DWS Group GmbH & Co. KGaA

DWS Q3 2018 Investor & Analyst Conference Call

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Transcript

Speaker Key:

OF	Oliver Flade
NM	Nicolas Moreau
CP	Claire Peel

Oliver Flade

Good morning everybody from Frankfurt. This is Oliver from Investor Relations and I would like to welcome everybody to our third quarter 2018 earnings call. Please be reminded as always that the previous Deutsche Bank analyst call outlined the asset management segment results, which have a different parameter basis to the DWS results we are presenting today.

Also, as always, I am joined by Nicolas Moreau, our CEO, and Claire Peel, our CFO. Nicolas will start today with some opening remarks, and then Claire will take you through the presentation. For the Q&A afterwards I would ask everybody to limit yourself to the two most important questions so that we can give as many people a chance to participate in the Q&A session as possible.

I would also like to remind you that the presentation may contain forward looking statements which may not develop as we currently expect. I therefore ask you to take note of the disclaimer at the precautionary warning of the forward looking statements at the end of our materials. And now let me hand over to Nicolas.

Nicolas Moreau

Well, good morning everybody and welcome to this third quarter results conference call for DWS. I am very happy to present these results to you today. I would like to begin by wishing a very happy birthday to my CFO, Claire Peel, and I hope that she will be happy with the present we are making to her today.

So this quarter we've continued to make a very good progress in further developing our business. We have been effective in our cost management. We have been focused on our growth initiatives. And we have continued to develop our strategic alliances as reflected in our agreements with Tikehau on one side and Generali on the other side.

Profitability has increased through further cost reductions and stable revenues. Our management fee margin has remained in line with our medium term target, and our cost income ratio has fallen to 69.2%, driven by cost efficiencies which have delivered as expected, and in some areas even better than anticipated.

Flows have improved from Q2, but continue to be impacted primarily by the US tax reform as well as challenge in the European retail market which is at a very low level compared to last year. However we've seen sustained inflows in our European listed ETPs, and inflows in our real estate and recently launched infrastructure funds. This is very encouraging, given that both are areas we have previously identified for growth and that are emerging products.

Product innovation remains at the heart of DWS. This quarter we launched the first US money market fund to apply ESG criteria in the US, and we have seen good improvement in the performance of our flagship funds. Tied to that, we've made greater efforts to further strengthen our distribution capabilities.

We have formed co-operation agreements that will deepen our relationship with Generali. We will become one of their few preferred asset managers, and we will work with them to expand our distribution in France, Switzerland, Italy and Germany, especially with regard to unit linked solutions products. And we continue to enhance our collaboration with Deutsche Bank on the retail side as well as on the institutional side.

Our relationship with Tikehau Capital has also evolved following their participation in the IPO. We have formed a strategic alliance to identify possible distribution and product opportunities. Collaboration is already strong as we aim to jointly launch a special situation strategy in 2019. We have also seen further investment from anchor investor Nippon Life, and continue to build our relationship with Harvest Fund Management in China.

Finally, I'm pleased to announce that we have introduced a stock acquisition right plan for all our employees, enabling our people to share the future success and growth of DWS through equity linked rewards.

All in all, Q3 has been another productive quarter for DWS. The company is in good financial health, cost efficiencies are delivered as expected, and growth initiatives supported by our new product launches, strategic alliance and enhanced distribution will support our net flow targets in 2019 and beyond. I look forward to answering your questions, but in the meantime let me now hand over to Claire Peel, our CFO, who will take you through our Q3 results. Claire.

Claire Peel

Thank you and welcome to everyone today. I'll be presenting the key financial developments and recent activities for Q3 2018, starting with four key highlights. Adjusted profit before tax increased by 27 million to 177 million in Q3 18, up 18% compared to Q2 18 and up 27% from Q1 18. Increased management focus on cost efficiency initiatives and fund performance has delivered positive results over the quarter. Adjusted cost income ratio improved to 69.2%, down from

74.1%, demonstrating continued progress towards our target of below 65% in the medium term.

