AXA 1H13 conference call transcript

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Mr. Mattieu ROUOT, Head of investor relations, AXA

Good afternoon everybody, or good morning, welcome to the AXA earnings presentation for the first half of 2013. Today, we will have a presentation led by Henri de CASTRIES, our Group Chairman and CEO. Denis DUVERNE, our deputy CEO and Gérald HARLIN, our Group CFO. As usual the presentation will be followed by Q&A. And with this Henri, I hand over to you.

Mr. Henri de CASTRIES, Chairman & CEO, AXA

Thank you Mattieu; good afternoon Ladies and Gentlemen, I go quickly with Denis and Gérald through the presentation to leave us as much as possible for questions.

First half of 2013

I think that the performance is a strong one with a combination of sound growth and improving margins. This is reflected in underlying earnings, they are up 16%, 11% on underlying earnings per share basis which puts us at the top of the range compared to our Ambition AXA ambition. Adjusted earnings are even up more, because they are up 26%. This is including the capital gains we have made on the disposal of some of the BNP Paribas shares where our remaining stake is now 2.9%. So, I think this is positioning us well. We intend to keep the amount of realized capital gains on a recurring basis within this range of €300-500M and the payout ratio as you know is 40-50 %, we have no intention to change it.

Underlying earnings

If you look back since we have started Ambition AXA have grown at an average of 6%. The performance of this half is helping lift it a little bit.

Return on equity

If you look at the return on equity of 16.5%, there is some seasonality in it, but what we want to show there is that we are comfortably in line with the 2015 Ambition, where we have set a goal of 13-15 %, we are even for this half slightly above that.

Operating cash flow

The operating cash flows is in line there too with the trajectory and the debt gearing is up 26% largely unchanged and there too - well on track.

More interesting may be for you, what is the business mix?

We know that our intention has been to have the General Account decline in proportion and to increase the amount of Unit-Linked products, because this is in the best interest of the clients, but also in the best interest of the shareholders because of the margins.

If you look at what has happened this semester, it is very much in line with the previous evolution, Unit-Linked is continuing to go up and has now moved from a little more than 30% in 2010 to more than 40% now. General Account has been reduced by approximately 50% over the last three years, this is in an environment where margins are continuing to improve and particularly noticeable in the fact that the General Account business is profitable again. It was already profitable, I would say marginally 5% last year, it is now 10 %. So, overall the NBV margin is at 33% which we think is a good and solid performance.

Property & Casualty
The Property Casualty business growth rate over the middle-term 4%, we are achieving this semester a good combined ratio below 96%, 95.7% and this despite some natural catastrophes and despite the fact that as we had told you in the past, the amount of boni extracted from previous years has a tendency to get slightly smaller. So, a solid performance in P&C, Denis will come back to that into more detailed.

Capital Management
Capital Management has remained active. We have undertaken during this semester a couple of transactions which are very symbolic from that standpoint:
- We have sold the MONY portfolio for approximately €800M.
- We also have initiated the disposal of the management company of AXA Private Equity.

So disposals in mature businesses or mature countries to free up capital for acquisitions in the emerging and we are particularly pleased with the transaction we have made in China, acquiring 50% of Tian Ping, the P&C Chinese player, with the intention to develop it as a direct player in the Chinese market.
Chinese people are buying 17 million cars a year whereas in the US only 13 million are sold. Many of these cars need insurance. The number of cars sold is going to increase, so it is really a very attractive market for P&C players going forward and the ambition we have with our partner as this partner has been saying, is to build the GEICO of China.

The efforts to reposition the Group towards high growth markets are continuing. There too, if you take a look at medium-term perspective since 2010, the growth rate in APEs has been 22% for the life business, it is continuing this semester. The life operations in the fast-growing countries are contributing to 16% of the Group total APEs. In the P&C, the growth rate has been 17%. It is now contributing to 14% of the Group revenues. So, you see that the target to get to 20% is perfectly reachable now with businesses which are sound and producing very decent margins.

In the semester, we have seen further growth from our ICBC venture in China. As an example, 39M for our share in APEs, we see that as a good evolution.

On Efficiency, we are well on track with our efforts, both on the savings side and on the investments to prepare the future. I do not think I need to insist on that, we had initially €1.5Bn savings' target, we have brought that up to €1.7Bn. I think, it is fine.

Our Solvency level is comfortable. It is up to 204%, this is not taking into account the positive impact of the transactions which have been undertaken during the first half, they would have lifted this ratio by a couple of points, a little more even. We think we are very comfortable at this level. This is not an issue at all. We have put as an indication the Solvency 1 number, even if we think that Solvency 1 is now irrelevant.

The businesses which have been challenging over the recent years are gradually recovering. If you look at the General Account Savings business, as I told you, our intention is to progressively reduce the proportion of this business in the total mix, so the net flows are negative. The margins are going up, moving up from 4 to 10 %, this is good. Unit-Linked is growing significantly for the semester.

The proportion of Unit-Linked products in the new sales in France is now around 30%. At the bottom of the market, it had gone down to 11-12%, so this shows you that the risk appetite of the clients in some of the key markets is gradually coming back.

In the US, the Variable Annuities (VA) portfolio has been behaving well this semester and I would mention also that the decision we took in terms of hedging at the end of last year has proved to be particularly appropriate. VAs have been producing decent Underlying Earnings.

Last but not least, Asset Management, flows are now for the second half-year back into a positive territory with €12Bn of net new inflows coming mostly from AXA Investment Managers, but coming also to a lesser extent from AllianceBernstein which is gradually recovering.

