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## PRESENTATION

### Operator

Good day and welcome to the Aegon second quarter results 2016 conference call. Today's conference is being recorded. At this time I would like to turn the conference over to Mr. Willem van den Berg, Head of Investor Relations at Aegon. Please go ahead sir.

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### Willem van den Berg - Aegon NV - Head of IR

Thank you. Good morning everyone and thank you for joining this conference call. We will start today's call with a summary of our second quarter 2016 results followed by a brief overview of the strategic and financial rationale behind the Cofunds acquisition. Please also review our disclaimer on forward looking statements, which is at the back of our presentation. After prepared remarks, CEO Alex Wynaendts will be joined by our Chief Financial Officer, Darryl Button, to answer your questions. Alex, go ahead.

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### Alex Wynaendts - Aegon NV - CEO

Thank you Willem and good morning to everyone. Thank you for joining us for our second quarter 2016 earnings call. This was clearly not a satisfactory quarter from an earnings perspective as earnings were affected by lower interest rates and adverse claims experience in US and made a book loss from the divestment of our annuity portfolio in the UK. Later in my presentation I will outline the five-part plan that is being implemented in our US business to improve our results.

I'm pleased that our sales and in particular our deposits remained very solid. This is a clear indication that we are successfully repositioning our business by providing attractive solutions to an expanding customer base.

The acquisition of Cofunds, which we announced today, together with the earlier announced acquisition of BlackRock's DC business, firmly positions our UK business as the leader in the fast-growing digital platform market.



Our capital position increased to an estimated 158% during the quarter, despite adverse market impacts as a result of the management actions we've taken. Based on our solid capital position and year to date capital generation, we are announcing an interim dividend of EUR0.13 per share. This dividend will bring the total capital return to shareholders this year to an expected EUR950 million.

Here on slide 3 it shows the development of our Solvency II ratio during the second quarter. As you can see, the Solvency II ratio increased as the negative impact of lower interest rates was more than offset by management actions in both the Netherlands and the UK, including the divestment of the UK annuity portfolio.

In the Netherlands our Solvency II ratio increased significantly from around 135% last quarter to 154% this quarter, and I will discuss the actions we have taken to achieve this on the next slide.

In the UK market movements had a negative impact on the capital ratio as interest rates dropped to an all-time low following the Brexit vote. Additional interest rate hedges that we put in place before the vote, together with a capital release from the second reinsurance deal related to our annuity portfolio, did however more than offset the extreme movement in interest rates.

And I would like to remind you that the 145% solvency ratio in the UK does not include the benefit of the Part VII transfers of our annuity book. These transfers are expected to add another 15 percentage points to the ratio next year after completion of the transfers.

As to the US, our RBC ratio remains solid and is at the high end of our target range. The decline compared with the previous quarter was mainly driven by the payment of a dividend to the Group, in addition to the impact of lower interest rates.

Let me now discuss the actions we have taken in the Netherlands in more detail. Following the first quarter movements in our Dutch Solvency II ratio we conducted a thorough review of the methodology and the outcomes and identified four key areas of improvement.

The first was implementing additional hedges pre-Brexit to reduce our sensitivity to market movements, particularly to declining interest rates. The second was a more thorough application of the volatility adjuster mechanism in the Netherlands. The third was changing our expense assumption in stressed conditions. We have a strong track record of managing expenses and we felt the previous approach did not properly capture the actions we would take to bring down costs in the longer run. And the fourth, our other model and data refinements.

In addition, we've made several refinements by using more granular data in our models. The main impacts of these refinements and the other management actions is a reduction in SCR, resulting in an increase of the Solvency II ratio.

Slide 5 provides a summary of our latest Solvency II sensitivities for the Group and for our main units. These updated sensitivities reflect both the management action we've taken and the year to year -- year to date market movements.

Although our sensitivities have increased to a certain degree, they remain low. Today I would like to focus on three of these key sensitivities. Our sensitivity to interest rates, to the ultimate forward rate, UFR, and to credit spreads.

So firstly our sensitivity to interest rates. Changes in the sensitivity reflect the UK annuity portfolio divestment, adjustments made to hedges in the Netherlands and the lower level of rates in the US. In the extreme scenario of interest rates dropping another 100 basis points from current levels, the Solvency II ratio of the Group and our main units would remain within our target range.

Secondly, our sensitivity to a lowering of the UFR by 50 basis points. This would reduce our Group Solvency II ratio by 7%. The impact on the Dutch solvency ratio is obviously larger at 19% but would still be manageable.

And thirdly, our sensitivity to credit spreads. The sensitivity increased in the first half of the year, partly as a result of the extreme market movements.

As you can see on slide 6, our holding expense -- our holding excess capital position increased to EUR1.1 billion during the quarter. The holding received EUR600 million in dividends as varied units upstream capital. Three-quarters of this was from our largest unit, the US. Other significant



contributors were asset management and our business in Spain and Central and Eastern Europe. Together these units upstreamed a total of EUR140 million, underlining the importance of these business units in increasing the diverse nature of our business.

This quarter we spent around EUR200 million on the second tranche of our share buyback program and EUR150 million on paying the cash part of the final 2015 dividend. And in the third quarter we'll pay an interim dividend of EUR0.13 per share, an increase of 8% compared with last year. This will bring our total capital return to shareholders this year to an expected EUR950 million, meaning that we're on track to deliver on the capital return plans which we announced in January at our Investment Day in London.

As I shared with you earlier, our underlying earnings of EUR435 million did not meet our expectations, and let me now run you through the main moving parts on slide 7. In the Americas earnings decreased to EUR270 million as a result of lower earnings from life, accident and health and variable annuities, while our other businesses performed in line with expectations. The principal drivers behind this decrease were declining reinvestment rates, adverse claims experience in both life and health businesses, and lower variable annuity earnings.

In Europe earnings increased by 15% to EUR160 million. The Netherlands delivered yet another quarter of solid results as earnings increased to EUR138 million. In the UK the positive impact of the accounting change relating to upgrading of customers to our platform was partly offset by lower UK life earnings following the disposal of the annuity portfolio.

Asset management earnings remained solid at EUR37 million, although they decreased as a result of the normalization of performance fees. Holding expenses declined to EUR33 million due to lower funding cost following the redemption of senior debt at the end of last year.

