

Q1 2017 Earnings Call

Company Participants

- Jarmo Salonen, Head-Investor Relations & Group Communications
- Kari Henrik Stadigh, Group Chief Executive Officer and President
- Ricard Wennerklint, Deputy Managing Director-P&C Insurance Holding Ltd

Other Participants

- Blair Stewart, Analyst
- Jakob Brink, Analyst
- Janet Demir, Analyst
- Matti Ahokas, Analyst
- Michael Igor Huttner, Analyst
- Paul De'Ath, Analyst
- Steven Haywood, Analyst
- Thomas Seidl, Analyst
- Vinit Malhotra, Analyst

MANAGEMENT DISCUSSION SECTION

Jarmo Salonen {BIO 1860650 <GO>}

Ladies and gentlemen, welcome to this conference call on Sampo Group's First Quarter 2017 Results. I'm Jarmo Salonen, Head of IR at Sampo. And with me at this call, I have our Group CEO and President, Kari Stadigh; our Group CFO, Peter Johansson; and our Deputy Head of P&C Insurance, Ricard Wennerklint.

We have the same procedures. As always, Kari will start with some highlights of the quarter, and after that, we'll get to your questions. Before handing over to Kari, let me remind you that you can follow this call live at sampo.com/result, and a recorded version of the call will later be available at the same address.

With these words, I'll hand over to Kari. Kari, thanks.

Kari Henrik Stadigh {BIO 1504152 <GO>}

Thank you, Jarmo. Welcome to the conference call on my behalf as well. How to describe the solid first quarter? Well, this time, I would like to start by looking at the total comprehensive income. Given our short duration in our fixed income portfolio and the good equity weight, as well as successful equity selection, our performance was very strong for the first quarter compared with the previous year.

And if insurance more than - If insurance more than doubled its comprehensive income compared to the last year to €268 million, which was 32% higher than the reported profit before taxes. Same goes for Mandatum Life where comprehensive income grew to €85 million, being 57% higher than the reported profit before taxes. And also it's good to note that the corresponding comprehensive income the year before was negative. All of this can of course then be seen in the Sampo NAV per share which grew €26.67 per share. Return on equity was also clearly above our

target levels. In the insurance operations at 37.5% in If and 24.3% in Mandatum Life. This created a perfect time for some buffer buildup.

In If Finland, we lowered the discount rate to 1.2%, the lowest among the peers, and it cost us €70 million. And it is also worth noting the discount rate in If Denmark is at minus 85% - minus 0.85% and in If Sweden at minus 0.03%.

In Mandatum Life, the discount rate for 2017 and 2018 was lower to 0.25% and for 2019, to 1.25%. This cost us €40 million. Even if we are well positioned, probably better than any of our Nordic peers, for rising interest rates or a steepening yield curve, this buffer buildup is necessary as it is likely that the interest rates stay low still for a while. This can of course be seen in our low running yields in our fixed income portfolios.

In If, the running yield is 1.7% but net of currency hedging at only below 1.5%. Likewise, in Mandatum Life, the running yield is 3.3% and net of hedging costs closer to 2.7%. The hedging effect has grown as we have deployed negative yielding cash into U.S. corporate bonds.

All of this good development has resulted in very strong solvency ratios for our insurance operations. Actually, the best ever numbers during Solvency II. If is at 261%, taking into account our partial internal model and Mandatum at 181%, taking into account the transition rules.

All in all, we are very confident on the prospects for the rest of the year. This best ever Q1 combined ratio at 87.4% excluding one-offs, bodes good for the rest of the year. However, given the unusually benign winter weather in all Nordic countries, let's not get too excited. These levels are not going to improve and require a very good environment to be maintained. So more of the same will prevail.

We now own more than 49%, actually I think 49.3% of the votes in Topdanmark, and we'll give the newly elected board time to settle, in their new role during Q2.

In Mandatum Life, we expect to finalize the valuation of the portfolio transferred to Danske in Q2, with a positive outcome.

Nordea has many significant projects ongoing, creating possibilities for significant value creation. During Q2, the main focus of course will be on their decision on re-domiciling the bank. All in all, given stable equity market development, I expect Sampo to perform well in line with the plan for the year. And as always, we are a dividend stock.

Jarmo Salonen {BIO 1860650 <GO>}

Thank you, Kari. And now, operator, we are ready for questions.

Q&A

Operator

Certainly. Thank you. We'll now take our first question which comes from Jakob Brink of ABG. Please go ahead, your line is open.

