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Bloomberg Transcript

Q4 2018 Earnings Call

Company Participants

- Denis Kessler, Chairman & Chief Executive Officer
- François de Varenne, Chief Executive Officer-SCOR Global Investments
- Frieder Knüpling, Chief Risk Officer
- Ian Kelly, Head-Investor Relations
- Mark Kociancic, Chief Financial Officer
- Paolo de Martin, Chief Executive Officer-SCOR Global Life
- Victor Peignet, Chief Executive Officer-SCOR Global P&C
- [05HFRJ-E Denis Kessler]

Other Participants

- Andrew J. Ritchie, Analyst
- Frank Kopfinger, Analyst
- Jonny Urwin, Analyst
- Kamran Hossain, Analyst
- Sami Taipalus, Analyst
- Thomas Fossard, Analyst
- Vinit Malhotra, Analyst

MANAGEMENT DISCUSSION SECTION

Operator

Good day, ladies and gentlemen, and welcome to the SCOR Group 2018 Annual Results Conference Call. Today's conference is being recorded. There will be an opportunity to ask questions after the presentation. To provide all participants an opportunity to place a question, please kindly limit your number of questions you place to two questions. At this time I would now like to hand the call over to Mr. Ian Kelly, Head of Investor Relations. Please go ahead, sir.

Ian Kelly {BIO 19976646 <GO>}

Good morning, everybody, and welcome to the SCOR Group 2018 full year results call. Before we start, can I please ask you to consider the disclaimer on page 2 of the presentation, which indicates that the financial results for the full year 2018 included in this presentation have been audited and that the group solvency final results are to be filed with the supervisory authorities by June 2019 and that these may differ from the estimates expressed or implied within this report. With that, we can commence the call. I give the floor to Mr. Denis Kessler, CEO and Chairman of the group, joined on this call by the entire COMEX. Thank you.

[05HFRJ-E Denis Kessler]

Thank you, Ian, and good morning, everyone. In a year which has been marked by entropic forces, including bulls and fortunate critical developments and (00:01:34), who once again demonstrate its ability to weather shocks and to continue to create superior value for its shareholder. The group has profitably dependent and even its franchise (00:01:47) in 2018, achieving a normalized return on equity in line with the Vision in Action target, a robust solvency position at the end of the year, at the top (00:01:59) part of the optimal range.

The most significant political risk that struck the group last year was the fiscal reform in the United States. It was introduced in the very last days of 2018 (00:02:12). It includes a provision, taxes (00:02:17) reinsurance premiums ceded to affiliated foreign subsidiaries. SCOR restructured its operations in 2018 to mitigate the impact of this fiscal reform, and hence maintain its competitiveness going forward.

Similarly, Brexit has been an additional complication last year as the practicalities of the United Kingdom's exit from the European Union are not yet fully known, we have prepared for (00:02:44). We have therefore created a new Paris-based P&C insurance company, P&C insurance company, to ensure the continuity of the services offered to our clients in the European Union.

Our Europe SE was approved by the French Supervisory Authority, the ACPR, in November 2018 and is now fully operational. Our insurance industry now dedicates much of its attention, effort, energy and resources to dealing with these kinds of issue pertaining to the refragmentation of the world, i.e., the ongoing sharpening of political, international and social tension. (00:03:28) nimbleness allows it to find appropriate solutions when faced with these (00:03:33).

As far as acts of God are concerned, Mother Nature has also been quite agitated in 2018 with two destructive hurricanes in the U.S., Michael and Florence; two powerful typhoons in Japan, Jebi and Trami; two wildfires in California; and other smaller events across various areas and regions. Managing such risks and covering these kinds of events is les soldats (00:04:02) as we say in French, the mission. We are there to help citizens and societies face this risk. We are here to alleviate the negative impact of this risk once it occur. And at SCOR, we are proud that during this second consecutive year of elevated natural catastrophe activity, we have once again accomplished the mission.

Meanwhile, SCOR's global footprint, (00:04:27) and go-to-market approach balance (00:04:30) the group to continuously extend and deepen its franchise. In this regard, I'm pleased to report that in 2018, for the first time in its history to cross (00:04:42) the €15 billion mark in terms of gross written premium. And a result of the group's strong underlying fundamentals, SCOR is pursuing its attractive shareholder remuneration policy.

