Q4 2014 Earnings Call - International

Company Participants

- Kjetil Ramberg Krøkje
- Lars Aasulv Løddesøl
- Odd Arild Grefstad

Other Participants

- Blair T. Stewart
- Daniel A. Do-Thoi
- David T. Andrich
- Gianandrea Roberti
- Matti Ahokas
- Paris Hadjiantonis

MANAGEMENT DISCUSSION SECTION

Operator

Good afternoon, ladies and gentlemen, and welcome to the Storebrand Analyst Conference Call. My name is Ann, and I will be your coordinator for today's conference. For the duration of this call, you'll be on listening only. However, at the end of the presentation, you will have opportunity to ask questions. I will now hand you over to Kjetil Krøkje to begin today's conference. Thank you.

Kjetil Ramberg Krøkje

Welcome, everyone, to Storebrand's fourth quarter 2014 conference call. My name is Kjetil Ramberg Krøkje, and I'm the Head of Investor Relations at Storebrand. Together with me, I have Group CEO, Odd Arild Grefstad; CFO, Lars Løddesøl; and Head of Guaranteed Pensions, Geir Holmgren.

In the presentation today, Odd Arild will give an overview of the development in Q4 2014 and Lars will give some more details on some of the elements in the results this quarter. The slides will be similar to the Analyst Presentation released this morning and are available on our Web page as well.

After the presentation, the operator will open up for questions. To be able to ask questions, you will need to be dialed into the conference call. I now leave the word to Storebrand's CEO, Odd Arild Grefstad, who will start the presentation on slide two.

Odd Arild Grefstad {BIO 5483351 <GO>}

Thank you, Kjetil, and welcome, everyone, to the presentation. The results of Storebrand is strong, totaling NOK923 million for the quarter and NOK3.032 billion for the year. The results are affected by some special items, which Lars will comment on in more detail. The transition of Storebrand's own pension scheme is the largest item in the positive net NOK477 million that we characterize as special items. We have reached the cost target of NOK400 million and will follow up the cost going forward related to a relative basis, a cost-to-income ratio of 60% as we announced in our Capital Markets Day. The transition from guaranteed to non-guaranteed – and insurance in the balance sheet and the result continues.

The result from the segment savings increased with 44% compared to last year. There is strong sales and return in the balance sheet and in the P&L, and the strong growth in asset under management with more than 10% growth for the year.

We have started up with paid-up policies with the investment choice, and I'm very happy to report that we have transferred close to NOK900 million for the full year. The buffer capital situation has strengthened significantly in the fourth quarter by NOK10 billion. And we have also set aside now NOK6.2 billion altogether for longevity reservation. That is half of what is required altogether. Despite falling interest rate, we have managed to increase the Solvency II ratio up to 148%. It means that our internal measures have canceled out the effect of the falling interest rates.

We now go to page number three. This shows Storebrand strategy, and it's still to manage the guaranteed balance sheet with more than 130% of Solvency II margin and to continue to grow our savings and insurance business.

Let's first take a look at the guaranteed part of the business, that's on slide number four.

We have transferred out approximately NOK30 billion during the last two-and-a-half year. In 2014, we moved out NOK15 billion from the guaranteed book of business. NOK11 billion was from the public sector – guaranteed public sector in Norway, NOK3 billion was in the Swedish business and NOK1 billion, as I already have mentioned, was then the paid-up policies converting into investment choice in the fourth quarter.

I'm also very pleased to see that NOK8 billion of our assets within the public sector have moved into closed pension fund solutions that was sold to municipalities during 2014. The cost program is completed with more than NOK400 million delivered. And we also see that we have been able to take some additional measures when it comes to risk reduction also in the fourth quarter, reduced equity exposure, and better tailoring the assets to the liabilities of the business in a more segmented way.

Then, I – yes. That was slide number four. Then, I move to slide number five. And this is an important picture for us. The focus in the fourth quarter has very much been to strengthen our solvency capital position in a falling interest rate environment. The effort to strengthen the solvency position has been a clear target above the prioritize the short-term IFRS profits.

Some of the most important measures, consolidations we have made is; one, to increase the longevity reserve instead of leaving results to the risk equalization fund and for profit sharing. We have also significantly strengthened the buffer capital that is mainly the market value adjustment reserve, but also additional statutory reserves, and excess value on bonds at amortized cost. Increase on these three element is more than NOK11 billion in the third – in the fourth quarter.

And we have also done some strengthening of the technical provisions in SPP, where we have been able to use the conditional bonuses into the technical provisions, that has also strengthened the solvency position altogether. And this is done also altogether with a better risk management after matching principles altogether.

So together, all these measures has contributed to the strengthening of the Solvency II position, with approximately 20% points. This compensates the reduction in the fall in the Solvency II position as a consequence of the decline in the interest rates.

