

Q3 2017 Earnings Call

Company Participants

- Christian Sagild, Chief Executive Officer & CEO of Topdanmark Forsikring
- Lars Thykier, Chief Financial Officer & CFO of Topdanmark Forsikring

Other Participants

- Asbjørn Nicholas Mørk, Analyst
- James R. Oram, Analyst
- Paul De'Ath, Analyst
- Per Grønborg, Analyst
- Steven Haywood, Analyst
- Vinit Malhotra, Analyst
- Wajahat Rizvi, Analyst

MANAGEMENT DISCUSSION SECTION

Operator

Good afternoon, ladies and gentlemen. Thank you for standing by, and welcome to the Topdanmark Q3 Results Conference Call. At this time, all participants are in a listen-only mode. There will be a presentation followed by a question-and-answer session. I must advise you, the conference is being recorded today, Thursday, the 26th of October 2017.

And I would now like to hand to your presenter today, to Christian Sagild. Please go ahead, sir.

Christian Sagild {BIO 15093649 <GO>}

Thank you. Good afternoon, everybody, and good morning to the USA. And thank you for joining us in this conference call. With me are, as usual our CFO, Lars Thykier; and Steffen Heegaard, who is Head of Investor Relations and Group Communications. We're holding this conference because earlier today we published our results for the first nine months of 2017.

And we are ready to take your questions. Please ask them one at a time.

Operator, may we have the first question, please?

Q&A

Operator

Yes, of course. Thank you very much, sir. And we do have a quite a few questions in the queue from Danske Bank, your first question comes from the line of Asbjørn Mørk. And your line is now open.

Q - Asbjørn Nicholas Mørk

Yes. Good afternoon. It's Asbjørn from Danske here. Couple of questions from my side. First of all, on the sort of the guidance for 2018 that you've given. If you could just elaborate a bit on how you

see the underlying claims ratio developing in 2018 versus 2017. If I look at your slide 4, for instance, the first three quarters of this year, it seems like claims trend other as you called is down 240 basis points versus the same period last year. I'm just wondering what is sort of the normal level here? So, how should we expect those trends to develop in 2018 and onwards? Thank you.

A - Christian Sagild {BIO 15093649 <GO>}

Well, if you take the guidance for 2018, we are taking the actual assumed combined ratio for 2017, we are adjusting for the run-offs, we're adjusting for the good weather, and then we adjust for what we call trends in combined ratio additionally. It is on slide 13 (03:23) and that is basically saying that, although we calculate what you call or what we may also have called underlying, it is basically just taking out of the equation, the weather and the run-off results. So, talking about - and large claims, of course, also. But talking about a trend that should remain low is not included in the guidance for 2018. So, you can basically say that we expect that we will revert to a normal level of those types of claims that has proven to be very beneficial in 2017.

Q - Asbjørn Nicholas Mørk

But does that also apply for, you can say, non-large claims? So, basically, fire claims and then medium-sized claims and the like?

A - Christian Sagild {BIO 15093649 <GO>}

Yes. It does.

Q - Asbjørn Nicholas Mørk

Okay. Thanks. Then on your digitalization investments in 2018, should we expect this to continue at the same level in 2019 and onwards? How should we see that?

A - Christian Sagild {BIO 15093649 <GO>}

We don't know yet. But you could expect it to continue into 2019, at least.

Q - Asbjørn Nicholas Mørk

Okay. Then on the competitive environment, how do you see - especially, I guess, on the corporate side, workers' compensation development here? How has that been in the last couple of months?

A - Christian Sagild {BIO 15093649 <GO>}

I think the competition may be slightly less aggressive than it has been.

Q - Asbjørn Nicholas Mørk

Okay. And then, a final question from my side on your life insurance. It seems like when I look at your regular premiums, that they're growing quite slowly in Q3 year-over-year, it was sort of the same we saw in Q1. Q2 was better but seems like your regular premiums are not really growing at that - at big pace while you do have a lot of growth to your single premiums.