So, what is our intention now?
Continuing the efforts, especially given the fact that Denis and myself, we intend to continue to work for at least an additional 4-years. Our first priority is to deliver Ambition AXA, but we have to prepare for the future and beyond the Ambition AXA, because the very strong feeling we have is that technologies are going to transform the business faster than what many people anticipated. A combination of big data and digital is transforming both the understanding of the risks and the underwriting, and the distribution and the customer intimacy of these companies and these businesses.

So, rather than seeing as a threat, we see it as a great opportunity to try to stay ahead of the competition and we are working hard at understanding what is going on and trying to benefit from it. So, that is what I wanted to share with you before leaving the floor to Denis and Gérald. Thank you.

Mr. Denis DUVERNE, Deputy CEO, AXA

Thank you Henri; good afternoon everyone, we are going to talk with Gérald about the details of the financial performance. I will start with the Group earnings, a solid 16% growth as you have seen, a growth in Life, P&C, Asset Management that I will comment further, International Insurance, a slight decline coming from a combination of lower investment income and higher taxes at AXA Corporate Solutions for a large part. You see also that Banking had a solid first half and Holdings are pretty much in line with the previous years.

Looking at the Underlying Earnings development, you see that we have a strong contribution from Life, P&C and Asset Management. You see a negative €46M on Forex which is largely explained by the translation of our Japanese Earnings into Euros. There was a very strong decline of the Yen, the performance of our Japanese entity is very good and has largely offset that decline, but the Forex had a negative impact on our Earnings overall.

Adjusted Earnings had a very strong performance at +26%. Henri mentioned the BNP Paribas sale. Otherwise, we had approximately the same level of impairments as last year, but slightly higher capital gains even excluding the BNP Paribas disposal.

Net income is what matters most for the price, I know that you are significantly more sophisticated, so the main impact on net income are related to the mark-to-market of some elements of our P&L. Most of our derivatives are benefitting from hedge accounting, but some don't, mostly in the US, so for some we are not eligible for hedge accounting, that is the biggest negative. The second one is the mark-to-market of the non-consolidated funds that are in AFS P&L so available for salethrough P&L instead of AFS through OCI.

Exceptional operations – It is impacted by the disposal of MONY even though the disposal will only take place in the second half, but we take the negative impact now according to the accounting principles.

Restructuring costs – We have restructuring cost as we reduce our expenses year on year. This year, we have a more important impact coming from the write down of lease-hold improvements in the US both at AXA Equitable and AllianceBernstein where we have reduced staff considerably and we are vacating space as we sublease those spaces we have to take some write-downs.

On the Life side now, first talking about new business, it was up 8% in mature markets and 15% in high growth markets, a total of +9%. Asia continues to perform extremely well with a growth of 24%, Asia excluding Japan. This is partly offset by CEE which is done 29% as a consequence of the continuation of the negative reforms on the pension side after Hungary, we saw Poland; in Poland, they are now talking about a quasi nationalization of the second pillar of pension funds; so may be more bad news to follow, but clearly we have been disappointed by the CEE.

New business margins have increased by 4 points. This is an increase pretty much across the board, both in mature markets and in high growth markets coming from what Henri mentioned earlier, the improvement of our business mix which you can see in more details here with a growth of Protection of 9%, quite strong in Switzerland on good pensions, quite strong in Asia and Japan and also good growth in France and a margin of 54%. Unit-Linked is also progressing nicely at +21% with a 27% NBV margin, the growth here is quite strong in the UK and in the US as well as in the MedLA (Mediterranean and Latin American region.

G/A Savings

On the contrary is down 17%, in line with what we had mentioned before. The NBV margin is improving however, we were at 5% last year. We were negative two years ago. So, our margin on G/A Savings, thanks to re-pricing and redesigning of the products has improved.

Mutual funds

Our sales have grown 19%. This is coming from the UK and the US. The NBV margin is not significant as you know, because this business does not use any capital.

When you look at the net flows, you can see that we have tripled our net flows compared to a year earlier, €3.9Bn net flows against €1.3Bn in the first half of last year. Again, the allocation is in line with what we have announced, positive flows in Protection and Unit-Linked, negative flows in G/A Savings.

Looking now at the earnings, on the Life side, you see that the earnings are growing by 15% and the growth is explained by the growth in Savings and more importantly in Unit-Linked, but on the Protection side we see a slight decline of earnings coming from less favourable claims developments in France, Japan and the US.

On Unit-Linked, you see that we are doubling our pre-tax earnings, thanks to higher fees in revenues, because of the equity market performance, but also much better performance of our VA portfolio in the US.

P&C

Moving now to P&C, revenues are up 2%. They are up 1% in Personal lines in spite of a price increase on average of 3%. The portfolio is growing in Direct and high growth. We see a decline of volumes in mature markets more particularly in Belgium and Germany where we increase prices and I will show that indicator, more than the competition.

Commercial lines are compensating that with a growth of 4%, average price increase of 3.3%, but a portfolio growth, not only in high growth markets, but also in markets like the UK and France.

Looking at the price situation, on the left part of the slide, you see the price increases that we have implemented on our portfolio, 3% in Personal lines, and 3.3% in Commercial lines. You can see some very high numbers like 7.9% in Germany in Personal lines and 5.3% in Belgium. We have deliberately accepted to lose some portfolios to radically improve the positioning of the portfolio in those two markets where prices were positively oriented in the market and we thought it was the right time to accelerate the price increases.

On Commercial lines, the situation is also quite impressive in France with a price increase of 5.4% and an average of 3.3%.