The Solvency II position, inclusive transition measures, is limited. The Solvency II position, inclusive transition measures, is very limited impact by the changes in the interest rate level and by the first – all the way up to the 1st of January 2016. And it's now estimated to 148% and that is approximately 20 basis – percent point, the increase from the third quarter.

If we then move to slide number six, we have a total reserve strengthening of NOK12.4 billion to do for longevity. The longevity reservation is strengthened by NOK2.7 billion in 2014. There's been a direct contribution on NOK121 million in the fourth quarter. That is the NOK90 million that we used to see and, of course, the basis. And on top of that, we have included NOK31 million that is supporting the transfer of the paid-up policies into paid-up policies with investment choice.

There is also some indirect contribution like the foregone profit sharing. And also, as I already have mentioned, the use of the risk result directly into reservation. I'm we're pleased to see that now, after the first year of this program over seven year, we have been able to reserve half of the total amount needed. We also know that we are expected to contribute NOK2.2 billion with the results over the next six year, and after that, it's NOK4 billion left for the last six year to reserve made up of additional return on the policyholders' funds.

If we then move to slide number seven; this is an illustration that shows the expected return in the most challenging portfolio, the paid-up policies, going forward. Of course, the low interest rates is challenging for a business with annual interest rates guarantees. However, we have been able to build up an asset allocation and a profit capital situation in this portfolio that ensures good returns going forward.

The expected return in the paid-up policies is high enough to cover for the interest rate guarantee and also the needed buffer building for longevity over the next period until 2020 when this is expected to be finished.

Then after 2020, we know that the interest rate guarantee will fall down to approximately a 3% level – down below the 3% level and expected return even with today's very low interest rate level, going forward, should be enough to also cover for interest rate guarantee thereafter. And also know that there is a big shift in the balance sheet from guaranteed to non-guaranteed. So, we feel very comfortable about the capital situation altogether even in a low interest rate level.

If we then move to slide number eight, it's to point out that the growth side of the business are experiencing very strong growth, especially in our asset management business and with our unit-linked reserves.

And moving into slide number nine, you see that the paid-up policies with investment choice has been a very important focus area for us in 2014. The early stages of this process has been very promising, around 3,500 customers and NOK900 million have been converted to paid-up policies in the fourth quarter. And so far this year, together with the fourth quarter, we have been able to convert NOK1.5 billion and almost 5,000 customers all together.

Moving into slide number 10, we see that the growth in the unit-linked premium has been strong in 2014 and it's expected to also be very strong in 2015, also because we experienced a very strong sales, new customers coming into the company and increased savings rate and income growth altogether. It's worth mentioning that this is the first year where we see unit-linked payments exceeds their guaranteed premiums altogether. And this shift will, of course, continue as we see it into 2015.

So, that's so far. And I now leave the word to Lars that will give more insight into the numbers and the results for the fourth quarter.

Lars Aasulv Løddesøl

Good afternoon, everyone. If you look at key figures on page 12, you see how the result of NOK923 million is composed by net profit sharing and loan losses by mainly discontinued business and one-off items, which is a fairly large item of NOK477 million this quarter, and the result before profit sharing and loan losses which is the highest quality component of the earning.

And even in a quarter where we've had a low financial return and where we had to strengthen our -we had a weak disability result and strengthened disability reserves, we still have a quite strong underlying result before profit sharing and loan losses.

On the lower part on the left-hand side of this picture, we see the solvency ratio over the (0:13:25) group and the solvency capital has been built up consistently quarter-by-quarter, and indeed by 20% or NOK10 billion through the year of 2014 according to the work and the priorities that Odd Arild has been through.

On earnings per share, I'd like to – these are our earnings per share after tax. And I'd just like to comment that the tax cost has been estimated to around 20% for the year 2014. When it comes to customer buffers, there's been a decrease in buffers in Sweden – customer buffers in Sweden and an increase in Norway. And the reason for the decrease in Sweden is because we've strengthened longevity reserves for certain portfolios. And we've been able to take the reserves strengthening from these customer buffers in Sweden. The consequence is an expected higher result going forward and an improved solvency position.

Moving over to page 13, the numbers. However, due to the one-off effects or the special items that we have briefly commented upon, these numbers are difficult to understand in terms of value drivers going forward. Therefore, I would like to move you over to page 14, where we talk a little bit more about the special item and thereby be able to see the value drivers in the underlying profitability afterwards.

So, basically, the special items can be contributed to three different things. The first and most important thing is that we have closely defined benefit plan for Storebrand in Norway. The consequence is the positive effect in the accounting of NOK571 million, which is accounted for as a lower-operational cost.

