

Q4 2014 Earnings Call

Company Participants

- Lars Møller, Director-Investor Relations
- Morten Hübbe, Chief Executive Officer
- Tor Magne Lønnum, Chief Financial Officer

Other Participants

- Christian Hede, Analyst
- Gianandrea Roberti, Analyst
- In-Young Chung, Analyst
- Jakob Brink, Analyst
- Mika Koskinen, Analyst
- Paris Hadjiantonis, Analyst
- Per Grønborg, Analyst

MANAGEMENT DISCUSSION SECTION

Lars Møller

Yes. Good morning, everyone. This is Lars Møller, Head of IR at Tryg. And we are here to present our Q4 and Annual Result for 2014. And with me today, I have our CEO, Morten Hübbe; and our CFO, Tor Lønnum, with me.

And with this short introduction, over to you, Morten, please.

Morten Hübbe

Thank you, Lars. And if we turn to slide three, we're pleased to announce the best fourth quarter since Tryg IPO'd some 10 years ago. With a combined ratio of 83.7%, we increased the technical result in the quarter by some 40% and for the full year some 22%. Of course, the quarter has been helped by some DKK300 million lower weather claims, as well as higher run-off gains. On the other hand, we've had roughly DKK150 million higher large claims year-on-year in the quarter.

Clearly, the underlying main driver is our efficiency programme, which now has resulted in almost DKK1 billion. And also, we see that despite a write-down of our domicile premises of roughly DKK100 million, also our pre-tax result is up some 20%. If we look at the top-line for the fourth quarter year-on-year, it was down 2.4% in the fourth quarter 2013 and down 0.1% in 2014 fourth quarter. So, we're stepping in the right direction, but,

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realistically, we're expecting also pluses and minuses on the top-line in 2015 and then in 2016 a more stable top-line around the inflation level.

If we turn to slide four and we'll look at the full year. As I mentioned, technical result is up some 22% or more than DKK500 million. Clearly, we had a helping hand from the one-off gains relating to Norwegian pensions in Q2 of some DKK135 million. We improved the combined ratio 3.5 percentage points for the full year.

The top-line improved from minus 2.7% in 2013 to minus 1.1% in 2014. So, clearly, not finalized, but a step in the right direction. We delivered return on the equity of 23% post-tax. And we suggest to the AGM an improvement of the dividend from DKK27 per share last year to DKK29 per share and also a split of our share in 1:5 at the AGM.

If we turn to slide five, we point some of the main events in 2014. Clearly, the most important probably is that, at the Capital Markets Day, after successfully delivering DKK950 million of savings in the old efficiency programme, we target a new DKK750 million of efficiency measures towards 2017. At the same time, we've set ambitious targets for our customer development in a fashion that makes customers and earnings go hand-in-hand, by focusing on customer loyalty, customer satisfaction and the amount of products per customer to become broader.

We also decided to do another DKK1 billion of buybacks programme in 2015. We shifted our provider of IT maintenance during 2014. And we've made significant progress in our project of price differentiation and also build upon that our customer lifetime value initiatives to make sure that we continuously improve the quality of our portfolio, as well as our competitive position.

If we look at slide six, we see how the four different business areas contribute to the earnings improvement. And there's no doubt that the two main drivers has been Private lines, our biggest business areas, with a combined rate of 82.5% and also an improvement of 21% in the technical result and, clearly, an improved trend on the top-line and customer development in Private lines; and also, the second driver, Commercial, with a combined ratio just below 80%, an improvement of the technical result of more than 30%.

I guess elevating Commercial from an area which is just four years, five years back actually didn't have any positive technical result to now a significant result of DKK785 million, but clearly further behind Private lines in terms of top-line. Sweden and Corporate also at satisfactory levels of around 92% in Sweden and some 89% in Corporate.

If we turn to slide seven, we show our strategic initiatives for 2015. We are not exactly inventing the wheel with four new initiatives, but rather building upon the four previous and I would say successful recipes we've used in 2014. We will further enhance our price differentiation. Being historically an old mutual company, we still have significant potential to improve our price differentiation and also our customer lifetime value modeling.