Looking at the market pricing trends on the right side of the slide, here you do not have any insight into our own intention you have an insight of what we expect the markets to do. We see a continuation of price increasing in France and Germany. We see prices levelling out and sometimes coming down in the UK, Switzerland, Belgium and Southern Europe. In Switzerland, it is not a worry because our combined ratio is around 90%. It is obviously slightly more worrying in Southern Europe because of the recession there is some price competition.

P&C by market, you see that mature markets overall is zero, High growth markets, a growth of 15%, Direct a growth of 7%.

In terms of combined ratio, an improvement across the board with our Direct portfolio which is not yet mature, now getting to 99.9 % of current year combined ratio which is quite an achievement given the level of growth. Overall, a current year combined ratio improving by 0.9pts to 97.5%.

Earnings on the P&C are growing by 10%. This is because of the combination of the good current year combined ratio evolution in spite of slightly higher weather events, 0.7% of mature catastrophes of which €73M of impact of the German flood, slightly lower positive higher development at -1.8% to an all-year combined ratio of 95.7% slightly better than our medium-term target of 96%.

Investment income was almost stable with asset yield stable at 3.9%.

Asset Management

On the Asset Management side, we had the second semester in a row of positive flows both at AXA IM and AllianceBernstein. AXA IM had a very nice first half with €10Bn of positive flows. AllianceBernstein had a very good first quarter, a more subdued second quarter with positive flows of only $200M with the announcement of the tapering off of QE2. What happened was a liquidity squeeze in Asia in emerging market which led to outflows in retail in Asia for AllianceBernstein and in spite of a very strong institutional performance, this negative flow in retail led to a positive, but close to zero net flows in the second quarter.

Underlying earnings for Asset Management went up by 24% as a consequence of a positive leverage coming from a growth of expenses of 7% against the growth of revenues of 12%.

I would like to hand over now to Gérald. Thank you very much for your attention.

Mr. Gérald HARLIN, CFO, AXA

Thank you Denis. So shareholders' equity is going down from €53.6Bn to €51.5Bn. Let me highlight two drivers of change starting with a decrease in net unrealized capital gains, explained by the rise of interest rates; the Euro rates went up between 30-40bps on the 10-year T-bond, they went up by 70bps; it explains the –€2.5Bn.

The Forex movement net of hedging instruments is linked to the investment in non-Euro subsidiaries - I mean Japan, the UK and Switzerland.

Economic solvency as explained by Denis and by Henri, pretty stable and we are at 204 % including the net proceeds from MONY which should arrive in third quarter or fourth quarter, we should have to wait. You can see on the right hand side that the higher sensitivity is coming from the interest rates.

On the debt gearing, the debt level is quite stable at €12.9Bn. We have two new issuances in January for €1.6Bn which are offset by €0.9Bn senior debt reimbursement and €0.5Bn sub-debt of early redemption and that explains that the total debt is pretty stable.

Debt gearing is at 26%, we should be at 25% including the proceeds from the closed MONY portfolio disposal. Interest coverage moves up from 9.3 to 11.6 mostly explained by the high level of adjusted earnings.

A few slides now on ALM, Asset Liability Management, starting first with the asset yield which is stable, for Life art 3.8%, for P&C at 3.9%. On the left hand side, you can see the Asset allocation which did not move a lot, mostly in Fixed Income, Govies and Corporate bonds. You can notice that our listed equities went up from 3 to 4 %. Duration is pretty stable. We are managing duration gap close to 1-year.

The next slide is on current investment policy in the first semester, we have been investing €29Bn, on the bottom left, at an average of 2.9%. You can see that we have been investing 41% in Govies of which €4Bn on European peripheral countries, mostly Spain and Italy, 31% in Corporate bonds and I would say the rest in more diversified high quality and less liquid assets.

Life investment spread – starting with investment margin which went up from 72bps on a yearly basis to 77bps within the guidance of 70-80bps, you remember may be that for 2012, we were at 78bps. On the left hand side, you can notice that the Inforce business, we have a significant spread of a guaranteed rate at 160bps, and for new business, it is much higher 240bps. It should be noticed that the General Account Savings business is sold mainly to attract Unit-Linked business.

On the last slide, we tried to highlight the sensitivity of a rise of 100bps on interest rates, starting first Underlying earnings, positive for Underlyign earnings because it means investing at a higher yields. It is negative for Net Income as explained before by Denis, because we have some economic hedges which are not eligible for hedge accounting. Embedded value is positive; these figures are the sensitivity of the 2012 and 2012 EEV, +5% for 100bps in interest rate. For the US, it is even much higher, +23% and taking volatility plus market evolution, sensitivity should be twice this level. Economic solvency is up, so it is directly linked to the interest rate.

I hand over to Henri now for the conclusion.

Mr. Henri de CASTRIES, Chairman & CEO, AXA

Thank you Gérald, my conclusion is going to be brief, because I am not going to repeat what has already been said. I think it is a strong quarter showing progress on all the key fronts. We look at the future with a mixture of caution and confidence, confidence in our own acts, caution as far as the world and in particular Europe is concerned, but we think that we are well aligned with our long-term goals.

So thank you very much and now, let the floor asks questions.

Q&A session

Mr. Farooq HANIF, Citi

That chart of disposal of mature businesses and reinvestment into high growth, the €3.5Bn gap, what have you done and what will you do of that money? That is question one.

A second question about that mortality profit dip is quite significant, I mean if we look back historically, it is quite a big drop, I mean, would that recover in the second half, can you explain a little bit more about it? Thank you.