A regular cash dividend of €1.75 per share will be proposed at the next Annual General Meeting, which will be held on April 26, 2019.

In addition, we have successfully completed the €200 million share buyback program, fully in line with the commitment made to our shareholders in July 2017. In terms of capital structure optimization, the merger of the 3SE legal entities is well on track. Subject to regulatory approval, we expect it to be completed by early 2019 providing a solvency benefit of up to €200 million.

Let's go to page 4. I'm proud to say that in a year once again marked by exceptional events, SCOR delivered a solid set of results with net income of €322 million for 2018 translating into a return on equity of 5.5%. Furthermore, SCOR's underlying profitability is excellent. Normalized from the exceptional events of 2018, the return on equity would stand at 9.4% and hence exceed the Vision in Action profitability target of 800 basis points.

(00:06:14-00:06:26) part of the optimal range of 185%-220% defined in the Vision in Action plan. This is a result. After accounting for dividend and share buyback, thanks again to its nimbleness, agility and robust capital shield, SCOR successfully absorbed shocks thus guarding the group from severe losses.

SCOR delivered strong and managed endogenous growth in 2018 with premiums up 7.1% at constant exchange rates compared to 2017. The growth was balanced between both of the group's business engines, mainly driven by a development in Asia-Pacific on the life side and in the U.S. on the P&C side as further demonstrated by SCOR Global P&C's strong January 2019 renewals. We achieved a normalized technical profitability, demonstrated the group's underlying technical fundamentals remain very strong.

On the P&C side, the 2018 P&C combined ratio remains below 100% despite the numerous natural catastrophes that took place last year. Normalized combined ratio stands at 94.7%, below the 95% to 96% Vision in Action assumption paying witness to the quality of SCOR Global P&C's book. SCOR Global Life because a (00:07:56) robust life technical margin of 7% in 2018.

Finally, SCOR Global Investments delivered an elevated return on invested assets of 2.8% in 2018, largely driven by a continuing increase in the income yield. Basically, all three of our group's engines are delivering. Even though (00:08:22) we have not managed to achieve the group's global profitability target of 800 bps above the risk-free rate due to the exceptional weight of natural catastrophes and the cost of the U.S. tax reform, the group is certainly profitable and its underlying technical fundamentals are very strong.

Let's move on to slide 5. These three graphs illustrates how SCOR continued to deliver a combination of diversified growth, solid recurring profitability and strong solvency in 2018. SCOR's growth potential, long-term value creation capability and shock absorbing capacity are confirmed year after year.

Moving on to the next slide, if we look at the total shareholders' return, which is the sum of the share price appreciation and the dividend paid to shareholders, SCOR stands out from its peer group. By value shocks, (00:09:22) SCOR total shareholder return have reached 49.1% since the launch of the Vision in Action plan in September 2016.

Let's move on to slide 7. SCOR is pursuing its strong shareholder remuneration policy. Cash dividend of €1.75 per share would be proposed at the next general assembly on April 26. We continue to optimize our capital management, thanks to a proven and consistent process, first, by ensuring the group solvency is in the optimal range. Second, by allocating capital to support equity value creating growth in the future. Third, by defining the amount of a sustainable dividend accordingly. And finally, if appropriate, by assessing any excess capital leftover for shareholder repatriation or future use.

In 2018, the completion of the share buyback program led to a 66% increase in the capital return to shareholders compared to 2017.

Looking forward, SCOR's ambition is intact and we have every confidence in the group's ability to continue its solvent and profitable growth, and push through with strong value creation in the years ahead. SCOR is uniquely positioned to significantly benefit from the positive long-term trends that the reinsurance industry offers.

Meanwhile, the group is on the move and actively preparing for the future, constantly improve the tools, processes, and our model. We are supporting the only credible blockchain initiative in the insurance sector and partnering with numerous insurtechs to see what innovations are going to emerge and shape the insurance and reinsurance world.

