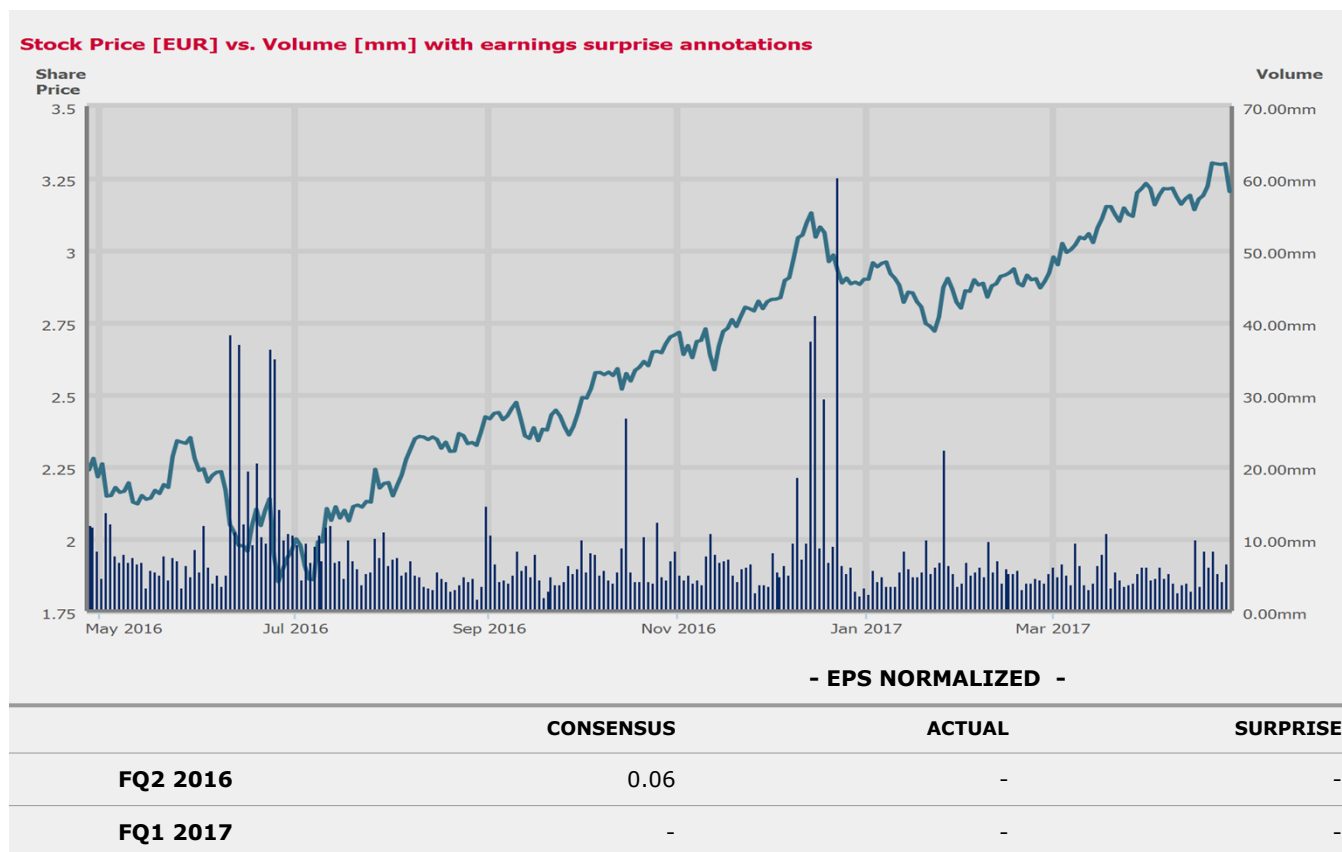
Wednesday, July 26, 2017 10:30 AM GMT

S&P Capital IQ Estimates

| | -FQ2 2017- | | | -FY 2017- | -FY 2018- | |
|-----------------------|------------|---------|----------|-----------|-----------|----------|
| | CONSENSUS | ACTUAL | SURPRISE | CONSENSUS | CONSENSUS | GUIDANCE |
| EPS Normalized | - | - | - | 0.27 | 0.29 | - |
| Revenue (mm) | 6113.00 | 6398.50 | ▲4.67 | 23721.13 | 24887.38 | 31000.00 |

Currency: EUR

Consensus as of Jul-19-2017 3:01 PM GMT



Call Participants

EXECUTIVES

Fernando Mata Verdejo
Executive Director

Natalia Arana

Ramón Carrasco
Group Chief Risk Officer

Presentation

Natalia Arana

Good afternoon, and welcome to MAPFRE's result presentation for the first half of 2017. As in previous quarters, Mr. Fernando Mata, MAPFRE's CFO and member of the board, will take you through the key highlights and main trends of the quarter. And I will also help him with the Q&A session. Also in this occasion, it's a pleasure to have Mr. Ramón Carrasco here with us, MAPFRE's Chief Risk Officer. He will give us an update on MAPFRE's Solvency II figures as well as ongoing developments on the implementation of Solvency II.

We continue working to improve our financial disclosure in response to the feedback we have received. We have included a slide and a spreadsheet data focusing on quarterly standalone figures. We hope this information helps you better understand our results. I would also like to point out that our financial statements and management report, along with their corresponding audit reports, are available today in both English and Spanish on our website. At the end of the presentation, we will answer all the questions that were sent to the specified e-mail address. As usual, the Investor Relations team will be available after this call if you have any further questions.