Let me now explain in greater detail on slide 8 what measures we are taking to address the shortfall in our earnings in the Americas.

As you are well aware, low interest rates in the US are not only leading to declining reinvestment yields but also to changes in customer behavior and lower margins on new business. These developments all have an impact on our earnings and at the same time we have to deal with significant regulatory changes and adverse claims experience. We are however determined to take all necessary actions to offset these adverse impacts and improve our profitability.

Let me provide you with an overview of our five-part plan which is being implemented across our business in the US. So first, we are increasing the monthly deduction rates on certain blocks of our universal life products based on expectation as to what the future cost will be to provide this coverage, all in line with policy guarantees as to maximum rates to be charged. At the end of 2016 we expect to have implemented 75% of these increases and we will start seeing the full impact of these increases on our earnings by the middle of next year.

As you are aware, we're also actively pursuing for rate increases on long term care policies to compensate for the continued increase in claims. We have filed requests in 20 states and have seen better progress now than a few months ago.

Second, we continue to launch new products and redesign existing products to secure profitable future growth. Furthermore, we're also exiting products that no longer meet our objectives, which should lead to cost savings in the medium term.

And third, we will continue to explore all options to dispose of non-core and lower return businesses. Selling part of our run-off business in such a low rate environment is however proving to be a challenge, but the scope of the current assessment is now broader than just the run-off businesses.

And fourth, we are today announcing that we are in the process of rationalizing our location strategy in the US which will lead to a reduction in our geographic footprint.

Fifth, we will accelerate the pace of our expense savings program in the US, as you can see on the following slide.

So I'm pleased that we have made strong progress towards reducing our expenses in the first half 2016 and we are ahead of schedule in realizing this year's expense saving target. In the US we made very strong progress as the completion of our voluntary separation incentive plan led to headcount reduction of approximately 600 people and yielded significant savings.



As a result, this quarter we have already achieved our expense savings target for the full year with \$60 million of savings instead of the original target of \$40 million. And going forward, we'll continue to accelerate the pace of our expense savings.

In the Netherlands and at the holding we're also on track for our 2016 expense savings and making good progress towards our 2018 target. But here I would like to underline, as I've done before, that our expense savings program is being executed in such a way so as to ensure that the high customer service levels are maintained.

It also goes hand in hand with continued investment in the business. We are for instance continuing to invest in digital capabilities, utilizing the very latest technology that both supports customer experience and simplifies our business at the same time.

I'd like to now turn to slide 10 which illustrates how the exceptional items impacted on net results this quarter. As you can see, the main driver behind the net loss of EUR385 million is a book loss on the divestment of our own annuity portfolio in the UK. This divestment was a key step in executing on our strategy to optimize our portfolio, and it reduces our exposure to both financial market and longevity risk going forward.

Through these transactions we have significantly lowered both our credit spread and interest rate exposure and successfully freed up GBP0.5 billion of capital. The financial turmoil and uncertainty following the Brexit vote underscore why the decision to sell our UK annuity book was in the best strategic and financial interest of our Company.

Fair value items were not a sizeable factor this quarter, and the losses amount to EUR378 million. The majority of these items were caused by the impact of decreasing interest rates on our hedging programs, and this was mainly related to the accounting mismatch between assets and liabilities on an IFRS basis in the Netherlands. These hedging programs are in place to protect our capital position and have proved to be very effective.

Let me now turn to our strong deposits on slide 11. We are pleased with our strong deposits in retirement plan and asset management, which have been supported by increased distribution strength following last year's acquisition of Mercer's DC business and the stake in La Banque Postale asset management.

This quarter the number of pension participants in the US and the UK and the Netherlands increased by 15% to 11 million plan participants, a reflection of the trust customers are placing in us. Net deposits amounted to EUR1.2 billion in the quarter as they were impacted by anticipated contract discontinuances from the Mercer block. We expect elevated contract discontinuances to continue throughout 2016 with net deposits increasing thereafter.

Life and protection sales were down 11% and 8% respectively. This decline reflects our continued focus in profitability of sales and on the next slide I will elaborate on the actions we're taking to maintain the sales at a profitable level.

As rates have continued to trend lower and lower, we're actively redesigning and withdrawing existing products and launching new ones. This often means repricing capital intensive products and replacing them with capital light alternatives. An important achievement this quarter is that Aegon was the first company in the Netherlands to receive approval to launch a general pension fund, so called APF.

This pension pooling vehicle enables separate financial administration for multiple pension plans and allows smaller pension schemes to benefit from economies of scale while complying with complex pension regulation.

Our general pension fund called Stap leverages our industry-leading administration and asset allocation capabilities. We have already secured a large contract and are in an advanced stage of closing two others, strongly positioning us as the leader in the pension market.

I'm now concluding on slide 13. Although this was a challenging quarter from an earnings perspective, it was also one in which we strengthened our capital position and made a series of significant steps in the execution of our strategy. We are accelerating the actions we are taking to transform our Company, to increase our returns and to become a more customer-centric organization. I'm therefore confident that we'll continue to make significant progress towards our 2018 targets.



This concludes my prepared remarks for this quarter's results. But before Darryl and I take your questions, I would like to spend a few minutes to talk you through the acquisition of Cofunds, which we announced today.

This acquisition is a unique opportunity to further accelerate the execution of our UK strategy. The acquisition of Cofunds, together with the recent acquisition of BlackRock's defined contribution business, gives us a market-leading position and scale in the workplace savings and retail platform market. We are able to use this scale and our existing technology to drive GBP60 million of expense savings, reducing our combined digital cost base by 25%.

What's more, this acquisition enables us to rapidly develop our distribution footprint, gaining opportunities in the retail advisor space where there's minimal advisor overlap, and a new business relationship with Nationwide, the UK's largest building society.

But before I give you more color on these benefits, let's first take a step back to explain how today's announcement fits well with our strategy.

I'm on slide 16. Five years ago we embarked on a strategy to transform Aegon UK into a cost efficient and scalable digital platform business. This enables us to not only compete on administration but also an investment solution, asset management and customer guidance. And since then we have built a very successful award-winning platform that services all segments of the market.