The group has tremendous potential for continued profitable growth and long-term value creation as a global Tier 1 reinsurer. SCOR is an independent company and master of its own destiny. We're actively preparing our next three-year strategic plan, which will be presented in September. This would be an opportunity for SCOR to confirm its objectives and to set out the ways and means chosen to achieve these, leveraging a Tier 1 status for global and deep franchise (00:11:50), the prime rating, the expertise-driven human capital.

Let me now hand over to Mark for the financial details. Mark, the floor is yours.

Mark Kociancic {BIO 17852409 <GO>}

Thank you, Denis, and good morning, everyone. So let's begin on slide 8. I will walk you through the financial highlights for the year. 2018, SCOR underwrote €15.2 billion gross written premiums, representing a 7.1% increase over 2017 at constant exchange rates, or 3.2% at current exchange rate. This top line growth was driven by the strong contribution of both business engines. SCOR Global P&C grew at 6.7% and SCOR Global Life by 7.3%, both at constant exchange rates.

In spite of heavy nat cat experienced in 2018, P&C returns profit with a net combined ratio for the year at 99.4%, including a 12.6% nat cat ratio. On a normalized basis, the P&C

combined ratio stands at 94.7% and that's better than the Vision in Action assumption. The life technical margin is strong at 7%, also in line with the Vision in Action assumption.

Finally, SCOR Global Investments delivered a return on invested assets of 2.8%, supported by an equity gain and by the increase in recurring yield, which is 2.4% for the year and 2.6% in the fourth quarter.

Overall, SCOR's net income for 2018 stands at €322 million. This is a 12.6% increase compared to 2017. This translates into a return on equity of 5.5%. Return on equity would stand at 9.4% when normalized for the high nat cat volatility and the U.S. tax reform impact of €68 million in 2018. This is well in line with our Vision in Action profitability target of 800 basis points above the five-year risk-free rates.

SCOR's solvency position remains very strong at 215% at the end of 2018, in the upper part of the optimal range of our solvency scale.

Let's move to page 10. SCOR generated very strong operating cash flows of €891 million. Both divisions contributed strongly to the operating cash flows.

SCOR Global Life provides strong cash flow, partially offset in the fourth quarter by the one-off impact of payments relating to the U.S. tax reform, with 2017 benefiting from elevated technical business cash flow from two Financial Solutions transactions.

SCOR Global P&C also provides robust cash flow in line with expectations. Overall, the total liquidity of the group is strong and stood at €1.2 billion at December 31, in line with our asset allocation assumption.

Let me now hand it over to Frieder, who will give you more details on the solvency and capital generation of the group.

Frieder Knüpling

Thank you. Mark. Slide 11 shows the development of the group solvency position during 2018. There were two main drivers of change that caused (00:14:59) solvency. The operating impact of plus 18 percentage points was very strong and resulted from significant capital generation by our business engines in 2018, combined with a very modest SCR growth giving a favorable risk return profile and improved diversification of the business expected in 2019.

This more than offset the combined effect of the share buyback program, which has been executed in 2018, and the planned dividend. Other movements of the solvency position were minor, including the effect of the U.S. tax reform.

In total (00:15:38), the solvency ratio increased to 215% and spend at the upper end of the optimal range, in line with our Vision in Action objective.

Slide 12 provides more details on the composition of the operating impact. That means the Solvency II own funds generated by the business during the year with two main drivers. Value of new reinsurance business written during the year of €450 million and the expected contribution by the in-force business, up €442 million.

Aggregate variances compared to the fixed results were relatively small (00:16:19). Overall, the business engines created almost €800 million of Solvency II own funds, demonstrating towards value generation capacity.

Moving on to page 13. SCOR's risk profile continues to be dominated by insurance underwriting risk in line with our stated risk appetite. In comparison, the contribution of the market and credit risk to total capital requirements is smaller.

The Life and P&C underwriting risks continue to be very well balanced. The level of diversification at this level of aggregation has further improved, 50%, which is clear indicator of the strengths of SCOR's business model. It is built on the continuous maximization of diversification, which, in turn, is the basis for optimizing the group's capital efficiency and profitability.