Mr. Denis DUVERNE, Deputy CEO, AXA

The difference between the €8.5Bn and the €5Bn is what we did in terms of deleveraging; basically, we have strengthened the balance sheet and deleveraged and that's what has happened during the period.

Mr. Farooq HANIF, Citi

On what you have done recently, are you basically saying that you are going to build up a liquidity buffer? Will this come to a balance at some point.

Mr. Denis DUVERNE, Deputy CEO, AXA

The stuff that we have done recently and you must have noticed one element which was new in disclosure this time, so we announced the disposal of MONY which is €800M. We announced the disposal of our AXA Private Equity which is €510M, but €315M in the first place, minus our investment, let's say €300M, so that is €1.1Bn and we said that we were investing €500M in Tian Ping. We added €300M of future investments to fund growth of the business, so the gap between the two is not a big amount it is only €300M of difference between the two.

We are not building a treasure chest at this point. We believe that we should continue to strengthen the balance-sheet by retaining significant part of our earnings and continuing to keep our pay-out between 40-50% of adjusted earnings. We believe that is prudent in the current circumstances given the uncertainties on the financial market, the uncertainties on Solvency II, the uncertainties on higher loss absorbency related to our SIFI designation, all of that means that we do not plan to change our pay-out policy so far.

Mr. Henri de CASTRIES, Chairman & CEO, AXA

Gérald HARLIN is to take the question on mortality.

Mr. Gérald HARLIN, CFO, AXA

May be, you can go to page B19 on the appendix. In fact, we had some positive one-offs in the past on mortality and morbidity and we did not benefit from this this year. Another way to explain it is the fact that we had a combined ratio on Protection & Health which was at 94% and this semester it was at 90-95%. So, on a technical side, I cannot tell you exactly what will be the future, but anyway with a growth of the top line, we should still keep improving our combined ratio.

Mr. Denis DUVERNE, Deputy CEO, AXA

But to your question of whether this is a one-off or a permanent trend, we see that more as a one-off than a permanent trend.

Mr. Farooq HANIF, Citi

Those actions you specified, were dealing with particular problems in that particular quarter. Okay. Thanks.

Mr. Oliver STEEL, Deutsche Bank

You talked about having increased your equity weighting and also the weighting in corporate bonds, I am just wondering where have you done that and what does it do to your re-investment rates going forward?

Mr. Gérald HARLIN, CFO, AXA

It has been done in different countries. It's spread over most of the countries except in the US because as you know we don't own equities in the US. It is mostly on the shareholders' fund. So, it is an investment of roughly speaking of €3Bn in 1H13.

Mr. Nick HOLMES, Société Générale

A couple of questions, first on the US, GMIB reserves, to be specific on these, now seem to be significantly in excess of your net amount of risk over 200%. I wondered whether there might be any scope at some future date to return some of those reserves which have somewhat depleted earnings in the past, but not very seriously; I know a lot of them are hedging gains.

Second question is on Asia, obviously, you made some big investments in China and I wondered if you could share with us what your thinking and aspirations are going forward, I mean, do you see potential for more joint-ventures in that region, for South-East Asia as well? What is your ambition?

Mr. Henri de CASTRIES, Chairman & CEO, AXA

I start by answering the China question and I will let Gérald and Denis then on the US.

In China mainland, we now have two ventures, the first one is with ICBC and the second one is with Tian Ping. The first one is in Life, we have 27.5 % with a possibility to grow up to 30% over time of the venture, but we have the management. On the Tian Ping side, it is just fresh and in the process of approval by the CIRC. It is a 50/50% venture.

The two partners are of a very different nature. ICBC was until very recently the largest bank in the world and is still the largest bank in China, state-owned, very powerful, state-owned company culture in China.

In Tian Ping, the shareholder is a Chinese businessman of the new generation who has started selling bags on street corners, has moved from bags to shares, he has made millions, billions; very entrepreneur-minded and extremely flexible has assembled technically a very good management team, very different cultures.

We have to learn to live with these different cultures. This is point one. We have to make these two joint-ventures successful. I don't think we need anything else. Within two quarters in China on the Life side, we have moved from being one of the many foreign insurers to being the largest one by far. If you rank us among Chinese companies, we are now probably number 10 on the Life side, number 10 or 11 and growing.

So, the idea of the venture is to benefit from the distribution strength of ICBC. And we think it is going to work and I will remind you that the venture is supposed to become profitable end of 2015, something like that, which means particularly fast if you look at the economics of any Life operation anywhere. The only place where a venture has become profitable that fast is in Indonesia, in the venture with Mandiri which has been for us a huge success.

On the P&C side, the game is exactly what I described to you in my presentation. The Chinese automobile market is the fastest-growing one in the world and will be become the largest one. It is under-insured. They have no significant direct player. Tian Ping is today a small company. It is between number 10 and number 20 in the market, but it is profitable and has a lot of room for expansion, because they have a license to operate direct on the whole territory which is a very big competitive advantage at least for a while. So, making these two ventures a success over the next 3-5 years is the priority number one.

Could we do other things in Asia? As you have seen, we announced yesterday the fact that now we have an agreement with the Singapore Post Office where we are dislodging one of our beloved competitors. It shows that we have the ability to grow through bancassurance or similar channels in Asia.

If you look at our presence in Asia, we are now the largest international P&C player in Asia. We are not the largest one by far on the Life side, but in P&C, we are the largest one. We keep developing these ventures with banks. If we can do additional deals to strengthen our distribution there, we would love to do that. We are looking at India where we hope that the government is going to lift the 26% hurdle on foreign investment, because this would open for us the possibility to increase our stake there.

