Q3 2015 Earnings Call

Company Participants

- Christian Sagild
- Lars Thykier

Other Participants

- Christian Hede
- In-Yong Hwang
- Jakob Brink
- Niccolo C. Dalla Palma
- Per Grønborg

MANAGEMENT DISCUSSION SECTION

Operator

Ladies and gentlemen, thank you for standing by and welcome to the Topdanmark's Results for the First Three Quarters of 2015. I must advise you the webcast is being recorded today on Monday, November 16, 2015.

I'd now like to hand the webcast over to your presenter today, Christian Sagild. Please go ahead.

Christian Sagild {BIO 15093649 <GO>}

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 are holding this conference because earlier today we published our results for the first three quarters of 2015. We are now ready to answer your questions. Please ask them one at a time.

Operator, could we have the first question, please?

Q&A

Operator

Thank you. Your first question comes from the line of Jakob Brink of ABG. Please ask your question.

Q - Jakob Brink {BIO 7556154 <GO>}

Thank you. I have some questions regarding the capital and the transfer to Solvency II. I think it was in the Q1 report you mentioned that there would be potential for expected future profits to be calculated as a percentage of Group premiums instead of the premium reserves. I was just wondering – we have heard some slightly different comments from some of your competitors. So I was just hoping if you can give us some more details on that and maybe if DFSA have guided you in connection with also the model improvement a few weeks ago on that specific topic.

And also on Solvency II, I was wondering about the discounting curve. It looks like the AOPA end of October curve is basically in line with the end of October FSA curve, is that correctly understood; i.e., that we should expect only a marginal change to the impact of discounting when going over to Solvency II?

And then, finally, on a different topic; on price changes. You mentioned earlier in the year that you would lower prices with around 5% on motor. How – what is the progress on this? Do you still need to do some of those changes or is it all basically factored in by now? Thank you.

A - Lars Thykier {BIO 16427122 <GO>}

I can recall this from the first quarter's accounts, but the basic thing when we are talking insurance contract is, that insurance contracts are regarded as an investment in Solvency II and in the future Danish accounting rules. That is that when you expense (02:40) the acquisition cost and the insurance contract is concluded, the insurance contract represent some kind of value.

The expected net cash flow of the insurance contract is discounted through the day where the accounts are made up to calculate the present value. That is that if an insurance contract is to yield a positive net cash flow of DKK 100 million over next year, we'll (03:10) in the balance sheet.

In the Solvency II balance sheet, the value of insurance contracts is booked as expected future profit and reflected in shareholders' funds. In the future Danish GAAP balance sheet, it would probably be named service margins.

Concerning the curve, you are right that the difference between the current curve and the curve we will have after January 1 is, the difference is very small, given that the company that uses the curve has asked for and got the permission to volatility adjustments. But this is – you have to apply it and we have applied but we have not got the permission yet.

A - Christian Sagild {BIO 15093649 <GO>}

Jakob, you asked about the price development in motor. What happened in Q2 was that we introduced a new motor tariff. And if you took the old motor tariff and change that into the new motor tariff, that meant a discount – a lowering average of 5%. Those 5% does not materialize at once, but it represents a competitiveness in the market to have the lower prices on the new motor insurances.

We have seen through 2015 that we have lost more customers than we have gained; and therefore, we have a slight drop in our market share in motor. And this is due to a very – a quite fierce competition. I think that we have now seen that most of the companies have introduced their motor tariffs, and I think that we are probably moving towards a more normalized competitive situation. But the effect of new customers having lower prices on average than customers leaving us will still have an effect in 2016. And I think that we, also in 2016, will see an average drop in the motor premiums.

So that is one of the reasons why we guide minus 1% in 2016 and the other reason is that we still expect some larger accounts in the commercial line business to accept offers that we will not compete with from some of our competitors.

Q - Jakob Brink {BIO 7556154 <GO>}

Okay. Thanks for that. Just one follow-up on the capital. So those new items of Solvency II, they will most likely then boost your solvency position. I guess you could argue that you already – today you basically have those capital elements available. It's just not included in reported capital. How does – or how are you looking at that? I mean, will you actually treat this as extra capital or is it just extra reported capital?