Q - Jakob Brink {BIO 7556154 <GO>}

Thank you very much and good afternoon. I have two questions, please. The first one is regarding the Finnish growth which again is into negative territory. Could you maybe give some more details on how we should we look at this going forward and what keeps driving it into that much negative 2.8?

The second one is a bit more overall and regarding what you just mentioned, Kari, in Nordea's headquarter decision. Could you maybe share with us some details on what would be best for Sampo, and does this even have a - or is this something that will impact Nordea's decision, i.e. what countries would they headquarter in? Many thanks.

A - Kari Henrik Stadigh {BIO 1504152 <GO>}

On the (07:39), firstly, of course, there is the effect of the still fairly low growth in the Finnish economy, so that gives an effect on the commercial and their corporate business. In addition to that, we have lost some market share particularly within the retail motor business driven by price competition basically, a lot of marketing from some of our competitors.

A - Ricard Wennerklint

On Nordea, I don't think that we, as an owner, has any other agenda than creating shareholder value. So as the company, as Nordea has publicly said, they are going to do a very thorough analysis on what is in the best interest of the company, its operations and its shareholders. And probably they are going to come out before summer holidays. So this is just a decision with no emotions.

Q - Jakob Brink {BIO 7556154 <GO>}

Okay. Thank you.

Operator

Thank you. We'll now move to our next question which comes from Thomas Seidl of Bernstein. Please go ahead.

Q - Thomas Seidl {BIO 17755912 <GO>}

Yeah. Thank you. Good afternoon. Three questions first on capital €159 million group solvency, if I pick on this number, but I can look at any other capital number, this translates into a minimum excess capital of €2 billion. So should we expect management to do something about this over the next one or two years or do you just leave it at this very high level, and from here, probably only increasing?

Second question, P&C, when I look at the P&L investment income up 45% but fixed income running yield down as you mentioned 10 bps to 1.7 bps. But does that mean we have seen another quarter of pretty high realized gains presumably equities? And the third point, when I look at the reserve release in the P&C business, you still report, as I understand numbers correctly, 1% release, setting off 6.7% headwinds. So in reality, you have released 7.7% and hence going forward should we now expect much higher reserve releases going forward?

A - Kari Henrik Stadigh {BIO 1504152 <GO>}

And maybe on start on capital, you - Thomas, you're well aware of that we have a tradition of being strongly capitalized, and we want to continue to be strongly capitalized in order to be able to react if there are opportunities in the market. In an overheated equity market, there are not that many opportunities, but this will not be just a straight line going forward. There will be ups and downs. So we want to maintain a strong capital buffer.

Luckily, you didn't (10:37) anything about the dividends in the same sentence. So that also gives us some room to maintain our stance that every year, we propose an increasing dividend.

Q - Thomas Seidl {BIO 17755912 <GO>}

Sure. And in terms of opportunities, is it fair to assume you stick within the Nordics maybe adding Poland as a potential region?

A - Kari Henrik Stadigh {BIO 1504152 <GO>}

No, actually, we have – if you remember both the insurance business and the bank have exited Poland. So, I wouldn't keep Poland on the map. We concentrate on the Nordics. And last year, you could see us increasing our leverage marginally when we increased our shareholding in Topdanmark to 49.3%. So, if there are opportunities that are correctly priced so that we can create shareholder value, then we do it.

Q - Thomas Seidl {BIO 17755912 <GO>}

Okay. Thanks.

A - Ricard Wennerklint

(11:38) 7.7% that you came up with is a very high number and it's not something that should be used as a guide for future run-off results. The net prior-year gain that we see this quarter is, however, a good indication of where we expect to be if inflation continued to stay low. So, around €50 million is not a surprising net prior-year gain of an individual quarter.

Q - Thomas Seidl {BIO 17755912 <GO>}

Yeah. But is rising interest rate and the very low discount rate you have in all these markets, I guess, beyond this normal run of €50 million, you could add a little bit from a rising interest rate?

A - Kari Henrik Stadigh {BIO 1504152 <GO>}

Before Richard – Ricard answers, I just want to comment that it's very clear that as a stock, we are better geared and hedged against rising interest rate or a steepening yield curve than any of our competitors because we have the low – short portfolio in our fixed income.

Then we have the discount rates really low, lower than our peers, for instance, in Finland, as I described. And then, of course, we are a significant owner in a bank which would benefit a lot from rising interest rates.