We've had great experience to date, upgrading over 200,000 existing customers with around GBP4 billion of assets. While continuing with our own customer upgrade program we will work with advisors to support upgrades to new modern digital solutions as part of the Cofunds acquisition. Customers can then consolidate more of their savings in one place rather than being restricted to one product solution or to an outdated investment proposition.

In the past few months we've announced several strategic transactions that enable us to accelerate the strategic transformation of our UK operations from a traditional life insurance and pensions company to a platform business. We have divested our annuity portfolio, acquired Cofunds and BlackRock's DC business, and by doing so we have reduced our exposure to longevity and financial market risk, while at the same time adding additional capabilities and significant scale to our platform business.

As you can see on slide 17, the acquisition of Cofunds and the recently announced acquisition of BlackRock's DC business enables us to complete our strategic transformation into a market-leading digital provider. After these acquisitions we will be number one in the retail platform market and number three in the workplace savings market. We're also able to provide services to orphaned customers.

The platform market is growing rapidly and we expect the size of this market to be over GBP1 trillion by 2020. This will be made up of business from the retail advisor market, corporate and non-advisor business, and we're well positioned to benefit from our scale across all of these markets.

Cost synergies are a key element in the acquisition announced today, and as you can see on slide 18, we will be taking out over 25% of the combined digital cost base following the acquisition. And we're very confident that we can deliver the GBP60 million of cost synergies for two reasons. First because we have a scalable platform technology that we can leverage to replatform the Cofunds business. Second Aegon UK has an excellent track record of delivering on expense savings.

A further benefit of replatforming the Cofunds business is of course that this also brings significant advantages to our customers and their advisors. The benefits include less paperwork, a broader investment range and integration of pensions on the platform.

By combining the strong heritage of the Aegon UK business in pensions with the market-leading capability for ISAs and general investment accounts brought by Cofunds, we will be able to offer a full proposition to each of our chosen markets. Offering a wider range of products in combination with limited overlap in distribution network is expected to lead to attractive cross-selling opportunities.

Slide 19 shows just how attractive this transaction is from a capital perspective. The net capital investment is limited to EUR50 million as target expense savings will enable us to reduce expense levels of Aegon existing insurance business and therefore realize a capital benefit of EUR150 million.



Our capital light strategy is expected to result in predictable growing capital generation going forward. Post-integration of the Cofunds transaction we expect our business in the UK to generate GBP70 million of capital per year and growing as the platform grows. The incremental GBP50 million of capital generation from the Cofunds acquisition reflects the expected addition to net underlying earnings.

So let me now summarize why this acquisition of Cofunds is so attractive to us. Firstly, it requires only a modest net investment of GBP50 million to generate an incremental GBP50 million of capital generation per year. Secondly, the transaction has a payback period of only three years and it contributes to achieving the Group return on equity. And thirdly, Aegon UK maintains a solid capital position which will enable it to resume dividend payments to the Group 2017, in line with our earlier guidance.

So Darryl and I are now happy to take your questions on both this transaction and our second quarter results. Thank you.

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## QUESTIONS AND ANSWERS

### Operator

(Operator Instructions). Ashik Musaddi, JPMorgan.

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### Ashik Musaddi - JPMorgan - Analyst

Yes hi, good morning Darryl, good morning Alex. So just a couple of questions. Can you give us some thoughts about the capital generation and dividend upstreaming? It looks like the UFR benefit in Netherlands has gone up quite a lot, so what does it do to your guided EUR250 million of capital generation in Netherlands? And if rates don't go up or interest rates don't go up, then would you be comfortable upstreaming dividend from Netherlands in two or three years or do you think that because underlying capital ex UFR is very weak it will drag the capital remittance from Netherlands?

Secondly, you mentioned in one of the slides that UK will start upstreaming capital next year. But how should we think about it? Shall we think about like GBP20 million a year because Cofunds cost savings will not come in two or three years' time? So how should we think about that?

And third question is can you give us some thoughts about US capital as well because in third quarter you'll be doing this cash flow testing as well as updating your assumption. So what could be the drag on your US capital and are you feeling comfortable with your US capital at the moment? Thank you.

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### Darryl Button - Aegon NV - CFO

Okay Ashik, this is Darryl. I'm going to try and hit those in order, I think basically capital questions for the big three units. Yes, the impact of the UFR is larger now that rates have dropped significantly over the last two quarters and you'll see the sensitivity that we provided, it's about double of what it was back in January. So we're saying it's about 19 points for a 50 basis point drop on the UFR.

That does have a flow-over impact to cash generation in the Dutch operations. We are downgrading the EUR250 million per year down to EUR225 million because of that additional UFR.

You did ask about dividend expectations in the Netherlands I think was your second question. There I would just say first of all we're feeling a lot more comfortable about the capital obviously in the Netherlands at the 154% ratio where we are, but there is an important conversation and debate happening on the UFR in the Solvency II curve, and that's an EIOPA discussion that's happening in the second half of this year. I think you know the proposal from EIOPA is to drop the UFR by 50 basis points spread over the next three years. So we obviously want to watch that debate play out and see where that goes. That obviously would have an impact on our Dutch capital ratio.



In terms of dividends, I actually still expect to receive a dividend from the Netherlands this year but I would say albeit something lower than the EUR250 that we got into earlier, but frankly that's a decision that we're going to make in the fourth quarter when we have the knowledge of the whole UFR discussion.

In the UK I think we tried to show you where we think capital generation gets to in the UK and when we put all the pieces together we're going to come out around that GBP70 million and expect to grow from there. But I think the other thing you need to think about as you think about 2017 is that as we put all these pieces together the actual capital investment from the acquisition is fairly minor because of the expense synergies. And then we still have some release of capital coming from the Part VII transfers. So I think when we put all the pieces together and find ourselves in 2017 we'll have some balance sheet strength that can supplement that GBP70 million from a dividend perspective. And that's the way I would think about that.

And then finally I think your last question was in the US on cash flow testing. Yes, rates are lower so we know that we will have an incremental impact on cash flow testing. I don't think it's going to be of a variety that I would call material disruption from the cash flow we expect to receive in dividends from the US. We are and continue to ride at the higher end of our RBC range in the US. But I see some modest compression on RBC ratio from cash flow testing but not enough to disrupt the dividend flow.