So, I would say in Asia, in China, I think that we have what we need. It is up to us and our partners to learn to live together and transform that into significant successes. In other places, it is going to be more expansions through the acquisition modes we have developed over the last five years.

US VA, Gérald, your favourite subject?

Mr. Gérald HARLIN, CFO, AXA

Nick, your question is, is I well understood. It is how you explain that the net amount at risk decreased quite significantly, we are at €4Bn and our IFRS reserves did not decrease, we still are at twice the amount, i.e., almost €9Bn versus €4Bn. I would explain this way that is the €4Bn correspond roughly to the intrinsic value. Keep in mind that most of our reserves are mark-to-market. They are on the market consistent basis which means that you have intrinsic value, that you have the time value of money, that's mostly it. That is why your following question was, could we expect to have a decrease of these reserves? The answer is yes, but over time. It is not something immediate.

Mr. Denis DUVERNE, Deputy CEO, AXA

It can take 40 years! Just to give you a sense of timing…

Mr. Henri de CASTRIES, Chairman & CEO, AXA

But we'll still be there!

Mr. Nick HOLMES, Société Générale

As a follow up, just very briefly, I mean 40 years is a long time. I mean if markets were very, very good, would you possibly consider releasing something?

Mr. Gérald HARLIN, CFO, AXA

If the market would be very, very good, in such a case that means that the policyholder behaviour could change and in such a case; but after a while of good and positive experience, we could imagine to review our reserves. We could review the way we compute the reserves in order to calculate the policyholder behaviour. This is possible, but you can understand that we are cautious and it is not after a six-month or a few months' improvement that we can say, it is ok, we can release some reserves.

Mr. Nick HOLMES, Société Générale

That's great, thank you very much.

Mr. Ralph Hebgen, KBW

Two things, one is on systemically important financial institutions, you are on the list. Perhaps, you can share with us your thoughts of why you are on the list, what were the driving, reasons for you to be included, and second, of course, is there any possible impact on your economic capital requirement, how would you handle this.

The second one is just a numbers' question which is related to the realized gains. If you look at the gains harvesting, do you exclude the gains generated from the partial sale of BNP, it looks as if you are really in the middle of your targeted guidance range, but that is a guidance range for the full-year. So, it would be interesting to see how you think about gains harvesting in the second half. Thank you

Mr. Henri de CASTRIES, Chairman & CEO, AXA

On the systemic risk, we see it as a distinction. It is not being Knight of the Garter, but it is close to it. I was saying to some of you, in France, we have a say for that, we say when you have a very prestigious circle, you have to badmouth it but try to be part of it!

I think the reason for which we are there is the regulators and the supervisors wanted to capture the large institutions. Whatever has been said about the criteria, I think that size has played and I would say that the diversity of our geographical exposure has also played. There has been no surprise on who is on the list so far. So, for us, it is not a surprise. I don't see that as a threat; on the contrary, what we have to watch closely is two things:

(1) We are very much in favour of transparency and disclosure, we hate bureaucracy. We hope that the needle is going to be well-positioned, because if this ends up by sending additional thousands of pages to the supervisors who are never going to be read or never going to be helpful to really understand what is driving these companies, I think it is going to be a waste of time and money.

(2) The second point is about higher loss absorbency (HLA), they will have to define an approach, but I would remind you that the situation of insurers is very different from the situation of banks. In banks, they have a common standard which is Basel III which does not exist in insurance. The US and Asian companies as an example are not measured in terms of solvency the same way as European ones. So, this has to be mitigated by the relative tightness of the requirements Solvency II versus the rest of the world, and given the fact that Solvency II is probably the most demanding system on earth, we look at what is going to come out from this debate closely, but I would not say in a pretty relaxed way, we think that this will have to be taken into account. I think that some of our competitors who were on the same list as us have made statements exactly in the same direction this morning or yesterday.

Mr. Denis DUVERNE, Deputy CEO, AXA

As regards your second question, you know that our guidance €300M to €500M of capital gains for the year, on average, we expect to remain within that range.

Mr. Ralph Hebgen, KBW

Even though you have already basically generated €400M in first half?

Mr. Denis DUVERNE, Deputy CEO, AXA

Yes.

Mr. Andrew CREAN, Autonomous

I have three questions. You've given guidance on your spread margins in the Life businesses of 70-80bps during a period of falling interest rates. As interest rates rise, is there a pressure on that spread margin as you have to push up crediting rates with interest rates. Now, how do you see that?

Secondly, your cost to income ratio in your Asset Management division is crudely 78% which is high and obviously a residue of problems you had. Could you give us some idea as to where you aim to get that cost to income ratio down to and over period?

Thirdly, economic capital, there was no visible effect in the coverage ratio from the rise in interest rate. If you did not do US on equivalence which is where interest rates raise more, how much would your economic capital have improved?

Mr. Gérald HARLIN, CFO, AXA

Your first question is on the investment margin between 70-80bps. For the time being, I said last year that we could expect to be at around 75bps and I don't expect that any increase of the interest rates will have an impact.

Why? Because, as you can imagine, in a lot of countries we are not locked by any guaranteed interest rates. It would be the case if interest rates would go much higher. That means that we can expect to keep this type of margin to a certain level. If rates would move up by 150bps to 200bps, in such a case, we might be under pressure. As you know to avoid this in the countries where we could consider that our margins are under threat, there, we are benefitting from the present market to buy options in order to protect our margins.