Fernando, the floor is yours.

Fernando Mata Verdejo

Executive Director

Thank you, Natalia, and good morning, good afternoon, everyone. A pleasure to be here again. Let me take you through the highlights of the period.

As you can see on Page 4, the increasing premiums was the main driver of our solid revenue growth as financial income was affected by lower reinvestment yields across LATAM and Europe. During this period, we have seen an increase of over 8% in premiums with nearly 10% growth in the Life business and close to 8% in Non-Life. Growth was affected by 2 large policies: in 2016, a large group savings policy for over EUR 130 million and in June 2017, a multiyear policy in Mexico for almost EUR 500 million. Excluding this, premiums will have increased by over 5% with nearly 16% growth in the Life business.

We've seen positive trends in the majority of the business units. In Spain, I would like to mention the strong performance of the Life business, thanks to the launch of new products and campaigns. Retail Motor and Health are also growing, thanks to the economic recovery. In the U.S., the Motor segment in Massachusetts has performed well, thanks to tariff increases. Also currency movements, mainly the Brazilian real and to a lesser extent, the U.S. dollar, have also had a positive impact on premiums.

Let's move to the next page. The combined ratio stands at 97.2%, 40 basis points lower, despite the effects of Coastal El Niño. You remember the heavy rains on Peru. This is by far the largest cat event of the period with nearly EUR 58 million of losses incurred, adding approximately 80 basis points to our combined ratio. The loss ratio fell by 20 basis points. We've seen positive performance in the following countries. In Turkey, the Motor loss ratio improved by nearly 6 percentage points, thanks to a stricter underwriting policies and tariff increases. In Spain, the Motor loss ratio fell by 70 basis points. And in Brazil, in Non-Motor lines, the combined ratio fell nearly 5 points to 80.1%. This excellent level helped offset the difficult market environment in Motor.

On the other hand in the same period, 3 large claims impacted the GLOBAL RISKS unit, which reported a loss of EUR 30 million for the first time in its history. Regarding expenses, our strict cost containment initiatives led to a decrease of 20 basis points in our expense ratio to 27.4%, well below our strategic target. This improvement was especially remarkable in Italy, thanks to the business restructuring implemented last year as well as in Spain with a 60 basis point reduction and in Mexico with a 5 percentage point reduction.

Finally, the net result grew by over 9%, reaching EUR 415 million with an ROE of slightly over 9%. This reflects excellent performance of our core units, mainly Iberia and MAPFRE RE as well as the relevant

improvements of businesses that have undergone restructuring processes, especially Turkey, Colombia and Italy.

Please turn to Slide 6. Shareholders' equity decreased by nearly 3% in the period, mainly as a result of the depreciation of several of our currencies, especially the Brazilian real, which has fallen almost 10% this year as well as the U.S. dollar and the Turkish lira, which have both depreciated close to 8%. Assets under management continue to grow steadily, supported by the rally in equity markets and the positive evolution of the mutual and pension fund businesses with over 8% growth as a result of the successful implementation of MAPFRE's strategy to grow in asset management. On the other hand, the increasing interest rates in Europe seen during the quarter has led to slight decrease in the value of the investment portfolio.

Let's now turn to Slide #7. In this slide, we have included quarterly standalone figures. Regarding the main impacts in the quarter, it's worth mentioning the following. Premiums in Iberia have fallen in the quarter as a result of the seasonality effects in Health and the concentration of life savings campaigns during the first quarter. Regarding claims experience, despite additional losses reported from the Coastal El Niño in Q2, we've seen a lower level of large catastrophic and industrial claims in Brazil, LATAM North and MAPFRE RE. In Spain, there has been a pickup in frequency in Motor and a large fire claim.

Regarding real estate, the sale of a building in Madrid [indiscernible] consolidated gain of EUR 29 million. As we mentioned last quarter, we have applied more conservative methods to value our land portfolio, which resulted in additional provisions with a net impact of almost EUR 9 million. There were also some one-offs impacts from corporate transactions during the quarter. First, the full consolidation of ABDA as of June 1 resulted in a EUR 13.5 million net gain. This is due to the update of the fair value of the initial 20% stake that we worked 4 years ago. Second, selling agreement of the DUERO life and pension and the sale of the annuity business in Peru generating net gains of almost EUR 6 million and EUR 4 million respectively.

Please turn to Slide 8 to look at premium trends by regions in more detail. As far as units, the core of our business represents 75% of MAPFRE's premiums. Over 16% comes from MAPFRE RE. The remaining is split between GLOBAL RISKS and assistance. I would like to point out the following. Iberia accounts for over 27% of total premiums. The variation in this region amounts to 4.4%. LATAM represents 31% of the total premium with over 22% growth, largely due to LATAM North, where the already mentioned PEMEX policy has pushed the premiums. International accounts for 16.6% of premiums. North America premiums are up over 2%, mainly due to the growth in Retail Motor in Massachusetts. And finally, MAPFRE RE represents over 16% of total premiums, showing solid growth overall in Non-Group business and also due to the inclusion of the reinsurance program of the direct business in Italy we mentioned in the first quarter presentation.