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**Ashik Musaddi** - JPMorgan - Analyst

Thanks. Just one follow-up on this dividend thing -- sorry Netherlands thing. One of your competitors said I think last quarter that based on first quarter interest rate decline their cash flows or capital generation went down by EUR100 million, and given what we have seen in second quarter, it would have been a lot more as well. And you're kind of guiding just a EUR25 million drop. So what are we missing here? Any thoughts on that? Just a quick one, sorry.

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**Darryl Button** - Aegon NV - CFO

I can't comment on our competitor. We're not seeing numbers that big.

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**Ashik Musaddi** - JPMorgan - Analyst

Okay.

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**Darryl Button** - Aegon NV - CFO

But I would say we maybe had some prudent estimates in the EUR250 million to start with. But we're not seeing that kind of drag. I think the other impact also is -- the thing you have to also keep in mind is that the new business is quite low right now in terms of any capital intensive DB business in the Dutch business. That's also extremely low and that has a beneficial impact on capital as well.

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**Ashik Musaddi** - JPMorgan - Analyst

That's very clear. Thanks Darryl.

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**Darryl Button** - Aegon NV - CFO

Yes.



**Operator**

Albert Ploegh, ING Bank.

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**Albert Ploegh - ING - Analyst**

Yes, good morning all. A few questions from my end. Sorry to come back to the Dutch cash flow outlook. You mentioned the UFR impact is only an additional EUR25 million, so the management actions taken itself in the first half, that will have done basically no structural negative impact on the cash flow outlook? That's my first question.

The second question is if I look at the dividend upstreamed in the first half or in the second quarter, the around EUR600 million, I also saw of course contribution from asset management in Central and Eastern Europe of about EUR140 million. How should I see that number? Is that basically the majority that you expect from these units in the first half or can we still expect something for the second half?

And then the question, a bit forward looking as also previously alluded in my previous question on the assumption reviews, you already gave some answers on the cash flow testing. We saw some US competitors making already some adjustments in the second quarter and some also material. How do you look at those reviews? With a certain element of confidence or can we expect maybe some material -- more of course non-cash items but some material impact in the third quarter from that? Thank you.

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**Darryl Button - Aegon NV - CFO**

Yes hi Albert, it's Darryl. I'm going to try and take those. The first answer is a short one. We don't see any impact from the management actions on the Dutch solvency ratio on the EUR225 million. So really the EUR250 million is down to EUR225 million on the UFR and there's no impact on the management actions from that.

On the dividends upstreamed, we did receive dividends from asset management, a few other places. I would also say there was an extraordinary dividend that came up from Spain as well and that related to the Santander joint venture acquisition that we had on that distribution relationship. So there was some capital that was trapped in that for a period of time and that's released itself and so that is in that EUR140 million. I wouldn't certainly expect that to reoccur.

And then on the third question, I think on the Q3 assumption changes, you were commenting on some of the things that have been going on from some of our US competitors. A couple of things. There are a couple that have moved their long-term interest rate assumptions. If you look at that, they've moved them now on top of where ours already are, so I think there's probably not a lot of pressure for us to look at that 4.25% 10-year US Treasury assumption. We're really middle of the pack on that assumption.

And then in terms of the rest of it is we're just in the middle of our normal process where we'll take a look and review all our actuarial and economic assumptions for the third quarter and I don't have any real insight one way or another to share with you today.

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**Albert Ploegh - ING - Analyst**

Okay. Maybe two small follow-ups, first of all on the -- looking back at the Capital Markets Day in January, if I'm not wrong I think you guided basically from a holding free cash flow of EUR1 billion post holding cost. I know your remark on the Netherlands that you do still expect some dividends in the second half of the year. So with all the moving parts in the first half, is there any need to update that guidance or do you still feel reasonably comfortable?

And then on the revisions, I also saw one competitor mentioning some industry report, I think it was more on a GMIB book. I know it's not a material book at Aegon but do you -- what can you comment on that?



**Darryl Button** - *Aegon NV - CFO*

Well on the first one, on the net operating free cash flow of EUR1 billion, that really is the EUR1.3 billion of the operational free cash flow that we have across the units minus EUR300 million of holding and that's your net EUR1 billion. That's still pretty close to being a good number right now. The only real downgrade we've had is the EUR250 million in the Netherlands down to EUR225 million and then a modest downgrade in the UK if you will on the GBP70 million instead of the GBP100 million. But if you factored that into it, I think you're pretty close, maybe a little bit downward pressure on that but not far off.

And then on your last comment on the GMIB, maybe I didn't quite get the question but the GMIB still is a material book for us in terms of -- we haven't been selling it since 2002 but that is still the book that's the source of the \$60 million loss through fair value items below the line that we take every quarter.

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**Albert Ploegh** - *ING - Analyst*

Okay, maybe we can take it offline but I thought there was some industry report on behavioral assumptions that took one of your peers to take some charges.

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**Darryl Button** - *Aegon NV - CFO*

Oh there was a large GMIB writer in the US that took some large assumption changes this quarter. There was -- you can go back and have a closer look at that and I'm happy to have an offline conversation with you on that if you want.

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**Albert Ploegh** - *ING - Analyst*

Okay, no worries. Thank you.

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**Operator**

William Hawkins, KBW.

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**William Hawkins** - *Keefe, Bruyette & Woods - Analyst*

Hello. Thank you very much. Can you just be clearer now about what incrementally is under review in the US? I'm assuming long term care falls into that but if you could just be a bit clearer?

And then specifically on long term care, can you just remind me of the size of the reserves you're currently carrying? Roughly what are the rate increases that you're asking for in these 20 states and do you have any issue there about what you think you're going to be able to achieve versus what you actually want to achieve on that, because clearly it's a highly regulated line?

And then secondly, in the variable annuity book, if I'm not correct you're now no longer sticking with that 70 basis point margin that you guided to just in January. So you've already alluded to a couple of things but can you just be clear about what's gone wrong in the past few months and what we should be thinking that 70 basis points should be in the future? I'll leave it at that for now. Thank you.