It is a one-off item in the quarter. However, with the change from defined benefit to defined contribution scheme, we will see less volatility and, over time, lower-operating cost in the company. So, this is part of the cost reduction and cost control program.

The second item I would like to point out is that in Sweden, we've done a review of the reserves in different parts of the portfolio and versus dissolved ATP compensation. That is a historic coverage that is no longer needed and that is no longer given to Swedish employees. And we've been able to dissolve the reserve related to ATP compensation. As I said, it's no longer an insurance that we give.

On the other hand, we have strengthened longevity reserves and also reserves for future costs related to tax that is accounted for here under what's called special items financial results SPP. What we've done is that we've strengthened the reserves by a total of NOK1.3 billion, and then we've taken NOK1 billion out of the conditional bonuses of the client, which we saw on the previous page, and NOK300 million or NOK322 million of shareholders' contribution in order to strengthen these reserves, and that comes in terms- it comes as a negative financial result.

So, for the Swedish business as a whole, the plus NOK322 million and the minus NOK322 cancel each other out. It's actually coincidental that these numbers are exactly the same, but the effect is therefore neutral for the Swedish business, but it comes on through different profitability lines.

The third and last special item that I would like to comment is what Odd Arild has already commented upon, that previously we've been able to build part of the result in the guaranteed business to a Risk Equalization Fund, which is 50% of a surplus. On the other hand, 50% has been given to policyholders.

Through a letter from the FSA received in October is that we should not bid the risk equalization fund as long as we're under reserved for long life. And, therefore, the NOK98 billion is given back to customers, as well as NOK98 million contributed into the risk equalization fund is now being – is being put into longevity reserve strengthening, and will continue to be done so for the next years. So, this will reduce income from the risk result in this period.

So, all in all, these items account for NOK477 million. And if we deduct them from the result lines and the Storebrand's overall results overview on page 15, we see that the fee and administration income is up 0.4% year-on-year. It's actually if you deduct the corporate bank and the public sector of 5%, so when you take out the discontinued business. The risk result life and pension has stronger than last year due to the fact that we now have longevity tables, and despite the fact that we have taken out the risk adjustment – the risk equalization fund that I mentioned.

Insurance payments and claims account for putting in (18:59) together, insurance results. And we can see that there's been higher claims in the fourth quarter because it's cold and slippery in Norway, and also, the disability results are weaker, and we'll continue to build disability buffers which we started in the third quarter. We now feel that the buffers are adequate and are – that are finishing this part of the disability reserves strengthening.

On operational cost, they are down for the full year. It's up in the fourth quarter compared to the fourth quarter 2013, and that is a result of more market spending and more market activity connected with all the stakes that we've achieved in the fourth quarter.

The financial result is strong for the full year, somewhat weaker in the fourth quarter giving a result before profit sharing and loan losses of NOK541 million for the quarter. The net profit sharing and loan losses, that's primarily profit sharing for Swedish business, which is again strong for the full year. That is weaker than the market has reason to expect in the fourth quarter due to the sensitivities that we've given in the supplementary information.

The reason why it's weaker than we can expect on the sensitivities is due to the very significant fall in interest rates and the turbulence in the financial market in the fourth quarter, where our sensitivities has not been given – has not been giving a full picture on when that movement are as big as they were.

Provisions for longevity, you are used to see NOK90 million per quarter on this line. As Lars said a moment ago, the charge is NOK31 million higher now due to the fact that we have transferred NOK900 million into paid-up policies with investment choice. And some of these paid-up policies have been under reserved for long life, and we have on average contributed about 3% of the reserves to strengthen longevity before the transfer. That gives us a result before amortization and write-downs, excluding non-recurring items, of

NOK445 million, and you add on the special items and you end up with NOK923 million for the quarter.

So, that's just a brief overview of the result. And you will find, on the following pages, more breakdown into different (0:21:26) and value and business sectors, but I won't go through that in detail now. We'll be happy to take any questions.

Kjetil Ramberg Krøkje

Operator, we'll now open up for questions.

Q&A

Operator

[Operator Instruction] The first question comes from Daniel Do-Thoi from JPMorgan. Please go ahead, your line is now open.

Q - Daniel A. Do-Thoi {BIO 17019775 <GO>}

Hi. Good morning. I just have three questions on – all on solvency, actually. You mentioned earlier about three or so key measures that you've taken over the course of the quarter to offset the 20 percentage point drag from lower rates. Could you just give us a feel for sort of the – roughly how much each measure contributed?

And then secondly, can you just comment on the sort of ongoing P&L impact that we should expect as a result of these measures that you've taken, so looking into next year? And then lastly, I guess, on the sensitivities, the updated sensitivities, the growth impact from a further 50 basis point decline in interest rates is, I guess, broadly unchanged. But just wondering how we should think about the net impact going forward, i.e., are there any other offsetting measures or internal measures that you can take to reduce this gross 20 percentage point impact for every 50 basis points? Thank you.

