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CONFERENCE CALL PARTICIPANTS

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PRESENTATION

Operator


I will now hand the conference over to Alex Wynaendts. Please go ahead, sir.

Alex Wynaendts - Aegon NV - CEO

Thank you. Good morning, and I’d like to thank you for joining us for this discussion of Aegon’s second quarter 2012 results. Today joining me here, we have Jan Nootgedagt, our CFO; Willem van den Berg, Head of Investor Relations; and Michiel van Katwijk and Darryl Button.

I trust you’ve seen our other announcement today, and we announced that Darryl will be taking up his new role here in The Hague as the Head of the Corporate Financial Center as of September 1. And Michiel will be relocating to Baltimore in the US where he will succeed Darryl as CFO of Aegon Americas. These appointments reflect our determination to better leverage the considerable knowledge and expertise and experience we have within our Group globally and we believe this will ensure even greater synergies and insight as we pursue our strategy of operating one Aegon.

Before turning to our second-quarter results, let me remind you to take a moment to review our disclaimer on forward-looking statements which is at the end of this presentation. As always, we look forward to your questions after the presentation.

So, despite the persistent challenges of the general economic environment that you’re well aware of, we are really pleased to present a strong set of results for the second quarter. The growth of our business combined with a consistent focus on reducing costs as well as the stronger dollar and British pound led to a 10% increase in earnings. An increase of 27% in total sales is a clear indication of the continued strength of our franchise.
In particular, we continue to see strong demand for our core business of providing retirement services which resulted in the 45% increase in gross deposits for a total of EUR9.8b. Our pension business in the United States as well as Aegon Asset Management were the main drivers of the increase in deposits.

And finally, Aegon’s strong capital position and cash flows support our decision to declare an interim dividend of EUR0.10 per common share.

Here on slide three we provide you with a quick overview of our progress toward our 2015 targets. I want to take the opportunity here again to repeat what we said earlier and namely that in view of the current challenging environment and financial markets, we expect to deliver our target at the lower end of the range we provided. I will address underlying earnings and cash flows in more detail a little later in our presentation.

And now turning to underlying earnings on slide four, as indicated, the growth of our business, the implemented expense savings and the more favorable currency movements were the main contributors to the increase in underlying earnings. Earnings in the Americas benefited from growth of our US pension business. This was offset by lower fixed annuity earnings which we’re continuing to deemphasize, in addition to high employee benefit expenses and the allocation of Corporate Center charges.

Results in the Netherlands were positively impacted by higher earnings in pensions and in our distribution business. These positives, however, were more than offset by higher claims on disability products. We’re taking action, including the repricing of products, to reverse this negative trend, although we expect to see continued pressure on non-life earnings throughout the year, and this as a result of the difficult economic environment in which we’re in.

In the UK, earnings more than doubled as a result of our successful cost reduction program. And earnings in our new markets were lower mainly due to exclusion of Aegon’s partnership with CAM in Spain which we’re in the process of exiting.

Today we’ve also announced the sale of our 50% stake in our partnership with Banca Cívica to CaixaBank. The proceeds of the sale of our 50% stake in insurance joint venture will amount to EUR190m and we expect a book gain of approximately EUR35m which will be leading to total returns since inception of 12% per year.

Aegon Asset Management, as in the previous quarter, reported strong earnings, the result of performance fees and increased fees income from high asset balances.

On slide five, you can see that the second quarter net income was substantially impacted by the one-time EUR265m charge that we announced this past May to improve unit-linked production in Netherlands. This negative impact was partially offset by favorable results on fair value items, lower impairments and realized gains on investments.

As we have made clear, the trust of our customers is essential to the long-term success of our business, and we believe that adopting the principles as recognized by Ministry of Finance to be best-in-class in the Dutch environment is in the best interest of our policyholders as well as Aegon’s other stakeholders.

We continue to make good progress with reducing expenses in our key businesses. And as you can see on slide six, in the first half of the year we realized cost reductions of EUR90m, driving the 5% lower year-on-year operating expenses. I want to make clear that reducing and pursuing operational efficiencies are an integral part of how we manage our day-to-day business. At the same time, however, we will continue to invest in new propositions such as our new Aegon Retirement Choice proposition in UK as well as a new online banking platform which we’ll soon be rolling out in the Netherlands.

Slide seven, I’ll touch briefly on the new money investment yield in the US. Although the US risk-free rate has been falling to historically low levels, we are still able to realize a new money investment yield of slightly below 4%, as this as a result of the credit spreads on the high-quality fixed-term securities we continue to invest in.
investment activity on the overall book value deals, approximately 85% of our existing portfolio, is limited. This is a result of our (inaudible) strategy to match our assets and liabilities from both a cash flow and duration point of view.

Now turning to slide eight, the total market consistent value of new business for the quarter was impacted mainly by lower interest rates. However, I would like to highlight the significant actions we have taken to offset the steep drop in interest rates and to support our determination to continue to sell profitable products in the current environment. These actions include repricing, redesigning, or the withdrawal of our products that are no longer profitable in the current interest rate environment. And as such, we're confident that our disciplined approach to pricing will enable us to increase profitability of new sales going forward.

Let me now give you some more detail on our sales during the quarter here on slide nine. We were especially pleased with the 27% increase in total sales to EUR1.6b. This is mainly the result of the 45% increase in deposits totaling EUR9.8b. Again, the strong level of deposits was attributable to our US pension business as well as institutional flows within Aegon Asset Management.

New life sales benefited from stronger sales in the US; however, sales in Netherlands and in UK were lower. Accident and health sales also demonstrated strong growth, a result of our leadership position in providing travel insurance in the US and the fact that we have attracted a new distribution partner in this attractive market.