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**Alex Wynaendts** - Aegon NV - CEO

Let me give you an answer. So what we're saying on our US business is that -- by the way as part of an ongoing review, we -- our acceleration review about all our products and business lines. We think we need to rationalize our product offerings, particularly in our life area. We have a too wide range of products, which are all slightly different from one another because they are sold through different distributors. There's clearly an opportunity here to rationalize the product line, to look, by the way, at what products we want to continue, what products we want to redesign or exit. All in line with our stated objective of having products that are both attractive to our customers and attractive to us.

So you need to look really at the -- more at the long -- at the life part of the business. Let me remind you, long-term care is a business we haven't been selling for over 10 years, so it's more of a runoff business that we talk about. Although we have introduced a new type of long-term care product, which is a very different product because it's not at all with open benefits. The new product line long-term care has very defined benefits and is not at all subject to all the discussions we're having about rate increases. So we need to make sure that there are two parts to that -- that you're well aware of it.

In terms of rate increases, yes, we are filing and have filed and pursuing it quite actively with over 20 states. The 20 states represent 70% of our business, long-term care. And at this point in time what I would like to say is that we are feeling better about the progress we're making. I don't want to be explicit on which states we have had what approvals, but I can assure you that we have made good progress in having approvals.

I also believe that the environment is changing, particularly with the recent bankruptcy which was announced by Penn Treaty, which makes clearly the point to the regulators also, because the judges have been very clear about that, that one of the reasons the company went bankrupt is that regulators did not afford and did not allow rate increases that should have taken place. So you probably hear us speaking now clearly more positively about the outcome of the rate increases, which we're able to get through long-term care than you've heard us speaking for some time.

In terms of the variable annuity, I will give you a general comment and if you have further questions certainly Darryl can chip in, but I would say here we're seeing a number of things. First of all, we're seeing that margins are declining and margins are declining because of low interest rates, means that we are earning less margin than we did in the past. We're also seeing that with our efforts, as you remember, on our efforts to reduce our GMB book with our ALSO program, we're also seeing a margin compression because that business had higher margins than the margins we have right now.

And finally, we see that new business is effectively replacing older business at lower margins all as a result of lower interest rates. So in terms of guidance it is clear that in today's environment it is difficult to hold on, on the 70 basis points which we have guided you, but we're also operating now in a significantly different environment with interest rates much lower, with a big uncertainty about sales outlook because of the Department of Labor and the combination of that has led to a margin compression of where we are.

What we're doing is taking steps here. We can be very explicit. We have actually restructured significantly our wholesale organization and that means we have limited the number of wholesalers plus the people around that support them. We've given them bigger territories so that we can hold on, on our best wholesalers while having a less large number of wholesalers that are selling.

So we're here also adjusting our business and structure to the environment, which, because of the rates as they are today, combined with the uncertainty around DOL, is clearly making it more difficult to hold on, on the larger margins.

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**William Hawkins** - Keefe, Bruyette & Woods - Analyst

Thank you. I'll probably come back offline, but on the variable annuity comment, I mean I can see very clearly that the world has changed since January and therefore there are incremental headwinds, but to the extent of the 70 basis point margin was effectively an in-force figure, I'm surprised that that would lead to such an apparently material and quick change in the in-force figure. Anyway, I'll come back offline on that, but I'm just a little bit surprised.

**Alex Wynaendts** - *Aegon NV - CEO*

Yes, we'll come back offline, but please keep in mind what I just said. It's about a runoff of a part of the business at high margins, related to our efforts to release capital for GMIB and it's also effectively what we see, net deposits are lower than they were because our gross deposits are lower. That means we have more new business at lower margins.

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**William Hawkins** - *Keefe, Bruyette & Woods - Analyst*

Okay. Thank you guys.

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**Operator**

And our next question comes from Nadine van der Meulen of Morgan Stanley. Please go ahead.

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**Nadine van der Meulen** - *Morgan Stanley - Analyst*

Good morning. With regard to the US RBC ratio, the drop in the RBC ratio, can you maybe elaborate a little bit more on the drivers behind that, apart from the equity market, perhaps? Because I was under the impression that lower rates, given the sensitivities that you've given before, would actually be a positive impact on that ratio?

And maybe in light of US capital would you mind giving us an indication of where the surplus of the AA S&P requirement is in the US? Because a year ago you mentioned that that was EUR1 billion. You said that it was quite volatile. It dropped to I think around EUR600 million when we talked about it at the Investor Day. And last quarter no update was given, so I was wondering if you could give some details around that? Thank you very much.

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**Darryl Button** - *Aegon NV - CFO*

Yes, hi Nadine, it's Darryl. First of all, on your first question, The RBC ratio dropped primarily from the dividend that was paid from the US and so we upstreamed about \$500 million of dividend to the holding and that's the -- primarily the biggest drop.

I would point out that actually our sensitivity has now changed in the US. Rates are now at the point we used to talk about with rates would go down we'd have a short-term boost to the RBC ratio and vice versa. We're now down to the point where rates are so low that rates dropping and dropping from here or even where they are now, lower rates does not boost the ratio, because of cash flow testing concerns that we have. So there's no benefit in the quarter from dropping interest rates. I think actually we took a small provision for cash flow testing that'll be only -- it's an annual calculation so that will only be firmed up at the end of the year, but the biggest drop is the dividends.

On your second question -- actually we're not disclosing any longer the excess over S&P AA. We've moved over to only talking about the RBC ratios, and that really, primarily, I think as you know, we manage multiple different capital metrics in the US. But the RBC ratio has to flow through into the Group ratio and the Solvency II. They are correlated, obviously, so we're going to continue to discuss RBC ratio and that's also very consistent with what our US peers do as well. So sorry, I'm not going to give you that number.

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**Nadine van der Meulen** - *Morgan Stanley - Analyst*

All right. Thank you.

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**Operator**

And our next question comes from Mark Cathcart of Jefferies. Please go ahead.

**Mark Cathcart - Jefferies - Analyst**

Yes, hi Darryl. I've got a couple of questions. First one is I just wondered if you can talk about your assumption of GBP70 million cash from the UK. Have you assumed further margin pressure in the platform industry as a whole, given the current headwinds in the UK? So I wondered if you could talk about your assumptions on how you expect margins to progress within the UK platform market generally, because they seem to be quite negative at the moment.

Second, in relation to your interest rate sensitivity in the Dutch market, you had negligible interest rate sensitivity at the beginning of the year. This has exploded to, I think, largest in the entire sector. Was that mainly because you took off the hedge at the end of January?