Quarterly net outflows of 2.7 billion were driven by US tax reform and institutional equity redemptions offsetting continued ETP inflows in Europe where we're ranked number two year to date with 14.5% market share, and inflows to our real estate and infrastructure funds. We also see improvement in our flagship fund flows over the quarter.

Moving on to the financial performance snapshot, starting at the top left AUM was up slightly to 692 billion, with favourable market performance offsetting negative impacts from net outflows. Moving to the top right, revenues were flat quarter on quarter at 574 million. And management fee margin of 30.5 basis points is down slightly compared to Q2 due to lower average fee margin in fixed income and alternatives.

On the bottom left, adjusted costs fell by 7% to 398 million, driven by an 11% decline in general and admin expenses. This helped improve the cost income ratio to 69.2%, down from 74.1% in the previous quarter. Adjusted profit before tax is 177 million, an increase of 18% from Q2, as a result of lower costs and stable revenues.

Let's recap on the financial performance over the three quarter of 2018. Profits have grown steadily in the year to date, despite a number of headwinds in 2018. Adjusted revenues are up 3% since Q1, supported by positive market performance and the appreciation of the US Dollar, and costs have fallen 5% over the same period, driven by reduced DB Group service charges and efficiency measures as we have recalibrated our platform.

Together these have resulted in a lower cost income ratio of 69%, down from 75% in Q1 and 74% in Q2. And adjusted profit before tax has increased significantly to 177 million, up 27% compared to Q1.

Moving to the market environment, markets were resilient during the summer months in Q3 18, largely driven by US equity performance. But investor sentiment remains negative following a succession of geopolitical events. This continues to impact retail investor activity in Europe, with notable declines in activity and passive industry flows compared to 2017. Rising interest rates also continue to negatively affect fixed income absolute returns.

Moving to AUM, AUM increased 1% to 692 billion in Q3 18. Six billion of assets were contributed by positive equity market performance, with an additional one billion from FX movements. Together, these more than compensated for quarterly outflows which I will now explain in more detail.

Net outflows of 2.7 billion in Q3 18 were driven by further outflows relating to US tax reform, institutional equity redemptions and weaker active retail demand in EMEA. Without the US tax reform headwind, our flows would have been positive over the quarter and our investment in Chinese fund manager Harvest contributes 2.3 billion of inflows in the quarter, not included in the total reported net flow of DWS.

Looking at the flows by asset class, alternative inflows increased to 0.6 billion, up from 0.1 billion in Q2. This is driven by real estate and recently launched infrastructure debt funds, attracting a combined 1.2 billion of inflows. Retail demand remains strong for our open end real estate fund family Grundbesitz, which saw its AUM exceed ten billion threshold in August. Together, these more than compensated for continued liquid real asset outflows over the quarter.

Passive flows were distorted by a single institutional investor redeeming 1.7 billion of short duration cash equivalent assets in response to US tax reform, adding to the 3.4 billion outflow already pulled in Q1. This redemption offset sustained growth in European listed ETPs as reflected by our number two ranking in the year to date period with 14.5% market share.

SQI, our systematic and quant investments, continued to register institutional inflows in Q3 following two mandate wins in Germany. However, these were offset by a re-tender of a specific mandate, half of which came this quarter and some to come in Q4. Fixed income flows improved significantly quarter over quarter, supported by stronger institutional sales in EMEA and APAC.

Insurance fixed income flows were positive in contrast to outflows earlier in the year, driven by new client inflows including investment from Nippon Life. US tax reform had a negative impact, a theme I'll revisit later on, and active equity outflows of 2.5 billion can be attributed to negative investor sentiment in retail and institutional markets, with investors making asset allocation changes in response to market uncertainty.

