FINAL

Bloomberg Transcript

Q2 2017 Earnings Call

Company Participants

- Jarmo Salonen, Head-Investor Relations & Group Communications
- Kari Henrik Stadigh, Group Chief Executive Officer and President

Other Participants

- Ida Melvold Gjøsund, Analyst
- Janet Demir, Analyst
- Matti Ahokas, Analyst
- Paul De'Ath, Analyst
- Per Grønborg, Analyst
- Youdish Chicooree, Equity Research Analyst

MANAGEMENT DISCUSSION SECTION

Jarmo Salonen {BIO 1860650 <GO>}

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

We'll have the same procedures. As always, Kari will start with the review of second quarter developments. Before handing over to Kari, let me just remind you that you can follow this call 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, please.

Kari Henrik Stadigh {BIO 1504152 <GO>}

Thank you, Jarmo. Welcome to the conference call on my behalf as well. Sampo's insurance operations had a very strong second quarter, as usual, maybe best ever among them, the best ever combined ratio for the first six months.

P&C insurance profit before taxes was up 14% and the life insurance profit before taxes was up 23% compared to the corresponding quarter last year. Nordea published their results already a while ago and you have all seen them. So I leave that part for a possible Q&A.

On capital, in general, it is worth noting the extraordinary strong position all of our corporations enjoy. IF's Solvency II ratio with a standard model is higher than ever before at 225% and also, for Mandatum Life, the Solvency ratio with a standard model and transitional is highest ever at 205%. Nordea's ability to generate capital is also remarkable and its core Tier 1 ratio improved to an all-time high number at 19.2%. The strong capital position in all our entities, together with a very strong cash flow, our operations generate from a very good basis for a proposal to increase our dividends also next spring as planned.

I would like to finish my opening remarks with some comments on our strategic positioning. We can clearly see that our clients demand a very simple and easy access based on a digital offering. Nordea has a massive transformational project going on in this area and IF is investing more than ever in IT platform and new software. Both companies have decided to have the best digital offering available in the Nordic market. Nothing less is acceptable for market leaders with the biggest scale benefits among their peers.

In P&C insurance, specifically, IF, with the smallest branch network among its peers and the only one with the true Nordic reach, is best positioned to benefit from this development. The investments in the new platforms must also deliver gradually cost based (03:30) savings. IF has for many years been committed gradually improving cost ratio and Nordea stated in their release that their costs in 2018 would return to the level of 2016. All this, of course, based on investments in our digital future.

To conclude, our short-term outlook is very good and therefore, we have lowered our guidance for our combined ratio with one notch, but also our strategic positioning in the digital world is right in the sweet spot. So all-in-all, a dividend stock based on stable and predictable earnings as always.

Jarmo Salonen {BIO 1860650 <GO>}

Thank you, Kari, and operator, we are now ready for the questions, please.

Q&A

Operator

We'll take our first question from Ida Gjøsund with Carnegie.

Q - Ida Melvold Gjøsund

Yes, good afternoon, Ida from Carnegie here. Four questions from me, please. Firstly, on the combined ratio, on the group level, if I deduct large claims and reserve releases, the underlying combined ratio actually slightly improved in Q2 compared to the same period last year. Is this positive development coming from the price increases you have undertaken to address recent claims inflation in motor?

And secondly, on the combined ratio in the private segment, it is 1% up in Q2 year-over-year. What are the drivers of this development? And third, on the business in IF Norway, adjusting for FX effects, the underlying growth in Norway seems to be increasing. Can you elaborate a bit on what the drivers of this are?

And last, on the continued negative growth in Finland, last quarter, you mentioned price competition in the retail motor business, any updates on the market conditions, and when do you expect this to improve? Thank you.

A - Jarmo Salonen {BIO 1860650 <GO>}

Thanks for all the questions on IF P&C. We've had what I see is a very, very strong first half year this year. And the change in the combined ratio compared to last year is by non-life standards very small, but of course, it is we have improved the cost level slightly, as Kari mentioned, I think for the ninth year in a row, off the top of my head and we aim to continue to do that.

When it comes to the precise development of the claims inflation compared to rate increases, well, claims inflation is very, very low, by and large in the Nordic region, between 1.5% and 2%. And rate increases are to the same tune and the difference is so small. It is difficult to say exactly what the outcome in two decimals will be from that.

Private business area is basically the same combined ratio as last year the same period. We had more prior year gains last year than we have this year, so that's the reason for that.

Norway, your third question, that's probably the most significant development this year. We've come to the, I guess, predictable point in time where the previously aggressive newcomers to the market have been forced to stop being so aggressive. The likes of Nemi, especially Vardia, but also Storebrand are much less visible in the market and we have positive customer exchanges with them this year. And of course, we all know the background for that. If you are too aggressive over a long – protracted period of time, you run into financial difficulties, as it's pretty apparent from Vardia's development.

Finland, well, the Finnish market has gone through a half year of turbulence where there was a change in the law around motor third-party. The customers were made aware of this and have been very active in the market. The first company to adjust the product to that was LähiTapiola. They won a lot of customers in the first quarter, we came out in May and have won back a large number of those customers. And I would cautiously expect a more stable development in the Finnish market going forward than this.