Third question is you talked about no comment in relation to the modelling review Q3. I think you said that on the call just earlier. But previously you've always voiced confidence that you wouldn't have any more modelling mishaps. I wondered if you could comment on that. And as an aside, can you confirm that the cash at the holding is actually all funded by debt elsewhere within the Group? Thank you.

**Darryl Button - Aegon NV - CFO**

Okay, Mark, sorry, I was still jotting down the last -- I think I missed the last question. I'll come back to you on that.

In order -- the GBP70 million -- yes, our guidance on where we're coming out, we think in cash generation from the UK, that does reflect our view of continued margin compression in the UK. So that is -- we've made some estimates around that. We do see that pressure and we've built that into that estimate.

On the Dutch interest rate sensitivity, it is markedly higher than what we had before. I think it's a combination of, yes, largely we did change some of our hedging programs. We had -- when we were hedging on our full IFRS basis we had quite a bit of over-hedging in place, particularly as it relates to the owned funds in Solvency II.

There is a -- without going too long here and too much dilemma, there is an issue on -- a philosophical issue on whether or not you hedge the denominator in Solvency II. You can create or destroy economic value by protecting things that move around, like for instance longevity and credit risk have an interest rate element to it. If you hedge that you'll gain or lose on those hedges and while those underlying longevity and credit unwind that interest rate hedge won't unwind. So that is a philosophical issue we continue to struggle with in terms of do we protect capital or do we protect the economic value of the organization?

We did move the hedges towards Solvency II in first quarter. We backed away from that position somewhat in the second quarter, as we -- when we did that pre-Brexit. So we're somewhere positioned in between the two right now. What that means is we have losses on IFRS if rates fall, which is exactly what we have in our fair value items this quarter and we have owned funds or economic gains in Solvency II, which we also have this quarter.

This interest sensitivity really comes from the denominator impact in the SCR. That, combined with the fact that rates have now dropped to a new structural low level has also made us more exposed as well. So it's a combination of all of those things. Also just the more granular approach that we've had to the modelling as well. So I would say it's all of those factors and that's all built into the sensitivity that we're sharing with you today.

Your third question was on Q3 foresight. Yes, so -- (multiple speakers).



**Mark Cathcart** - *Jefferies - Analyst*

You've expressed confidence and I just wondered how confident you felt now, given what US peers have been saying?

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**Darryl Button** - *Aegon NV - CFO*

Yes, and I think you are specifically asking modelling versus assumption changes and I think it is important to separate those. So I continue to believe that we have the modelling issues behind us and I don't really see any further impact from models. In terms of assumption changes, yes, it's what I said before. It's still early in the process and we're working through those and I'm really not in a position to give any foresight into where I see the assumption changes going, definitely.

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**Mark Cathcart** - *Jefferies - Analyst*

Yes. And in relation to the UK I still struggle there because you were suggesting that Retiready was going to break even and then break even again and then break even. How aggressive have you been in terms of those platform assumptions? Because I think in reality platform is regarded as a loss leader in the UK life industry, not a key business.

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**Alex Wynaendts** - *Aegon NV - CEO*

Mark, maybe I like to add something to this whole debate. As you probably will very well know, this is a very changing environment and so we have embarked on a -- and I'd like to give you a broader answer because I think that would be of interest to also the broader group. The reality is that we are moving and have moved, quite aggressively from a traditional model of life insurance and pensions towards a platform model.

It's a very significant change. And in the meantime what we are seeing is that, as you could expect, that in the margins the platform business had been declining. On the other hand, it's not uniform because parts of our books in our platform have been upgraded from our old books, so all the customers that have been upgraded, effectively we have seen pretty limited margin compressions because we're able to upgrade customers from the old book on to the platform while we're providing them a better service capability that allowed us to justify to hold on the margins and we have seen limited margin erosion.

Where we see most of the lower margins of course is when you look at the business with advisors, and it brings us exactly to the point that it's all about scale. And this is a scale game and therefore, this acquisition of Cofunds -- and I would like to bring Cofunds in here -- brings us 750,000 new customers, brings us GBP77 billion of assets, as you can imagine and you can calculate very easily, at a pretty low margin. This is a much more effective way for us to attract new customers in an environment where it's all about scale.

This whole game is scale and what we're trying to do here is use and leverage the platform we have in the UK, which is a recognized state of the art platform, recognized by lawyers on the pension side, by advisors and also by the part of the business that I would say is non-advised, do it themselves, or orphan customers. And what we try to do is put -- use that to drive scale and therefore also to maintain our margins in this business.

Having said this, the biggest part of the margins we look -- we believe forward, are not only about record keeping. Because you're right, record keeping fees are going down. We see that very clearly in the US, for example, where in some parts of the business it's very marginal. It's all about providing a service, providing investment solutions and I've mentioned that in my introduction and also starting to be more active on the guidance area. And that is where we'll be able to earn better margins than what you would be earning if you would be only in an administrative record keeping kind of platform.

So it is a combination of quite a number of factors where you have declining margins and spread, as you rightfully point, on the record keeping part, which you offset by scale and by providing additional services.

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**Mark Cathcart** - *Jefferies - Analyst*

Did you at any stage consider letting someone else become a market leader in platform -- i.e. exiting the UK entirely? Or was it always your intention to maintain a position in the UK?

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**Alex Wynaendts** - *Aegon NV - CEO*

Look, we have a very successful platform, which was built with modern technology, which is very scalable. As you know, we had BlackRock's DC business, which was moved to our business, effectively BlackRock entrusting their customers to our platform. I think it's a clear sign of recognition of the platform. And we think that if we have such a capability and we are able to take advantage of what I think is a unique opportunity to in one go get a significant amount of assets on your platform, this is certainly something which is very interesting. And being the market leader in this market is very important, because I said to you, it's all about scale.

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**Mark Cathcart** - *Jefferies - Analyst*

And in relation to Dutch dividends, Darryl said wait and see in relation to the decision on UFR. If the UFR is minus 20 bps, minus 20 bps, minus 10 bps, over the next three years, in that situation could you let us know or tell us whether you believe, in that situation you'll be able to upstream dividends, or is it just a general question mark over Dutch dividend paying capability? It seemed too ambiguous how you expressed it.