A - Ricard Wennerklint

Yeah. And in addition to that, of course, is you would see increased interest rates, that could give an effect on prior-year gains, but actually both positive and negative. So, I wouldn't change my indication of future run-off result, to be honest.

Q - Thomas Seidl {BIO 17755912 <GO>}

Okay. And on the gains in the P&C investment income?

A - Kari Henrik Stadigh {BIO 1504152 <GO>}

Well, I think that we have been targeting €50 million per quarter, and that is roughly the investment income. There's of course, some downside pressure from the running yield. So it's dependent on the equity development, but plus/minus something like that.

Q - Thomas Seidl {BIO 17755912 <GO>}

Okay. Very helpful. Thank you.

Operator

Thank you. We'll now move to our next question which comes from Paul De'Ath of RBC. Please go ahead.

Q - Paul De'Ath

Yeah. Hi there. Couple of questions, please. Firstly, on the markets in P&C. So half of your peers in Norway and Denmark have been making quite a lot of noise around the fact that there's increasing claims inflation within the motor market. Is that something that you are also seeing? And are you increasing your prices accordingly in those markets as your peers are?

And then the second question was just on Topdanmark and your holding there. And it's - you have increased the shareholding again in the quarter compared to what you've reported for the year. I'm just wondering kind of what average price you're buying it at, and you continue to have an appetite to buy more shares in Topdanmark if the price is right? Thanks.

A - Kari Henrik Stadigh {BIO 1504152 <GO>}

Let's start with the market declaring inflation in motor. Yes, higher in the first quarter than what we've seen maybe on average the last one or two years. And are we reacting with the price changes, yes, of course.

A - Ricard Wennerklint

On Topdanmark, our stance is completely unchanged. We have, for several years, been interested to increase our shareholding in Topdanmark, but only at the right price. These add-ons that we have made now, they have been on the level of DKK 177 per share. So DKK 6 below our bid price.

Q - Paul De'Ath

Okay. Thanks.

Operator

Thank you. We'll now go to our next question which comes from Michael Huttner of JPMorgan. Please go ahead.

Q - Michael Igor Huttner {BIO 1556863 <GO>}

Thank you. On the non-life combined ratio guidance which include in the quarter, my question, I suppose is really linked with Thomas Seidl's question about reserve release. If you built up this buffer in Finland of using this lower discount rate, it's something that we could see released or used maybe some time during the course of the year? In other words, could this improve the combined ratio further from this current guidance level that you have potentially?

The second question is, on the dividend outlook, you made a comment that the transaction with Danske would be attractive, at an attractive valuation and I just wondered whether, I have no idea how it could be. But I imagined since you mentioned it's in a fairly material amount, this would be - could be used for the dividend this year, or would you spread it over many years?

And then the last question which is my favorite question, my favorite - worry - and I never know how to ask it. As a management team, you've been incredibly successful and also incredibly united. I mean the core team has been together since, I don't know, 2002 or something. And my worry is always, what happens when this changed? I mean, I'm getting older, maybe in Finland people don't get older so quickly but at some stage, things change and how is this likely to impact how Sampo functions? Thank you.

A - Kari Henrik Stadigh {BIO 1504152 <GO>}

(17:34) on the first one, combined ratio, the guidance we have given is the sort of net combined ratio for this year and whether you see the changed discount rate, and the reserving changes in Finland as a buffer is, of course, fully dependent on how you see long interest rates developing.

A - Ricard Wennerklint

On the dividend side, I think that our stance is there also unchanged, that we wanted to build a dividend history and increase the dividend gradually every year. And it should be graphically beautiful, as I have said a million times (18:14) and – but we shouldn't get excited. It's not a logarithmic curve. So gradually, we are going to increase it in the coming years as well. And of course, if we get the nice sales gain from the Life portfolio, it's only a small piece in that puzzle.

However, I think the proceeds of that are going to use partly maybe internal dividends, partly it will be consumed to capitalize the Life company, and maybe they find some small add-ons where they could improve their position here in Finland. So it's threefold.

On the management team, I think it's very clear. We have worked for a long time together, but not all of us. Some – there has been some back and forth going. We have – some people have left and come back and some new recruitment. So my stance is the following. I have never nominated anyone who is not better than myself. So I think that if my colleagues have followed this principle, there are excellent successor for each and every one of us.

So if some of us would be left under a car, there is a person of the same or better quality waiting. So we have a very detailed succession plan. Actually this morning, we had the Sampo P&C board meeting and this was thoroughly discussed. We normally do it once a year. So there wouldn't be any changes if (19:47) or something happens.

