Y 2019 Earnings Call

Company Participants

- Lars Thykier, Chief Financial Officer & Member of the Executive Board
- Peter Hermann, Chief Executive Officer & Member of Executive Board

Other Participants

- Derald Goh
- Jakob Brink
- Mads Thinggaard
- Martin Gregers Birk
- Per Gronborg
- Youdish Chicooree

Presentation

Peter Hermann {BIO 20507411 <GO>}

Good afternoon, everybody, and good morning to the USA. Thank you for joining us in this conference call. With me is Lars Thykier, the CFO; and Steffen Heegaard, Group Communications and IR Director. We are holding this conference because earlier today, we published the annual results for 2019. And before we start with the questions, we will just take a minute to give a brief explanation on unexpired risks as mentioned in the report and also the result on illness & accident, we think that will benefit the process. So I will give the word to Lars, and he will explain. And afterwards, we will take questions. So Lars, will you start?

Lars Thykier {BIO 16427122 <GO>}

Thank you very much. If I could draw your attention to Slide number 4, which shows schematic handling of the unexpired risk of future losses that is in this quarter results. I think it is a wonderful invention by the International Accounting Standards Board. That should make things easier for you to understand. Try to imagine the company that was established long time ago. The premium -- this is an insurance company of course, this insurance company has a premium of 100 every year, and it has claims of 105 every year. Sometimes in the past, the CFO has put aside DKK 5 million to cover unexpired risk or future losses.

Each and every year the company receives 100 in premiums and it pays out 105 in claims meaning, that the technical result will be minus 5 and the claims ratio 105. This goes for the first year, I have it on the table here. That is time plus one. Claims ratio of 105, then time plus two, claims ratio 105. And if we look at time plus three, again, we will receive

100 in premiums from the customers and we will pay out 105 in claims. But the CFO has realized that next year, the claims ratio will be worse claims will increase. And then he must put aside the reserve for expected future losses. In this case, I've used 15 as expected future losses. And this means that 15 of the premium is reserved or moved to reserve from for future losses. And the premium is down to 85, while the claims stay at 105.

The technical result in time plus three is minus 20 and the claims ratio is 124. The premium growth will be staggering minus 15%. And still the cash flows are exactly the same as the year before 100 in 105 out. In time plus four, the claims will be 120. The technical result will be 20 -- or minus 20 as it should be. The claims ratio will be 120, as you would expect, but there will be a huge growth of 18%, even though the paid premiums are the same every year and so are the claims.

So when there is a change in expected claims and you have a product where -- which is having combined ratio above 100, then this will range moves in the key figures, as you can see here. T plus three that is like Topdanmark in 2019. Our premiums are lower than they should be. Next year, they will be higher than they should be, and our claims ratio is worse than to be this year, and while it will be normal next year.

If we look at Slide 7, I suppose?

Peter Hermann {BIO 20507411 <GO>}

Yes.

Lars Thykier {BIO 16427122 <GO>}

You can see, how the actual figures are in Topdanmark in '19. Last year, we had DKK39 million in surplus in illness and accident. But 150 of these 39 million were run-off gains, meaning that before run-off we had a loss of minus DKK 111 million on illness and accident. We have claims that are DKK64 million higher than we had last year. And then we have to make this artificial reserve for future loss of DKK 40 million. So premiums are reduced by DKK 40 million. So DKK64 million more in claims and DKK40 million debt in premiums. And then there are some changes in expenses and premiums and so on. And that means that the total difference between '18 and '19 is actually DKK 183 million. You may ask what happens next year. But as you could see from the model I showed you, we will have a pretty huge premium increase. On the other hand the claims ratio will be right. So that has -- it has had quite an impact on this account. And that's why we try to explain it. It's not that I am very keen on explaining separate products, but now I've done it this time. I hope you can use it for something.

Peter Hermann {BIO 20507411 <GO>}

Yes. We hope that helps a little on the questions coming. So we're now ready to answer your questions. So operator, please ask them one at a time. And operator, can we have the first question, please?

Questions And Answers

Operator

(Question And Answer)

Thank you. (Operator Instructions) Our first question comes from the line of Jakob Brink form Nordea. Please go ahead.