On the economic capital which was your third question, economic capital excluding the US equivalent would be roughly at 170%, slightly improved from around 160% last year.

Mr. Denis DUVERNE, Deputy CEO, AXA

On the Asset Management cost to income ratio, clearly this ratio was under pressure in a period where assets were going out and the challenge was to bring the cost down at the pace at which the revenues were coming down. We did that, but we effectively saw our margins slightly decline. This is because we have kept our distribution footprint largely intact.

I believe it was important to do that because as performance improves, we do have the distribution capacity to have net inflows and we are seeing that now in the last two semesters. You see the positive leverage that we showed in the first half with a positive gap of 5 points between the expense growth and the revenue growth.

We have this operational leverage favouring us now and I expect that we could get to at least a margin of 30% or a cost to income ratio at 70% or lower in the medium-term. That depends on the continuation of the positive flows, but we do not expect to further decrease of our distribution footprint when we have all expertise or most expertise going right in terms of investment performance. We expect the positive leverage to gradually bring down our cost to income ratio.

Mr. Blair STEWART, Bank of America ML

The first questions is just for a clarification on the technical result. I think that you said initially, unless I heard it wrongly, the experience previously had been exceptionally good and that this year was more normalizing towards a standard run rate or did I pick that up wrongly?

Mr. Gérald HARLIN, CFO, AXA

What I said is that we had some positive experience in the past. I am not saying that we won't get any positive experience in the future. We can expect that everything equal we had a relatively negative experience in the first semester.

Mr. Denis DUVERNE, Deputy CEO, AXA

Gérald phrased it this way we usually have positive mortality gains basically. So, we were surprised this first half not to have positive mortality gains as much as we used to have.

Mr. Blair STEWART, Bank of America ML

It is clear, thank you.

The second question is just on the investment yield. It is stable in P&C. I think that previously you guided towards 10-15 % drop per annum, I just wondered whether it was changing.

Thirdly, the interest in your comments around Poland, if the second pillar is nationalized, what would be the impact on your business?

Mr. Gérald HARLIN, CFO, AXA

On investment yield, yes indeed. I told you that we could have a 10bps decline. In fact, what we have been doing is that we have been investing €29Bn that I presented at a relatively high rate. Why? Because we were quite successful in diversifying and we decided not to invest in traditional Govies or in low yielding corporate spreads which are taking an additional risk. First, we decided to invest €4Bn in sovereigns and it is proven to be the right choice. Second, just to give you an example, when we are investing in loans which are equivalent of single A-loans, we can get 100bps if you buy a bond and you get 200bps if it is a loan, but illiquid. That's mostly it.

Mr. Denis DUVERNE, Deputy CEO, AXA

It is right to say that we did expect to have maybe slightly lower yields on our new investments this year, and we plan not to have a lower yield in fact than what we had last year.

Mr. Henri de CASTRIES, Chairman & CEO, AXA

These gentlemen are very modest; the reality is that they have managed investments very well.

Mr. Blair STEWART, Bank of America ML

And on Poland?

Mr. Henri de CASTRIES, Chairman & CEO, AXA

On Poland, the stake is €400M of embedded value and a couple of tens of millions in terms of yearly earnings, so nothing major, but it is worrying us regarding Central and Eastern Europe, because it happens after Hungary. I think that these countries are shooting themselves in the foot. The reality is that they do that for a sort of accounting trick.

Poland has a constitutional limit on debt versus GDP at something which is I think 60%, they are getting close to this limit. And due to the interpretation of the Eurostat rules, they have the feeling that if they "nationalize" the second pillar, take the bonds which are held by the pension funds, and substitute themselves as a state to the obligation of the pension funds towards the pensioners, they will be able to eliminate in their consolidation the debt which is represented by the bonds without having to take into account the future obligation of the pensions.

This is a Ponzi scheme which is allowed at this stage seemingly by Eurostat rules for as long as it will last. We did not see like that much in

Hungary, but should this become true in Poland, we should become very aggressive from a legal standpoint, in Brussels and elsewhere, because we think that would be nationalization and that this would justify indemnification.

We are not the biggest ones in this market, I mean players like ING and Aviva are much larger than we are, but our very firm intention is to fight for our interests, the way we fight in rugby. Meaning, not always successfully, but most of the times successfully.

Federico Salerno, MainFirst

Just on the US restructuring, how is it proceeding? What kind of costs should we expect for the second half relative to the €120M you had in the first half?

Mr. Denis DUVERNE, Deputy CEO, AXA

The US restructuring is essentially done. We have vacated a number of floors in our main Manhattan building. The rightsizing has essentially been done. So, you should not expect additional significant restructuring expenses in the US. The rightsizing has been completed over last year and the first half of this year.

Mr. William ELDERKIN, Goldman Sachs

A couple of questions; first, you mentioned you thought Solvency I measures were irrelevant from that I can understand. What is your perception of which metrics the French regulator is looking at the moment?

Mr. Henri de CASTRIES, Chairman & CEO, AXA

Solvency II, they are looking at both, but the reality is what matters for them now is Solvency II.

Mr. William ELDERKIN, Goldman Sachs

The second question was you obviously benefited in line with your peers from substantial improvements in claims frequency. What is your sense of how things can improve from here?

The final question was in your presentation, you talked about substantial technological shifts shaping, changing your business model. Can you give us an example of the kind of things you have in mind?

Mr. Denis DUVERNE, Deputy CEO, AXA

Could you repeat the question on claims?