A - Lars Thykier {BIO 16427122 <GO>}

You are completely right. The individual solvency regime we have now included the same items as Solvency II (06:31). So there will not be more capital cover when we change to Solvency II. We regard these extra elements as, what we call, an accounting illusion, because it doesn't change the fundamental value of the company. And that means that this extra capital will not be – will not trigger any more share buybacks.

Q - Jakob Brink {BIO 7556154 <GO>}

Okay. Thanks a lot.

Operator

In-Yong Hwang of Goldman Sachs. Please ask your question.

Q - In-Yong Hwang {BIO 18784369 <GO>}

Hello. Good afternoon. This is In-Yong Hwang from Goldman Sachs. Two questions for me. Just one on run-offs, it's not as high as last quarter, but still quite high and higher than your kind of 1.5% to 2% guidance. Is it still the same third-party liability and kind of change of ownership insurance that you were talking about in the last quarter and where that's coming from?

And just a bit of detail on how often you kind of look at reserves to determine whether you've got too much, I mean, just especially in the context of your Nordic peer in Norway got into (08:02) much higher bonus levels going forward in the next couple of years.

And my second question is on your buybacks. You converted to the safe harbor method going forward. I wonder – does that affect anything in terms of whether you get closer to your guided level of buyback? In the last few years we've seen Topdanmark for – quite a few hundred million short of the kind of the announced number in terms of the buyback achieved during the year. So I wonder whether that actually makes it more likely that you would get closer to the DKK 1.95 billion that you've announced for this year at all. Thank you.

A - Christian Sagild {BIO 15093649 <GO>}

If I can answer the last question for you regarding the buyback. The fact that we use safe harbor method enlarge the window that we can have buybacks performed, since they can start tomorrow but continue up until February 10; whereas we would be in a silent period. The report states that we will – that we have asked Danske Bank to perform a buyback of DKK 564 million from now and up until February and that is the remainder of the buyback of DKK 1.95 billion, which is still the potential buyback or stated buyback for 2015.

So apart from this small time lag, the buybacks will be performed to DKK 1.95 billion. And going forward, we will probably not use – I mean, we will, of course, state how much buyback has been performed by January 1 also, but we will use these windows between reporting dates to announce buybacks for the future quarter.

A - Lars Thykier {BIO 16427122 <GO>}

Concerning run-off. The major part of the run-off this quarter has been in illness and accident and in liability. We look at the reserves every quarter, but we do not have runoff for every business line every quarter. We just have to – we look at it from time to time we close (10:25) and this means that (10:29) in the runoff stream.

I don't know. Did that answer your question?

Q - In-Yong Hwang {BIO 18784369 <GO>}

Yup, yup. But I guess you probably keep the same comment you just made in the last quarter that I think you mentioned something like the 1.5% to 2% is a bit too conservative in the near term. Is that correct?

A - Lars Thykier {BIO 16427122 <GO>}

It probably is. The 1.5% to 2%, that is looking forward. When we make up our reservations for claims this year, we look at kind of conservatism in the reservations, which should be 1.5 percentage points to 2 percentage points.

Q - In-Yong Hwang {BIO 18784369 <GO>}

Thank you.

Operator

Thank you. Your next question comes from Per Grønborg of Danske. Please ask your question.

Q - Per Grønborg

Yes. Good afternoon. It's Per from Danske. A couple of questions from my side as well. First going back to the issues that Jakob asked about on capital. You now got your Solvency II models approved. I would assume that this implies that you know how much capital you will need going forward. But what you don't need – what you don't know is how much of the existing balance sheet you're able to include in your capital available going into 2016. Is that correctly understood? That was the first question.

A - Lars Thykier {BIO 16427122 <GO>}

I don't think so. We need to know whether our volatility adjustment is approved or is not approved. That is an outstanding point, Per. But I think we have a pretty clear picture of our base capital in 2016.

Q - Per Grønborg

And (12:26) what your capital need will be in 2016 will be approved you have now and assuming you will get the volatility approved?

A - Lars Thykier {BIO 16427122 <GO>}

There are still a few small items that we'll have to adjust, but it'll be close to the individual solvencies that you see now, or the base capital we show in the sheets.

Q - Per Grønborg

So to the individual solvency need, you show somewhere in the report?

A - Lars Thykier {BIO 16427122 <GO>}

Yeah, in the presentation.