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**Darryl Button** - *Aegon NV - CFO*

Well, I mean Mark, let me try to be more clear on that. So first of all, in relation to the issue of Dutch dividend in general, we're obviously feeling much better about the capital ratio of where we stand today. I did try to highlight that if you drop 50 basis points on the UFR curve, granted that would be spread over a three-year period, but that's 19 points off of our ratio, so that moves us from high end to low end, although you could obviously spread that out over the next three years.

I think you also have to consider that the ratio -- just the journey we've been on, so the ratio has moved around quite a bit lately, between the first quarter and the second quarter, so we do want to see that stabilize. That's not market volatility. As I mentioned before it was really just our more thorough application of the models and getting into the granular data. We still had some growing pains in getting through that.

So we need to see some stability to that ratio. We need to see where this UFR debate comes out, because it is material on the ratio. But if you factored all -- those are all the things that will go into our management decisions in terms of when and how much to upstream dividends out of the Dutch organization.

That being said, I'm fairly comfortable repeating what I said before. I do expect to take a dividend out this year, albeit somewhat lower than the [250] that we mentioned earlier.

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**Mark Cathcart** - *Jefferies - Analyst*

But at some stage you do expect to go back to a [225] dividend paying capability?

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**Darryl Button** - *Aegon NV - CFO*

Yes, very much so. I think that's the cash generation that I see coming out of the business. So we have to sort out where the ratio is coming out, where our sensitivities are, where we're comfortable in that. But yes [225] is what I would peg as the cash generating and ultimately the dividend capacity out of the Dutch organization.

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**Mark Cathcart** - *Jefferies - Analyst*

Okay, thanks Darryl. That was excellent. Thank you.

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**Operator**

Our next question comes from Nick Holmes of Societe Generale. Please go ahead

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**Nick Holmes** - *Societe Generale - Analyst*

Oh, hi there. Thank you very much. Three questions. First is just coming back on the mortality and long-term care losses in the US that have appeared in Q2, I just wondered if you could give us a little bit more color on those? And do you expect the rate increases you're filing to basically fix that problem?

Then secondly, just very quickly, just wondered what your thoughts on the DOL reforms are at the moment, what is your latest thinking there? And then third and finally, perhaps more of a difficult question, I wondered if you could comment on your thinking about the variable annuity policyholder behavior assumptions that you have at the moment. Clearly MetLife has thrown this issue into the open as an industry issue. And I just wondered, Darryl, whether you could give us some thoughts, going into Q3, as to whether you feel comfortable with your assumptions? Thank you.

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**Darryl Button** - *Aegon NV - CFO*

Hi Nick. I'm going to take the first and the third, if that's okay. Mortality and long-term care -- the mortality I would really put that in the line of just normal fluctuation. That's really not a very big number. We've seen -- we've changed our mortality assumptions, as you know, earlier and we've seen fluctuation around the mortality in line with this, pluses and minuses. So keep in mind, we are and have retained more life mortality risk in the US, as we're carrying less reinsurance than we used to a few years ago.

So I would just very much put that in line with normal fluctuation. And we've seen pluses and minuses around our assumptions.

On the long-term care, where we've had a couple of quarters now with a poorer performance, we are seeing termination rates in terms of people coming off claim, as is the cause for the higher claims -- it's deteriorated. And to specifically your question, yes, rate increases helps that issue and as we continue to make progress on the rate increases that provides a significant offset to that.

On the third question was on variable annuity policyholder behavior, you specifically referenced Met. We did update our policyholder behavior assumptions on the variable annuity last year, actually and we feel pretty good about our assumptions, so we've done a lot of what was -- what Met has done already, with one exception. They flipped the old GMIB product over to fair value accounting and that probably is a big source of the hit that they took.

We do not have our old GMIB product on fair value accounting. We still have it on the SOP 03-1 accounting, which does create that mismatch between the hedges and the accounting and that is the source of the \$60 million drag in fair value items every quarter that we flag. So that's probably the one main difference that we have. But I think a lot of the assumption changes we've already made those -- taken those and feel good about what we have.

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**Nick Holmes** - *Societe Generale - Analyst*

Thank you for that. That's very reassuring. Just quickly on that last point, would you keep the SOP 03-1 basis, going forward? Is -- you won't do what Met did?



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**Darryl Button** - *Aegon NV - CFO*

Yes, I can't -- yes, I can't comment on that. I have no plans in the near term to change that. I guess I could say that and I'm not going to commit to anything in the longer term.

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**Nick Holmes** - *Societe Generale - Analyst*

Okay, thank you.

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**Alex Wynaendts** - *Aegon NV - CEO*

So let me take the DOL question. Very briefly, because effectively, there's not very much more to report right now than a quarter ago. What we see here is that in most cases our consumers are not really aware of the changes. What we're seeing is distributors, they have been very busy looking what the impacts of the rule are and also trying to assess to what extent they will use exemptions, as you know, that's to be part of the whole debate, who's going to use what exemptions under this rule.

So we are engaging and starting to engage and communicate with our distributors to know where they are. But what I would like to say here is that we're making ourselves ready. We have already products that are suitable under the new DOL environment and we'll continue to make those products ready, and hopefully by the end of Q4 we should be in a pretty good position.

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**Nick Holmes** - *Societe Generale - Analyst*

And just very quickly, following up, Alex, your thoughts on the impact on sales going forward? Any --

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**Alex Wynaendts** - *Aegon NV - CEO*

Again, difficult to say, because I think in this environment of very low interest rates obviously the products have become less attractive because of the increased pricing on the guarantees. It's difficult to say where we have seen the overall market effectively coming down.

Now the question is to what extent is that reflected already in the market as it is today? Well, we probably expect a further decline in sales overall in the market. That's not necessarily meaning that for us we will see the same impact, because as you know it's also related to what part of the market's qualified and what part is not qualified.

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**Nick Holmes** - *Societe Generale - Analyst*

Right. Thank you very much.

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**Operator**

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

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**Bart Horsten** - *Kempen & Co - Analyst*

Yes, good morning. I have a few follow up questions on some of the topics already addressed. First of all, on the interest rate sensitivity in the US, obviously the decline -- further decline in interest rates has a negative impact. But an increase in the interest rates obviously, according to the

sensitivity table, has no impact, or at least no impact on your Solvency ratio. So I was wondering whether you could explain that mismatch between a downward and an upward change in interest rates? And what would be a potential impact if the Fed would decide to increase the short-term interest rates? Would that have any impact on your profitability or on your Solvency?