I will now focus on the drivers that have impacted DWS flows during 2018. Following strong inflows in 2017, we have seen a shift to outflows in 2018, largely driven by two key developments: The US tax reform impacting institutional flows, and negative investor sentiment coupled with flagship fund under performance affecting retail flows in EMEA.

Looking at the institutional channel first, we have reported 11 billion of global institutional outflows relating to US tax reform in the year to date, half of which was driven by one client. When US tax reform came into effect late last year, we anticipated an effect but it was difficult to assess the scale.

Nine months on it has continued to affect our low margin mandates, spanning fixed income, cash and cash equivalent passive funds, but with an average margin of around five basis points. Looking forward, we do expect further significant outflows, although we see some continued risk but with a much smaller exposure. In the insurance channel, we anticipate a low margin redemption in Q4 of a similar magnitude to the single outflow reported in Q1.

Moving on to retail, we have seen a negative shift in European retail fund flows in 2018, driven by a combination of negative investor sentiment and flagship fund under performance. Active funds have been the key driver of retail outflows in EMEA, a trend seen widely across the market as investor concerns grow over geopolitical instability, and retail industry flows in the region have slowed by more than 75% compared to last year, impacting passive as well as active flows.

This theme has played out across our retail funds, most prominently in active equity and active multi-asset, with fund performance also contributing. Passive inflows remain stable in the year to date, despite a wider slow down in the market. Flagship funds were challenged at the start of the year, leading to net outflows, which we now see improving. Let me now look deeper into these flagship funds.

Our active equity flagship top dividend and multi-asset flagship concept Kaldemorgen are showing signs of recovery after a difficult start to 2018. First with top dividend on the left. After a positive 2017, the fund started to experience negative relative performance in Q1 as its strategy to pick stocks with high dividends did not align with market growth in 2017 while tech names that distribute little or no dividends dominated index growth.

Weakened US Dollar was a further headwind, however we have since seen significant improvement. Cumulative performance turned positive in Q3 18 with the fund achieving a four star Morningstar rating, leading to notable decline in net outflows. Intensifying engagement with core distribution partners has also had a positive impact on fund flows.

Moving to concept Kaldemorgen, the fund reported outflows in Q1 as its conservative investment approach lagged peers in performance returns. It has since seen a positive turnaround, with performance moving into positive territory, and ahead of most of its peers year to date. This has helped the fund to attract small inflows in Q3, reversing outflows earlier in the year, a trend we see continuing so far in Q4 18.

Let me now move on to revenues. Adjusted revenues are flat this quarter at 574 million. Management fees continue to represent the majority of quarterly revenues, increasing by nine million compared to Q2. I will discuss the asset classes shortly. Performance and transaction fees were down eight million, primarily due to lower transaction fees in alternative this quarter. Other revenues declined by three million as a result of a negative change in fair value guarantees, while our Chinese investment, Harvest, contributed ten million in revenues and 32 million in the year to date.

Moving to the margin breakdown by asset class. Overall management fee margin at 30.5 basis points is down slightly from Q2 but in line with medium term guidance. Equity management fee and margins were up, including an effect from the transfer of an additional legal entity in Asia over the quarter. Multi asset margin increased to 40 basis points with stable revenue contribution quarter on quarter.

Fixed income margins down slightly as a result of retail outflows, offsetting institutional inflows, and cash management fees and margins remained in line with previous quarters despite inflows. Intra quarter average cash balances continue to be higher than the starting AUM balance. For passive, higher management fees are a result of continued AUM growth supported by ETP inflows. And in alternatives the margin was down slightly due to liquid real asset outflows offsetting incremental real estate and infrastructure revenues.

Moving on to costs, at the end of Q3 18, DWS reports 3422 FTE. This is a net increase of 126 FTE compared to Q2 and relates to the transfer of four EMEA coverage branches and a legal entity in Asia from DB Group to DWS. This reflects progress on transitional changes. Starting with comp and benefit costs, adjusted compensation and benefit costs of 178 million were down slightly quarter on quarter, with efficiencies compensating for transferred head count.