A - Odd Arild Grefstad {BIO 5483351 <GO>}

Thank you. Try to comment on this and also, of course, we'll use some of the rounding here (0:23:13). Starting with the solvency numbers; I think it's quite evenly on these four different elements that I have spread out, that's up to around 20%. We have been able to strengthen longevity above the level we were supposed to do during the year. And I'll say there's the full effect of that, but that was somewhat underestimated when we came out with our numbers in the third quarter. So it's more a full effect of the total NOK2.7 billion build-up compared to the NOK1.8 billion that should be built up during this year. So, that is an important part of it. That is, more or less, one part of it.

Then it's also the case that we have been building other buffers, like in special the market value adjustment reserves. That is a very strong increase in the fourth quarter. And we have been very focused on measuring that. We have realized some losses also to make sure that we have build-up the market value adjustment reserve, and that together also is a very good impact on the solvency position and gives 3% to 4% points altogether.

And then, it's clear that the issues that we have done in Sweden, where we have introduced conditional bonuses that has not been very effective for solvency purposes, been able to transform that into technical reserves on the insurance side is also a very strong effect on the solvency sale (0:24:51) ratio.

And then, altogether, all the small items with segmentation, making sure that we have the right risk matching of asset/liabilities in the different portfolios, altogether it's also some reductions of equity portions, because when we are more tailor-made, we can use – we have use of the excess return that we can take out the expected from the equity market. So, that, altogether, is also a very important element in it. It's also, of course, we were working to the model altogether. So, it's somewhat changing the model in itself, but this is the main element. It's actually things that is done with the business and it adds up to a 20% point increase.

Going forward, on the P&L effect, I would say it's – what brings into my mind is two element that goes the different ways. As we have said, we use to take a part of the risk result over the P&L. It's more like an hybrid type of equity because it's equity that we build up in this place. And there is a reserve that is not common multiple to use for everything. It can only be used for negative risk results. So, in that way, it's something between equity and debt actually.

But anyway, it's been under IFRS, to taken over in the result, NOK98 million this year. It will be lower numbers going forward. But this is an element that we not – will expect to see for the next couple of years through the P&L.

On the other hand, the strengthening of the reserves in Sweden should bring into a situation where we have stronger risk result in Sweden going forward that goes in the opposite direction. I don't know if Lars or anyone has other elements from this that they'd like to draw – bring forward?

A - Lars Aasulv Løddesøl

Yes. No, we will continue to build this underlying solvency through continued building up of capital and results and the whole (0:27:10) part of the results back in the life business. And the transition to non-guaranteed products continues and the growth in non – sorry, the growth in non-guaranteed products increase. And the guaranteed products are slowly maturing in terms of shortening the duration and lowering the guarantees.

So, there are a number of things that over time will decrease the capital charge related to the guaranteed products and the capital build-up from the non-guaranteed products. So, these are some of the measures that – and we will look at other things as well in terms of fully coordinating our models with the final Solvency II requirements, et cetera.

A - Odd Arild Grefstad {BIO 5483351 <GO>}

I'll also say that when we do our planning or forecast on solvency ratios, of course, we expect to have increase (0:28:01) in the underlying solvency ratio during 2015. There's a lot of measures that is under performance to come into the balance sheet results. And as we have shown in the fourth quarter, we are also working with this to be completed and give effect in first quarter or second quarter and the rest of the 2015.

A - Lars Aasulv Løddesøl

And in terms of sensitivities, you can see on slide number five that when we managed to keep the underlying solvency without transition rules stable from Q3 to Q4, the effect of the transition rules increased from approximately 24 percentage points to approximately 47 percentage points. That is a consequence of the different capital position in the Solvency I and Solvency II and the traditional – sorry, the transitional rules take one minus the other and add it on to the capital and then you write it off over the next 16 years. And so, this is the way the transitional rules work.

So, if the interest rate that will fall or one of the other sensitivities happen in the first quarter, and you may see that you have an underlying movement, which is impacted pretty much according to the sensitivities shown here, while the effect with transitional rules up until January 1, 2016 will be rather stable. So – but after 2016, then these sensitivities will be registered also for the headline number.

Q - Daniel A. Do-Thoi {BIO 17019775 <GO>}

Okay. But just a follow up, I guess I was just wondering, if over the course of the quarter we see another 50 basis point decline in interest rates, I understand that the ratio with transitional rules would remain broadly unchanged, but the line (0:30:08) would come down by roughly that sensitivity, so 20 percentage points?

A - Odd Arild Grefstad {BIO 5483351 <GO>}

Everything equal, it will come down with that sensitivity. But as we have shown this quarter, of course, we will perform a lot of measures also going forward that will – where we will try to mitigate such movement in the interest rates.