Q - Jakob Brink {BIO 20303720 <GO>}

Thank you very much. Three questions, please. The first one on page -- what you just discussed last, sorry for that. But the runoff gains or the decline in runoffs from -- on Page 7 in the illness and accident result. Could you maybe just give us a bit more details on why it's down so much this year? That was the first question.

A - Peter Hermann {BIO 20507411 <GO>}

Yes. Actually, we make provisions for each and every claims here. But at some point of time, we were a bit concerned about the development in illness and accident. So we chose to keep one -- or not to release one claims here is runoff while we, in '18, had two claims here that were ready. We have only one claim here in '19.

Q - Jakob Brink {BIO 20303720 <GO>}

So just to understand when -- if you do this, bridge on Page 7 into 2019, everything else equal, it should be -- the runoff of minus 96 would be zero?

A - Peter Hermann {BIO 20507411 <GO>}

No, not necessarily. We do our best to put aside reserves in the right size. And if we do it exactly the same way and the risk doesn't change, in that case it'll be zero.

Q - Jakob Brink {BIO 20303720 <GO>}

Okay. And just, I guess a follow-up on illness and accident is, we've talked about this before, but is there any willingness in the industry to get this product repriced to get a better balance?

A - Peter Hermann {BIO 20507411 <GO>}

Yes. There is a willingness, but it is as if the cost also it, so to speak, doesn't work very well. We hear Danica, they want to increase prices. We have PFA, they want to increase prices and you hear Topdenmark, we want to increase prices. We need to increase prices. And actually, I think that if we don't do it, we'll probably hear from the regulator.

It is our definite intention to be -- to look very keenly on pricing in accident in 2020, and we have already put some initiatives to work. So we think that it should be possible to keep the snowball, abase, so to speak.

A - Lars Thykier {BIO 16427122 <GO>}

Well, you can see an indication of this, we are indicating a growth in regular premiums in life for 2020 of zero -- around 0% after a growth of more than 14% in 2019. And this is an indicator of that we are executing steps in order to produce better results on illness and accident.

Q - Jakob Brink {BIO 20303720 <GO>}

You said before last, and I don't know if that was intentionally. But I think you said before that if -- it sounded like this mechanics in your Page 6 only worked, if it was a deterioration of the profitability. So what if it's exactly an improvement, if you get through the prices? Will the mechanics work differently then or the opposite way or...

A - Lars Thykier {BIO 16427122 <GO>}

It will reverse. So if we don't break down the combined ratio, that will be really....

A - Peter Hermann {BIO 20507411 <GO>}

It works the same way to a typical amount.

Q - Jakob Brink {BIO 20303720 <GO>}

Okay. Great. And then final question on the -- I have read what you write about the life insurance guidance, but it's a pretty big drop in the guidance compared to what you had a year ago. So maybe a few more words, if possible, would be nice. Thank you.

A - Lars Thykier {BIO 16427122 <GO>}

Yes. In the first place compared to '19, we expect a much, much lower return on shareholder funds. We had a very good investment result in '19, and until the imvestment result in '20 will -- it is very unlikely that it is being just as good. But I have had...

Q - Jakob Brink {BIO 20303720 <GO>}

I meant also just from the initially one year ago, I think that was DKK230 million.

A - Lars Thykier {BIO 16427122 <GO>}

Yes. So there are some differences. I'm just on my way. We -- in life, we use the samples for setting. That is an industry wide or in general accepted asset or assumptions about asset returns by everybody in the industry. We have to use this to apply with a codex And that has been changed before Q4. So that has brought down the expected returns on all asset classes. Expected income on mortgage bonds or government bonds has been brought down from 1 percentage point a year to 0.3 percentage points. Property has been brought down from, I think from 6.1% to 5.6%. Shares down to 5.5% and it was on. So we simply have lower assumptions about what the income is going to be. We are talking about a decrease of around DKK45 million just due to these assumptions. Then we have -- yes, that's by far the most important part. But besides this, we have an expectation that our new IT system would work from 1st of April. Unfortunately, we have had to make a lot of manual handling of cases that the system should have been able to handle. And, this means that we are spending more money on making the system work, and we're spending more money on the employees that we expected to do last time. So the expense result we're looking into -- in '20 will not be good.