Looking at adjusted general and admin expenses, we saw the largest decline in DB Group charges. This represents the recalibration of group service costs as we embed internalised head count, finalise the separation from Deutsche Bank Group and right size services consumed. There is a small amount of year to date alignment, but the lower run rate is anticipated to continue.

We also saw a decline in DWS functions in DB entities following the transfer. And non-comp direct costs are slightly down with improvements from efficiencies offsetting higher regulatory and dyssynergy costs. Together, these drove down total adjusted general and admin costs by 11% quarter on quarter to 220 million, and total adjusted costs have fallen by 7% quarter on quarter, out performing our expectations and with continued investment in our growth initiatives.

Let me provide a refresh on our investment in Harvest Fund Management. As a reminder, DWS owns a 30% stake in Harvest Fund Management in China which contributes a steady income to DWS. Harvest has attracted four billion of inflows year to date, including 2.3 billion of inflows in Q3, and resulting in a total AUM of 109 billion. Harvest flows were not included in the total reported net flow of DWS, and DWS has recognised 32 million of accrued income from Harvest year to date 2018.

Moving on to specific fund launches, as Nicolas mentioned earlier today, product innovation remains at the heart of DWS and will be fundamental to supporting our growth initiatives. In Q3 18, we launched a number of funds across fixed income, ETP and multi asset. Fund launches include two ESG funds in the Americas, the ESG Liquidity Fund, the first money market fund of its kind to apply ESG criteria, and the MSCI EAFE ESG Leaders and ESG Equity ETP.

Other notable launches include our Deutsche Invest Asian IG Bonds and multi-asset fund to funds in EMEA, which have been launched with one of our distribution partners. We have a number of fund launches planned for Q4 2018, subject to demand assessments and approvals. This product pipeline spans alternatives, active and passive funds, with ESG and thematic equities remaining a key feature of our portfolio. I will now pass back to Nicolas for concluding comments.

Nicolas Moreau

Thank you, Claire. The third quarter has been very promising for DWS. We are on track to deliver on our cost income ratio target of below 65% in the medium term, driven by further cost efficiency efforts. We've seen the largest decline in DB Group charges, which have decreased faster than anticipated, and with opportunity for further improvement.

Profits have increased significantly, reflecting stable revenues and lower costs. The management fee margin remained in line with the medium term target, in spite of flow challenge, and our flagship funds are showing good signs of recovery. We have been building our product pipeline for Q2 18 to support our net new money growth target for 19 and beyond. That will be supplemented by our strategic alliances, our alliance agreement with Tikehau will open future fund opportunities and our co-operation agreement with Generali with enhanced distribution.

Continued collaboration with Harvest and Nippon Life will also further expand our international footprint. Our dividend payout target of 65% to 75% remains a high priority, and we remain highly committed to executing our strategy and delivering on our medium term targets as communicated. And now I will hand over to Oliver for Q&A. Thank you.

Oliver Flade: Yes, thank you very much Nicolas. Operator, we are ready for Q&A now, and again if I could remind everybody in the queue to limit themselves to two questions please.

Operator: Thank you. Ladies and gentlemen, at this time we will begin the question and answer session. Anyone who wishes to ask a question may press star followed by one on their touchtone telephone. To withdraw your question, you may press star followed by two. If you are using speaker equipment today, please lift the handset before making your selection. Anyone who has a question may press star followed by one at this time. One moment for the first question, please. First question comes from the line of Jacques-Henri Gaulard with Kepler Cheuvreux. Please go ahead.

Jacques-Henri Gaulard: Yes, good morning everyone. So two questions. The first one, you've lost quite a lot of people recently, particularly Tim Albrecht to Berenberg, and I was wondering if this would dent your budget for inflows and you would have to take into account some client losses as of next year. I'm not talking about the end of the year, because I understand he's staying quite a while.