Now moving to the performance of our US business, here on slide 10 we provide you with an overview of the margin development of our US pension business. As you can see, the market is very competitive, and as a result, fees have been declining over the last several years. However, as the slide clearly demonstrates, management has been successful in addressing the margin compression by increasing scale and by proactively reducing expenses which more than offset the decline in the fee rates. And as a result, our margin has improved to 24 basis points and tracks well with our medium-term expected margin of 25 basis points.

Another area where we continue to make good progress is our variable annuity business, and you can see this on slide 11. New business profits are under pressure as a result of lower interest rates. However, as we continue to raise rate, we have maintained a strong focus on writing profitable business. We’re improving new business margins through a range of actions which include changing fund and benefit options as well as increasing fees.

VA sales during the quarter increased 7% over Q1 as the market has seen the exit or downsizing of quite a number of competitors. Our VA margin declined to 74 basis points which was due to the adverse mortality experience on all the products that have death benefits only but also lower interest rates caused an increase in the claim costs for GMIB products. But we remain comfortable with the medium-term 80 basis points margin that we have previously indicated.

We continue to achieve strong sales momentum in our core US Life and Protection business, as evidenced by the 16% increase in life sales and 18% increase in sales of accident and health products as compared with last year, and you can see this on slide 12. As I mentioned a few slides ago, accident and health sales benefited primarily from a new distribution partner added in the third quarter last year.

Underlying earnings improved considerably compared to the first quarter as mortality results returned to expected levels. Improved persistency on the term life book also contributed to higher earnings. Most of our new life product sales such as indexed universal life as well as whole and term life were profitable this quarter. However, our fixed universal life joint survivorship product was not. As I indicated, we’re addressing this by the repricing, redesigning, withdrawing or suspending these products to counter the effects of a persisting low interest rate environment.

In slide 13 we provide you with further detail on our Dutch mortgage business. We have been successful on gaining market share, which is due to our focus on delivering a consistently high-level service and by realizing the benefits of fully automated processes. In addition, a number of players have left the market or are restricted in their funding capabilities.
the sales connected to the mortgage. Underwriting in this business is fully based on loan-to-income. And moreover, our prudent approach to underwriting is reflected in the low impairment level of only 3 to 4 basis points annually that we’ve experienced to date.

Impairments, as you can see, in the quarter, on slide 14, continued at the low levels we’ve been experiencing for the past several quarters. Impairments are mostly linked to the US housing market. I also want to make clear that given the turmoil in Europe, approximately 70% of our general account assets are held outside the Eurozone.

On slide 15 we provide you with Aegon’s total exposure to all fixed income securities related to peripheral European countries, which as you can see is limited to 0.6% of our general account portfolio. On the graph we give you an overview of our exposure to the peripherals, including the (technical difficulty) of our joint ventures with Civica and CAM which I’ve indicated we are in the process of exiting. Once we have concluded these exits, our exposures to peripherals, being most Spain, will be reduced by approximately EUR700m.

I’m now pleased to turn to slide 16, about Aegon’s capital position at the end of the second quarter, which as you can see, continues to be strong. Our IGD ratio increased to over 216% from the level of 201% at the end of the first quarter. The IGD ratio in the Netherlands increased substantially as a result of a change in the yield curve to discount liabilities. The use of the so-called ultimate forward rate prescribed by the Dutch Central Bank had a positive effect of 35 points on the IGD ratio in the Netherlands and 8% on the total.

Once again, I want to emphasize a point we consistently make. In the current environment, we believe that maintaining a strong capital position and a strong capital buffer is not only prudent but is essential. At the end of the second quarter, excess capital at the holding totaled EUR1.6b, considerably above the minimum buffer of EUR750m we aim to hold.

You’re aware that one of our key financial targets is to increase operational cash flows by 30% by 2015 from the normalized level, 2010 level, of EUR1b to EUR1.2b. And as you can see on slide 17, during the second quarter, operational free cash flows, excluding the impact of the market and one-time items, totaled EUR296m, which puts us on track to achieve our targeted level of operational free cash flows.

On slide 18 we provide you with Aegon’s capital base ratio which amounted to 74.6% at the end of the quarter. As we have communicated with you, our target is to achieve capital base ratio of at least 75% by the end of 2012, and we are clearly on track to deliver accordingly.

Now let me conclude. Despite the persistent turmoil of the current economic environment, Aegon’s businesses performed well during the quarter as evidenced by strong sales, improved earnings and a continued strong capital position, all a confirmation of the continued execution of our strategy.

We have a clear focus on ensuring that all our products and services offer long-term value for our customers while at the same time delivering value for our Company. We are determined to further improve the profitability of our new business, particularly in the current low interest rate environment, and are implementing a broad range of management actions to achieve this. We will continue to identify costs and operational efficiencies across all our businesses while also making the necessary investments to support our long-term growth and to exploit the benefits of technology to get closer to our customers and deliver quality service.

Our disciplined risk and capital management has enabled Aegon to deal effectively with the challenges inherent in today’s global market environment while pursuing our strategic objectives to deliver sustainable earnings growth. This discipline supports our decision to pay an interim dividend of EUR0.10 per share.

Thank you for your continued interest in our progress, and we'll be very happy to take your questions.
Farooq Hanif - Morgan Stanley - Analyst

Just a few questions. Firstly, on variable annuities, one of your peers in the US, European peers had some further problems with policyholder behavior. I was wondering if you can update us on lapse experience, how that’s going, and also the issue of partial withdrawals, whether that affects you.

Secondly, when do you make a decision on how much free cash flow is upstreamed to the holdco? Is that at the end of the year? What are the constraints on this? And how much is upstreamed in the second quarter?