On Slide 9, we'll take a look at the evolution of profit in these regions. Results show the consolidation of our profitable growth strategy in Spain. And we are also starting to reap the benefits in EMEA and LATAM. Iberia continues to be the key contributor to profit with a 53% share. It's worth mentioning the improvement in the Motor combined ratio, almost 2 percentage points to 93.5% as well as the contribution of the Life business. LATAM has improved in the first half, mainly thanks to good performance in the Life business in Colombia and Peru. International shows significant growth, thanks to the excellent performance in EMEA, especially in Turkey and in Italy, where losses have been significantly reduced.

MAPFRE RE net result increased by 12.5%, supported by lower frequency and significant gains in cat losses. Profit contribution from the U.S. business is also remarkable. On the negative side, as we said before, GLOBAL RISKS was hit by several large claims. We will give you more details on this later. Finally, the reorganization process continue at MAPFRE ASISTENCIA, where recovery is taking longer than expected. The assistance unit has varying costs from the cancellation of unprofitable contracts and the closing of some operations. Overall, the improvements in the larger businesses, mainly Iberia and RE, were strong enough to offset losses in other smaller units.

Please now turn to Slide 11. [indiscernible] with a lot of information, by the way. I would like to comment on the main drivers of the evolution of the net result as well as extraordinary items. This chart shows a variation from the net result for both premiums. First, I would like to explain the changes in Non-Life.

There was an over 20 -- EUR 85 million increase in underlying technical result, thanks to improvements in underwriting and cost-containing initiatives. The U.S. dollar depreciation has also helped to reduce claims cost in both LATAM and MAPFRE RE. This was offset by a EUR 57.6 million loss due to the Coastal El Niño, mainly affecting GLOBAL RISKS and MAPFRE RE. The non-technical result had a EUR 30 million positive impact due to the extraordinary expenses in 2016 that we haven't had this year. The EUR 73 million reduction in underlying financial result is due to the U.S. dollar depreciation and lower reinvestment yields in Brazil and in the euro area. There was an over EUR 8 million reduction in the level of realized capital gains net of write-downs.

And now regarding the Life business, profit increased by EUR 50 million due to the improvements across the board, Iberia and Colombia being the most relevant. There was a reversal of provision in the bancassurance channel in Spain amounting to EUR 29 million already reported in the first quarter. In addition, there were several corporate transactions that had a EUR 26 million impact on pretax results during the quarter. The figures and breakdown between Life and other activities are fully disclosed at the bottom of this slide. Further, taxes have decreased as a result of a different business mix, Spain is the largest contributor, and a reduction of taxes in the Brazil, thanks to the Agricultural business, as you know, which has the tax reliefs. Lastly, the increase in noncontrolling interest is due to better performance of bancassurance subsidiaries as well as the appreciation of the Brazilian real.

On the next page, we'll look at trends in Non-Life premiums. Non-Life premiums have grown by 7.8% with an excellent performance in our main markets. In Iberia, growth was notable in Retail Motor, 3.3% year-on-year and over 7% in June. The average premium grew slightly higher than the market as usual and the number of vehicles insured increased by almost 50,000 during the first half of the year despite fleet cancellations. In fact, we're growing above the market at a 4.7% rate.

Regarding LATAM North, premiums include the 2-year PEMEX policy. And excluding this impact, premiums would have fallen by 4%. MAPFRE Mexico showing an over 38% reduction in Motor premiums in local currency due to the portfolio review we're carrying out. In Brazil, solid local currency growth in Industrial Risks and Agricultural lines helped to offset the difficult situation we're living in Motor.

In United States, higher Motor premiums in Massachusetts have been supported by tariff increases. In the other states, premiums have fallen by over 7% in U.S. dollars as a result of lower underwriting activity in some of them. In EMEA, growth in Germany and in Italy has been remarkable. In Turkey, premiums have fallen as a result of the strong depreciation of the Turkish lira. Number of vehicles insured has fallen by over 340,000 in the last year. In additional, the others' premiums have fallen by 15% in local currency in the current quarter.

Please turn to the next slide. MAPFRE's focus on cost containment and strict underwriting continues showing results. Improving claims trends in several main markets helped to offset other negative developments. In Spanish Motor, we see the stability in Baremo related to claims cost and a positive evolution of VERTI's business, good evolution on increasing Motor. In Mexico, there have been improvements in General Insurance and Health lines, although Motor is still having difficulties. The U.S. is benefiting from tariff increases and a solid performance of the Homeowner line with a remarkable combined ratio at 71.5%.

In Turkey, tariff increases and the rate improvements in Motor have led to a nearly 6 percent point fall in the claims ratio, very remarkable. In MAPFRE RE, the combined ratio has fallen by 4.5 percentage unit points, thanks to absence of relevant claims and the excellent performance of the U.S. business. However, this quarter figures were affected by 3 large claims in GLOBAL RISKS totaling almost EUR 50 million. 2 were already reported in the first quarter, the Coastal El Niño and a fire in a refinery in Abu Dhabi. And in the second quarter, there was a large claim in a power plant in Panama.

As you can see on Page 14, the Non-Life financial result fell over EUR 80 million compared to the previous year. Over half of this fall is due to lower foreign exchange differences, driven by the 8% depreciation of the dollar in this period. The remainder of the fall is claimed by lower financial income in Brazil due to several cuts in the selling rate, which is now at 10.25% compared to the high of 14.25%. Realized gains are slightly lower than the previous year's figure and include the EUR 48 million pretax gain in Iberia from the sale of a building in Madrid.

On a consolidated level, this capital gain is reduced by EUR 10 million [indiscernible]. Also we booked in the second quarter an additional provision line amounting to almost EUR 12 million. Finally, we have to point out the high level of unrealized gains of nearly EUR 180 million on our actively managed equity and mutual funds portfolios. These give us leverage to take advantage of future market opportunities in the second part of the year.