And my second question also relates to the restructuring plan, the five-part plan of the US. Could you give a bit more financial detail? Because as far as I can tell, you have not changed your cost savings target, so could you give some more financial color on these plans?

And my final question is a small one. On the net deposit growth in the US it was in the second quarter close to zero, where you had a gross inflow of \$10 billion, I think you briefly addressed some Mercer impacts. Could you highlight what the impact going forward will be, what you expect on that? Thank you.

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**Darryl Button** - *Aegon NV - CFO*

Oh, let me jump in on the first one, Bart, on the US interest sensitivity. So what you have to understand is there's two competing dynamics on the US interest rate sensitivity. The old dynamic is still there, where if rates fall we have gains on low rate hedges that come into cash and come into our statutory earnings in the US and that creates a positive. And if rates go up then we have a loss on those same hedges and that reduces our US statutory earnings.

So that sits there in the background, unchanged. The new dynamic is that if rates fall we are in a position where we're starting to post additional cash flow testing reserves, just because of the nature of that overriding cash flow testing mechanism.

So when you factor those two things in -- and they're asymmetric -- and when you factor those things and add them together you get this asymmetric net result that you're seeing in front of you.

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**Bart Horsten** - *Kempen & Co - Analyst*

Okay.

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**Darryl Button** - *Aegon NV - CFO*

I think on the -- did you want, Alex, on the financials for the --

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**Alex Wynaendts** - *Aegon NV - CEO*

Yes, for the five-part plan. I'd like to remind you, Bart, we have given ourselves and we shared it with the market in January on the US, a \$40 million target of expense savings for the US. We have already achieved \$60 million, so we are well ahead. What I will not do at this stage is give you more explicit numbers, but what it is all about is accelerating the base of our cost reductions. I've mentioned specifically a number of items. And in our December IR conference in New York we will provide you with more financial numbers.

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**Bart Horsten** - *Kempen & Co - Analyst*

Okay.

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**Alex Wynaendts** - Aegon NV - CEO

But I can assure you, we have a plan behind it but it's now too early to share this with the market because with these things you've got to do the sharing at first internally, discuss this with the people and at the locations that are involved, before doing that externally.

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**Bart Horsten** - Kempen & Co - Analyst

Okay.

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**Alex Wynaendts** - Aegon NV - CEO

And on Mercer, yes, the story is a simple one. When you take over a block of business from a provider with around \$80 billion of assets, it is an expected -- and by the way also priced in us -- that we would see some lumpiness in these deposits. Often, as you know with these plans, they get reviewed a number of times and let's say every five years and when there's an event, for example Mercer being acquired by Aegon is an event that sometimes triggers pension reviews and then you see -- it's very normal to see that you are effectively losing a number of these contracts. Many cases these customers were already prepared to make a change and then the takeover is a trigger event.

We do expect indeed this continues for the Mercer block. That is anticipated, probably to continue a bit until the end of this year.

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**Bart Horsten** - Kempen & Co - Analyst

Okay. Thank you. And maybe just on a set rate rise, would that impact your business immediately or is that a lagging effect?

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**Darryl Button** - Aegon NV - CFO

Oh yes, on the Fed. Sorry, I forgot that part of your question.

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**Bart Horsten** - Kempen & Co - Analyst

Oh, no problem.

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**Darryl Button** - Aegon NV - CFO

Yes, actually, the short rates really don't do much for our business anywhere. And so in terms of impact on earnings or on cash generation out of the US it's really the longer term rates that matter. So you have to then just cross over. Does the Fed increasing rates in the short term, is that something driven by whatever bullish nature that's driving that and does the market already pick that up? And what happens to the longer term rates is what really matters to us.

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**Bart Horsten** - Kempen & Co - Analyst

Okay. Thank you.

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**Operator**

And our next -- and our final question, comes from Steven Haywood of HSBC. Please go ahead.

**Steven Haywood** - HSBC - Analyst

Good morning guys. I think you've previously said about reviewing and disposing your runoff businesses that require interest rates to go up before you achieve any kind of attractive prices. Has this changed? Are prices going to be unattractive now and continue to be unattractive? And will you be able to sell these businesses or review these businesses, should I say, at the unattractive prices?

And then my second question's on your holding cash capital buffer. I just wanted to work through one of the equations, one of the calculations you've done. There's a EUR200 million share buy back in Q2. And then you've paid EUR0.13 per share dividend to around 2 billion shares. Now that's around EUR300 million cost. So I'm just trying to work out why you've only accounted for about EUR400 million negative in your holding company cash capital buffer for the dividend and the share buyback in the second quarter. Thank you.

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**Alex Wynaendts** - Aegon NV - CEO

Let me take the first question. Yes, we did say that for runoff businesses, which, as you know, we would like to dispose of because they're not adding much to our earnings. Well, there is a big amount of capital which is [threatened] there that we would be looking at rates of 2% to 2.5% on the US Treasury.

Now we are looking again at the different options we have and we believe that effectively we could be able to do a transaction that would be attractive for us from an IFRS and a capital position, at lower levels.

I'd like to remind you also here that there's a counterparty risk that we have to take into account because we are not selling a legal entity. We are effectively reinsuring to another entity. And therefore it's a combination of pricing, market conditions and the counterparty risk. It's more complex than purely a pricing.

And just on the holding expenses, which you need to take into account, is that the script has been bought back after the end of the second quarter and if you take that into account your equation should work well.

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**Steven Haywood** - HSBC - Analyst

Okay, so there's an additional bit to come out in the third quarter?

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**Alex Wynaendts** - Aegon NV - CEO

Yes, correct.

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**Steven Haywood** - HSBC - Analyst

Excellent. Thank you very much.

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**Alex Wynaendts** - Aegon NV - CEO

Right. I'd like to thank you all for participating on second quarter call and I wish you a great day. Thank you. Bye-bye.

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**Operator**

Thank you. That will conclude today's conference call. Thank you for your participation ladies and gentlemen, you may now disconnect.



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