A - Peter Hermann {BIO 20507411 <GO>}

And then for 2021, we think actually this will turn, because both the expectation to the system, and also that we can look into efficiency gains on a later stage, and that we think that it'll be better in 2021 seeing on the cost side.

Q - Jakob Brink {BIO 20303720 <GO>}

So what level are we roughly looking at in '20 and '21?

A - Lars Thykier {BIO 16427122 <GO>}

We don't guide for '21.

Q - Jakob Brink {BIO 20303720 <GO>}

Okay. All right. Thanks a lot.

A - Lars Thykier {BIO 16427122 <GO>}

You're welcome.

Operator

And the next question comes from the line of Per Grnborg from SEB. Please go ahead.

Q - Per Gronborg {BIO 15910340 <GO>}

Yes. Good afternoon. I will continue where Jacob ended. The sales and admin result minus DKK22 million in '19, plus DKK25 million additional loss in the next year, plus DKK17 million in one-off disappearing. This implies that sales happening will be in the magnitude of the mid 60s. Is that correctly understood?

A - Peter Hermann {BIO 20507411 <GO>}

Cost side, you mean, what was the question, sorry...

A - Lars Thykier {BIO 16427122 <GO>}

Could you repeat?

Q - Per Gronborg {BIO 15910340 <GO>}

Sales and admin results in lift was minus DKK22 million in '19, you're guiding for DKK25 million extra cost, and you're guiding for DKK17 million one-off positive disappearing. This must imply that sales and admin mix must be in the mid-60s, right?

A - Lars Thykier {BIO 16427122 <GO>}

Right.

A - Peter Hermann {BIO 20507411 <GO>}

Yes. That's correct.

Q - Per Gronborg {BIO 15910340 <GO>}

And there are no comments on, what the benefits will be for the new system? Will this ever go to sale or will this consistently be a significant drain on profit?

A - Lars Thykier {BIO 16427122 <GO>}

No, that is not the expectation. I think I have warned you again and again that in connection with the implementation of the new system, we will probably have a kind of trough in the income in life because the expenses are so big. It is expected that the life system will improve efficiency substantially when it is (inaudible).

Q - Per Gronborg {BIO 15910340 <GO>}

Okay.

A - Lars Thykier {BIO 16427122 <GO>}

Let me add, far better customer service and lower admin costs.

Q - Per Gronborg {BIO 15910340 <GO>}

But this should imply that over time we should expect sales and admin to go towards zero. Is that a fair assumption?

A - Lars Thykier {BIO 16427122 <GO>}

I will be sorry if we couldn't, over time get it positive.

Q - Per Gronborg {BIO 15910340 <GO>}

Okay. Perfect. Then on the return on the investments belonging to the equity, you guide for DKK130 million lower than it was last year. That must imply that we are somewhere in the mid 50s. What is the equity base that you multiply the return that you -- despite that you get from the association's assumptions? What size of...

A - Lars Thykier {BIO 16427122 <GO>}

2 point something, two point something.

Q - Per Gronborg {BIO 15910340 <GO>}

2-point-something billion?

A - Lars Thykier {BIO 16427122 <GO>}

Yes.

A - Peter Hermann {BIO 20507411 <GO>}

Okay. Perfect. Then one more on life. You addressed that -- you hope that you'll be able to price up waste products. The natural question is, to what extent have you -- are you locked into multi-year pricing with the contracts you have sold to brokers?

A - Lars Thykier {BIO 16427122 <GO>}

That was -- when you -- he's running -- right on. This means that it will be difficult and it'll take time to make the impediments that we want to make. Of course, we have the possibility to -- even though we have a contract that is multi-year, we can cancel it, but it'll be unusual. So that will probably not happen. Any comment, Peter?

A - Peter Hermann {BIO 20507411 <GO>}

I think it's fair to say that, yes, it is -- you point at something that is a problem but it'll also take into consideration that we -- our key segment is actually the small and medium-sized businesses. So we don't have the same troubles as maybe some of our competitors in terms of health care giving long contracts. So a bigger part of our portfolio, do not have these kind of year-long contracts. But we, of course, also have this kind of -- in our portfolio.