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

(08:37) also that benign weather, winners always need a little bit luck also, so hasn't (08:43) the weather helped us somewhat during the first half year.

A - Jarmo Salonen {BIO 1860650 <GO>}

Yes, Kari. I was hoping you wouldn't say that, but yes, that's correct. We of course had the best winter than that we've seen in many, many years, and in addition to that, we've had a summer completely without thunderstorms and floods, which usually occur to some degree in Denmark and Norway.

Q - Ida Melvold Gjøsund

Okay. So this half year was better in terms of weather than last periods or last year?

A - Jarmo Salonen {BIO 1860650 <GO>}

I think this was the best weather year from an insurance perspective for a long, long time.

Q - Ida Melvold Gjøsund

Okay. Perfect. Many thanks.

Operator

We'll take our next question from Matti Ahokas from Danske Bank.

Q - Matti Ahokas {BIO 2037723 <GO>}

Yeah. Good afternoon. It's Matti here from Danske. A question, please, firstly, on the Swedish non-life business, (09:45) elaborate a bit on the claims development there, were there any prior year losses or what was the reason for the weaker development?

The other question is I noticed that you've stopped reporting the Solvency margin according to the partial internal model. And if you would have reported that, would that show the similar development as the rest of the group in terms of the Solvency margin or maybe what was the figure if you would have published that? Thanks.

A - Jarmo Salonen {BIO 1860650 <GO>}

On the Swedish combined ratio, first, there is no significant development there at all. We've had two large losses in Sweden in the second quarter that make the results slightly, you could say, worse, but it's still a decent combined ratio, but slightly worse than they would otherwise have been. And that's the whole reason for any change from last year.

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

On the internal model, actually, we have a partial internal model on IF Sweden. Now, when we finish the branchification of Finland, then, we will, of course, broaden the internal model for IF Finland also.

A - Jarmo Salonen {BIO 1860650 <GO>}

Which is an application that will take another six months with the Swedish authorities.

Q - Matti Ahokas {BIO 2037723 <GO>}

That was the reason you didn't publish the figure?

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

Yeah, actually, so for external purposes, there is really no need, because the standard formula, that's the one we have to use when we calculate IF Group capital position and also when we calculate Sampo Group capital position. And the relevant or the actual limiting factor in the – for IF is the rating, single A rating target.

Q - Matti Ahokas {BIO 2037723 <GO>}

Right. It would just be nice to see it anyway.

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

Okay. We can show it next week when we have the (12:00).

Operator

We'll take our next question from Paul De'Ath with RBC.

Q - Paul De'Ath

Yeah. Hi there and a couple of questions, please. Firstly, just on the combined ratio, you talked I think last quarter out being almost essentially this being a peak level of profitability and it could be difficult to maintain the combined ratio at this level. Is that still what your kind of longer-term view and if so, how long do you think you can keep it at these kind of levels? First question.

And then, the second point is just on the Solvency ratios, obviously very, very high in both IF and Mandatum. At the moment, do you have any kind of view on a target of rating range for the Solvency ratio? Do you feel that that's too high at the moment or you're quite happy for the ratio to keep moving up over time? Thanks.

A - Jarmo Salonen {BIO 1860650 <GO>}

I'll take the first question. I'm not sure I call it or anyone here call it a peak level, but I just say that inflation and rate changes are not very different from each other, and they're both very low. And of course, the expectation from that would be that the combined ratio doesn't move very quickly from where it is at the moment in the market.

I'm actually pleased with the first six months also from the perspective that Kari detailed in his first words and that's that we have been able to continue to invest in modernization, in concentration and in the web offering to our clients and that of course won't – will drive any changes for the longer future and I'm not going to speculate about how long that development will take. Other than that, we are the market leader in that development and we aim to continue to be that, together with the cost advantages that that gives us.

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

Yeah. We don't have any target levels for the Solvency ratios. I think that we are clearly over-capitalized as a group in many aspects. At this moment, we haven't had any need to optimize our capital structure. One day if that would come, then it would be different. I was today educated that some very big Central European insurance companies, they are stress testing themselves so that if they take the 2007-2008 scenario and the equity drop-off that's mainly due they would still want to maintain 135% Solvency ratio after that.

We are, of course, much, much higher than that, because the effect of a crash like that would be roughly 53% on our Solvency ratio. So if you deduct 53% from the numbers I mentioned in the beginning, we are still clearly over-capitalized. So if need be at one moment, then we have ample room to release capital or invest in something attractive.

Q - Paul De'Ath

Excellent. Thanks.

Operator

We'll take our next question from Youdish Chicooree with Autonomous Research.

Q - Youdish Chicooree {BIO 17430923 <GO>}

Good afternoon, everyone. I've got two questions, please. The first one is your main Norwegian competitor has flagged – has seen worse underlying trends in property and workers' compensation. So I was wondering whether you're seeing similar type of trends in that market. I appreciate your results are solid, but just wondering even if anecdotally you're seeing these trends.