A - Lars Thykier {BIO 16427122 <GO>}

That's true.

Q - Asbjørn Nicholas Mørk

I was just wondering if there is anything you can do to sort of revert that trend or is it something that we should be focusing on?

A - Lars Thykier {BIO 16427122 <GO>}

It's a signal for us - (05:33) I don't really know whether this is a changing trend or whether it's just a coincidence.

Q - Asbjørn Nicholas Mørk

Okay. Fair enough. That was all from my side. Thanks.

Operator

Thank you very much indeed. Now your next question comes from the line of Paul De'Ath. Please state your company name and then ask your question please, sir.

Q - Paul De'Ath

Yeah. Hi there. It's Paul De'Ath from RBC. I'll kickoff with a question on solvency if I can. The solvency ratio has gone up again and is now, I think, 239%. And you also mentioned that it's going to go up by another 13 percentage points when you issue some more debt in November. Looking at that, it looks like you've - you're going to be issuing another DKK 350 million of debt to replace around DKK 55 million that you redeemed, if I'm reading it correctly...

A - Lars Thykier {BIO 16427122 <GO>}

No. No. No. Sorry, but we are redeeming DKK 406 million and we are issuing DKK 400 million.

Q - Paul De'Ath

Okay. I guess, it still comes back to the - your solvency ratio is still pretty high for the type of business that you're running. How should we think about the capital position going forward and what you might be doing about that? I guess, that's the first question.

A - Lars Thykier {BIO 16427122 <GO>}

That is - the question that is pretty hard for us to answer. The board has not made any decisions yet. We think that, as a board of management, we think that this is a very high solvency ratio, but it's for the board of directors to decide.

Q - Paul De'Ath

Okay. I guess, we'll leave that one there. And then, my second question was just again on the 2018 guidance. Because you talked about, obviously, the 0.5% to 1% hit to the combined ratio from the digital investments, but the expense ratio is expected to stay around 16%, which is probably in line with where we are at the moment. And so, are you assuming therefore that you're going to make sort of other efficiency gains to offset the investments in digital over the next few years? Is that the right way of thinking about it?

A - Lars Thykier {BIO 16427122 <GO>}

Yeah. We are running a continuous program on efficiencies and some of the gains that we expect to achieve will only show up next year.

A - Christian Sagild {BIO 15093649 <GO>}

And also there'll be a split of the gains between what hits the costs, the expense ratio, and what hits the claims ratio.

Q - Paul De'Ath

Yeah. Sure.

A - Christian Sagild {BIO 15093649 <GO>}

Because claims and in cost (08:36) could also be lowered by investments in digitization.

Q - Paul De'Ath

Yeah. Absolutely. Thanks.

Operator

Thank you very much indeed, sir. Now your next question from HSBC comes from the line of Steven Haywood, and your line is now open, sir.

Q - Steven Haywood {BIO 15743259 <GO>}

Hello there. Just a few questions for me, please. Can you just tell me what happened to your shadow accounting in the life insurance business in this third quarter?

A - Christian Sagild {BIO 15093649 <GO>}

The shadow account is formally approaching DKK 30 million this year, but we don't expect it to have any value. So, that's the reason why we don't describe it in the text of the year report.

Q - Steven Haywood {BIO 15743259 <GO>}

Okay. Thank you. And the new tier 1 loan you're going to be issuing, can you give any details on the currency, these - whether it's fixed or floating and any idea of the coupon expected?

A - Christian Sagild {BIO 15093649 <GO>}

We have not decided on fixed or floating. We have not decided on coupon, but it will be issued in Danish Krone in rather big sizes, DKK 1 million, at least.

Q - Steven Haywood {BIO 15743259 <GO>}

Thank you. And on your run-off going forward in 2018, do you sort of - do you have any visibility on what level of run-off you expect, whether it's in amount or percentage of premiums here?