The second question, I would like to come back on your partnership with Tikehau. You mentioned a special situation fund. I was under the impression that they were private debt specialists and I was wondering if that was included into the scope of partnership you have with them, so if you can elaborate that would be very helpful. Thank you very much.

Nicolas Moreau: So regarding Tim Albrecht's departure… So we have not lost a lot of portfolio managers. We've lost one portfolio manager in the past year, so we have a very high retention coming to PMs. He has a big bench behind him and the team have taken over the management of the funds. So we haven't lost assets and

	we don't anticipate to lose assets on the Deutsche equity strategies. German equity strategies. As today in fact clients put us on watch, but depending on the performance of the fund we won't see any change.
	Regarding Tikehau, the special situation fund is a debt special situation fund, so just to let you know that that's what it is. So looking at the underrated debt and trying to make value out of it. In fact we get prepared for an eventual turnaround of the market. We believe that with the increase in volatility we will see an increased number of special situations in the market.
Jacques-Henri Gaulard	Thank you very much.
Operator	Next question comes from the line of Arnaud Giblat with Exane. Please go ahead.
Arnaud Giblat	Yes, good morning. Two questions please. First on costs. In the split out of your cost base, the variable component of the compensation seems to be about 12% of the total cost base. I'm wondering how we should think about what is variable in your cost base in the event of a significant market downturn. How much more effort could we be looking at in terms of variable cost?
	And secondly on surplus capital. Could you provide us an update of where you're at? The Deutsche Bank Q3 report seems to indicate that the capital requirement for the asset management business is about 618 million. So I know it is different parameters. Any add [?] that you could provide there and where that leaves you in terms of surplus would be helpful. Thank you.
Claire Peel	Thank you for the question. So if I pick up first on the cost base and how much of the cost base is variable. We can see within the quarter of Q3 we very specifically had variable compensation costs of 50 million and of course there's an element of that which is deferral from prior year and there's an element which is accrual of cash in current year. So some of it within that is fixed, some of it is variable. I'd say about half and half.
	Otherwise, in the head count population the non-variable part of compensation costs, of course that's always a lever that we can leverage in upturn or downturn in a market environment and as much as we can't act fast we can always review how we want to manage the population from an FTE standpoint.
	If I look at general and admin expenses, we have a non-comp cost base within the quarter of 176 million and there's around a third of that which I would point to being related to transaction

costs, outsource charges, indices and so on, so an element of variability in that part as well.

On your question on surplus capital, I would point very specifically to the DWS perimeter in that regard, and our surplus capital remains stable and increasing with retained earnings.

Arnaud Giblat

Thank you. Could I have a quick follow up, specifically on the outlook for surplus capital. Because if I understand, your partnership with Tikehau will involve co-investing in funds and the level of investment Tikehau usually make in their own funds is quite elevated. Should we be expecting a big consumption of capital from this partnership?

Claire Peel

So it's correct that the investment of co-investment is something that we used to leverage our capital base and we have taken that into account in our growth projections in terms of doing more investments from a co-investment standpoint. But that's all taken into account in our guidelines, so we wouldn't see a significant change in the investment capability that we have from our surplus capital.

Arnaud Giblat

Thank you.

Operator

Next question comes from the line of Stuart Graham with Autonomous Research. Please go ahead.

Stuart Graham

Hi. Thank you for taking my questions. I had two, please. Firstly, how much of your AUM comes from Italy? I think you've got 173 billion of EMEA AUM, so how much of that is Italy? And then the second is you mentioned the stock appreciation plan. Could you maybe just give some details? How big is it? How does it work? What are the KPIs that need to be achieved in order to trigger gains? Thank you.

Nicolas Moreau

Okay, we've got 20 billion of AUM in Italy, both in retail and institutional. So that's out of nearly 700 billion. Regarding the stock appreciation rights, we've got two programmes. One for the top management, roughly 80 people in the company. One for the rest of the staff.