Q - Per Grønborg

In the presentation. Okay. I'll try and look in the presentation. My final question, where was conversation, that discussions now are – it has basically decided that retirement age will be increased by one year. There's two more years to come down the road. How do we see the 2015, 2016 profit impact from those changes?

A - Lars Thykier {BIO 16427122 <GO>}

In first place, we make reservations until 70 years, so this will not impact the reserves. But I mean, the industry will have to cope with this change in retirement date and that might mean that some of our colleagues will increase the premiums, but I don't see any impact on our combined ratio.

Q - Per Grønborg

You already provisioned as based on 70 years.

A - Lars Thykier {BIO 16427122 <GO>}

Yes.

Q - Per Grønborg

Retirement age. Okay. Perfect. Thank you.

Operator

Thank you. Your next question comes from Christian Hede of Nordea. Please ask your question.

Q - Christian Hede {BIO 18642300 <GO>}

Yes. Good afternoon. It's Christian from Nordea. I just have a few follow-up questions. One is on the shadow account and life insurance business. Do you know what the treatment will be going forward, and do you have any news to share with us?

Another part would be if you could talk a bit more about what you call the loss of unprofitable industrial customers. I understand there is workers compensation. And how you see the competition going forward as well? And then just to clarify because I wasn't paying enough attention, did you say that you would issue buyback sizes, buyback programs every quarter? Thank you.

A - Lars Thykier {BIO 16427122 <GO>}

(14:49) shadow account. We have not received the guidelines for new – for contribution in the future yet. But it is our expectation that the shadow account one that is the shadow account concerning the return on investment there. That it will disappear and we'll have to run off the existing shadow accounts within five years. And if we are not able to make up the missing income within these five years, we'll have to write it off.

A - Christian Sagild {BIO 15093649 <GO>}

With regards to the workers comp, you're absolutely right. The competition in workers comp is quite fierce. And for some reason, we feel that some of our competitors are using other methods of tariffing than we do. We see quite a severe loss of portfolio. We have lost, for instance, to protect the small Norwegian company we lost more than DKK 50 million in portfolio in workers comp on a net basis. And what we see is a price policy that we cannot recognize in the claims patterns (16:11) that these customers have produced in the past.

So we are looking at competition that we will simply not participate in. We are being (16:22) some 30% on price levels that would cover the average claim cost, marginal costs and this of course is something that we'll not accept. So this is to some extent, of course, affecting the competition in workers comp right now.

Q - Christian Hede {BIO 18642300 <GO>}

Thank you. And the buybacks every quarter?

A - Lars Thykier {BIO 16427122 <GO>}

I don't think we said anything about this.

A - Christian Sagild {BIO 15093649 <GO>}

But, well, did you ask the question, Christian, about that?

Q - Christian Hede {BIO 18642300 <GO>}

Yeah. Yeah. Because I wasn't paying enough attention, so I heard that you would say how much you would buy back each quarter, but maybe I was wrong. So I was just asking whether that's correct or not.

A - Christian Sagild {BIO 15093649 <GO>}

We will report through the Safe Harbor method how much we authorize Danske bank to buy back in the next open window.

Q - Christian Hede {BIO 18642300 <GO>}

Okay. Thank you.

Operator

Thank you. Your next question comes from the line of Niccolo Dalla Palma of Exane BNP Paribas. Please ask your question.

Q - Niccolo C. Dalla Palma {BIO 16052945 <GO>}

Hi. One more question please on Solvency II. Could you – were the DKK 4.7 billion of estimated (17:31) capital remain completely unchanged even after the final adjustments and is that the number we should compare to the DKK 6.7 billion on slide 20 of available capital going forward?

A - Lars Thykier {BIO 16427122 <GO>}

What we need to have is a reasonable surplus of base capital above the solvency capital required. But the Solvency II elements, they are quite volatile and for this reason, we will probably continue stating that the DKK 4.7 billion of (18:14) funds, hybrid capital and Tier 2 capital is the number that we are aiming at.

Q - Niccolo C. Dalla Palma {BIO 16052945 <GO>}

Okay, very clear. Thanks.

Operator

Thank you. There are no further questions. Please continue.

A - Christian Sagild {BIO 15093649 <GO>}

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

Operator

Thank you. That does conclude our webcast for today. Thank you for participating. You may all disconnect. Speakers, please stay on the line.