Please turn to the next slide. Now we can take a look at the evolution of the Life business in Iberia. Premiums grew by 9%, thanks to the successful launch of the new savings products and sales campaigns, especially unit-linked. There are also improvements in margins across the board. Realized gains include the impacts from the sale agreement of UNIÓN DUERO life and pensions and the reversal from the provision in the bancassurance channel as already mentioned. In Brazil, premiums have grown by over 9% as a result of the appreciation of the Brazilian real. In local currency, they have fallen by around 5% as a result of the lower lending activity in the bancassurance channel. High margins in Life-Protection helped offset the decline in financial income. LATAM South reflects an EUR 8 million gain for tax annuities from the sale of the annuity business in Peru. We've seen improvements in Colombia as well as a result of the portfolio cleaning measures taken last year and they are also boosting our results.

On the next slide, we will look at the evolution of our capital base this year. Shareholders' equity fell by EUR 267 million in the year to EUR 8.8 billion. The decline was largely driven by market movements: first, several of the main currencies depreciated, especially the Brazilian real, the U.S. dollar and the Turkish lira; and second, [indiscernible] in financial assets available for sale, which reflects 2 opposing movements: first, an increase in the value of equity investment in the [indiscernible] market; and second, a decrease in the value of fixed-income investments due to the current yields in Europe, largely mitigated by shadow accounting.

On Page 17, we'll take a look at the investment portfolio. Our investment strategy has continued in line with the first quarter with slight reduction in fixed-income assets, mainly reinvesting in equity but also in alternative assets. We were also active in primary markets. Regarding asset allocation, exposure to government debt has gone from 58% to almost 55% and corporate debt from around 21% to 20%. On the other hand, equity and mutual fund exposure have it increased by 1 percentage point.

Now turning to Page 18. We summarize our capital structure and debt position. On the left side, you can see the composition of the capital structure, which amounted to EUR 13.5 billion and the largest of which is equity with 81% of the total. During the quarter, we partially paid back the syndicated credit facility, which finished June with a balance of EUR 320 million compared to EUR 480 million at the end of March. Also this past Monday, we've redeemed our outstanding subordinated bond that was issued in 2007. On the right side, you can see our leverage of nearly 20% and our interest coverage at 21x earnings before interest and tax. Both figures are favorable compared to our peers.

Please now turn to Slide 19, where Ramón Carrasco, our CRO, will present the Solvency II figures. Thank you, Ramón. [indiscernible]

Ramón Carrasco
Group Chief Risk Officer

Thank you, Fernando. Good afternoon. It is a pleasure to be here today. The solvency information that we are presenting today corresponds to March 2017. The 211% Solvency II ratio is based on a high-quality capital structure of more than EUR 9.6 billion in eligible own funds with a high share of unrestricted Tier 1 capital. The proportional increase in Tier 2 capital this period is due to the fact that these figures include the subordinated bond that was called on the 24th of July, along with the subordinated debt issued in March of this year. Excluding the called bond, the pro forma Solvency II ratio will be 198% with 93% of Tier 1.

MAPFRE's fully loaded Solvency II ratio, excluding the impact of the transition on measures for technical provisions and equity, stands at 192%. In the first quarter of the year, the figures reflect the first phaseout of the transitional measures for technical provisions and equity, which as you know are effective for 16 and 7 years, respectively, starting in 2016. The impact of the matching adjustment is limited, around 5%. But

it is a very useful tool in case of significant spread increases, in which case [indiscernible] will be much higher.

On the next slide, we include information about the composition of the Solvency II eligible own funds. As you can see, we start with IFRS equity, valuing the participations not included under Solvency II and intangible assets at 0. The value of subsidiaries under equivalence. And this is Mexico, the United States and Brazil and is adjusted. And they're valued by recognizing [indiscernible] in line with local rules. Real estate and other assets are valued at the market value. Accounting provisions are valued under Solvency II criteria. Finally, subordinated debt is aggregated to get the total eligible own funds.

The figures on the right of the chart show the evolution of the funds in the quarter. As you can see, the most important increase is due to the subordinated debt issued in March. On the other hand, there was a reduction stemming from the difference between accounting and Solvency II provisions, which is explained by 2 factors. First, Solvency II provisions have gone up because expected profits corresponding to future premiums are recognized only in the annual calculation. Second, the reduction from the phaseout of transitional for technical provisions had an impact of EUR 50 million.

Please turn to Slide 21. The composition of the capital requirements is stable compared to the previous quarter, given that this is calculated annually. On the next slide, we will take a look at recent developments in Solvency II implementation. MAPFRE continues evolving its capital models. We are currently restructuring processes to streamline Solvency II calculation to move up and [indiscernible] Solvency II figures. Analyzing the feasibility of using the equivalence method in Puerto Rico, analyzing the best treatment for the Indonesian insurer ABDA, where our stake went from 20% to 51% in the second quarter. We have decided to split this entity from the Solvency II parameter as we're already doing with all our small entities. Finally, we are adapting our longevity, mortality and Motor underwriting models in order to be able to calculate regulatory capital for Spanish entities.