(00:17:11) solvency is resilient to financial market movements with all of the sensitivities shown on page 14, leading to a solvency position at the upper end or above the optimal range.

As a reminder, SCOR does not use any long-term guarantee or transitional measures, and its solvency position is not sensitive to the level of the ultimate forward rate.

With this, I'd like to hand over to Victor for his comments on the development of the P&C portfolio.

Victor Peignet {BIO 6287211 <GO>}

Thank you, Frieder. Good morning. 2018 was another year marked by natural catastrophe, although not as badly as 2017. 2018 and 2012 are the second costliest nat cat years on record, with insured losses of around $80 billion. Costliest years are 2017, 2011 and 2005, with inflation-adjusted insured losses ranging from $130 billion to $140 billion. Therefore, 2018 appears to have continued a six- to seven-year nat cat cycle that started back in 2004.

It's worth noting that this cycle has been dominated by three peak periods of two years, 2004 and 2005, 2011 and 2012, and 2017 and 2018, each recording insured nat cat losses of more than $200 billion with 2017-2018 being the highest at around $230 billion.

2018, beyond the six losses that received wide media coverage – two hurricanes in the U.S., two typhoons in Japan, and two wildfires in California – the market has been impacted by a large number of smaller, but still significant events all over the world. This unusual loss profile, with a high frequency of medium- to high-severity losses, has always been monitored by SCOR's Enterprise Risk Management system and stands well within our risk appetite as an earnings event.

Because of the number of medium- to high-severity losses sustained in 2018 and because of the size of each loss for our peers, 2018 scenario mostly triggers recoveries from our proportional retrocession. Explains the gap between 2017 and 2018 in terms of percentages of recovery, down from 50% to 30% in rounded figures. Despite this loss activity, and thanks to the quality of our underwriting and to the management of our portfolio, we have produced a positive net technical result for 2018. Our net combined ratio stands at 99.4%.

2018 is also marked by high number of very large man-made losses in refining, aluminium, mining, large construction projects, and cyber. Their impact on us has been contained, thanks to the selectivity and the control line sizes (00:20:10) of our per risk underwriting. Our net combined ratio normalized of nat cat and reserve release stands at 94.7%.

It's very satisfying to see that this technical performance is accompanied by continued growth at a steady rate of 6% to 7% a year. Second (00:20:32) consecutive year of intense nat cat and man-made losses following more than a decade of continuous risk-adjusted price reductions in the industry explains the beginning of a market reaction that became increasingly visible in the run-up of the 1/1 renewals. This long-awaited movement is currently restricted to loss-making business and appears too limited for now, but it is encouraging for the spring and summer 2019 renewal.

On this note, I'll hand over to Paolo for his comments on the Life division.

Paolo de Martin {BIO 15930577 <GO>}

Thank you, Victor. SCOR Global Life records another successful year in 2018, both in terms of growth and profitability. The total year, we've been able to record gross written premiums on €9.1 billion, achieving effectively the Vision in Action assumption one year ahead of the plan at constant exchange rate. This represents a strong increase year-over-year at constant exchange rates up 7.3% or 3.6% at current exchange rate.

The strong growth was mainly driven by the expansion of the franchise in Asia-Pacific with the Protection business in the region growing at over 34% compared to 2017. Asia-Pacific now represent a material share of the Life division, both on premiums and results.

Growth has also been supported by new Financial Solution (sic) [Solutions] (00:21:49) deals, reflecting strong demand across U.S. and Asia-Pacific market, as well as by development of the Longevity business in the UK. The overall premium growth is in line with the Vision in Action assumption of 5% to 6% over the cycle.

On the profitability side, we see a strong increase in the net technical results standing at €589 million, up 7.9% at constant exchange rate. The technical margin at 7% is in line with the Vision in Action assumption. The performance of the in-force portfolio is in line with the expectations and the new business underwritten continues to exceed the group ROE target. Life division continues to be a key contributor to the value creation of the group.

I will hand over to François for details on our investment portfolio.

François de Varenne

Thank you, Paolo. Moving on to slide 17, SCOR Global Investments portfolio reached €27.2 billion at the end of December 2018, with an invested asset portfolio of €19.1 billion compared to €19 billion at the end of June. The positioning of the investment portfolio is in line with the Vision in Action target asset allocation.