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Number two, our customer experience. We will further enhance our focus on increasing the Net Promoter Score, our customer retention rate and the number of products. And, clearly, we see that as an important driver also of efficiency and of earnings quality.

Leading in efficiency covers our new efficiency measure of DKK750 million on claims procurement and on costs, which will be the main driver of earnings improvements in the coming year. And also, we see IT stability continues to being important, adding upon that further focus on digitalization, which will enhance sales, service and efficiency, helping the cost measure as well.

On slide eight, we show the quarterly improvement in efficiency. We delivered some DKK117 million in the quarter. On claims, particularly in property, but also workers' comp, we see a positive impact. In the cost side, we see working with IT sourcing, but also, at the moment, working with finance sourcing will be drivers of earnings improvement. And then we see the fact that we've done more digitalized communication with our customers, have reduced our cost as well.

On slide nine, we show our continued focused on reducing the cost ratio. If we look at the full year, the 14.6% cost ratio looks very promising, but bear in mind the one-off impact of DKK135 million from Q2. And if you adjust for that, the full year is at 15.3%, an improvement of 0.3%, but still further improvement we will take during the coming years.

If we look at the quarter in isolation have improved year-on-year from 15.4% to 14.9%, which we think is a strong level for Q4. And we see that we have further reduced the number of headcounts by 161 people, excluding the purchase of Securator.

And then if we turn to slide 11, we elaborate slightly on how the four business areas contribute, both to the technical result and the top-line. And, clearly, if you look at the annual numbers, Private lines now reaching a technical result of DKK1.6 billion, worth mentioning, Commercial lines DKK875 million. And, clearly, those are the main drivers of improving the technical result.

If we look at the top-line, Private improves the most together with Corporate, Private from minus 2.2% to 0%, Corporate from minus almost 3% to a plus of just about 1%. And, clearly, if we turn to the quarterly numbers, we see that the underlying improvement in claims are mainly from Private and Corporate. And we see that the top-line improves gradually to minus 0.1%.

And then over to you, Tor.

Tor Magne Lønnum

Thank you, Morten. If we continue on slide number 12 and look at customer retention, we can see that there is a continued, positive development in Private Denmark, up to 89.6% in retention level. We see that there is a small reduction in Norway. We see that on the Commercial lines, there is a positive development in Denmark, an improvement, whereas you can see that there is a decline in the Norwegian market. Although you can still see

that the decline is coming after a long period of improving the retention rate and thus should be considered more as a normal fluctuation.

If you look at slide number 13 and look at the development in average premium, you can see that there is a continued, positive development in average premiums in Norway, both for house product and for the motor product. In terms of the motor product in Denmark, you can see that there is a weaker development. It's a negative development in average premium.

There are a few drivers in terms of the average premium. It's related to competitive pressure and discounts. But it's also related to the fact that as we have mentioned for a number of quarters that there is people moving to smaller and safer cost.

In terms of the underlying claims ratio, as is mentioned on the slide, we actually see that there is a significant drop in the claims ratio as well. So profitability is sustained. In Q1, we will introduce a new car tariff, which we think will actually improve our situation in terms of market, being able to sustain our market position.

If we move on to slide number 14 and talking about Private Sweden. You can see that the Sweden retention level are more or less on a normal level. We see that the Nordea portfolio, as is shown isolated, has moved more or less back to what you can see is the average for the portfolio and really indicates that the pressure we had on the portfolio in the beginning seems to be leveling out. In terms of the profit development, it's slightly weak result in Q4. It's due to seasonality and some one-off effects. Among others, we have some significant run-off gains in the quarter last year.

If we move on to slide number 16 and looking at the claims development. As I think Morten mentioned earlier, we see that we have an underlying improvement overall in the quarter by 0.3% overall. We see that there is a 1.8 percentage point improvement for the full year. And, in particular, I'd highlight the fact that we do have an improvement of 1 percentage point in Private.

If you look at the Corporate, Commercial and Sweden, it's a more mixed picture. You see that there are some weakening in terms of Commercial and Sweden, some improvement in Corporate, although I would call it more normal fluctuations, in particular, Commercial coming from a very low level.