And lastly, you say that you're going to be at the lower end of your targets, but would you say that this applies to your cash flow too? Based on what you're doing this year, it seems like you're going to get towards the upper end of your targets on cash. What are the negative headwinds that we are ignoring? Thanks.

Alex Wynaendts - Aegon NV - CEO

Thank you, Farooq, for your question. On variable annuities, today we have shared with you where we are on the variable annuities. We’ve shown you our results. We will be going through a process of checking all the assumptions [and more] validation in the third quarter, and we’ll be communicating with you at third quarter.

Darryl, is there anything you want to add on this one?

Darryl Button - Aegon NV - Head of the Corporate Financial Center

No, not really. The third quarter is when we go through and do the full annual assumption review, Farooq. I would just that the trends have been what we've been communicating in the past, the actual absolute lapse rates continue to be very low and the utilization rates on the benefit itself also continue to be low. And that's as trend we've seen in the last couple of years; we've built that into our assumptions. And we'll be taking a harder look in the third quarter as we always do based on the last year of experience, but we've been just seeing that trend continuing to emerge.

Farooq Hanif - Morgan Stanley - Analyst

Okay.

Alex Wynaendts - Aegon NV - CEO

Thank you, Darryl. Yes, on the cash flows being upstreamed to the holding, well, you get an indication of the impact if you look at slide 18 that we shared with you, the impact on our capital base ratio, which is 1.5. But in general, we upstream during the second parts of the year more than we upstream in the first part of the year to the holding.

In terms of your question of my comment on achieving the low end of the range of the targets, I more specifically here mentioned the growth in underlying earnings and the return on equity targets. As you can see in the other target of the amount of fee-based business, actually last quarter we even had reached our targets, we’re just a bit lower now. So that clearly is well on target. And I believe for cash flows the same would apply.
Farooq Hanif - Morgan Stanley - Analyst

Can I just come back on one point, and that is the upstreamed capital. That 1.5% impact, what is that, and I'm sure I can work it out, but what is the actual amount that you upstreamed to the holdco?

Alex Wynaendts - Aegon NV - CEO

I'm just checking with Michiel because in principle I don't think we disclose these numbers. Michiel, you want to add something here?

Michiel van Katwijk - Aegon NV - CFO of Aegon Americas

It's around EUR0.6b, Farooq.

Farooq Hanif - Morgan Stanley - Analyst

Okay.

Michiel van Katwijk - Aegon NV - CFO of Aegon Americas

First half.

Farooq Hanif - Morgan Stanley - Analyst

Yes. Okay. Thank you very much.

Operator

The next question comes from Robin Buckley. Please go ahead, sir.

Robin Buckley - Deutsche Bank - Analyst

Yes, good morning. Three questions if I could. First of all, just on the US Life and Protection business, where I guess the results recovered from a weaker number in the first quarter, could you just talk about what's actually going on in terms of driving that result? Is it mortality profitability that we're seeing coming through at a normalized level we could expect to continue in the future? And what's the impact of lower interest rates on that business? I know you said you're redesigning some products. I'm just trying to get a feel of what the run rate there could be.

Second question is just related to the dividend. You kept the interim flat with the final of last year, which I think is historically how your dividend policy used to be. But could you just talk about perhaps what we could expect from a final dividend in terms of any growth? And related to that, just the Dutch regulator's comments about not paying out substantial amounts of dividend, does that have any impact on you either in terms of the Dutch business or indeed at the Group level?

And then the final question again is just related to the Dutch business. Could you just comment on what the yields are that you are getting on Dutch mortgages at the moment in terms of new money and also just how that compares to guarantees? Thank you very much.
Thank you, Robin. On the life and protection business, what we’re seeing this quarter is a return to a normal, I would say, normal levels, expected levels of mortality. We also see some positive of improved persistency in the term life. In terms of interest rate impact, clearly the impact is mostly on the new business, as I shared here, we’ve shared you about our investment of new money yield. What we also showed that is that impact is relatively small compared to the large in-force where we have a book value yield of around 5%.

But clearly, in certain new business, it is clear that low interest rates have an impact, because we want to consistently meet our profitability targets. And that means that we have had to reprice for this, we re-priced significantly for this, redesigned product, and in some cases even withdrawn products entirely because we could not make them meet our profitability requirements. So the impact I can see is most notably felt in terms of new business as a consequence of our absolute determination to sell profitable business going forward.

Darryl, I think you want to add here too?

Darryl Button - Aegon NV - Head of the Corporate Financial Center

No, I think -- I mean that's fairly well-covered. Just in terms of numbers, we did say last quarter we thought our mortality was soft by about EUR25m, and we did see that come back, and that's the earnings comeback that you see. And I do see that's sustainable going forward, so that's the largest driver of the earnings this quarter. I would say the persistency results were above expectation in the quarter a little bit. So we were a little strong this quarter on persistency.

On the low interest rate side, as we've said, it has a modest impact, as Alex said, going forward. We've quantified that in the past and we see that hitting us for about EUR10m a quarter this year, possibly growing to EUR20m next year if rates stay at the low levels that they're at.

Alex Wynaendts - Aegon NV - CEO

On your question relating to dividend, yes, the Dutch Central Bank has indeed brought the new regulation around the ultimate forward rate, the 4.2, but the Central Bank at the same time has made it very clear that they would not expect dividend payments coming out of this increase of capital position. As you know, in our business, we have IGD ratios well above 200%, also we have them well above the 200% in our Dutch business, even excluding the effect of this measure. So for us, I think the impact from that point of view should not be -- should be negligible. So in terms of dividends, I hope I've given you a clear answer here.