Q - Per Gronborg {BIO 15910340 <GO>}

One should expect, if you go to the brokers center, you try to charge materially higher risk pricing. That must impact other part of the pricing, meaning the asset management fee. One must assume that, that must be coming down. When I look at your asset management company, we don't really see any trend in the income there, despite volumes are materially up. Can you help us decompose, what's happening to the asset management fee? I assume it's performance fees that is offsetting the underlying organic growth.

A - Lars Thykier {BIO 16427122 <GO>}

In the first place, I would like to stress that on the performance -- on asset management fees, we are the cheapest company in the market. And it'll remain so. We don't see any specific reason to reduce expenses or asset management fees further.

The asset management company lives from money that is created from other places in group. And the asset management company has to pay for this. You could regard itas a marketing contribution or whatever. But the asset management company has to pay life to get access to the money that life generates.

A - Peter Hermann {BIO 20507411 <GO>}

That is part of the cost result in life.

Q - Per Gronborg {BIO 15910340 <GO>}

Okay. Okay. So basically, we should not expect asset management company's profit to grow in line with the assets generated in the life company?

A - Lars Thykier {BIO 16427122 <GO>}

There will be some kind of distribution. The asset management company will probably increase its bottom line as time goes by, but a major part of the gain will be seen in the sales and expenses in life.

Q - Per Gronborg {BIO 15910340 <GO>}

Okay, that's -- okay. Perfectly. One final question. This unexpired risk we discussed on Page 6, 7, what were -- this impact you had on 2019, how big of that impact was into the fourth quarter?

A - Lars Thykier {BIO 16427122 <GO>}

The fourth quarter...

Q - Per Gronborg {BIO 15910340 <GO>}

Was that -- was anything of this hitting the fourth quarter? Is this primarily explaining some top-line issues going into next year?

A - Lars Thykier {BIO 16427122 <GO>}

No. Actually, that complicates things further on. If you remember the discussions we had last year.

Q - Per Gronborg {BIO 15910340 <GO>}

Yes. I remember those, yes.

A - Lars Thykier {BIO 16427122 <GO>}

There was a distribution of this unexpired risk over the year, which makes things absolutely impossible to understand. And this means that the premiums we had in Q4 last year was very low. So actually, there's positive impact on premiums of around two percentage points in Q4.

Q - Per Gronborg {BIO 15910340 <GO>}

Okay.

A - Lars Thykier {BIO 16427122 <GO>}

While there was a negative impact on claims of some -- around the same size.

A - Peter Hermann {BIO 20507411 <GO>}

So I think, the 2 percentage points in premiums is in the report. It is stated that we have a growth of 4.4 before taking care of these changes in unexpired risk.

Q - Per Gronborg {BIO 15910340 <GO>}

So the...

A - Lars Thykier {BIO 16427122 <GO>}

So sorry, it is fixed 4.4. But if we clean it for changes in unexpired risk, it goes down to 2.4.

Q - Per Gronborg {BIO 15910340 <GO>}

That's 2.4. And profit would have basically been 2 percentage points on combined ratio better in Q4 if you hadn't had this effect?

A - Lars Thykier {BIO 16427122 <GO>}

No.

Q - Per Gronborg {BIO 15910340 <GO>}

Okay. That was not what you said.

A - Lars Thykier {BIO 16427122 <GO>}

No, no. There are two effects. There's a pretty negative effect from the claims where we have increased our expected losses and has a positive effect for unexpired risk, which is lower than it -- or the transfer from -- to unexpired risk is lower than it were last year.

Q - Per Gronborg {BIO 15910340 <GO>}

If I -- If we look at Q4 isolated to 2019, this has -- this effect has -- there have been no effect from the expired risk hitting the profit. Of course, you have improved your profit year-over-year due to this unexpired risk thing. But it has no impact specifically on Q4 this year?

A - Lars Thykier {BIO 16427122 <GO>}

Oh, yes. That's around DKK40 million in extra premiums in Q4 from this change in future losses.

Q - Per Gronborg {BIO 15910340 <GO>}

Yes, but you, have not had -- you have DKK40 million that's premiums, that is hit in Q4, and we talked about hit earnings in Q4. Is that correc?

A - Lars Thykier {BIO 16427122 <GO>}

Compared to '18, they'll hit premiums and thereby, the claims ratio will be better and the technical result will be better. The top line is DKK40 million higher.

Q - Per Gronborg {BIO 15910340 <GO>}

Okay. Thank you. I got it. Thank you.