Mr. William ELDERKIN, Goldman Sachs

I think you along with many of your peers have benefitted from substantially improved claims frequency. What is the scope for that improvement to continue?

Mr. Denis DUVERNE, Deputy CEO, AXA

In terms of claim frequency, as you know it is to some extent tied to the economic environment. So to the extent that European growth has been pretty subdued to say the least, it has a positive impact on claims frequency. I mean if we are not in a downright recession which could increase arson fires and other sorts of things, people drive less, there is not too much overwork and night shift and so on, so claims frequency is better and to the extent that European economy does not rebound massively in the second half, and nobody believes that would happen, we should expect claims frequency to remain along the same lines.

What can affect the claims' situation for us could be the weather. As you saw we had an amount of weather events that was higher than last year at 0.7point of combined ratio, but probably lower than the long-term trend which we put, given our portfolio mix at 1%, so we cannot plan anything in terms of natural catastrophes. So, you could imagine that natural catastrophes could be higher in the second half than it had been in the first half. Overall claims frequency should not change much in the second half versus first half.

Mr. Henri de CASTRIES, Chairman & CEO, AXA

On the last part of your question, this is going to be absolutely fundamental for the business. If you look at what is the real essence of the insurance business, it is in fact accessing and understanding data to price risk and deal with policy holders.

So, the first thing which is happening is that an incredible amount of data is now available in a way which was not-existent years ago and can be handled in a way such as it gives a better understanding of the risks. This is going to enable for those who are going to understand the way to access these data, this is going to enable a much more accurate pricing if you can manage to do that. I mean, usually, insurance companies owned a lot of data, but it happened that there is now available in the cloud, much more than used to be available, much more easily.

There are a number of questions to surrounding that. Can you access it? Do you understand how to understand and use it? Could other players, not necessarily coming from the insurance industry, do that and use it as a competitive advantage? That is question Number one, with a very big "legal" question which is going to affect this and the next point which is: what is the limit between customer intimacy and respecting privacy? I think it is going to be the big legal debate for the next generation. I think that the debate on privacy surrounding internet is going to grow the way the concerns on climate change have grown over the last 10 to 15 years. This is a big, big legal question.

Industries which are living out of using data, on individuals, have to ask themselves the question. Do they know what they are going to be the rules or how they are going to change? This is the first very fundamental shift of which I think we need to have a view.

The second point is relationship with the customer. We have the Direct business. We have traditional networks. The Direct business is growing fast because it is a business where most of the transactions are done through internet.

Our traditional networks are very solid, very resilient. They have a high degree of "traditional customer intimacy". The game is not a win/lose game. It can be a win/win game. If we can convince our traditional sales forces to move to multi-access and to digitalize themselves quickly, they will become multi-access and keep a competitive advantage when compared to Direct players who are more siloed. I think that the customer is willing to have multi-access providers.

So there, what we need to do is to use all the technological revolution, of course to develop the new channels like Direct, but also to transform the traditional ones. On one hand, it is a big task because they start by being defensive; on the other hand, it has already happened in the past, at least twice. When they moved from writing to using the phone and when they moved from using the phone to using computers. So, you just have to convince the old generation to change and you have to recruit new guys who are natives in these technologies. Did I answer your question?

Mr. Jon HAWKING, Morgan Stanley

Do you think there will be a deal on Solvency II this year? If so, what you think is going to end up?

Mr. Henri de CASTRIES, Chairman & CEO, AXA

It is difficult to say. I am sure that Christmas will still be on the 25th of December, I am less sure that Solvency II… No, I mean we hope that there will be a deal, because if there is no deal this year, the risk is a postponement because of the new European elections, the new Parliament, the new Commission and so on and so forth.

So, I think that the sensible players in the industry are pushing for a compromise. It has to be a compromise. The deal on the current basis of the proposal from the EIOPA is not going to happen. So, there has to be a compromise. The trilogue is going to start again early September.

We hope that progress will be made because for the large cross-border players, the alternative is not a very pleasant one.

I mean if you are a local mutual, you can say I don't care, I am going to deal with one regulator and we will find arrangements. If you are cross-border, the alternative of having 28 different regimes is not a very pleasant thing. So, what we hope is that the compromise is going to be found. If you ask the same question to the very vast majority of the large European players, I guess they would give the same answer because the industry is very well aligned on that.

Mr. Farooq HANIF, Citi

You don't give cash flow data and you have been clear about that. I was just thinking more qualitatively. Are you finding that if you wanted to take capital out now, let's say from the US, from European countries, from Asian businesses, you could because your local statutory or rating agency solvency or economic solvency is strong enough. Are you finding it basically if you wanted to have more central liquidity that you could do that, I can understand that you would not; if you want to grow in Asia and if you want to avoid washing money around and incurring tax penalty of functional cost, but are you finding now that you have basically more control and less subsidiarization? Thank you.

Mr. Henri de CASTRIES, Chairman & CEO, AXA

I would say qualitatively that the guidance that we have given that we expected a remittance ratio of the order of 75% remains valid. We do not have any indication that this remittance ratio would have to significantly go down or could significantly go up. We are pretty much in the same position.

Mr. Farooq HANIF, Citi

I am sure we are all modelling that, but what I mean, is it by choice or by force?

Mr. Denis DUVERNE, Deputy CEO, AXA

I would say that corresponds to the economic situation of our various operating subsidiaries.