Let's move on to Slide 23 to give you a quick overview of MAPFRE's embedded value figures. The full presentation is already available on our website. First of all, we must mention that we have changed the methodology of the calculation from European embedded value to market consistent embedded value. 2015 figures have been adjusted accordingly. Embedded value has proven resilient despite a challenging market environment. Our total embedded value grew by 44% in 2016. And over time, our embedded value remains high, over 10%. This improvement in Spain by the inclusion of Burial business of MAPFRE España as well as the Life businesses of BANKINTER VIDA in Portugal and MIDDLESEA VALLETA in Malta, the positive impact from the deviation of actual value from expectations which primarily reflects adjustments of financial investments.

This is all from my side, Natalia.

Natalia Arana

Okay, thank you very much, Ramón. Thank you very much, Fernando. We hope you have found this presentation useful and that we were able to touch upon the main topics that interest you. And now as noted, we will try to answer all the questions as time allows. Nevertheless, if there are any remaining doubts after the presentation, please feel free to contact the Investor Relations team, and we will be more than happy to help you with whatever you may need. Now we are going to start with the first -- with the Q&A session.

Question and Answer

Natalia Arana

The first question comes from Farquhar Murray from Autonomous. He asked the following questions regarding extraordinary. Please could you explain the additional Coastal El Niño losses in Q2 2017? Why are these larger than in Q1? And why this was not flagged as results in May?

Fernando Mata Verdejo

Executive Director

Yes, thank you. I mean, it was an event that was difficult to capture in terms of claims. And the losses were large, mainly in GLOBAL RISKS and MAPFRE RE, approximately 2/3 affecting MAPFRE RE in retention and 1/3 to GLOBAL RISKS and a small proportion impacted Peru, I mean, the insurance operation. I mean, it was due to the low retention that their company has. Recognition of the effects of the claims taking place above all in the second quarter because of these negative loss development in the second quarter, it was new claims [indiscernible]. And also there is an increase [indiscernible] in the risk costs of some claims and affecting mostly MAPFRE RE. I want to point out that this cat event is not a well-known catastrophic event in the reinsurance market. But it has had a significant impact for MAPFRE both in insurance and reinsurance business. I mean, the figures, I can't disclose it. I mean, for Peru, it was the gross before the -- I mean, in terms of claims, the net profit contribution for Peru was EUR 2 million and MAPFRE RE was EUR 33 million, more or less and Global approximately another EUR 23 million, totaling EUR 58 million before taxes [indiscernible].

Natalia Arana

Also Andrew Sinclair from Bank of America Merrill Lynch would like to know or to have some color on the development of prior year results in the period. Have there been any notable releases or [indiscernible]?

Fernando Mata Verdejo

Executive Director

Thank you, Andrew. I mean, nothing relevant to comment as in previous years. As we said, the average cost from Baremo is quite stable during the first quarter in 2017 and in line with our [indiscernible]. Regarding the special provision that was accounted for in previous year in order to cover those deviation in the former Baremo, the amount remains the same. And we will update, I mean, situation in the year-end in order to propose any releases.

Natalia Arana

Now taking advantage that Ramón is here, we are going to -- we have some Solvency II questions. The first one comes from Farquhar Murray from Autonomous. What are the adaptations MAPFRE is hoping to make to the Solvency II internal model with regard, for instance, to Motor underwriting risk and mortality? Should we expect favorable changes in the SCR from this exercise? And what is a realistic time frame for reaching a conclusion on this?

Ramón Carrasco

Group Chief Risk Officer

Well, thank you, Farquhar, for the question. We're currently -- as you know, we're currently reporting Solvency II figures with a standard formula. We already have internal models only for internal risk management purposes. What we are doing now is adapting our internal models in order to use them to calculate regulatory capital requirements for the Spanish entities, which we expect will lead to lower capital requirements for these entities.

Natalia Arana

Also, regarding Solvency II, Andrew Sinclair from Bank of America commented: your Solvency II ratio looks strong on your trade rating also, which you have previously mentioned as a binding constraint

has been put on positive what? Can you tell us how you see your excess capital versus the trade rating constraint? Do you have plans to put any of this excess capital to work?

Ramón Carrasco
Group Chief Risk Officer

Thank you, Andrew. This positive outlook is really a very recent event. As we have mentioned before, we feel comfortable with our current capital position and it is aligned with our risk appetite and rating objectives.

Natalia Arana

Now we'll start with a set of questions regarding Brazil. The first one comes from Andrew Sinclair, Bank of America Merrill Lynch and Sophia [indiscernible]. Could you please give us details of Non-Life pricing dynamics in Brazil?

Fernando Mata Verdejo
Executive Director

Thank you, Andrew. Well, Brazil is quite -- we live in a difficult situation due to the tough competition. As you know there are big guys in this market in Brazil. MAPFRE is quite big as well, but there is a lot of competition. What we've done is -- rather than being in this war price what we're trying to do is to fulfill the process of sanitation of our portfolio, focus on our strategy of profitable growth. And also we have to reduce our pension expenses particularly our [indiscernible] expenses where they're quite low, being more competitive in terms of expenses rather than further price reduction.

Natalia Arana

Also, can you talk more about complicated situation in Motor in Brazil? What is the outlook there?

Fernando Mata Verdejo
Executive Director

Well when we say complicated situation, it was because the -- it was the integration of the combined ratio for automobile. It was like, if I remember well, [indiscernible] like a 3 percentage points. It's tough competition and regulatory change that we already mentioned in previous presentations. [indiscernible] has implemented 30% reduction in the tariffs for compulsory insurance. And -- but in that case, it is different than Turkey. This is important to take into account and this coverage has quite low weight in our MAPFRE Brazil portfolio. Our operation in Brazil is very well diversified and other good performance line of business allow us to offset the current negative trend in automobile. So overall, I mean, we are quite happy with the resilient performance of the Brazil.