In terms of the mortgages, we don't disclose the yields, but I will ask is IR to come back to you and to provide you a little bit more color. What's important to realize is that it is indeed a market which is attractive. It's a market where 80% of our business now, of our new business, has a Dutch State guarantee. And what you need to make sure is that you get all your processes in place, that it's about making sure you have the right processes in place.

And on top of that, we are operating in a segment which the one which is -- another one which is most in demand which is up to EUR250,000, EUR300,000, people who are looking for fixed rate for a long period of time. And as you will imagine, for an insurance company, these are very good asset liability match because we are looking for longer-term liabilities. And that's also why it supports -- it allows us to fund these mortgages in an attractive way. That has been driving our business.

Also important to note is 60% of our life sales actually have been -- sorry, 60% of our mortgage sales have led to a life sale too, and so there's really good cross-selling opportunities there. So, not only looking at mortgage but looking at the mortgage plus the life sales just makes it an attractive business, and we are really very well-positioned there.
Okay, thank you. Can I perhaps just come back just on the dividend, just to be a bit more blunt, should we be expecting growth in the dividend for the full year? Is that within your plans?

Alex Wynaendts Robin, we are just now announcing that we’re paying a dividend in August. We are also saying that this remains an uncertain, volatile environment. At this point I’m not going to give you any indication on which direction dividend will go.

What is important, and we said that consistently, we have a dividend policy that’s based on the strength of the balance sheet; it’s based on cash flows being upstreamed to the holding. We need to be able to finance these dividends, we’ve been consistent. We’re clearly looking at an attractive yield and obviously we’ll take that into account. But today I’m not going to make any -- give you any color about what we expect our dividend to be in May 2013.

Robin Buckley - Deutsche Bank - Analyst

Okay, that’s great. Thanks very much.

Operator

The next question comes from Albert Ploegh. Please go ahead.

Albert Ploegh - ING Wholesale Banking - Analyst

Yes, good morning all. A few questions from my side. To start with, the impact of the low-yield environment, can you update a bit on what you’ve done in the second quarter in the US in terms of -- especially on the universal fixed life, on withdrawing products or repricing? I think you already mentioned this as well in Q1. So, did you get anything additionally in the second quarter? And if the yield environment stays as it is, what more actions can you take to mitigate the impact, as I guess there are some limitation at some point to repricing?

Second question, on the variable annuities, which reflect, the margin declined to 74 basis points and that ambition of 80 basis points is kept in place. Do you expect to return to that level already in the second half or is it a bit more long-term ambition?

And the third question is on the US RBC ratio. On the slides you mentioned that was a fixed annuity co-insurance transaction. Can you give a bit more color on that transaction and what the impact has been and if any more actions are planned in the US business? Thank you.

Alex Wynaendts - Aegon NV - CEO

Thanks, Albert. In terms of low yields, low investment, I think what we’re trying explain is that the main impact really is on the new business, and it is on the new business because we want to maintain our disciplined pricing. And that is really what we’re seeing. And therefore, with low interest rates, you just see that certain products get tougher and tougher to be repriced, you’re right. We are redesigning products, we’re adjusting products, we’re repricing some of them. But there comes a point where a product is not relevant anymore or interesting anymore for a customer. And then we also want to make sure that the products we sell make sense for the customer as they makes sense for us. We have to make sure that that is the way we go forward.

So there is a point indeed that you can’t be repricing more than what we have done. But I think what’s important here is just as you shift towards other product lines, product lines that are much less sensitive to interest rate, accident and health is for example a very good example, these products are much less sensitive to interest rate, and therefore very pleased to see that we’re showing very good growth in these areas.

Darryl, I don’t know if you want to add anything to this.
Yes. Absolutely, first and foremost, exactly what Alex just said, is we’re focused on selling the products that aren’t interest rate sensitive in this environment. And the good news is we’re very diversified in our distribution and product suite. We’re focusing on term, indexed universal life, variable universal life, supplemental products, accident products, all of those. We have a full suite of products that aren’t exposed to the low-rate environment. And we’re getting good growth in those sales.

For those that are most exposed, in particular, our most exposed product was our second-to-die joint survivor product. We pulled it this quarter. It was just too far outside to get back to profitability with simple pricing changes. And so that came off the shelf this quarter. And that had the most significant impact in the quarter. For the other remaining fixed ULs, secondary guarantee products, we have further product and price changes planned for the second half.

Alex Wynaendts - Aegon NV - CEO

On the variable annuities, what I said is that margin declined, but I said it was due to adverse mortality experience on all the products that had death benefits only. So, really it’s a mortality issue and we expect this to return to a normal level and no reason to believe that there is a trend. And if you would exclude the effect of that adverse mortality, effectively you are already at the 80 basis points, and that’s why I’m saying -- I said in my speech that we remain comfortable with our medium-term 80 basis points margin. Of course, keep in mind that previous quarters we were at higher margins.

In terms of the fixed annuity co-insurance, it was a EUR1.5b transaction. It was an attractive transaction where we’re able effectively to raise capital at the low cost of capital. That’s (technical difficulty) I want to say about that.

Albert Ploegh - ING Wholesale Banking - Analyst

Okay. Okay, thanks very much.

Operator

The next question comes from Ashik Musaddi. Please go ahead.

Ashik Musaddi - JPMorgan - Analyst

Yes, hi. Three questions. First is on the capital, the required capital release that you announced, you have made an addition to required capital of EUR42m on slide number 17. Can you give more color on that, due to low interest rate, and which part of your business have you put in more capital, and is there any release of capital from some business? Any color on that?