If we move onto slide number 17 and look at large claims, weather claims and run-off. As Morten mentioned, there is a significant increase in large claims this quarter, up DKK150 million. We see that there are a couple of particular types of business that have that kind of claim. It's related to seismic and it's also related to fish farming, although we don't see it as a particular negative trend.

If you look at the weather-related claims, as Morten mentioned, of course, there was a significant drop in weather-related claims, some DKK300 million. I would highlight though that if we move into 2015, we have seen significant storms both in Norway and Denmark here in January. So, I'd say that it's more or less accidental whether it's on this

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side of New Year's Eve or on the other side. And we do see that there are claims in the area of slightly above DKK100 million related to the storms here in January.

If we look at the run-off gains, you see that there are slightly higher run-off gain this quarter. It's actually 7% run-off gain which elevates the run-off gains to approximately 6% for the full year. Going forward, as we communicated on our Capital Markets Day in November, we will see a likely higher probability of run-off gains. Historically, the run-off gain has been in the area of 4% to 6%, whereas we, for the next strategy period, expect run-off to fluctuate around the current full year level.

If we move onto slide number 19 and look at the investment results. We had a good performance in equity prices in the fourth quarter, although relatively volatile. So we actually realized a 3% return on the equities which elevated the equity return for the full year to 10%. As Morten mentioned, the portfolio is, of course, impacted by the write-down of the domicile here in Copenhagen which reduces the return by slightly less than 1%.

If we move to slide number 20 and look at the capital structure, there is a continued, positive development in the capital buffer. It's at 51% despite the increased dividend that Morten mentioned. We have initiated the buyback programme and you see more or less weekly or the weekly reporting related to that. And, finally, I'd mention that the equity development, as you can see, is more or less stable. So a solid capital development as well.

And with that, I'll leave it back to you, Morten.

Morten Hübbe

Thank you, Tor. And just our last slide, on slide 21, where we reiterate our new financial targets as we stated them at the Capital Markets Day. For 2017, we have an ROE target after tax to be at or above 21%, at very low interest rate levels. We might add a target to reach a combined ratio at or below 87% and a target to reach an expense ratio at or below 14%.

Clearly, the main drivers will be our efficiency programme of DKK750 million for the coming period until 2017. But also our work with price differentiation will add to the quality and the margin in our portfolio, together with working with the customer experience, enhancing the customer loyalty, enhancing the broadness of the product coverage and also improving on the lifetime value and selection of these customers, and all-in-all to make sure that we continue a positive trend and the positive earnings momentum in the coming years.

And with that, we'll turn over to your questions.

Lars Møller

Operator, please.

Q&A

Operator

We have the first question from Mr. Per Grønberg from Danske Markets. Please go ahead, sir.

Q - Per Grønberg

Yes. Good morning. Impressive results. I just have a single question that I would like some comments on. If I look at the segments, I see that your combined rate, I think it was 27% on workers' compensation. Can you give some comment upon that? I guess it's primarily a prior year gain that is rolling it down to this level.

A - Tor Magne Lønnum

Yes. Per, that is correct. And, of course, when you look at the higher level of run-off this quarter, it's primarily workers' comp being a source. I'd just add to that comment that you also see some variances in terms of where the run-off result is stemming from. So you've probably seen that there are slightly higher run-off in Denmark, whereas it's actually a bit lower in Norway. So, of course, that impacts the geographical segments that you commented on.

Q - Per Grønberg

How much are there – I guess this is still related to the changed liability law back in 2004. How much are there still to roll back on the liability line or are you more or less in place now?

A - Morten Hübbe

I think you can both, Per, look at the liability law change but also the general margin on workers' comp also in older years than that. And I think we have sizable positive margins on both. And I think it's fair to say in the higher expected mean of fluctuating run-offs in the coming years, workers' comp will continue to be a significant driver of that.

Q - Per Grønberg

Okay. Thank you.

Operator

Our next question comes from Mr. Gianandrea Roberti from Carnegie. No. Excuse me. Next question is from Mr. Jakob Brink from ABG. Please go ahead.