Natalia Arana

Also, in terms of the agriculture insurance market, can you tell us more about this market -- evolution of this market in Brazil?

Fernando Mata Verdejo
Executive Director

Well, this line of business is quite difficult to predict. As you know, agriculture insurance has a teen growth in premiums in local currencies. But in any case, this has been extremely difficult to anticipate the evolution of this business because it depends on government aids and I'm not sure the interest apply -- interest rates apply.

Natalia Arana

In general, in Brazil, what are your expectations in terms of Life premiums in Brazil?

Fernando Mata Verdejo
Executive Director

Well, the Life business fell 5% affected by the drop in Life prediction insurance leading to personal loans from Banco Do Brasil. The evolution in the next quarter will depend on the recovery in the economy and also the distribution of personal loans from our bancassurance [tenant] Banco Do Brasil.

Natalia Arana

Now the next set of questions is with regards to the evolution of the business at MAPFRE USA. Andrew Sinclair, Bank of America would like us to provide details of Non-Life pricing dynamics in the U.S. market?

Fernando Mata Verdejo

Executive Director

Yes. As you may already know, we usually talk about the U.S. market and rather than U.S. market, we're talking about 50 different U.S. markets. So let's say that the U.S. market pricing dynamics vary from state to state. Some are Motor related than others that depends a lot on the local regulator. Our experience tell us that when the higher prices are necessary, the regulator is supportive and in the end they tend to be in line with the rest of the market. For example, during the quarter we filed for 3.8% increase in Motor tariff in Massachusetts that we expect to put in the market in a quite positive way.

Natalia Arana

Also, Michael Huttner, JPMorgan has some questions regarding the U.S. business. One of these is what is the action plan for the U.S.? I see a reference to minus 7% premiums outside of Massachusetts. And I would like to know if there a specific actions? Which states you are withdrawing from? Where are you in the most challenging state, which I think is New Jersey?

Fernando Mata Verdejo

Executive Director

Thank you, Michael, you've been around saying that New Jersey is a tough state. I already have mentioned we have already taken several measures in mainly reducing our sales and underwriting and commercial activity as well as increasing tariffs across the States. We're still analyzing our strategic planning in the U.S. We had different meetings, both at the corporate level and also in the U.S. and hope to give more detail in the coming months when the meetings for strategic view were completed in the third, fourth quarter. The short release will be, I'm sure available at the end of this year and our final geographic footprint will look like in the U.S. We have mentioned in previous forecast situation that both New York and New Jersey, they both are quite challenging states, but they're still. Surely this is still to be done. And we're quite comfortable with the current performance results in Florida and California, but we haven't yet taken formal final decision on the state we will operate in the future.

Natalia Arana

Now the next question is regarding strategy. Regarding the ROE target, Niccolo Dalla-Palma at Exane BNP Paribas and Michael Huttner at JPMorgan would like to know how confident is MAPFRE to reach the 11% target? Are you going to use real estate gains to bridge the gap?

Fernando Mata Verdejo

Executive Director

Thank you, Niccolo and Michael again. We said in many occasions this is the most challenging target. Had to be quite moderate and optimism since some units are not performing as expected. But still we believe that until 2018 we will try to achieve our strategic targets and the 11% ROE is one of these. We already mentioned many, many times we're not going to do cosmetic accounting in order to achieve this target. We don't realize those real estates that they are not at the right market price, nor the current unrealized gains on equity which we reported amounting at 3 of June of EUR 180 million. I'm rather than the real estate will be this year, to improve our ROE producing our capital base and realize gains and then putting in the profitable account and including our net result. But we're not going to do it. We will sell our real estate units and we will realize gains on the equity according with market conditions. The majority of the realized gains were made during the first quarter, during the second quarter we're quite passive and we're

waiting to have more evidence in the [indiscernible] both and other market rally in equities in order to not to lose good market opportunities.

Natalia Arana

Now we have an next set of questions regarding Iberia's operation. The first one is sent by Andrew Sinclair in Bank of America, Silvia Rigol from BBVA and Michael Huttner at JPMorgan. First one, can you please give us the net premiums earned by line of business, especially in Motor? What was the combined ratio in Motor for the second quarter stand-alone?

Fernando Mata Verdejo

Executive Director

Yes. Thank you. In Motor, the net premiums earned were EUR 956.9 million, approximately EUR 960 million in June 2017 and approximately EUR 470 million at March 2017. Stand-alone combined ratio for Motor in the second quarter of the year was 95% compared to 92% in the first quarter. As we explained during our first quarter presentation, the first quarter was superb in terms of weather conditions. And also, what we saw is quite stable figures in terms of frequency, and again, during the second quarter we see a rise in frequency due to an increase in both number of cars sold and also more mileage as well.

Natalia Arana

Also in Spain Motor frequency is up. Can you say what action you are taking there? What rate rises? And whether for Iberia the 95% combined ratio is one you are comfortable with?