Q - Daniel A. Do-Thoi {BIO 17019775 <GO>}

Okay. Understood. All right. Thank you very much.

Operator

The next question comes from Matti Ahokas from the Danske Bank. Please go ahead. your line is now open.

Q - Matti Ahokas {BIO 2037723 <GO>}

Yes. Good afternoon. Three questions, if I may? Firstly, just technically, the paid-up policies with investment choice, they're now booked, I guess, under unit-linked Norway, is that correct? And then, there was an NOK4.2 billion increase in unit-linked Sweden on the reserves, on other, and it's a fairly sizeable figure quarter-on-quarter. I was wondering if you could explain that a bit.

And the third question is regarding page seven. It's a very interesting chart you are presenting here. Could you talk a bit about the assumptions that you are using this – in this expected return? And for example, what are the current reinvestment yields that you're able to generate in Guaranteed Pension Norway? Thanks.

A - Lars Aasulv Løddesøl

The first question on paid-policies with investment choice, yes, they are a part of unit-linked Norway. And the second was Sweden. I guess you have both an effect from currency in the quarter. That, as Lars said earlier, was pretty neutral during the year, but it increased quite a lot in the quarter and we use end-of-quarter numbers on the balance sheet. So, a part of that (0:31:56).

And when it comes to returns and what we can reinvest to, I guess, the Norwegian swap rates now are at 1.7-ish (32:13). And over that we have different normalized risk premiums depending on different asset classes. More or less that (0:32:22) we are selective on where we invest now, given the current interest rate environment and our need for reinvestment.

A - Odd Arild Grefstad {BIO 5483351 <GO>}

It's also our portfolio that is declining, not increasing, so that is also an element, altogether with the total guarantees book of business. When it comes to the assumption, when it comes to return to build up this 4.2%, 4.1% return, it's very much based on held-to-maturity bond portfolio. That's typically 50% to 60% we assume out of this portfolio. Then, we have the real estate portfolio in Norway having a direct yield of around 4.8%, 4.9% that is added here, and that's also a substantial part of it. And then it's bonds at mark-to-market with actually a market value you have under that. And then, it's – it's very much – when you look at the paid-up policies, it's very low allocation to that. I will expect extra 5%, 6% to the point when it comes to these paid-up policies. So, of course, that is the element that might have some changes in the values here, it's a normalized expectation. But for 94%, 95% of the total portfolio is very much quite robust and quite secure return that we have added on as expected return going forward.

A - Lars Aasulv Løddesøl

And it's based on current interest rates also going forward.

A - Matti Ahokas {BIO 2037723 <GO>}

Yes.

A - Odd Arild Grefstad {BIO 5483351 <GO>}

So, Matti, basically looking at the actual yield in the different portfolios and the bonds that amortized closely is stable. And stable portfolio is a duration of some six-and-a-half years.

So – and then whatever come out of that and maturities reinvested at today's interest rate level.

Q - Matti Ahokas {BIO 2037723 <GO>}

So, basically, the portfolio, currently, I remember, was it 4.8% was the – was the held-to-maturity portfolio running yield, and this is basically based on the redemption of that portfolio?

A - Odd Arild Grefstad {BIO 5483351 <GO>}

Yes. Because it's based on the chart; based on both the redemption on that portfolio, it is also – it's also based on the issuance of new paid-up policies, which we reinvest at the current yield curve.

Q - Matti Ahokas {BIO 2037723 <GO>}

Great. Thanks a lot.

Operator

The next question comes from David Andrich from Morgan Stanley. Please go ahead, your line is now open.

Q - David T. Andrich {BIO 15414075 <GO>}

Hi. Good afternoon. Thank you for taking my questions. I was just wondering, in terms of the internal measures you implemented to help keep Solvency II stable on a look-through basis, so without the transition rules quarter-over-quarter, I was just wondering how far can you kind of shift the needle going forward? Say like on a scale from one to 10, how high can you turn up the volume on that? Are you kind of already at a nine then in terms of what you've achieved, or do you feel there's a lot more that you can achieve there?

And then second of all, I was wondering, in terms of the higher incidence of disability in the quarter, is that coming through mainly kind of on the DC side, or on the DB side, or pretty even between the two? Thank you.

A - Odd Arild Grefstad {BIO 5483351 <GO>}

We have a toolbox of available tools to strength Solvency II. And there is – there are uncertainties still related to the final outcome of how the rules will finally be set. And the effect of – or how many tools to use in the toolbox depends on the interest rate level and on the finalization of the rules. Obviously, we've done a lot of the easy stuff so far, but there are still things we are working on. And I don't want to go into detail about that.