Second question is on pension on slide number ten, you mentioned that the margin is decreasing but as a percentage of value, it is going up, can you give some color on where do we expect that to stabilize going forward, the margins on the pensions in the US?

And the third is on any color on economic capital, there has been a lot of noise about economic capital worth as the regulatory capital which AXA has highlighted at its presentation. So any color on your economic capital was it IGD, if you can give any color. Thanks.
Thank you. So on your first question around the EUR42m on slide 17, there is always a number of pluses and minus and moving parts and I will ask Willem from IR to contact you directly to try to give you a little bit more guidance there.

In terms of the margin of our pension business, what I was trying to show you today is that we have actually been able to maintain our margin of 24 basis points. In fact, the margin has increased in an environment which is clearly competitive. We are well aware of the fact that the margins are competitive but we operate in a segment where we are able to get reasonable margins and that is not -- that is because we are not in what we call the jumbo cases.

But the most important reason is that we are taking management action in reducing our expenses and we are able to do so because we have invested this is already some years ago, we have made significant investment in our administrative capabilities and that is what you see now paying off.

That means that it has been scalable so we can attract more business at lower cost. And you see this very clearly when you go to slide number 10 where you can see that the fees, so, effective -- the revenue as a percentage of assets and management have declined quite significantly, they've effectively declined by a third, while effectively our margin have remained stable and this is a result of scale but the fact that we invested in the capability and continue to proactively manage our expenses.

On this basis, I was able also to confirm that we will be on track to meeting our 25 basis points margin for the long term. And then I think this is actually a very good result.

Economic capital, yes, I know there has been a lot of talk, there has been an enormous amount of talk. We are involved -- AEGON is involved and I'm personally very much involved in all the discussions. What I think has become clear now is that still a lot is outstanding and it is far from clear how in a number of key issues like countercyclical premium, liquidity premium, matching premium, matching adjustment, how these will be resolved and these I can tell you, have a very significant impact on the numbers. That is why at this point in time, we believe it makes no sense for us to communicate with the market.

What we did see is we have our own economic capital framework, we have been working -- AEGON has been actually running our business on our own economic capital framework for quite some time. That means products are being priced on this basis, we run our asset liability on this basis, we run our hedging on that basis. But I feel that sharing this with you at this point in time, not knowing what the outcome is and making -- sharing numbers which are completely incomparable with others is not going to add any clarity and that is why we are waiting to get more clarity from Solvency 2 and I promise you as soon as we get the clarity, we will also be providing you the numbers.

We are running our business on an economic capital framework and all I can say is that based on what I see and what I hear, and what I expect the direction to go, we are comfortable with our position.

Ashik Musaddi - JPMorgan - Analyst

Thank you. Just a follow up on the fee revenue, when should we expect the fee revenues to stabilize or will it continue to go down like this or is there any particular level or a particular fee level that you are looking for?

Alex Wynaendts - Aegon NV - CEO

I assume you are talking about the fees in the pension business, Ashik.
Well, it is true that we see a pressure on fees and we see more pressure on the bigger tickets and on the bigger case than we show on the lower cases. On the other side, you also see some plays which will actually be leaving the ground, leaving the area, there are a couple of them even for sale.

And so it’s very difficult for us now to predict where the fee levels will go but I can tell you because that I can predict, is we will take the actions to address and mitigate fee reductions. And we’ll make sure that as such, we remain competitive while at the same time, we are able to meet our margin. And I believe that slide number 10 is a very clear demonstration of it.

Ashik Musaddi - JPMorgan - Analyst
Okay. Thank you.

Operator
The next question comes from Hans Pluijgers. Please go ahead.

Hans Pluijgers - CA Cheuvreux - Analyst
Yes, good morning. A few questions from my side. First, on the impact of currencies, could you give some feeling on the impact of currencies on the underlying pre-tax and in the sales?

Secondly, looking at the pension pipeline, a very good again, deposit inflow in Q2, could you give some feeling on where the pipeline is going and what do you expect, let’s say, for the coming two quarters?

Thirdly, on IGD impact in the Netherlands, what I think was relatively quite high from the ultimate forward rate, is because of the -- the book is relatively long, could you give some feeling on what the duration of the book is and why the impact was so high if you compare to some other players in the Dutch market.

And lastly, on the VA, two questions. First of all, some pressure on the margin partly driven by the mortality. Could you give the margin excluding the somewhat higher level of mortality so more, let’s say, normalized basis with mortality.

And secondly at the Q1 numbers, you indicated that new VA sales was still at somewhat lower spread than you were targeting, you said, well, maybe we'd would take some initial actions. Have you done anything in the meantime and what currently are the spreads on the new VA production?

Alex Wynaendts - Aegon NV - CEO
Yes, in terms of currencies, the currencies did have an impact, a clear impact. On the improvement of the 10% increase, we have around 9% of favorable currency effect. However, I want to make the point here is that we are also having growth but part of the growth is effectively offset by our management action of running off or deemphasizing our fixed annuity business. So what you see is that we are investing in the future, that we are growing the business as we want to be in the future, and particularly in the US, fixed annuities has been what -- around $14m lower this quarter compared to last quarter.
In terms of the pension pipeline, I don’t know what we disclosed on this, Darryl, but I know it’s an active period and there is always an element of seasonality in it. But do you want to say something more?

Darryl Button - Aegon NV - Head of the Corporate Financial Center

No, other than obviously we don’t put a direct guidance on where the pipeline sits but other than to say that we’re -- we set some stretch goals for the year and we are on track to deliver those and what I have seen so far in the pipeline looks pretty good and pretty robust and so I expect the year to continue and finish up strong.