Mr. Gérald HARLIN, CFO, AXA

May I add one point, as you know for the time being, we are subject to the local statutory rules and in Europe that means that we cannot expect to change, so we will see later on at the time Solvency II will be in force, then Solvency II will apply to the local on a solo basis and this will be different at that time, we believe that we might have more flexibility in order to improve the global scheme, but it is far too early to give you any kind of indication, we can consider that more or less, we are optimizing.

Mr. Blair STEWART, Bank of America ML

Just one question on the US business again; I know it is far too early to start thinking about changes of assumptions on reserving, but have you observed any changes in customer behavioural over the last couple of months into better markets and higher interest rates?

Secondly, how is the dialogue between yourselves and the New York State regulator evolved over the last six months given some of the comments they are making publicly about reserving, offshoring of reserves, anything else related to that?

Mr. Denis DUVERNE, Deputy CEO, AXA

I will try to respond to your second comment. There were a number of comments made in relation to the re-domestication by some of our US competitors of their Bermuda operations back to mainland US.

This is a move that we had anticipated ourselves last year when we moved from Bermuda to Arizona, I don’t see that we are under any specific pressure given that all operations are in the US continent subject to US taxation and so on, and so forth. We have seen no particular change of behaviour of the New York regulator vis-à-vis AXA in the recent past.

Mr. Gérald HARLIN, CFO, AXA

As far as your first question is concerned on customer behaviour, we can say that we are in line with our expectations. That means that it’s not worse at all, and what we have been doing last year is we are in line and that’s what I said before, we should need much more time and experience in order to change it, but we can consider that we are on the safe side.

Mr. Henri de CASTRIES, Chairman & CEO, AXA

Any other questions?

Mr. François BOISSIN, Exane BNP Paribas

Good afternoon everybody; a few questions please. The first one is on your cash position in the holding. How should we look at it, is there a minimum buffer you want to maintain there and what would be the amount available for M&A or cash distribution to shareholders?

The second question is on NBV margin. It has been improving consistently over the past quarters. What kind of level are you targeting? Can we expect more namely with higher interest rates?

Thirdly, on banking, you had a good semester. Is there something we should extrapolate or what drove basically the good performance in the semester?

And finally, what are your intentions with regards to your remaining 2.9% stake in BNP? Is it hedged against downside risk? Thank you.

Mr. Henri de CASTRIES, Chairman & CEO, AXA

We are not going to comment on your last question and I leave the two other ones to Gérald.

Mr. Gérald HARLIN, CFO, AXA

About the cash position, nothing to do, we should not make any confusion between shareholders' funds and funds which are managed in front of the reserves. The cash position that we have here is a cash position for liquidity. Of course this cash, I tell you that the average duration is a bit more than 7 years, this cash is including in it. So, if we decide for whatever reason to have a kind of bubble situation, this is part of it. So, it has nothing to do with a kind of buffer that will be put aside for investment.

Your second question was about NBV margin. NBV margin is higher than expected, higher that initially expected, but this is due to our business mix. We have no intention to change our business mix. This improvement in our business mix in favour of more Protection and Health, and more Unit-Linked business won't change.

What is the sensitivity to higher interest rates? As you know, it is positive, so the NBV margin is directly linked to the interest rates.

On your third question about the banking. On banking, we have an improvement indeed and you can see in the activity reports that last year we had a one-off in the French bank due to an advertising campaign and which is not the case this year. At the same time, in Belgium, we realized more capital gains than we did in the past. So, we can consider that the results that we posted in the first half is more in line with what we could expect. It is more what we did last year which was not really in line.

Mr. Henri de CASTRIES, Chairman & CEO, AXA

Do we have other questions on the phone?

Mr. Atanasio PANTARROTAS, Kepler Cheuvreux

Good afternoon to everybody. I have just two questions left. One is if you can provide us the impact of the acquisition cost in your Life business profit & loss in underlying earnings, specifying if there is after before taxes.
The second question is if you can give us some more colour or free cash flow generation during the first half. Thank you.

Mr. Henri de CASTRIES, Chairman & CEO, AXA

We did not understand your first question.

Mr. Atanasio PANTARROTAS, Kepler Chevreux

It is about the acquisition cost. You mentioned in the presentation that there was a less positive effect of the acquisition cost because there was an acceleration of amortization in your US business and if you can provide us what was the impact in the profit & loss underlying earnings in Life business of the acquisition cost?

Mr. Denis DUVERNE, Deputy CEO, AXA

You have a slide in the appendix on page 53 of the financial supplement. What I can tell you is that indeed we increased our DAC amortization. Last year, we did not in fact amortize, we increased our DAC, but we did not amortize. Why? Because we had this huge one-off in the US coming from the policyholder behaviour which was discussed before. Just to be clear, in the first half roughly we have been amortizing a bit more than €300M of DAC and of which US represent roughly €200M, that is the main difference.

So your question about the impact on P&L, this cannot be analysed in itself. If should be analysed and compared with the situation of last year where we had a huge one-off which was more than €500M corresponding to the adjustment in the US. What I can say is that the US contribution this year is higher than it was last year and roughly speaking, we are a bit more than €100M above where we was last year.

The second question is about the free cash flows. As you know we don’t publish any free cash flow in the first half. Nevertheless, what I can tell you is that we are in line. That means that the free cash flow is mainly three components. The first one is Life. Life is not very different, slightly we could expect that it would be in line with what we shared with you last year, and in P&C, the fact that we had improved adjusted earnings in P&C means that our cash flow should be slightly improved, so quite in line with what we have been discussing at the end of last year.

Mr. Henri de CASTRIES, Chairman & CEO, AXA

If there are no more questions we are going to stop. Thank you. We wish you a very good summer.