A - Lars Thykier {BIO 16427122 <GO>}

Okay. Great.

Operator

(Operator Instructions). And the next question comes from the line of Martin Gregers Birk from Carnegie. Please go ahead.

Q - Martin Gregers Birk {BIO 19920552 <GO>}

Hey, thank you so much. A question here on premium growth going into next year. Breaking it out on the quarter. I could imagine that the Nordea deal is going to be pretty back-end loaded. Is that correct? So we should expect two quarters of sort of slow growth and then growth sort of to pick up towards the end of the year?

A - Lars Thykier {BIO 16427122 <GO>}

Some of it -- for example, we have some indexation starting at the beginning of the year, that starts with some kind of growth in the beginning of the year, but that's true. Around the year, it actually is picking up fine. We have a good start. So we've seen a lot of leads. So we have seen good progress on that, but it's true that it will -- the Nordea deal, of course will be higher in the last part of the year. But just to say, the growth in the beginning of the year will also be affected by indexation.

A - Peter Hermann {BIO 20507411 <GO>}

Until now, and that's the first month, we have had a lot of returns, but there hasn't been policies yet.

Q - Martin Gregers Birk {BIO 19920552 <GO>}

Okay. All right. Thank you.

A - Peter Hermann {BIO 20507411 <GO>}

Welcome.

Operator

And the next question comes from the line of Derald Goh from Citigroup. Please go ahead.

Q - Derald Goh {BIO 20775137 <GO>}

Hi. Good afternoon. Just a quick question, please on your SME growth. So 5% for 2019 seems quite strong. Could you help break it down between how much of it came from volume rates and also things like some new products? I think you launched a new agriculture product. Has there been any impact?

A - Peter Hermann {BIO 20507411 <GO>}

There has been an impact from the indexation of the worker's compensation. And then we have actually had a very good growth, in general. The product you're talking about the Crop Insurance that we were very happy with, unfortunately, the farmers were not, at least not at the prices that we suppose we should have. So it hasn't sold very much yet.

A - Lars Thykier {BIO 16427122 <GO>}

I would say that most of the growth is due to volume. So we've had a net income of customers from most other companies in the -- both in the commercial area and in the agricultural area.

Q - Derald Goh {BIO 20775137 <GO>}

Great. Thank you. And just a quick follow-up. Going back to the underlying loss ratio, I think you again flagged some negative impact from motor this quarter. Could you give a bit more color behind the underlying drivers?

A - Peter Hermann {BIO 20507411 <GO>}

What we have seen during the last couple of years has been that the claims on third-party liability concerning personal injury has fallen very steeply. And this has been sufficient to cover the increase in -- what's it called? Motor comprehensive. But we see a negative development in motor comprehensive and positive development in personal injury. What has happened in Q4 is that we have put aside an extra reserve for third-party liability concerning physical things, not personal injury, but the stuff that our customers run their cars into has been more expensive. That can be other cars or bicycles or whatever it is.

A - Lars Thykier {BIO 16427122 <GO>}

So it's the same effect. You can see that on the motor comprehensive, we're seeing that it is getting more expensive to clear the repair of a car with all the sensors and technology. The same goes with the liability side of the things. That also means that we are looking into the pricing on the motor comprehensive on the north, we say more things side and not the personal side next year.

A - Peter Hermann {BIO 20507411 <GO>}

You'll see a slight skew where we don't or we will reduce third-party liability to some extent, and we will increase comprehensive .

Q - Derald Goh {BIO 20775137 <GO>}

Thank you very much.

A - Peter Hermann {BIO 20507411 <GO>}

Welcome.

Operator

And the next question comes from the line of Youdish Chicooree from Autonomous Research. Please go ahead.

Q - Youdish Chicooree {BIO 17430923 <GO>}

Hi. Good afternoon, everyone. I've just got one question, please. It's on your adverse claims experience in private property. It seems that throughout the year, you've had recurring issues around burst pipes et cetera. So I was wondering what actions are you taking to address this adverse development, please? Thank you.

A - Peter Hermann {BIO 20507411 <GO>}

I'm not sure I got that. Could you repeat, please?