A - Christian Sagild {BIO 15093649 <GO>}

No, not really. We intend to stay conservative. That's the basic and that means that in the normal year we will probably have positive run-off.

Q - Steven Haywood {BIO 15743259 <GO>}

Okay. Thanks. And finally, just a small question on your property portfolio. The occupancy rate has fallen from 98% to 96% in the third quarter. Is there anything that has materially happened here and if majority of portfolio is owner-occupied is that occupancy 100% or is that the one that's changing.

A - Christian Sagild {BIO 15093649 <GO>}

The major part is owner-occupied. We have a few smaller properties beside of this and one on the (11:00) to refurbish it, that's why.

Q - Steven Haywood {BIO 15743259 <GO>}

Okay. Excellent. Thanks very much.

Operator

Thank you very much, sir. Now your next question from Deutsche Bank comes from the line with Wajahat Rizvi. And your line is now open, sir.

Q - Wajahat Rizvi {BIO 19928187 <GO>}

Thank you very much for taking my question. Wajahat Rizvi from Deutsche Bank. Just three quick questions from me. First is the investment in digitalization and automation, when would you expect some of those benefit to flow through in the expense ratio or do you expect most of those benefits to be completed away with time?

A - Christian Sagild {BIO 15093649 <GO>}

I think that we are already seeing the first benefits of these investments materialize in the – on the bottom line. And what was the next question?

Q - Wajahat Rizvi {BIO 19928187 <GO>}

The next question is like on underlying improvement in the loss ratio. So, we saw big improvement in the underlying loss ratio in second quarter. It seems to have reversed somewhat in third quarter and you don't expect any of that in 2018 guidance. So, can you just explain some of the drivers there? What caused that improvement and why it has turned so quickly again in this quarter?

A - Christian Sagild {BIO 15093649 <GO>}

Was that the claim's ratio or the – it was the claims ratio, okay.

Q - Wajahat Rizvi {BIO 19928187 <GO>}

Yes. Underlying claims ratio.

A - Christian Sagild {BIO 15093649 <GO>}

The claims ratio, except for large claims and weather, has been very low in the first – actually, first eight months of this year.

Q - Wajahat Rizvi {BIO 19928187 <GO>}

Yeah.

A - Christian Sagild {BIO 15093649 <GO>}

But it wasn't as good in September. And I don't really know how much you think you can interpret from this fact. It has been a very good year. We think that some of this is to cater movements in this (12:46). And some of it – but we can't be exact, we don't know which part of this may be underlying improvement and how much is just statistics.

Q - Wajahat Rizvi {BIO 19928187 <GO>}

Okay. But you're not assuming any of that in next year, even though some of it is underlying?

A - Christian Sagild {BIO 15093649 <GO>}

Yes, I am. We have decrease our forecast from 90 to 91 plus.

Q - Wajahat Rizvi {BIO 19928187 <GO>}

Yes.

A - Christian Sagild {BIO 15093649 <GO>}

Yeah. We'll – we've decreased our forecast by 1 percentage point. (13:23)

Q - Wajahat Rizvi {BIO 19928187 <GO>}

Okay. Fair enough. And finally, can I ask Lars a question on solvency. Can you give us some sense of your solvency sensitivities? It seems like - that your solvency ratio is very sensitive to interest rate movements and moves quite a lot in the quarter based on what the Danish top rates (13:39) are doing? Can you just provide us some sort of sensitivity estimates at least to interest rates?

A - Lars Thykier {BIO 16427122 <GO>}

There are lot of things that move together when we make this solvency ratio. The major variable is the loss of loss-absorption capacity with our life customers. Interest rates are important as well because the currencies we have issued are becoming more valuable when interest rates fall but as it is now, it is the collective (14:12) potential we have in the life terminal that is the most important part.

Q - Wajahat Rizvi {BIO 19928187 <GO>}

You cannot - you're not able to quantify it like, let's say, 20 bps increase in interest rates - what would the impact on SCR or group SCR be?