Q - Jakob Brink {BIO 7556154 <GO>}

Yeah. I just have one follow-up question on Per's question, actually on run-off gains. I mean, historically, you've been talking about – I mean when you do your claims estimate then you have, let's say, a best estimate of DKK100 million and then you add a buffer of

DKK7 million. But you're now talking about a sustainable higher level of run-off gains. Is it then only coming from prior years over-reserving on workers' compensation in motor or is it also because that DKK100 million - the best estimate is actually too high that your models may be not factoring in inflation good enough or low inflation or what exactly is going on?

A - Tor Magne Lønnum

Yeah. Jakob, I think, first and foremost, to make sure that there aren't any misunderstandings, we are saying the same today as we did at our Capital Markets Day in November which is that we do expect a higher level of run-off gains in the strategy period. I.e., there is no infinity in terms of - or perpetuity in terms of run-off gains. On the contrary, of course, we do factor in a margin on the reserves, as you commented yourself. But it's important for us to say that it's not like we are saying that the current run-off level is something that will run into perpetuity.

Although I would add to the latter comment that when we look at the development in terms of margin, clearly, there has been - and that has been a continued trend that you all know about the fact that sort of the early vintages of the 2000s have shown a very favorable development. And that is something that we have continued to see for both in Denmark and Norway.

Q - Jakob Brink {BIO 7556154 <GO>}

Okay. Thanks, I guess. Thank you.

Operator

Now we have Mr. Gianandrea Roberti from Carnegie. Please go ahead, sir.

Q - Gianandrea Roberti {BIO 6786731 <GO>}

Yes. Good morning from me as well. I have three little question. The first one just to make sure I have got my number right. You have done DKK952 million out of the DKK1 billion old savings plan. And then when I look at the new savings plan, I think you mentioned before the DKK415 million we should expect DKK125 million out of the DKK750 million. Do I need to add the DKK48 million missing from the old savings plan or that goes in the DKK125 million? That's the first question.

My second question is that you mentioned that the claims ratio in motor Denmark is down 5% during 2013 and 2014. By the way, I like the word profitability sustained. It's probably a little bit more than sustained on that point. Does it mean that the combined ratio in motor Denmark is down 500 bps from the end of 2012 to the end of 2014 or it's actually down 1,000 bps? Can you clarify that? And also how has that developed in Norway? That would be quite interesting.

And the last question that I have, it's on the sideways reinsurance agreement. I think you had around DKK150 million in that agreement as per Q3 and few nasty weather has been

hit in Q4 and Q1. Can you just tell me how much you have so far under that agreement?
Thank you.

A - Tor Magne Lønnum

Yeah. Gianandrea, to question number one, yes, the remaining DKK50 million will come in - will be factored into the savings which is planned for the coming three years, i.e., it will be a part of the DKK125 million. And so that will be a part of the programme going forward. In terms of the last question, can you repeat that, please?

A - Morten Hübbe

Sideways.

A - Tor Magne Lønnum

The sideways cover, sorry. In terms of the sideways cover, yes, we do expect to get some recovery on the storms that we had here in January. I think you'll find in the annual report that we comment that there is somewhere around DKK80 million left before we get into the cover. So that will give you sort of at least an overview of what's going on around the reinsurance agreement.

A - Morten Hübbe

And I guess the DKK80 million that was left before we earn the money on the sideways cover, Gianandrea, is a 1 of January number. So prior to the -

Q - Gianandrea Roberti {BIO 6786731 <GO>}

Basically, if I assume that the storm has cost you DKK80 million, you are in a way home free or larger weather event until the 1 of July. That's the right way of thinking, correct, or -

A - Morten Hübbe

That's probably your wording and not ours but you are correct in the math.

Q - Gianandrea Roberti {BIO 6786731 <GO>}

Okay. Thanks.

Operator

Our next question comes from Mr. (24:42) from Exane Paribas. Please go ahead, sir.

Q - Lars Møller

Yes. Good morning, all. Guillaume (24:48) from Exane. I have a question on the foundation. Even though it's not in your hands, could you provide us with an update on anything you know and on the potential timing for discussions regarding the adaption of a policyholder dividend model? Has anything changed or has been accelerated compared to when you commented at the CMD last November? Thanks.