Q - Youdish Chicooree {BIO 17430923 <GO>}

Throughout the year, you've talked about adverse loss experience on property, namely due to burst pipes. So I was wondering what actions you're taking? Because firstly, it seems that you're raising prices still in line with the automatic indexation. So I was wondering whether you were doing something out on the claims side to mitigate the adverse experience of 2019.

A - Peter Hermann {BIO 20507411 <GO>}

We are looking on the selection of houses. There are some cohorts, obviously, where the risk is bigger than other. But you should assess this in combination with the other products the customer owns or has. If we get a customer who has a house, then he'll have car insurances, two car insurances, could be and insurance of dog and children and other content. And that means that the package as such is pretty profitable actually. But you're right, that if you look on house alone, then the insurances are not profitable.

Q - Youdish Chicooree {BIO 17430923 <GO>}

Okay, that's it. Thank you very much.

Operator

And the last question comes from the line of Mads Thinggaard from ABG. Please go ahead.

Q - Mads Thinggaard {BIO 15369662 <GO>}

Yes. Hi. This is Mads from ABG. Thank you for taking my questions. I have just -- the first one is just, if you could help a bit. Now you had some quarters with some upwards pressure on claims before one-off weather, et cetera. And of course, you discussed some of the components here. But going into 2020, do you have kind of a normal rate of change we should expect quarterly? Do you have kind of a picture of this at this point?

A - Lars Thykier {BIO 16427122 <GO>}

We do have -- I mean, sorry, I'm afraid I didn't get the question, right. Please again.

Q - Mads Thinggaard {BIO 15369662 <GO>}

Yes. Now we have had this upwards pressure on, I mean, what one could perhaps call underlying claims or claims before one-offs et cetera. And it's more -- do you expect more pressure going to 2020 this quarter year-over-year? Can you kind of picture that now?

A - Peter Hermann {BIO 20507411 <GO>}

The answer is no. I think we are seeing some pressure at some places. But in general, I don't expect to see any substantial increase in claims. You look a little positive. Do you disagree?

A - Lars Thykier {BIO 16427122 <GO>}

No, I don't disagree. And actually you can see that in our guidance for 2019 in the Q3 report for 2018, we guided a combined ratio of between 89% and 90%. And now we're guiding for a combined ratio around 90%. But that is -- but you have to take into account that the discounting since that has hurt the combined ratio by 1.6%. And therefore, you can actually say that the underlying development is improving in our time. 1.19%, actually.

Q - Mads Thinggaard {BIO 15369662 <GO>}

Okay.

A - Peter Hermann {BIO 20507411 <GO>}

1.5 actually.

Q - Mads Thinggaard {BIO 15369662 <GO>}

Thanks. And could you remind us a bit, what kind of initiatives are helping claims in 2020?

A - Peter Hermann {BIO 20507411 <GO>}

Both procurement -- activities within procurement. Its activities were then present when we mentioned motor comprehensive as -- maybe some price increases on that. So we have something that is more statistical, whereas, yes, from month-to-month or quarter-to-quarter, that's again we're unsure on. Maybe we'll not do anything about that. But in other places we can see that. For example, some of the specific coverage is on a car insurance, parking insurance and so on we can see that the claims ratio is not good, then we also look into price increases on that.

Q - Youdish Chicooree {BIO 17430923 <GO>}

Okay.

A - Lars Thykier {BIO 16427122 <GO>}

We are screening the portfolio all the time. And when we find, which we do all the time, of course, find customers that we don't expect to be profitable at the price having for the time being, they will have an individual price raise.

A - Peter Hermann {BIO 20507411 <GO>}

And the same as we said before about illness and accidents, we will look into how we can actually increase the result and make it better. So that's also with the underlying claims.

Q - Youdish Chicooree {BIO 17430923 <GO>}

Okay. Okay. Thanks for that.

A - Peter Hermann {BIO 20507411 <GO>}

Welcome.

Operator

As there are no further questions, I'll hand it back to the speakers.

A - Peter Hermann {BIO 20507411 <GO>}

Yes. Thank you for participating here and attending our conference with good questions. As you know, you're always welcome to call us, if you have any further questions, and then, of course, we'll be happy to answer them. So goodbye or good morning, whatever it is called where you are, but see you next time. Bye-bye.

A - Lars Thykier {BIO 16427122 <GO>}

Bye.