A - Lars Thykier {BIO 16427122 <GO>}

No. I know I can't do that.

Q - Wajahat Rizvi {BIO 19928187 <GO>}

Okay. Thank you.

Operator

Thank you very much indeed, sir. Now from Mediobanca, your next question comes from Vinit Malhotra, and your line is now open, sir.

Q - Vinit Malhotra {BIO 16184491 <GO>}

Yes, good afternoon. Thank you very much. Just on this comment on the large unprofitable customer of which, the last of them have gone away in 2016 year end. I know this was also already stated. But I'm just curious is this having some sort of a positive effect in this underlying claims ratio calculation or...

A - Christian Sagild {BIO 15093649 <GO>}

That is guesswork but we think that it will.

Q - Vinit Malhotra {BIO 16184491 <GO>}

Sorry?

A - Christian Sagild {BIO 15093649 <GO>}

I think - I say that that's guesswork. We can't really know (15:20).

Q - Vinit Malhotra {BIO 16184491 <GO>}

So, you've - okay, sorry, I can't hear you. And then the second question is if you could just update us on what's happening in the motor insurance. What do we do with the big focus in second quarter for all the companies in Nordic region? Is - has the situation calmed down or if frequency - I mean, for you, maybe never was a problem but any commentary would be very much appreciated? Thanks.

A - Christian Sagild {BIO 15093649 <GO>}

I mean, what we saw a quarter ago was a drop in the liability risk and an increase in the comprehensive risk and we haven't really seen any changes that is - have been more or less flat. So, the comments from some of our competitors in the market relating to the need to increase prices is a statement that we cannot recognize. We think that the claims inflation will be more or less in line with the index, so we don't have any need for price increases in that.

Q - Vinit Malhotra {BIO 16184491 <GO>}

All right. Fair enough. Thank you very much.

Operator

Thank you very much indeed, sir. Now from Citigroup, your next question comes from the line of James Oram. And your line is now open, sir.

Q - James R. Oram {BIO 19736003 <GO>}

Hi, good afternoon. It's James from Citi here. Two questions please. The first question, you mentioned last quarter that the fall in your solvency capital requirement is partly attributable to the rising rates in Denmark. They've dropped back down again in Q3, but we've seen another drop in the SCR. Can you give a bit of explanation of what's driving that this quarter and if that reduction in the SCR is sustainable over the next few quarters, because we've seen quite a big drop over the last year or so? That's the first question.

A - Lars Thykier {BIO 16427122 <GO>}

The drop in the SCR is due to the interest rate increase we have seen during this year and it is due to the increase in loss-absorption capacity with our large customers. The more our customers make, the bigger their buffers and the less the risk we have. So, if we see interest rates keeping at the same level as now or increasing, the SCR will decrease to some extent. And if we see a large drop in share prices for instance, then the SCR will increase.

Q - James R. Oram {BIO 19736003 <GO>}

Okay. Great. Thank you. And the second question is just going back to the guidance for next year. I appreciate there's some margin headwind from the lower premium indexing and the cost of digital investments, but your combined ratio targets have been quite conservative over the last few years, as in the initial targets. Is there a chance that that 90% to 91% combined ratio could also be conservative for next year? Thanks very much.

A - Christian Sagild {BIO 15093649 <GO>}

As we showed in one - slide 13, I think, we are reverting to 90% to 91%, which is basically saying that we think some of the very nice profitability in 2018 has been coincidental, so that's one thing. But basically, the 90% to 91% in that is an improved guidance, because last year we stated that that was excluding the investment of digitization, whereas for 2018, it's included - including the digitization investments.

A - Lars Thykier {BIO 16427122 <GO>}

It is very hard to make this kind of forecast to be reliable. If we just look at the SME market, for instance. We have had (18:53) and until 2016 (18:58) and now we have had a fantastic year in 2017. There is a lot of luck involved in this.

Q - James R. Oram {BIO 19736003 <GO>}

Great. Thanks very much.