But Solvency II is quite a sophisticated and complicated set of rules. And as we go through our economic models and adapt it to Solvency II, we do see ways to improve product profitability in different scenarios as set under Solvency II. And we see ways that we can introduce management actions and pricing features that are meaningful under Solvency II regime.

So, the purpose of Solvency II is to improve risk management and long-term profitability in the insurance business, and we see that Solvency II has helped us to become even better on this. And we will continue to strive to be excellent.

With respect to higher disability, we see higher disability, first and foremost, in the – both Swedish and Norwegian unit-linked portfolios. And it's not like it's a huge difference, but margins in this business are thin. So therefore, when you see an increase in disability, and, at the same time, we're strengthening some reserves, it does impact the quarterly results.

Q - David T. Andrich {BIO 15414075 <GO>}

All right. Thank you very much.

Operator

The next question comes from Blair Stewart from Bank of America Merrill Lynch. Please go ahead. Your line is now open.

Q - Blair T. Stewart {BIO 4191309 <GO>}

Thanks. Thanks very much. Good afternoon. I've got a couple of questions left. A lot of them have been asked. Firstly, on the transfers paid up with investment choice, I was wondering what impact did that have on your economic capital numbers given that you did almost NOK1 billion. It wasn't something you talked about having an impact. But I wonder if it did move the needle.

Related to that, given you're targeting NOK5 billion for this year, would you – or to get to NOK5 billion for this year, would you expect that to increase further the cost of the longevity provisioning? And again, related to that, are you still confident in your initial expectations as to how much of that book can actually be moved ultimately?

And then, I think I had one further question. Just on – again, just coming back to the new money rates, what you're investing money in today. You talked about the swap rate being at 1.7 plus a normal risk premium. I guess plus some real estate, et cetera, are you able to get the new money yield up above 2.5% to possibly 3% at the moment, or is that too high in this market? Thank you.

A - Odd Arild Grefstad {BIO 5483351 <GO>}

Okay. Let's start with the transfers. And yes, we have the target of NOK5 billion as we see it now. Around 3% of the assets that's been moved we need to top up with the long life resource. So that gives you the number, you saw NOK30 million and around NOK1 billion now in the fourth quarter. And we expect that ratio to be the same also going forward for the assets that we moved from and hopefully into paid-up policies within the investment choice.

And yes, we have our segmentation model and we still have the same target. We expect, of course, this also to continue off to 2015. We have put the target up for 2015. We also see that it's important for us to be in good contact with the companies and the employees in the company when they do change this from defined benefit to the incentivized contribution, then everyone will have a new pension scheme like we do in Storebrand ourself these days.

And that's a very good situation to do works at marketing to really make sure that we give the total message to all the employees in the company. And if this moves then the needle when it comes to Solvency II, well, one thing it will happen in the first quarter and the NOK1 billion in itself doesn't, of course, offset anything much. But going forward, expectation of being able to move this and also for the new paid-up policies that comes in, in a conversion from defined benefit into defined – into unit linked result. That gives of course a very important toolbox to also make sure that we have a good situation Solvency-wise out of the new paid-up policies. I don't know if anyone like to...

A - Lars Aasulv Løddesøl

Yes. I think we – on – on Capital Markets Day, we said that the old paid-up policies had up to 20% capital charge. So, if you have NOK1 billion time 20% capital charge and you transfer that into a new product, that has a negative capital charge or it contributes capital in a large company, then you can look at some of the capital consequences by using those numbers.

And in terms of reinvestment hurdles (0:42:04), I can confirm that between 2.5% and 3% is a reasonable reinvestment level at this stage.

Q - Blair T. Stewart {BIO 4191309 <GO>}

Okay. Thank you. Just coming back on the paid-up book, would you still expect the net – net-net for the book to continue to increase over the next coming years? Because whilst you're transferring out, of course, there's further transfers in from the closure of active DB schemes. How do you see that book evolving in size over the next two to three years?

A - Lars Aasulv Løddesøl

Yes, Blair. As we showed on the illustration on the Capital Markets Day we expect this to increase over the next years and go up to somewhere around NOK110 billion. But then there is a big uncertainty here relating to when transfers happened for defined benefit and also how fast people move in to paid-up policies with investment choice. So, it could be bigger and it could be smaller but I think that is the best guess for the three to five-year period. I don't know if any of you...

A - Odd Arild Grefstad {BIO 5483351 <GO>}

I also want to say that, that (0:43:22) taking into account (0:43:26) numbers. So, that is what we have put into our models. If we are to succeed with even a higher person into paid-up policies with investment choice or keep the assets longer in DB schemes that will be an upside on that calculation.

A - Lars Aasulv Løddesøl

Yes. If you look in the supplementary information, you see that the balance of paid-up policies increased by NOK12 million last year from NOK80 million to NOK92 million...

