

INTERVIEW

Prudence pays for Generali

Italian insurer focuses on buying 'what it understands,' and isn't keen on deals that are dilutive, CEO says



Giovanni Perissinotto, 56 years old, took the helm at Generali in 2001. The insurer has since bought or forged joint ventures with nearly 20 companies.

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ROME—The post-crisis world of low interest rates and looming capital reinforcement has wrought deep change on the financial-services industry, but Europe's insurers are well placed to prosper, said Giovanni Perissinotto, chief executive of Italy's Assicurazioni Generali SpA, the region's biggest life insurer.

Unlike banks, insurers aren't likely to face tax regimes designed to make them shoulder the risk of public bailouts, and the impending European Union Solvency II capital-adequacy requirements appear manageable, he said in an interview.

"I think we're in a comfortable situation as regards our capital ratios, given today's

Solvency II framework," Mr. Perissinotto said, talking in his Rome office, noting that the new regulations are still being debated and represent something of a moving target.

While rival insurers Allianz AG of Germany and France's AXA SA together raised almost €30 billion (\$41.08 billion) in fresh cash in the past two years, Generali raised only €2.6 billion, to fund the buyout of a mi-



nority stake in a domestic business unit.

Some investors worry the Italian company's traditional business model, decentralized across a slew of operating brands, is at risk if tougher capital rules squeeze margins and low yields on euro-zone debt push savers into new and less-profitable products such as unit-linked trusts. "But we think that if it's managed properly, traditional life insurance should be good," said Mr. [Perissinotto](#). "It's not dead, even under Solvency II."

Generali's performance so far this year suggests the company's strategic framework is sound. Operating profit at its life-insurance businesses—around 75% of the company's operating profit—rose 29% in the third quarter from the same period in 2009, accelerating from an already robust pace earlier in the year, according to third-quarter results released late last week.

At Allianz, operating profit in its life insurance business fell short of expectations, while AXA warned its own life-insurance margins would be hit on a full-year basis as a result of low interest rates.

Generali's Italian roots come in handy. Yields on Italian government bonds—which account for almost a quarter of the company's total €365 billion portfolio—have remained fairly high over the past two years while those on French and especially German debt have fallen dramatically. At the same time, Italian debt hasn't suffered a blowout like bonds from some of the smaller euro-zone countries.

The interest-rate differential between German bunds and Italian Buoni del Tesoro Poliennali is "good for us," Mr. [Perissinotto](#) noted.

"Life insurance is a spread business and we have a lot of ours in Italy, so higher rates benefit us," he said, adding that, all things being equal, an all-Italian life insurer would be doing "much better" than an all-German one in current markets.

At the 15-year maturity that is crucial for the long-term portfolios that insurers run, German bunds yield 2.78%, down sharply from 3.77% a year ago. Similar Italian BTPs now yield 4.71%, slightly higher than 4.32%

a year ago.

Shorter-term bonds, meanwhile, are yielding much less and are, as a result of the single currency, more homogenous. That means Italy has a steeper yield curve, which translates into wider profit margins on life-insurance products.

The relative stability of Italian bond yields also means the ability to match promises made in insurance policies is fairly stable. Moreover, historically higher Italian bond yields meant [Generali](#) was less tempted to search for yield on, for example, Greek debt. The insurer has practically no exposure to the euro-zone periphery, and what it directly tracks local liabilities.

"We've always been prudent. We try to buy treasuries of the countries where we have liabilities," Mr. [Perissinotto](#) said. "We kept this framework in place even after the euro was introduced." The euro-zone crisis has "changed the world," the chief executive acknowledged, but "we believe in the European Financial Stability Fund," the vehicle that will issue guaranteed debt to raise money for euro-zone member countries that can't borrow in the markets.

In the wake of the current crisis, European insurers dumped equities from their portfolios and ramped up their exposure to bonds to almost 90%, a level one analyst recently described as "scary" because of the consequent risk of capital losses should interest rates rise. But Generali's focus on what Mr. [Perissinotto](#) calls "buying what we understand" and matching geographic exposure to its operational commitments—in a sense ignoring the advent of the currency union—meant it didn't have to revamp its portfolio.

Instead, [Generali](#) has kept the share of equities in its holdings stable at 8%. It has raised its exposure to European corporate bonds by around two percentage points to 32%, a shift that has "gone well" and is likely to continue, especially for debt issued by utilities, pharmaceutical and energy companies, Mr. [Perissinotto](#) said. A further 38% of Generali's portfolio is government bonds.

One thing that isn't high up Generali's agenda is expansion through acquisitions.

Mr. **Perissinotto** said. "Of course our eyes are open," he added. "We just haven't found something that is not dilutive."

Generali has bought or forged joint ventures with nearly 20 companies since 2001, when Mr. **Perissinotto**, who is now 56 years old, took the helm—initially alongside co-CEO **Sergio Balbinot**, who is now general manager—thereby significantly expanding operations in emerging markets such as China, India and Eastern Europe.

But, Mr. **Perissinotto** noted, attractive insurance companies in those fast-growing regions are generally expensive now. "Shareholders are ultimately resistant to funding M&A expansion, given it would involve buying companies at higher multiples" than Western European companies such as **Generali**.

Raising equity to fund growth is also not in the cards. "We trade at a discount to embedded value. That makes it as if our sales force were thrown in for free," he said. "It's no time to do a capital hike."

One area where capital concerns are shifting the company's strategy is the bancassurance sector, in which insurers partner with commercial banks to gain access to the latter's retail distribution networks. "The preconditions of bancassurance deals have become too expensive," he said. The ventures end up requiring too much capital allocation, and the distributor ends up with the "upper hand in such deals."

Generali last year unwound Italy's biggest such joint venture, with **Intesa Sanpaolo** SpA, even though Mr. **Perissinotto** said he was "very satisfied" with the results. In the future "we prefer having several such deals to one big one," he said.

The future of bancassurance lies in a fee-based model, "commercial deals based on paying commissions," Mr. **Perissinotto** said, especially as banks will probably have to focus more on straight banking activity.