Q - Michael Igor Huttner {BIO 1556863 <GO>}

Great. Thank you very much. I hope nothing happens (19:53). Thank you.

A - Kari Henrik Stadigh {BIO 1504152 <GO>}

Nothing will happen.

Q - Michael Igor Huttner {BIO 1556863 <GO>}

Good.

Operator

Thank you. We'll now move to our next question which comes from Matti Ahokas of Danske Bank. Please go ahead.

Q - Matti Ahokas {BIO 2037723 <GO>}

Yes. Good afternoon. Two questions from my side, please. Firstly, on the decision to lower the discount rates for the Finnish annuities. If the interest rates seem to be kind of more or less trending up, but the annuities have to do this move now, could you a bit elaborate the reasons behind it? And the second question is, Kari, you mentioned that there were some kind of hedges in the fixed income portfolio. So the running yield was actually higher than it would have. How long will these hedges kind of continue or how long do you plan them to continue? Thanks.

A - Kari Henrik Stadigh {BIO 1504152 <GO>}

On the discount rates, I think there are many reasons. One is the continued level of very low interest rates. One is that we want to be fully reserved. And the third is that of course we have the possibility due to very good results and very strong balance sheet.

A - Ricard Wennerklint

Yeah, actually the – yeah, running yields are lower. So even if we deploy cash which yields maybe minus 0.4 or something even if we deploy that cash now in U.S. corporate bonds. Yes, there is a

yield pickup even after the hedging costs but at the same time, for instance, our high yielders are maturing.

So therefore, the running yields are actually lower than what were mentioned. So, if I repeat it, it was 1.7% running yield in If and it actually is below - after hedging cost below 1.5%. And in Mandatum, it was 3.3% and after hedging costs it's somewhere 2.6%, 2.7%. 2.7%, yes.

The hedges are in place as long as we have the dollar-denominated bonds unless we want to open a dollar position. So it's more a tactical issue here.

Q - Matti Ahokas {BIO 2037723 <GO>}

Great. If I just may have a follow up on the investment as well as the fixed income yield was very strong both in Mandatum Life and If. What was the reason for this interest rates haven't really kind of - or at least the level hasn't changed that much. How was it so strong?

A - Kari Henrik Stadigh {BIO 1504152 <GO>}

It's mainly the short duration in Sweden, and that - I would assume that's the main and probably the spreads have tightened also on the credit side.

A - Ricard Wennerklint

Yeah.

Q - Matti Ahokas {BIO 2037723 <GO>}

Okay. Thanks.

Operator

Thank you. We'll now move to the next question which comes from Janet Demir of Morgan Stanley. Please go ahead.

Q - Janet Demir {BIO 19462264 <GO>}

Hi. Thanks for taking my questions. Three questions from me, please. Just a follow up on the discount rates, I was wondering, is there a minimum discount rate required by the regulator or has all of that movement been at your discretion?

Secondly, you've given the running yields for P&C and Life, would you be able to give us an idea of the reinvestment yield as well, please, and where you're investing new money. Are you trying to pick up yield anywhere? And thirdly, just a follow-up on the Finnish motor market share. I was wondering if you have any plans to address the loss of market share, or do you think that your peers are actually being irrational in their pricing? Thank you.

A - Kari Henrik Stadigh {BIO 1504152 <GO>}

On the discount rate (23:53-24:00) and let me address the motor market share at the same time. Of course, we're planning to address this. However, we want to do it with the right prices.

Currently, in Finland, there's a lot of turmoil in the motor market with a lot of discounts being given left, right, and center. So, we are staying a bit on the sideline currently, but we're definitely planning to address this.

A - Ricard Wennerklint

On the running yield, I think that we have seen the running yield trailing downwards. But what is our reinvestment yield that is so dependent on what we invest. So, I think that you have a market view

which is as good as mine. There is nothing I can really add on this because it depends so much on what we find in the market.

Q - Janet Demir {BIO 19462264 <GO>}

All right. Thank you.

Operator

Thank you. We'll now take our next question will come from Vinit Malhotra of Mediobanca. Please go ahead.

Q - Vinit Malhotra {BIO 16184491 <GO>}

Yes. Gentlemen, good afternoon. Thank you very much. Just looking at the large losses being worse. I mean, over the last, say, nine quarters or 10 quarters, it's been roughly half the time it's been worse and half the time it's been better. So, that evens it out. But in the fourth quarter, we were discussing probably on the one-off settlement. Is there something that is remarkable in the first quarter as well also? I'm asking because the peers have not been reporting very big losses. So that's the first question on large losses.