Q - Blair T. Stewart {BIO 4191309 <GO>}

Yes.

A - Lars Aasulv Løddesøl

...that is probably as far as we can see, the largest increase in one year. But there will still be an increase in the next couple of years, but it will be decreasing in size.

Q - Blair T. Stewart {BIO 4191309 <GO>}

Yes. Okay. Thank you.

Operator

The next question comes from Paris Hadjiantonis from KBW. Please go ahead. Your line is now open.

Q - Paris Hadjiantonis {BIO 19703051 <GO>}

Yes. Hello and thank you very much for taking my questions today. I just have two. The first one is from this indirect charge where you used the risk result now rather than the equalization fund, and you have NOK98 million for this year. Is this a good number where we can do our forecast for the next few years or does it largely depend on what happens with the foregone charge – the charge from the foregone profit sharing which was NOK230 million this year?

And the second question is on the solvency. Basically, if you could give us a kind of an idea of the measures we have taken, whether these have impacted the required capital side or the available capital side. Thank you very much.

A - Odd Arild Grefstad {BIO 5483351 <GO>}

Okay. I can start with the first question about the risk equalization fund. For 2014, we spent NOK98 million (45:24) that in – we used as – which is the longevity reserves. And we expect that number to decrease going on. What you also can say is that when the contract on DB and paid-up policies are truly reserves regarding longevity, we don't need to use the risk equalization fund to the longevity reserves, and we have to look at that contract or contracts which means that going on the next years when more contracts are fully reserved, we will increase the risk result, decrease the amount spend to the longevity reserves, which should in – otherwise would have been (0:46:22). So, when we look at the number, NOK98 million for 2014, it will slowly go decrease during the next years.

I can also add that we have already some contracts that are fully reserved. And for these contracts, we are actually, also in 2014, put in a position where we, in some way built a little bit into the risk equalization fund. So, it's fair to say that this number will go down in a slow pace during the next year.

A - Lars Aasulv Løddesøl

And with respect to the risk capital or the solvency question you had, it's both this available capital and it reduces required capital. So, it's a balanced answer to that question. I don't want to go into a lot of detail on that. It becomes extremely complicated to do on a phone call.

Q - Paris Hadjiantonis {BIO 19703051 <GO>}

Okay. Understood. Thank you very much.

Operator

The next question comes from Gianandrea Roberti from Carnegie. Please go ahead. Your line is now open.

Q - Gianandrea Roberti {BIO 6786731 <GO>}

Yes. So, good afternoon from me, as well. I have a couple of questions, I guess, on the same tune that we have been discussing until now. Just perhaps a little bit more precise. This sensitivity you're showing, 50 bps down, it's around 20% on the solvency margin. Basically, the internal measures you have taken in this quarter have improved the solvency margin by around NOK5 billion. Would it be – how should we look at it? If rates go down 50 bps, do you have another NOK5 billion on internal measures that would put the solvency margin excluding transitional rules around 101%, or even a bit better, considering return earnings? Or, well, actually, you don't have another NOK5 billion to find like this. How we should really think about it.

And even more importantly, back to the dividend situation here, I think in past discussion the assumption that you should have had a solvency margin excluding transitional rule above 100% with some buffer to sort of make the FSA happy before paying dividend was the right assumption. In conversation that I had today, I don't know any more what is the right assumption. Can you spend some more in trying to tell us how do you see this point, which, I guess, is quite important? Thanks a lot.

A - Odd Arild Grefstad {BIO 5483351 <GO>}

Okay. Well, I think we have answered already on how we are building buffer capital. We are focusing on doing that every day, and that has been the main focus throughout fourth quarter. And have put emphasis on that rather than building short-term IFRS result. We will continue to do that. I think both me and Lars has given you some examples of what are working with, and we are very dedicated of doing that also going forward, even if the interest rates falls or rises as such. Okay, so...

Q - Gianandrea Roberti {BIO 6786731 <GO>}

That's not easy (0:49:32).

A - Odd Arild Grefstad {BIO 5483351 <GO>}

Yes. It's not easy to find NOK5 billion every quarter. I agree on that. But this quarter, we have been really also positive when it comes to the financial markets. They've been able to build buffers above the levels that should be expected in normal situation both in market value adjustment reserves and also when it comes to longevity reservation. And we have also been able to do some reclassification of the properties in Sweden.

This is some example of what we are doing. And as Lars said, we have a toolbox done. We have used a lot of the tools, of course, the easy way out, as they are still working for this on a daily basis, and I am confident that we'll also find build and solutions and good measures that we'll keep strengthening the Solvency II position going forward.