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A - Morten Hübbe

Well, I can comment on that. I guess the process is that the group of 70 representatives have during 2014 been working to find different modeling to do a customer bonus model, including solving the question that part of their historical fortune has been built also from Nordea life and how would that be handled in the process.

The process is now that they have the next discussion of this topic during February. Then they read or they look at the discussion again in March. So, I think the earliest possible decision could be in the middle of March, but I think it's a democratic process with 70 people involved. So, we need to have some respect for that process, but the earliest decision possibility, as I see it, is in the middle of March.

Q - Lars Møller

Okay. Thanks very much.

Operator

Next question is coming from Mr. Bin-Young (sic) [In-Young] (26:29) Chung. Please go ahead, sir.

Q - In-Young Chung

Hello. This is In-Young from Goldman Sachs speaking. So just one quick question on Sweden. We see that the Nordea portfolio retention is up and ex-Securator the premium change in the quarter seems to be about minus 5%. So do you have any comment on the Swedish portfolio, ex-Nordea? That, I think, up to 3Q was developing fairly okay. So, yes, just a question on Sweden, please.

A - Tor Magne Lønnum

Yeah. I think it's a mixed picture related to Sweden. As we comment, the Nordea portfolio is developing positively. We do have two other affinity agreements that have been terminated that will impact the revenues in 2015. And despite that, we actually see that the sales there in Q4 has been relatively good. So, it means that, for the full year, Sweden will probably be negative, but not as negative as we had expected. Based on that, I would reiterate what Morten said that for the full year 2015, the top-line guidance is between negative 1% and up to neutral. So exactly the same as we said on our Capital Markets Day.

Q - In-Young Chung

Sure. So the minus 1% to neutral, that's on a group level, isn't it, rather than for Sweden?

A - Tor Magne Lønnum

Correct.

Q - In-Young Chung

Yeah. Yeah. Thank you.

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Operator

Next question is coming from Mr. Christian Hede from Nordea. Please go ahead.

Q - Christian Hede {BIO 18642300 <GO>}

Yes. Good morning. This is Christian from Nordea in Copenhagen. I just have a question on your capital structure and I guess this is mostly a question on timing. In November, you were also talking about the option for issuing more subordinated debt when the rules are clear. So I'm basically wondering what is your best estimate for when the rules will be clear. Is that still going to be sometime mid-2015? Thank you.

A - Tor Magne Lønnum

Good morning. I think it's really difficult to say what the authorities will do or not do, because it will be based on what will happen around the regulation for the Natural Perils Pool. And we are, of course, hopeful that we should be able to give a comment about that in the first half. But to make any promises on behalf of others that we don't control, I think, is really difficult. But as you indicate, Christian, it will be important in terms of what we do related to the subordinated debt, which, as you mentioned, have a call date in November, December this year.

A - Morten Hübbe

So, I guess, Christian, you can conclude that hopefully we have news on the Perils Pool prior to November, but the actual call date of the existing sub debt is November. So, I guess, the latest timing where we will make a change would be Q4 2015.

Q - Christian Hede {BIO 18642300 <GO>}

Okay. Thank you very much.

Operator

The next question is coming from Mr. Mika Koskinen from SEB. Please go ahead, sir.

Q - Mika Koskinen {BIO 1557965 <GO>}

Yes. Good morning. Thanks for taking the question. I only have a very simple question on the investment income and relating to your write-down that you made on the domicile. Should I read this that, excluding the write-down, of course, your investment income had been DKK106 million higher? Would that have been a kind of normalized or normalized level of investment income or whether other one-offs impacting the investment income in one direction or the other?

And then, as I'm totally new or fairly new to the company, a question to you. Was this write-down communicated in before a year, was the underlying investment income actually a fair amount better than the consensus expectation was, if we adjust for the write-down?