Fernando Mata Verdejo

Executive Director

You put it right. We see an increasing Motor frequency in Spain as we already mentioned, approximately 1% of tariff rise for 2017 was fully reported to the suspected increasing frequency. And so overall, I mean the way we're going to offset the increasing frequency is increases in rates based on our weight. But also I should include the cancellation of unprofitable policies, mainly fleets and cost containing efforts will help us to reduce this increase in the loss ratio. So even though we can see increases in frequency in Spain, we think we are in the right path and in order -- well prepared to keep the current good levels of combined ratio. It is difficult to see a 95% is the perfect combined ratio. It's quite positive. But it's in line with our targets. We can get lower. We try -- we'll go for a 95%, let's say, a long-term sustainable combined ratio.

Natalia Arana

And regarding pricing dynamics in Iberia. What can you tell us about that?

Fernando Mata Verdejo

Executive Director

Yes. The pricing dynamics in...

Natalia Arana

In Non-Life?

Fernando Mata Verdejo

Executive Director

In Non-Life, yes. The pricing dynamics in Iberia are improving as we see because their economy we're seeing consumption and it's helping insurance premium. Approximately 500,000 new cars were added to the portfolio in fleet for Spain. And approximately 450,000 new cars sold during the first quarter. So I guess that the -- being new cars -- they will help us to move from compulsory insurance to full-coverage insurance and will help us to increase the premium average. At the same time, after the implementation of Baremo many companies are increasing tariffs on motor. MAPFRE is not doing this. We're trying to cover new deviations in coverage with tariff raises, but not for Baremo. Baremo was fully covered in 2015 and for us it's history. This just is current business.

Natalia Arana

There is one question regarding real estate disposal. More or less, you have answered that -- about that before, but they want to know if this -- that's the second disposal in 2 years? Have you got any other upcoming disposals you can flag?

Fernando Mata Verdejo

Executive Director

Well, I mean, it's difficult to predict market conditions and also those that we can't materialize during the second half of the year. Majority of our units dealt significant improvements in the main cities in Spain. They are 20 years older or even more and we have to either rebound with another investment in real estate or well to sell them because they are not in the best place in the prime rate place in the cities. There are number of 2, 3, significant buildings that they are in the market currently. But it's difficult to predict those capital gains we'll materialize during the second part of the year or next year. I mean, we are not hungry. I mean, we don't have this appetite in order to realize gains just only when the market price is the right one and at this time for our rotational buildings we'll make it. On the other hand, we're quite active as well in looking for new investment opportunities in both alternative business, alternative portfolios also in the real estate market. So we could see both in sale or buying new opportunities, both direct or indirect through pension -- sorry, through real estate funds or [indiscernible] or whatever the vehicle that we'll be covered for MAPFRE.

Natalia Arana

Now we have a question to -- a couple of questions regarding LATAM North. The first one comes from Farquhar Murray in Autonomous and Niccolo Dalla-Palma, Exane. They want to know why premiums are falling in LATAM North with PEMEX policy. Which businesses are experiencing decline?

Fernando Mata Verdejo

Executive Director

Yes. Thank you, Niccolo and Farquhar. Mexico P&C has been positive performance and that's Life. However, we are moving from commercial business to personal lines. And personal lines is the main business for MAPFRE and it's where we can apply our knowledge of doing best practice of our business knowledge. There is a 38% fall in premiums in motor in local currency as we reported. What we're doing is the application of stricter underwriting policies, fleet cancellation, rate adjustments and nonrenewal of loss-making contracts. We're analyzing as well some distribution channels from brokers and the portfolio is quite unprofitable and we concern in those portfolios. Has line of experience any level percent falling premiums in local currency to as well, to non-renewal of some group loss-making contracts. The rest of country, we're quite positive. Premium growth shows positive --favorable development in the Dominican Republic, and also Central American countries especially Panama and [indiscernible], Dominican Republic, Panama and Central America all the countries together, the 3 of them, they're reporting premium growth over 10%. So it's quite positive figure.

Natalia Arana

And also in LATAM North. They want to know what's the expected profitability of the PEMEX policy. Will that it cover effectively?

Fernando Mata Verdejo

Executive Director

Yes. As you know, this are very complex policy where the rate is distributed more than usual and that means that the retention is very, very low. So there is a quite low risk appetite for MAPFRE. And therefore the benefit is always reduced. Importance of this policy is the MAPFRE capacity to manage the GLOBAL RISKS of this nature. With the land insurance of global rates in LATAM. And I am not sure it was public tender so MAPFRE get in the renewal in that there are lot of confidence in MAPFRE as very good deliver in policies that side. So we're pretty confident that we will perform expected.

Natalia Arana

Now we are moving from Mexico to Turkey. This is about what are your expectations for premiums in Turkey?

Fernando Mata Verdejo

Executive Director

Yes, the business in Turkey evolves very positively. The figures are fantastic at the end of this first half of the year. The thing is, as you probably know, earned premiums are coming from the tariffs and premiums that we increased last year. So MAPFRE Genel Sigorta is adjusting tariffs to the new market conditions that we know well and implementing measures to reduce impact in the performance of the business. We reported the average premium for compulsory insurance for the second quarter was 18% approximately and quite low below our expectation this was according to the different geographical areas and also the segments of vehicles was 30%. So, so far the damage is being limited and overall we're quite optimistic. We believe that we can offset part of this loss with the increase in other coverage in other line of business considering the proper diversification of our portfolio in Turkey.

Natalia Arana

And in order to give you a little time up to relax. We are going to ask Ramón Carrasco a question about Solvency II. Michael Huttner from JPMorgan would like to know what -- how much is the benefit of the equivalence adjustment for Brazil and the U.S.?