A - Lars Aasulv Løddesøl

And if I may add, the way – the question forward, it seems to indicate that we first neutralize whatever comes. Obviously, we can't do that. We are working very – in a very high quality way to improve our length, to improve the product and improve the solvency position. It so happened that that neutralized pretty much 100%, the – all of interest rates in the fourth quarter. But it's quite obvious that we will be able to find either we're less than whatever comes from the interest rate sensitivity in the quarters ahead.

When it comes to dividend discussions, we have basically a target forward saying that we should be at par. We're 130% in the regulatory solvency position. That is the target we are watching when it comes to solvency. And of course, the movement in the fourth quarter in itself is very positive moving towards our dividend position.

Then, of course, it will be a powerful view from the board when that is the time for looking at that. And that will be forward-looking. It will be based on buffer capital situation, interest rates and everything. But the number that will measure us around is the headline solvency ratio of 148, as we speak.

Q - Gianandrea Roberti {BIO 6786731 <GO>}

Just one follow up on this, what happens if your solvency ratio excluding transitional rules fall to 90%, as an example, at the end of 2015, just to make the hypothesis here, right? How do you see that situation where one ratio it's well above what you are targeting and the other one is at 90%? How do we need to think about this?

A - Odd Arild Grefstad {BIO 5483351 <GO>}

Well, of course, a regulatory number is the headline number. That is what is put forward and that is what is needed and, henceforward, make sure that we have the right transition, 16 years period into Solvency II. And that is what is really the regulatory framework that we are measured against. Then again, of course, we also need to look forward how will, on a yearly basis, that headline solvency ratio evolve and we both will be in a situation where we are able to keep up the solvency ratio going forward.

So we have to take a total view of the company, of the results of the balance sheet in such a situation. But it's hard to just answer that question based on a point number of the headline solvency number and the underlying solvency number.

Q - Gianandrea Roberti {BIO 6786731 <GO>}

Okay. Thanks a lot. I appreciate that.

Operator

The last question for today comes from Daniel Do-Thoi from JPMorgan. Please go ahead. Your line is now open.

Q - Daniel A. Do-Thoi {BIO 17019775 <GO>}

Hi. Daniel Do-Thoi. Just a couple of follow-up questions. The first one was on – I want to ask about the operating cost this quarter, which I guess on an underlying basis was quite a bit ahead of what you had been reporting in terms of a run rate year-to-date. Also, in the context of – or at least my expectation that a lot of the cost savings that you were – that were scheduled for this year were very much back-end loaded. That was the first question.

The second one is on the Moody's credit rating downgrade. I just wondered if that had any impact in terms of your day-to-day operations, whether that's trying to win new business or whether – or growing in different parts of the business. And then I guess related to that, and the previous question on the dividend, how do you think about that when it comes to the year end, i.e., if you are ahead of your 130% with a good outlook, but you are still below your target A rating, how do you take that into account then? Thank you.

A - Lars Aasulv Løddesøl

With respect to the operating cost, as I mentioned, we've had a very, very high market activity in the fourth quarter, which has resulted in significant improvements in sales and also sales bonuses to the sales force. So, that explains most of the increase in operating cost in the fourth quarter. And as we have mentioned or as we have pointed out to you on the Capital Markets Day, we will continue to follow the cost level of group very closely, but we are allowing ourselves to look at this on the cost-to-income ratio as the result of the consequence that we see a lot of investment opportunities in new sector and new customers. And we need to be able to meet those customers in a prudent way. So, we will continue the cost focus. You do not expect cost to go significantly up, but we will measure this on a cost-to-income basis going forward in order to allow for profitable growth.

In terms of the Moody's downgrade, we have not seen that that has impacted sales or our daily operation in anyway. We've been on negative outlook for a long period of time, and as Moody's write in their report, basically, Storebrand and management of Storebrand does right things in a challenging microeconomic environment. They are concerned about low-interest rates, and that's certainly something that we are working on every day to deal with as well.

And on dividends, I don't know if you want to add anything more than what we've already said about it.

A - Odd Arild Grefstad {BIO 5483351 <GO>}

I think we're already been into that discussion. The number we are following very closely is the headline Solvency II number, and are very pleased to see that – this develop our 130% (0:56:11), that is a very good starting point for being able to take up dividends again.

Credit rating, we have our financial targets. So, a A target is absolutely a part of our targets. But that is also to be in a dividend position to pay dividends. So, I'm not sure that I can add anymore to that discussion at this point of time.

Q - Daniel A. Do-Thoi {BIO 17019775 <GO>}

Okay. Great. Thank you.

Operator

There are no further questions coming through. And I will hand the call back to Kjetil Krøkje for any concluding remarks. Thank you.

A - Kjetil Ramberg Krøkje

All right. Everyone, thank you very much for calling in on this fourth quarter call, and have a good day, and I hope to see some of you at the analyst conference tomorrow.

Operator

Thank you for joining today's conference. You may now replace your handset to end this call. Thank you.