And secondly, your fixed income running yield is now at 1.6% and I was just wondering what's the average reinvestment rate in your P&C business from fixed income at the moment. Thank you.

A - Jarmo Salonen {BIO 1860650 <GO>}

Our main competitor...

Q - Youdish Chicooree {BIO 17430923 <GO>}

Hello?

A - Jarmo Salonen {BIO 1860650 <GO>}

... (16:26) and also ourselves are seeing some competition in motor, workers' comp, maybe property, but the combined ratios in Norwegian markets are extremely low, and I don't expect them to come any lower. But we don't see any particular pressure that is new this quarter at all.

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

Reinvestment rates, I think we are below 1% depending on what we find there in different asset classes, but below 1% is the rate.

Q - Youdish Chicooree {BIO 17430923 <GO>}

Okay. Thank you very much.

Operator

We'll take our next question from Per Grønborg with SEB.

Q - Per Grønborg

Yes. Thank you. Two questions from my side. First, related to Mandatum, you are now provisioning additional €74 million for low weights (17:27). What if you should discount the full book on the Solvency II curve? How much additional would that require? That was the first question.

My second question is related to the holding company, now, we're now looking into some of the nitty-grittys, it looks like (17:44) somewhat off compared to what we saw last year. Can you give some guidance on what one way (17:50) should we expect for the holding company going forward? I'm aware that there's FX losses this quarter in the holding company.

A - Jarmo Salonen {BIO 1860650 <GO>}

On your first question full discounting with the swap curve, from the top of my head, I can't remember the number. But every 100 basis points is roughly €320 million to €330 million. So the negative effect would be big. But as you know, the guarantee book runs off roughly €200 million per year, so by the time when we have to use the normal discount rate. So Solvency II normal discount rate curve, then there is only a tail (18:37) left in Mandatum.

On the holding company level, we have – it's the dollar investments that we have. Nordea's €81 million, and of course, we saw a €20 million loss in Q2 and there probably continues to be a small loss also in Q3 because it's unhedged. But the running yield is so high, so we don't see any reason to hedge out the currency loss. But otherwise, the quarterly number was pretty normal on Q2.

And (19:18) third quarter.

It runs around €4 million to €5 million.

Q - Per Grønborg

€4 million to €5 million plus, minus?

A - Jarmo Salonen {BIO 1860650 <GO>}

Minus on the operation.

Q - Per Grønborg

Minus €4 million or €5 million? Okay. Yeah. Perfect. Thank you.

Operator

We'll take our next question from Janet Demir with Morgan Stanley.

Q - Janet Demir {BIO 19462264 <GO>}

Hi. Thank you for taking my questions. I have two, please. I was just looking at the risk ratio for Finland and I note that it has deteriorated somewhat versus last year. I wonder if you could comment whether this is just due to higher large losses or whether there's anything underlying affecting that.

And secondly, just looking at Mandatum, I wondered if you could comment on the business development there. I know premiums are down somewhat. And what is your long-term goals for the business? Thank you.

A - Jarmo Salonen {BIO 1860650 <GO>}

Especially Finland in Q1 was affected by lowering the discount rate from 1.5% to 1.2%. That's the only big effect this year and then, apart from that, actually, the risk ratio is better in Finland than last year.

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

On Mandatum, I think that we have to do a little bit of segmenting and see what the underlying businesses are. First, it has of course the consumer business which, to a large extent, will be sold or is sold to Danske. So as you remember, we agreed that they would buy the portfolio from us for €334 million. And it will take some time, because this is a portfolio transfer for this to close. It might be that it is by the end of next year – or not until the end of next year and then we deduct from this €334 million, €18 million plus per year from the purchase price, because it is producing to us more than that.

So this is one part of the business which we sold out. Then – and if you ask what is the present development, especially this part which is now sold, the volume in that part has dropped. Altogether, the volume was down 14% if I remember right. And at this moment, the volume is 50/50 divided between consumer business and corporate business.

The corporate business is something which we maintain and there we are actually the market leader in Finland. So our target is to continue to be the market leader with a big margin to the number two, we have more than 50% market share in that business in some products, up to 80%. We are going to be the leading corporate pension provider in Finland.

Then, the third leg is the wealth management business where we sell products under insurance wrappers (22:31) and also under mutual funds and that is the business which we want to grow and it is growing. There, we concentrate mainly on equities and alternatives nowadays, but we have a base in the fixed income part.

And the last leg is, of course, with profit portfolio which is in semi-run-off or run-off and there, we treat it as a hedge fund where we pay the policyholders the discount rate and we keep, as an owner, the upside. Was that...

Q - Janet Demir {BIO 19462264 <GO>}

Okay. Thank you.

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

Is that an adequate answer to your question? I hope so.

Q - Janet Demir {BIO 19462264 <GO>}

Yes, very good. Thank you.

Operator

At this time, I have no further questions in queue.

A - Jarmo Salonen {BIO 1860650 <GO>}

Thank you, operator, and thank you all for your attention. Have a very nice evening. Thank you.

Operator

And this concludes today's call. Thank you for your participation. You may now disconnect.