Let's maybe begin by the staff part which is a stock appreciation right that is provided. And that's an opportunity for all the team to participate in the future growth of the company. It has been effective on 15th of September 18, the OOR [? 00:29:27] date, and the participants will be able to participate in the increase of the share price over a certain period of time. The payments will be done via a cash settlement, and the award is tied to an average share price ring period within Q3.

And the number of units that have been allocated are tied to a percentage of the employee total comp reference. There is a four years exercise window and it's subject to a performance threshold which is limited, which is the fact that the year end 19 will be profitable.

Then we have the performance stock units that are for ATFGs [? 00:30:16], our managing directors and key executives, with an incentive to deliver on DWS strategy growth. That's performance shares unit, and the award has been linked at the ten day average in Q3 and the two criteria that are taken into account as performance are average net new assets between 3% and 5% between year 19 and year 20. And a cost income ratio below 65% in year 20. And then it's being transformed into stock using these two criteria, and there's a vesting period from that that is quite long. What else can I say on this one…

Stuart Graham: How big is it? Maybe if you could just say, how big is it?

Nicolas Moreau: We cannot comment on that. It's being included in our financials, so it's included in our cost income ratio. That's what I can say. Claire, you want to add anything on this?

Claire Peel: I would just add that the awards were announced during September, so there's a small amount of that taken into account in our comp and ben costs already in Q3 and, as Nicolas said, it's taken into account in the cost income ratio.

Stuart Graham: I guess my question is if I understand it correctly you've got to get a 3% to 5% net new money in 2019 and 2020 and you've got to have a cost income ratio of below 65% in 2020. I guess my question is, if that all works is it like a nice to have and people say: Okay, that's nice, it's like a 10% uplift in my comp. Or is it like: We get seriously rich if we achieve this?

Nicolas Moreau: No, that's a nice uptick in your compensation. It's not a buyout. It's a listed company, so that's not the case.

Stuart Graham: Okay. Thank you for taking my questions.

Operator: Next question comes from the line of Mike Werner with UBS. Please go ahead.

Mike Werner: Thank you. Two questions from me. I just wanted to know, as we saw a significant improvement in terms of the expense control in Q3, I was just wondering if there was anything seasonal in there? And outside of potentially variable comp if there's going to be a potential uptick in any of the expense categories as we go into the year end with Q4? And then second, with regards to the 3% to 5% net flow target, are there any macro or market backdrops that you are assuming? Or is this an all-weather target that you're aiming for? Thank you.

Claire Peel

Thank you. So on your questions about costs and seasonality specifically, we did indeed see a decline in our cost run rates in Q3 and we do consider that to be sustainable. There was a small amount of year to date adjustment in the figure, in the region of five million, so not material.

And of course there's always a little bit of quarterly fluctuation as you go through the year, so Q4 in particular we see the finalisation of the compensation awards, but not something that I would expect to significantly distort the run rate that we see going forward. So we're very satisfied with the cost decline that we see in Q3, and in fact consider that to be an acceleration of the efficiencies that we expect to achieve and take us towards our cost income ratio.

On your question of the net flow target of 3% to 5% and is it an all-weather target. Certainly it's a target that we're very committed to in 2019 and beyond, and we have a number of levers that we see supporting us in the achievement of that. If I first come back to the point of US tax reform which we've seen in 2018, that's contributed 11 billion of outflows this year. We don't see that as a dynamic that should continue certainly with that magnitude going into 2019.

And we start to see turnaround in fund performance, we see fund launches, collaboration efforts with distribution partners, with Tikehau, with Nippon Life, all of which is giving us confidence in our flow target going forward. We've certainly seen some market volatility in the early stages of Q4 and, yes, there is a sensitivity to the revenue line to some degree, but not something that we anticipate affecting the go forward net flow target.

Mike Werner

Thank you very much.

Operator

Next question comes from the line of Hubert Lam with Bank of America Merrill Lynch. Please go ahead.