Second question is on the reserve releases which were sort of very high after the Finnish discounting, those reserve releases, is it a fair understanding they're mostly Norwegian motor, maybe body injury? Is that still the source of these reserve releases in your case? Thank you.

A - Kari Henrik Stadigh {BIO 1504152 <GO>}

Actually, it's not Torbjörn who is here. It's Ricard Wennerklint, the Deputy CEO. But, Ric, go ahead.

Q - Vinit Malhotra {BIO 16184491 <GO>}

Oh, I'm sorry. I'm sorry.

A - Ricard Wennerklint

That's fine. First on the large losses, the number you get in the interim report, that's on the current year large losses. Then of course there's always movement in prior years. And that has, to some extent, influenced the first quarter, but nothing really to be treated as a one-off.

Secondly, reserve releases, Norway, yes, it's workers compensation and motor business, primarily.

Q - Vinit Malhotra {BIO 16184491 <GO>}

And with motor body injury being very low? Is that the trend? That's the correct understanding?

A - Ricard Wennerklint

The reason is, of course, that we have had two high reserves. And the reason for that is that we have been continually surprised by low inflation and, to some extent, falling frequencies.

Q - Vinit Malhotra {BIO 16184491 <GO>}

Okay. All right. Thank you very much.

Operator

Thank you. We'll now take our next question which comes from Blair Stewart of Bank The next question which comes from Blair Stewart of Bank of America. Please go ahead.

Q - Blair Stewart {BIO 4191309 <GO>}

Thank you and good afternoon. I think three, mainly follow-ups really. Firstly, Ricard. Just on the combined ratio, you said a very strong underlying combined ratio but it was helped by some very good weather in the quarter. I just wonder if it's possible to give some indication as to how the good weather impacted the underlying?

Secondly, just coming back to the motor market share loss. Is that only in Finland or is it more widespread? And you talked about taking some actions to address that. I just wondered if you could give a bit more detail on what those actions might be?

And finally, possibly for you, Kari. On the Life disposal, you talked about getting some news on that in Q2. I just wondered if you can give an indication as to how the discussions have been going relative to your initial expectations, either plus or minus? Thank you.

A - Ricard Wennerklint

Let's start with the weather in the first quarter. Yes, it was a very good winter season from insurance perspective in the first quarter. Very difficult to estimate but let's put it to the tune of 1% of combined ratio. Secondly, motor Finland, yeah, the competition in the motor business has been primarily in Finland. It's only in the retail segment, in the private segment. And the actions will be actually of several different types. It will be marketing, product changes and to some extent, new tariff, new pricing strategy.

A - Kari Henrik Stadigh {BIO 1504152 <GO>}

On Life, the portfolio transfer has been proceeding on the valuation of the portfolio transfer. The work has been done by outside valuator, and it has contained no surprises. It has gone exactly as planned and we will come back to this in Q2.

Q - Blair Stewart {BIO 4191309 <GO>}

Great. Thank you very much, gentlemen.

Operator

Thank you. We'll now take our next question from Steven Haywood of HSBC. Please go ahead.

Q - Steven Haywood {BIO 15743259 <GO>}

Good afternoon, everyone. The 87% to 90% combined ratio guidance, can you just give your thinking behind this guidance for the full year 2017? And considering that the first quarter combined ratio was near the bottom of the range, are you saying that combined ratio for the rest of the year should deteriorate? And then on your sort of branchification of If, is there any progress or any further discussions on moving some of the subsidiaries to branches? Thank you.

A - Kari Henrik Stadigh {BIO 1504152 <GO>}

On the guidance, yes, the first quarter was a very good winter quarter. And we can't really expect the weather to help us for the rest of the year. And we had some prior-year gains. So, of course, we try to stay conservative. But we can't really hope that the weather will help us with our guidance. I guess that explains the guidance.

Your second question on branchification, we're doing a change from the subsidiary we have in Finland to make that a branch out of our Swedish insurance company. Apart from that, no plans to change anything in the lead structure.

Q - Steven Haywood {BIO 15743259 <GO>}

Okay. Thanks very much.

Operator

Thank you. As there is no further question at this time, so now I'll hand it back to your speakers for any additional or closing remarks.

A - Kari Henrik Stadigh {BIO 1504152 <GO>}

Thank you all for your attention. Have a good evening.

Operator

Thank you ladies and gentlemen. That concludes today's conference call. Thank you for your participation. You may now disconnect.

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