Ramón Carrasco

Group Chief Risk Officer

Okay. Second part of question. The benefit mainly is not on capital requirements. It's allowing these entities to apply the wrong rules to calculate the capital requirements and so to be able to compete in the market in the same level playing field. It is intensive equivalence as you know the U.S. we include accordingly to what is expected by the European supervisor, where we are including 3x the authorized control level to these entities, in Brazil it's more or less the same. We are well capitalized there but -- and we feel comfortable with a lot of regulations that we are applying.

Natalia Arana

And also Michele Ballatore from KBW. Regarding -- he is asking regarding the insurance unit. And his question is could you please give more color on the strong underwriting performance of MAPFRE? 2Q's have historically have a lower technical profit or changed?

Fernando Mata Verdejo

Executive Director

For both MAPFRE and GLOBAL RISKS large claims are not evenly distributed through the year. Unfortunately, MAPFRE is properly diversified and what we've seen in GLOBAL RISKS we haven't seen in MAPFRE. So fortunate we're putting them together, the net result is quite positive. And focused on MAPFRE, we're seeing lower frequency of floods claim and cat losses, despite already mentioned coastal Nino. I'm not sure I would like to mention as well the profit contribution from the U.S. business which is quite remarkable. As you know there is a 30% quota share that is being seeded by our direct operations in the U.S. so the net profit contribution is being booked in MAPFRE. But the underlying region of this business obviously belongs to the U.S. business.

Natalia Arana

Okay. Let me see. We can -- yes, let me see -- because -- we are seeing lower -- sorry, Niccolo Dalla-Palma -- sorry, I'm not following the questions, Niccolo Dalla-Palma from Exane BNP Paribas has also a question regarding the disclosure of net premiums earned by line of business in Iberia. We can provide more detail on Motor, General, P&C and health and accidents in the Spain. Because it doesn't include their earned premiums to be able to reconcile the Iberia P&L. This is a question also we have received from Silvia Rigol from BBVA. This information has not been released yet, but if there are numbers will we release in 2 months and [indiscernible] with the technical accounts. Anyway, we think that we can give you these figures since you have asked about that. And if we talking about Motor, second quarter

premiums accumulated in Spain where EUR 956.9 million. In terms of multiple insurance, General insurance, they were EUR 710.9 million. And health and accidents, they were EUR 259.1 million. In March, in order to give you the idea of this stand-alone quarter. In March, the premium for Motor were EUR 469.5 million. In March, also General insurance these premiums were EUR 362.4 million. Health and accident these premiums were EUR 127.5 million. We can go through these numbers after the call if you need also but feel free to call us if you need not more details, but if you haven't got quite well a specific figure. Now there are more questions. I think these are the last questions we have received today. So there are several items of topics here. The Niccolo Dalla-Palma would like to know, you mentioned in an answer earlier that you could review the provision for Baremo at year-end. Your comment seem to suggest you might propose a release. Would you definitely say a release is more likely than an increase?

Fernando Mata Verdejo

Executive Director

Thank you, Niccolo. Very important question because perhaps, I wasn't enough clear when we mentioned this point. We had to differentiate both provisions. First is the current [indiscernible] provision for Baremo claims or for auto claims, which is being been update on a quarterly basis and reflects both the number of risk and also the difference in the adjusting periods and also average cost and so on. And the second is the extraordinarily provision that we allocated, we appropriated in -- 2 years ago, in order to cover deviation from the former Baremo, just in case of the prior years were in limbo because of Supreme Court decision, or whatever, I mean we'll be settled at the current -- at the new Baremo. Answering your question, I mean, it's more likely a release because the -- my view is that you will never -- with information we have now, it will be never an increase because so far there is no new sentences coming in order to settle current claims -- sorry, forming claims with the current Baremo. So as usual, at the year-end, we update our analysis on this provision but it is more likely a release that and my prediction, my forecast is that we won't have an increase.

Natalia Arana

There is one question. I think we -- it's been also already answered. It's regarding the suicide rate reduction that introduced for some coverage up to 30%. Is this already reflected in the numbers or will it feed through in the coming quarters?

Fernando Mata Verdejo

Executive Director

Yes, first this 30% is an average of the different segments and sort of vehicles. This will be reflected in the numbers gradually. It is quite similar to Turkey as well. In any case, we're talking about as a quite small portfolio in -- regarding the size of Brazil. So we do not expect [indiscernible] impact in our MAPFRE Brazil results as a whole. We'll be trying to offset to mitigate this effect with reduction of exposure, also canceling distribution channels [indiscernible] Brazil brokers that they are performing a negative on the results, that's it.

Natalia Arana

Okay. Thank you very much, Fernando. Thank you very much Ramón. That's all from the Q&A session. We haven't received any more questions. Thank you very much.

Fernando Mata Verdejo

Executive Director

Yes. Finally, I would like to thank you for your presence today. Want to close the session with a recap. Has been relevant growth in both premiums and net results and improvements in technical results. Net results is very positive. You had to bear in mind that there is a reduction in the current financial income. We are taking opportunities of the markets but we are being quite prudent with our unrealized gain on our portfolio in both real estate. And regarding our strategic plan, the initially focus on the profitable growth strategy are showing quite positive results. And we expect this trend to continue in the remaining part of the strategic 3-year plan. And finally, for those of you who are setting up for summer holidays, we will do the best. Be happy. And above all, safe holidays. Bye-bye, and thank you, again, for your presence.

Natalia Arana

Thank you, very much. Thank you. Bye.

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