Hubert Lam

Hi, good morning. Just a couple of questions. Firstly your equity margin went up quarter on quarter. I was wondering if you could try and explain the reason behind that and where you expect this to go going forward. Second question is on M&A. I'm just wondering if this is still something you would like to pursue, and what type of deals you're looking for and what do you think about the market as it looks today around M&A? Thank you.

Claire Peel

Thank you for your questions. Just first of all commenting on the equity margin. We seen an average management fee margin of 77 basis points in Q3, that's up from 75 in the prior quarter. That's partly attributed to the insourcing of another legal entity that's come into the DWS perimeter in Asia, so that has supported that to some degree. Also we saw positive movements in the markets within the quarter, so those are two factors that I would point to that mitigate the year to date impact that we've seen from the flow environment.

Nicolas Moreau

On M&A we are looking actively at companies that could complement our offer. I think market corrections in the past weeks have been quite encouraging as the price of the assets are going down while our cash is there. So patience is good. We are looking for the right opportunities and I think we should not change our guidance compared to where we were in our various presentations before.

We look at bolt-on, we look at things that could complement our capabilities, and we will be very cautious in terms of EPS accretion and ROE, but also on execution risk linked to culture of the people that we will integrate in our platform.

Hubert Lam

Sorry, just on that, in terms of complementing your offer. I was just wondering, any particular areas that you think you're currently lacking that you'd like to add on?

Nicolas Moreau

Yes, we are looking at quant, we are looking at solutions on the institutional markets, we are looking at various areas. We are looking also at the loan market even if platforms are today quite expensive. So we have various opportunities that we are looking at.

Hubert Lam

Great, thank you.

Operator

Next question comes from the line of Jean Sassus with Oddo BHF. Please go ahead.

Jean Sassus

Yes, two questions. First on the Deutsche Bank cost. What kind of trend should we expect from now? Should it go down further and at which pace? Point number one. And point number two, just to double check my figures. Ex US, the cost income of DWS should be probably already close to target of 65% or maybe lower. Is it correct?

Claire Peel

Hi, thanks for the questions. First commenting on the DB Group charges. You can see that there's been a sharp decline in the charges over the quarters that we've presented. 45 million and 31 million in Q3. The third quarter included a small amount of true up for the year, around five million, so that would adjust it to around 36 million, and we see that to be a good guide going forward, albeit there will be small amounts of fluctuation across quarters as is normal, but that's a good guide of what we would expect going forward.

We don't disclose our regional cost base, but it's correct that the US of course has a higher cost income ratio given a combination of the cost environment in the US and also the more heavily based institutional and fixed income and insurance basis of the AUM within the region.

Jean Sassus

Thank you.

Operator

Next question comes from the line of Anil Sharma with Morgan Stanley. Please go ahead.

Anil Sharma

Morning. Just two questions please. Just to quickly go back on the costs, just to make sure I've understood. If we compare what you were saying, Claire, with slide 20 it sounds like you've accelerated some of the costs saved, but can you just give us a feel as to where we are versus this expected timing column on both the tailwinds and also the headwinds? So have you deferred some investments which will either come in Q4 or they'll come next year. So that would be helpful.

And then just in terms of retail assets and flows, you gave some pretty helpful colour on some of the funds there and how they might be turning around, but could we get a little bit more detail around some of the dynamics? So for example what are the flows like in your captive retail channels such as your third party distribution and if there's any material or interesting significant changes going on there. Thank you.

Claire Peel

Thank you. So let me come back to costs, and it's indeed useful actually to recap on page 20 where we gave some guidelines on the cost tailwinds and headwinds, and we will cover this more specifically in the full year.

But to give you a guide of where we stand at the moment, on the cost efficiency initiatives where we had expected guidance of 20% to 30% to be achieved in 2018 of the 125 to 150 million gross savings, we're very much on track to achieve that at the upper end of the range through our ability to accelerate some of the cost savings in that area. So we're very satisfied with our progress there.