Alex Wynaendts - Aegon NV - CEO

Yes, and we have had a very strong first half, and we are gaining market share in certain segments as you know, the 43B, the health sector, we are absolutely a leader in that market so that should help us continue on the strong momentum.

Your question on IGD ratio, yes, it is true that the 35% impact on the Dutch IGD is relatively important but it is not surprising of the mix of our business. You know we have quite a lot of long-term business related to our pension business and as such, you will have therefore, a bigger impact.

Having said that, I also made the point that when IGD of around 260 in the Netherlands, even if you deduct the 35 basis points, we still have a very strong IGD ratio in the Netherlands. I think that is really the more important part of it.

In terms of VA, if the 74 basis points includes that mortality effect on these policies that have death benefit only, as I answered in the previous question, I effectively gave guidance and if you would exclude that mortality effect, and there is no reason to continue to assume it’s the same that you would then hit your -- that we would then hit our 80 basis points margin.

In terms of new VA sales, yes, we said that we are at the lower end in terms of our pricing requirements. That continues but that is why we are also taking actions. We have now clearly management actions for the rest of this year which should get us above -- back above our pricing requirements.

Is there anything you want to add, Darryl, in terms of what actions we are taking?

Darryl Button - Aegon NV - Head of the Corporate Financial Center

Well, in terms of the actions we have been taking more recently, we have been dropping withdrawal rates. We have been changing some of the fund lineups that we offer behind the product and increasing some fees, those are the primary levers that we have been pulling. And as we look forward, just with interest rates dropping yet to another low, we are going to take a harder look and actually make some changes around the volatility adjusted funds which is where we embed the risk management down in the funds. We will be using and strengthening those and eliminate some of the fund features that are offered in there in terms of we offer an own allocation methodology where you can have your own allocation -- personal allocation methodology, we will be pulling that back as well. And so there is a number of fund lineups that are lined up for the second half of this year and the combination of that with the other pricing and product changes we have made will get us back to our profitability by the end of the year.

Alex Wynaendts - Aegon NV - CEO

So as you can see, we are taking very clear actions in the variable annuity. We -- it fits in -- and determination having our products priced at the level we are comfortable that means -- at our pricing requirements, this is not only in the life protection business but also in variable annuities.
Good. Thank you.

Operator
The next question comes from Francois Boissin. Please go ahead.

Francois Boissin - Exane BNP Paribas - Analyst
Yes, good morning, gentlemen. Three questions please. The first one on interest rate assumptions, you still expect writing rates going forward, when are you likely to review those assumptions? And a connected question to this would be where do you face the reinvestment risk, i.e. for existing products with high guarantees, what are those and basically what can you do to mitigate this?

The second question-- then on mortgages, the book is already quite big with regards to your general account assets in the Netherlands, how bigger can the book grow? And the subsequent question is, what can you say about asset quality, do you see -- do you still the book at a very high quality book?

And the third question on Solvency 2, as you have basically been involved very much in the discussions and what is your take on where the framework is going? We have heard a few insurers losing faith in the new framework, what would be your position on that? Thank you.

Alex Wynaendts - Aegon NV - CEO
On interest rate assumptions, we always do you review in the third quarter and this year, we will be looking at the third quarter too. I just want to give you one element here and we have been publishing clearly, our interest rate assumptions in terms of risk-free interest rate assumptions. But I think you will need to look, we need to look more and more at our reinvestment deal; that means risk free plus spread on the investments.

So we will be looking at the culmination of the two but we will come back in the third quarter with our assumptions. In terms of where reinvestment of new money yield has most impact, Darryl, do you want to --?

Darryl Button - Aegon NV - Head of the Corporate Financial Center
Yes. And I think part two of that question was then what can we do to mitigate the risk? And maybe I will start with the second first. The most important thing we can do is make sure that we are pricing and putting product in the street that is not exposed to low interest rate environment and that is exactly what Alex and I referred to earlier in terms of sticking to our pricing discipline, focusing on products that do not have the low interest rate risk and pulling products or repricing those that do.

In terms of the in-force book, the back book where the pockets of interest rate risk that we have it's really in two places. Some of the long-tailed life business that sits out there, there is reinvestment risk. It does sit out sit out the curve several years where that mismatch exists. And then on our old book at GMIB, variable annuities, there is still some [RAW] interest rate hit risk in the hedges. On the...

Francois Boissin - Exane BNP Paribas - Analyst
On that, if I may, AXA basically just announced that they basically cancelled the new flows on their VA, on the Legacy VA book. Is this something that you would consider doing?
No, no, it’s not something that we would -- that we are currently looking at. So, we are just obviously in both books, we manage the interest rate risk in totality and using our duration and ALM strategies to minimize the risk and it is -- you have to put it in context so of the risk that we have, that is where it sits. But you have to put it in context with all of the other risk that we manage, the diversification across our book and we do have some products that are exposed to rising interest rate risk as well.

So you have to look at the netting across our ALM and again, the most important thing we can do is focus on the profitability of new business that we are putting in the market and making sure that we are hedging and managing the risk out of the chute on those products and that is exactly what we are doing.

Alex Wynaendts - Aegon NV - CEO

Yes, on the mortgage, on your question in relation to mortgages, our book is around EUR20b. We are adding around EUR2.5b in terms of new business, EUR2.5b of new business. But of course, we also have an outflow -- we also have mortgages maturing so it’s not that we are adding the full EUR2.5b to the EUR20b.

We believe that this is an asset of really good quality and 80%, as I said, of new sales has the state guarantee and if you look at the in-force, 55% of the portfolio has the state guarantee. So clearly, this is an asset which is an important asset for AEGON NL, an asset we are very comfortable with and in particular, in the segment in which we are -- and so there is not much more I would like to say about that.