Operator

Thank you very much indeed, sir. Before we move to our last question From SEB, you have a question from the line of Per Grønborg. And your line is now open, Per.

Q - Per Grønborg

Yes. Thank you all. I just only have a few things left. The first thing, on the guidance that you have discussed, 2018 guidance, but your 2017 guidance is it correctly understood that what you expect of earnings for Q4, that has not been impacted, looks like your guidance (19:50) on combined ratio level is totally driven by the better than previously anticipated Q3 outcome?

A - Christian Sagild {BIO 15093649 <GO>}

That's true.

Q - Per Grønborg

And that was all - that has also been the case when you upgraded the guidance here in the - after the Q2 report?

A - Lars Thykier {BIO 16427122 <GO>}

There's a slight impairment of Q4, it's not very much.

Q - Per Grønborg

Okay. perfect. Then, more to automatic, (20:12) we're seeing a shortage of manpower under construction sector seemingly becoming a larger and larger issue. Are you seeing any signs of that into your property claims that they are getting more expensive to settle? I was trying to save more money as I take into (20:30) account the higher claims inflation or how do you see this developing?

A - Christian Sagild {BIO 15093649 <GO>}

I think that it may sound a bit strange. I understand your logic perfectly, but we haven't seen price increases yet.

Q - Per Grønborg

Okay. But, that's the same as everybody else is saying. So, I just wanted to check that there were no new signals (20:51)? Thanks a lot.

A - Lars Thykier {BIO 16427122 <GO>}

Okay.

A - Christian Sagild {BIO 15093649 <GO>}

You're welcome.

Operator

Thank you, sir. And you do have a follow-up question from Vinit Malhotra. Your line is now open, sir.

Q - Vinit Malhotra {BIO 16184491 <GO>}

Yes. Thank you for the opportunity. This is just something I would need to check once that the follow-up (21:09). The - in the 1Q results, Christian, it was mentioned clearly Topdanmark's capital philosophy that is not to accumulate capital really, is that still maintained going forward? Thank you.

A - Christian Sagild {BIO 15093649 <GO>}

The strategy as far as capital distribution, is unchanged as of May 2017 when the board decided a minimum payout ratio of 70%, and here in my view the keyword is minimum, but also stated that we do not have an intention to build up unnecessary capital in the group. So, there has been no change in that, but of course we don't know exactly how the payout ratio will develop until Q4 when the board approves the Annual Report.

Q - Vinit Malhotra {BIO 16184491 <GO>}

All right. Thank you very much.

Operator

Thank you, sir. And a follow-up question now from Asbjørn Mørk. Please go ahead, sir. Your line is open.

Q - Asbjørn Nicholas Mørk

Yes, thank you. Just one follow-up on the capital model. So, if you can just guide us a bit on what kind of equity allocation you find appropriate for life insurance at this stage? You've said that there's been some change to loss-absorbing capacity throughout 2017. So, just, if you could give us any guidance on that? Thanks.

A - Lars Thykier {BIO 16427122 <GO>}

Are you asking for the complete (22:42)?

Q - Asbjørn Nicholas Mørk

Yeah. Yeah. Or, at least, in the capital model, how you would see sort of (22:48) there?

A - Lars Thykier {BIO 16427122 <GO>}

Yes. The SCI (22:50) in the last comment (22:51) is a little above DKK 1 billion. And we do not make a specific allocation of the extras between non-life and life.

Q - Asbjørn Nicholas Mørk

Okay. Thank you.

Operator

Thank you very much indeed, sir. And at this point, gentlemen, there are no further questions.

A - Christian Sagild {BIO 15093649 <GO>}

Okay. Thank you for taking the time to attending our conference. As you know, you're always welcome to call one of us if you have any further questions. We will be happy to answer them. Thank you and goodbye.

Operator

Thank you very much, indeed. And with many thanks to our speaker today. That does conclude the conference. Thank you all for participating and you may now disconnect. Speakers please stand by for me.

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