Likewise on the DB Group service charges, we had targeted a cost reduction compared to the amount in 2017 and we have over achieved in that cost saving in 2018 and have some more opportunity as we continue to recalibrate the platform going forwards. So cost tailwinds very much on track and I would say slightly accelerated.

On the cost headwinds, MiFID II costs, the 40 million is exactly in line. The dyssynergies have come in slightly higher than we had anticipated, but have been compensated for by cost efficiencies. And we have continued to invest in our growth initiatives as guided, albeit a small amount of that slightly lower, more driven by variable costs around transactional costs, but otherwise the investment that we've made into head count into our distribution platform and investment platform is very much on track. So hopefully that gives you a good guide of why we see our cost income ratio declining to 69% in the third quarter.

Anil Sharma — That's helpful, thank you.

Nicolas Moreau — Let me comment on the distribution. So first, we don't have any captive channels. We are preferred providers for DB. But I would say that the relationship is quite strong. We have had two new funds that were added on their preferred buy list in Q3, DWS Deutschland and DWS Top Europe. We have also continued with the ESG push with various mandates that were put forward.

In Italy and Spain also with the bank we are launching a new fixed maturity fund in Q4. And besides the development with DB Distribution, with our partner DVAG we have launched two funds called Champions Select on the focus for their unit linked business. It is focused product for the unit linked business and we should expect strong flows coming in these two funds.

Anil Sharma — Okay, that's helpful. Thank you.

Operator — Ladies and gentlemen as a reminder if you'd like to ask a question, please press star followed by one at this time. the next question comes from the line of Mohammed Mortuvela [? 00:42:58] with MainFirst Bank. Please go ahead.

Mohammed Mortuvela — Yes. Hi, good morning. Thanks for taking my question. I just have one. Could you give us an indication of the targeted size of funds for the launches and pipeline that you have on page 13 of your presentation?

Claire Peel — Hi, thank you for the question. First of all, maybe if I note your question on the size of the potential inflows. I would also just add on the fee margin we have a wide range which very much supports our average guidance of greater than 30 basis points across the funds that we have listed, from more equity funds at the higher end, alternative funds higher end and some of our ETFs at the lower end.

The target size on the alternative funds is quite specific. On the infrastructure side we would target [inaudible 00:43:55] billion, on some of the private equity solutions around half a billion. On some of the others, obviously we can't predict exactly but we see them all being strongly thematically targeted and identified to enable us to target some good flows to support the 3% to 5% going into 2019.

Mohammed Mortuvela: Okay, thank you.

Operator: The next question comes from the line of Christoph Blieffert with Commerzbank. Please go ahead.

Christoph Blieffert: Yes, good morning, it's Christoph Blieffert, Commerzbank. I would like to come back to the departure of Tim Albrecht. What is the amount of assets Tim had under management? And what is the split of these assets, retail versus institutional? Thanks.

Nicolas Moreau: So we are looking at the assets, but I think we are talking about… My memory is 13 billion. Yes. I think it's mostly 13 billion of assets under management. It's mostly all the German strategy funds. DWS Deutschland, DWS Investa and Deutsche Invest German Equity, DWS Aktien Strategie Deutschland. So that is mostly retail funds, owned into either unit linked products in Germany or retail products in Germany.

On top of it, we have some institutional clients in Latin America in these funds, but I would say so far we see a lot of stability, given that the successors Christoph Ohme and Hansjoerg Pack have worked with Tim for many years and they know both the portfolio, the funds, and they are very senior, experienced, and I have got full trust in them to take this job very well.

Christoph Blieffert: Excellent, thanks a lot.

Operator: There are no further questions at this time. I would like to hand back to Oliver Flade for closing comments.

Oliver Flade: Yes, thank you very much to everyone for dialling in today, and for any follow up questions please feel free to contact the IR team, otherwise we wish you a very good day.