In Solvency 2, yes, if I knew the answers, I would be more than happy to share it with you but I think the reality is that there is still a lot of uncertainty around the implementation, as you know, it’s a lot of discussions about the countercyclicality measures in what form, matching adjustments, matching premium, there has also been even a discussion about the need for grandfathering all the in-force, which obviously raises a lot of questions. So how do you administer that? What part of your business is grandfathered?

So these uncertainties are still there and what we now understand is going to be next is there will be an impact assessment, probably will be launched somewhere in October and we will then -- the industry will then be asked to assess the impact of different forms of propositions in relation to what is the liquidity premium. And that will take until March to get more clarity and so it is clear, this is going to take longer.

The one thing, at least, I am very confident about and that obviously is of very significant importance as you can imagine for our business with the US, is that there is no discussion about the need for a solution to equivalence and we call it equivalence, we might call it recognition, that is all very technical, but at the end, what will happen is that those companies that will be operating business outside of Europe will be allowed to use their solvency requirements which are prevailing in that country, so in the US, RBC for example, to be the basis of Solvency 2.

And this is not only for the capital position but it is much more important to ensure that there is a level playing field in these markets. We need to be sure that in the US, our Transamerica business competes with its peers, its large peers in the US on an equal basis and that now seems to be not a point of any discussion anymore and this is probably the most important thing for Aegon.

Francois Boissin - Exane BNP Paribas - Analyst

Yes, I appreciate that. Just one point on equivalence, are we talking RBC ratio above 30%, first question.

And second, are we talking equivalence for a certain period of time or is this like for an indefinite time at this moment in time.
The level of the equivalence in terms of RBC hasn’t been agreed but I would say that it would -- be most likely at the 200 level so that would be -- let us call it the 100 level in Solvency 2, and 200 level at RBC. That’s what’s now most commonly understood.

When we talk about the period of time, it has to do with the transitional measures and so it’s the transitional period until you get equivalence because the regulators on both sides and authorities on both sides won’t work out all the details so once there is equivalence, there is equivalence forever.

Where there has been discussion over a period of time, we talked about five years, five plus one, five plus five, is about the transitional period where we will be allowed equivalence without that being formally implemented so that as I said, the regulators have put in place their -- all the details. So equivalence is then forever.

Francois Boissin - Exane BNP Paribas - Analyst

Okay, thank you very much.

Operator

The next question comes from Raphael Caruso. Please go ahead with your question.

Raphael Caruso - Raymond James - Analyst

Good morning, everyone. Just two quick questions. Regarding the variable annuities balances [sheet], you provide in the financial supplements, it appears that you have a minus $1.3b impact of other. Could you give us some color on that, please?

And the second question is concerning your variable annuities margin which decreased to 74 basis points, that is just 88 basis points in Q1, so what do you plan to improve the variable annuities margins and to be more recurring on what point? Thanks.

Alex Wynaendts - Aegon NV - CEO

It’s a market impact., Darryl, do you want to say something? Otherwise we will ask IR to give you directly.

Darryl Button - Aegon NV - Head of the Corporate Financial Center

Yes, I’d have to look at the supplement but I believe it feels about like the size of what the market impact would be on the funds. I think the markets were down about 3% on a $40b plus book so it’s probably about -- I would think of it was the market --

Alex Wynaendts - Aegon NV - CEO

The underlying assets, which are there, but we will come back to confirm it to you.

And your second question, in terms of the margins, we have give you 74 and we said that it was an important element which was affecting the lower margin and that had to do with mortality on all our products which had a death benefit only and that mortality was -- happened to be higher in the second quarter. We don’t believe this is a trend and therefore, we believe this will return to normal in the future, in the next quarters, and if you exclude that impact, that I shared, we are back above the 80 basis points margin. So there is no reason to believe that we are not back at the 80 basis points margin because the mortality is not ongoing.
Okay, thanks.

Operator
The next question comes from Gordon Aitken. Please go ahead

Gordon Aitken - JPMorgan Chase - Analyst
Thank you. Just a couple of questions, please. First of all, in the Netherlands, how many large defined benefit pension schemes have you insured in the first half and what was the level of assets?

And the second question is in the UK, you said sales were down, you said this reflected the expected reduction in pension sales. Now as one of the last commission payers, I would have thought that you were being quite successful at the moment given the RDR doesn’t come into effect until the end of the year. Could you just add a bit more color here, thanks?

Alex Wynaendts - Aegon NV - CEO
In terms of defined benefit plans, I need to come back to you and look at the exact numbers. But let me tell you two things which are clear. First of all, it’s a difficult environment, and the environment is difficult in particular because the coverage ratio of these defined benefit plans are below 100. And that means that once you want to transfer them to an insurance company, you have to add cash so a lot of the corporates, what they are doing is they are waiting to get back to the level of 100 and at that point in time, it’s more attractive. So the low interest rate impact on the coverage ratio has clearly an impact on the sales.

The same thing is -- at the same time, we are very clear; we only want to sell products with -- where we make our margins. We do that on an economic capital basis, that means we integrate the effect of the markets and we integrate the state of low interest rates and we only want to be in the market if we can sell products that are priced economically and in this environment, it clearly, it is very different from our point of view and so for -- as a supplier but also from the other side, because as I mentioned, the element of low coverage ratio.

What’s important is we run our in-force, we have a large in-force, as you know we have been taking costs out, so we are improving our margins in our in-force, we are improving service levels, and with 24% to 25% market share, we are already effectively the dominant player.