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A - Tor Magne Lønnum

Yeah. Good morning. I think, first and foremost, yes, the DKK106 million had an impact on investment result, as you say, in Q4. Whether or not Q4 was normal, it's really difficult to answer. What I can say is that, as I mentioned, we had 3% return on equities isolated in Q4, i.e., 10% full year. And our expectations in terms of return on equities are 7% for the full year and it's at 6% on real estate. So, we do try to give some guidance in terms of the normalized investment result. What I'd highlight is, of course, the fact that we have seen a new interest rate drop and, of course, that will have an impact on our investment return going forward.

Q - Mika Koskinen {BIO 1557965 <GO>}

Absolutely. Okay. That's fair enough. Thanks very much.

Operator

We have the next question from Mr. Paris Hadjiantonis from KBW. Please go ahead, sir.

Q - Paris Hadjiantonis {BIO 19703051 <GO>}

Yes. Good morning. Excellent set of numbers today. I was wondering if you could comment a bit on the impact that the FX movements and basically the depreciation of the Norwegian currency is going to have on your earnings capital and growth for next year and the years after. And if you could also explain the lower tax rate that we saw in this quarter. Thank you.

A - Tor Magne Lønnum

Yeah. If you take the FX movement, first, I guess, first and foremost, it's important to understand that we try to hedge the currency risk related to the equity exposed in the Norwegian branch. So capital movements overall should be more or less neutral. It's not a perfect hedge, but it should be more or less neutral. We do see some deviations there.

In terms of overall impact related to profit with the current level of exchange rates against the Norwegian krone, it could have - if we hypothetically say that it stay at the same level for the full year, it could have a DKK50 million impact on the profit level. So it's not a very significant number.

In terms of the tax rate, it's clearly impacted by the fact that equities have been a major driver for investment return. And that actually impacts the tax rate significantly for the full year and also for the quarter. So, that's the main deviation point in terms of the tax rates.

A - Morten Hübbe

We might add that, I guess, for Norway, we've seen in the previous years a rather high GDP growth relative to the rest of Europe, as well as a rather high developed new car sales, et cetera. And it will be interesting to see in the coming years how the lower oil price and the impacts of the surrounding industries in Norway - how that may impact the longer term GDP development in Norway, as well as new car sales and car insurance

sales, et cetera. So, I guess, it is likely that that growth will be slightly lower in Norway in the coming years and that we'll have to work slightly harder for top-line in Norway in the coming years.

Q - Paris Hadjiantonis {BIO 19703051 <GO>}

Excellent. Thank you.

Operator

We have a follow-up question from Mr. Gianandrea Roberti. Please go ahead, sir.

Q - Gianandrea Roberti {BIO 6786731 <GO>}

Sorry, just to go back, I had a question that I don't think we discussed yet. It's the claims ratio in motor in Denmark. I didn't quite understand when you write that it's down 5% during 2013 and 2014. If that's a cumulative 5% or how should I read it? And how has that developed in Norway, if you can give us some comment as well? Thanks.

A - Tor Magne Lønnum

Yes. We haven't discussed it, Gianandrea. Sorry. I was actually going to comment on it. But the number of 5 percentage points is what you can find in and out to the annual accounts movement from 2013 to 2014. So, it's not a cumulative effect. In terms of the development in the Norwegian market, we do see the same kind of positive development in risk margin in Norway as well. So there is a sustained, good profitability in the motor product.

Q - Gianandrea Roberti {BIO 6786731 <GO>}

Tor, just to make sure I understand this correctly because I haven't seen the notes in the annual account. But, typically, you reported the product profitability on a consolidated figure, right, not on geography by product?

A - Tor Magne Lønnum

Yes.

Q - Gianandrea Roberti {BIO 6786731 <GO>}

So when you're saying the notes of the account, are you referring to the then Tryg motor book or what?

A - Tor Magne Lønnum

Yes.

Q - Gianandrea Roberti {BIO 6786731 <GO>}

Okay. Thank you.

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Operator

There are no further questions registered at this time. Please go ahead, speakers.

A - Lars Møller

Yes. Thank you very much for taking the time to call this morning here. And I just wanted to remind you that on the last page of the presentation, you can see where we'll be on the road show in the coming period. And all of us are looking very much forward to meet you around. And thank you again. And have a nice day to all of you. Thanks.

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