The question on The UK is an interesting one because we do pay some commissions on new business but we also have announced that we have greatly reduced the amount of commissions and that is what you see reflected in our sales. So it is true that we continue to be active in the market but only on conditions which we feel make sense. We have reduced greatly our commission levels and overall commission payments and that is what you see reflected in the sales.

But what is most important for us is not so much the new sales, it’s to maintain our book, our in-force and that is why we are putting a lot of efforts in the retention of our in-force. That is in relation to service levels because that effectively is what is going to drive value.

Gordon Aitken - JPMorgan Chase - Analyst
Thank you.
Alex Wynaendts - Aegon NV - CEO

On non-life, hello?

William Elderkin - Societe Generale - Analyst

Hi, good morning, everybody. It's William Elderkin from SocGen. I've got four questions, please. First of all, on the Dutch non-life business, can you just give some more details of exactly what is going wrong and how you are fixing it and over what time period you are going to be able to fix it?

Secondly, on The UK pensions business, I think the earnings in the quarter of about GBP5m, that seems a very long way away from the level of 2014 and 2015 earnings ambition that you have. Again, can you sort of outline how you are going to get to that level of target earnings?

In terms of the US variable annuity business, it seems somewhere there must have been a negative effect from a drop in the US swap rates over the first half of the year particularly on the back of the unhedged GMIB book. Where in your numbers did that show up?

And then finally, can you make a comment in terms of the overall strategic structural outlook for the Dutch pensions business on the corporate side, are you going to see M&A opportunities and do you have any appetite there?

Alex Wynaendts - Aegon NV - CEO

Thank you.

Operator

The next question comes from William Elderkin. Please go ahead.

William Elderkin - Societe Generale - Analyst

Hello.

Alex Wynaendts - Aegon NV - CEO

(technical difficulty) -- lot of noise. On our non-life business, it is really the disability segment in the business and what you see is a combination of a number of issues here is that the environment is just very difficult, the economic environment, that means people are claiming quicker than they used to claim. And so we are doing a number of things.

First of all, we are ensuring that all claims that are being processes are being proper claims. That is step number one. That is something which by and large, we have not concluded. The second thing is we are looking where we need to adjust the pricing, we are able to adjust the pricing and we will be adjusting our -- and have been adjusting our price in the quarter and so I expect to see an improvement in the disability segment in the second half of this year.

You probably will have noted that it is not only an issue in relation to Aegon, all the players in this segment are seeing that very significant deterioration as a direct consequence of the economic environment but we are taking the steps and the measures to offset that and we are looking forward to seeing the second -- sorry, the second half this year to clearly improve.

In the UK pension, there are a number of elements. First of all, this quarter was hit by some effect of persistency, we already are -- we get somewhat of a volatile environment so persistency had a negative impact. The markets had a negative impact, our business is very sensitive to the markets
And the reality is that we share this with you that we need to be even more efficient with our expenses and that we will be needing to take more cost out, we will be doing so. And so these are the three elements which are affecting the UK pensions, some of them are more market-related and others are in our control and I can assure you that those within our control, we will action on them and we will be taking further cost down in the coming years.

On the GMIB, I will give it to Darryl to answer the question.

**Darryl Button - Aegon NV - Head of the Corporate Financial Center**

Yes, the biggest impact from the low rate environment on the GMIB obviously is in capital, there is a small impact on earnings but it is fairly small in the quarter. In terms of capital, you actually have two different things going on.

In terms of our operational cash flow, which is driven more on our S&P capital model, it's in there in terms of a hit to the operational free cash flow and this speaks to the other question that was raised before in terms of the release of required surplus. There would be a hit in there for the low interest rate environment on the GMIB and that was largely offset by a strong earnings quarter and capital initiatives that we initiated in the quarter, in particular, the fixed annuity co-insurance was an example of one of those.

On the RBC ratio, it is actually hard to find because of what is called the smoothing mechanism in that RBC ratio and effectively, what that smoothing mechanism does is it defers some of the current year economic environment into the next year and the net result here was actually from the first quarter, a lot of the favorable market movements in the first quarter got deferred to next year. When we'd go through the second quarter, and those markets reversed, that deferral for next year came back into the current year and it smoothed it out so the RBC ratio actually was largely neutralized this quarter from the impact of interest rates.

**Alex Wynaendts - Aegon NV - CEO**

And, William, your final question, the pension market is clearly an interesting market in the Netherlands. There is a big segment sale of defined benefit -- the defined benefit plans which will be looking for a solution, a long-term solution. And as I shared earlier, in the low interest rate environment right now, this transfer is difficult because the coverage ratios are below 100.

We also want to make sure we price these products correctly on the (background noise) and that is the basis on which we will be looking at this market. I also want to reiterate here your question was more on a strategic point of view, the importance -- and I keep on doing it, of maintaining a strong capital position. The strong capital position we have today is one we are pleased to have but also one which we feel is essential, an essential part of our strategy. And that is where our priority is.

**William Elderkin - Societe Generale - Analyst**

And quickly come back to my last -- what I was really getting at with that question was do you have any appetite for any potential M&A opportunities within the Dutch market specifically?

**Alex Wynaendts - Aegon NV - CEO**

As I just said our priority is to maintain our cash position -- capital position, strong capital position and maintain a buffer. That is what our priority is.
Thank you very much.

Operator

There appear to be no further questions. Please continue with any other points you wish to raise.

Alex Wynaendts - Aegon NV - CEO

Well, if there are no further questions, actually it's exactly 10 o'clock here in the Netherlands, 9 o'clock in The UK. Thank you all for listening in and look forward to seeing you soon and speaking to you soon. Thank you very much and have a good day. Bye.

Operator

This concludes the Aegon second quarter 2012 results conference call for analysts and investors. Thank you for participating, you may now disconnect.