Liquidity is stable at 5% of the invested assets, in line with the target level defined for the strategic plan. The share of corporate bonds in the invested asset portfolio is stable since Q3 2018 (00:23:08) at 49%, close to the maximum of 50% defined for the plan. And the duration of the fixed income portfolio is at 4.3 years, slightly below the levels shown three months ago.

Our fixed income portfolio remains at very high quality with an average rating of A+ and highly liquid. Indeed, at the end of December, expected financial cash flows from the fixed income portfolio over the next two years stand at €5.4 billion, providing strong financial flexibility and allowing SCOR to see reinvestment opportunities.

SCOR Global Investments deliver an elevated 2.8% return on invested assets for the full year 2018, which is supported by a continuing increase in the income yield, 2% in 2016, 2.1% in 2017 and now, 2.4% during 2018. During the last quarter, our income yield reached 2.6%, highlighting the relevance of the portfolio rebalancing implemented since the launch of Vision in Action.

This quarter, financial contribution was boosted by a large capital gain of €87 million realized on the sale of an equity co-investment. Our reinvestment yield stand at 2.9% at the end of December 2018, still significantly above our current income.

Under current market condition, we expect the continuing increase in our income yield for 2019. It should increase for the third consecutive year at around 2.5%, strengthening the invested assets' financial contribution quality. The annualized return on invested assets could be comprised between 2.7% and 3% for the full year 2019.

With this, I will hand it over to Ian for the conclusion of (00:25:02).

Ian Kelly {BIO 19976646 <GO>}

Thank you, François. On page 18, you will find the next schedule of events starting on April 26 with Q1 2019 results and Annual General Meeting, as well as the conferences, which we are planning to attend across the first half of 2019.

With this, let's start the Q&A (00:25:25).

Q&A

Operator

Thank you. We will now take our first question from Kamran Hossain from RBC. Please go ahead.

Q - Kamran Hossain {BIO 17666412 <GO>}

Hi. It's Kamran Hossain from RBC. Couple of questions. First one is looking at the, I guess, the Solvency II earnings during the year, new business contribution is particularly strong and that €450 million definitely above what you had flagged in late September, the €300 million level. In that €450 million for this year, are there any particular one-offs or is that a reasonable number to assume going forward? I mean, if you do have the number for last year, the corresponding number, that would be really helpful.

And the second question just on capital. Would it be possible to get an update on the AAA surplus and whether actually the merger of the 3SEs will do anything there at all? Thank you.

A - Denis Kessler {BIO 1498477 <GO>}

Frieder?

A - Frieder Knüpling

So, the new business level, which was included in this economic valuation slide, which you were referring to was flagged as being conservative level. So, it's not surprising that what we've actually created in 2018 is above that.

New business value, I mean, as you know, that this is more volatile than other metrics. So, it depends on deals which materialize on profitability on the market and so on. But having said this, the amount which we generate in 2018, I mean, there's no one specific one-off deal in it which drove this in a particular way.

So, I think it's a reasonable starting point of what you should expect in the future with, yeah, ups and downs as I mentioned. And we haven't disclosed the number for the previous year, but the level was approximately in the same order of magnitude. So, there's nothing unusual about new business value in 2018.

Q - Kamran Hossain {BIO 17666412 <GO>}

Thanks.

Operator

We will now take our next question from Jonny Urwin from UBS. Your line is open. Please go ahead.

A - Denis Kessler {BIO 1498477 <GO>}

I think there was a second question for Mark.

A - Mark Kociancic {BIO 17852409 <GO>}

So on the second question, your question had to do with the S&P Capital level. So, we are still significantly above the AAA threshold for S&P Capital. Not so much has changed for us and that's the fact (00:28:43).

Q - Jonny Urwin {BIO 17445508 <GO>}

Hi. Jonny Urwin here. Should I go now?

A - Ian Kelly {BIO 19976646 <GO>}

Yeah. Go ahead, Jonny.

Q - Jonny Urwin {BIO 17445508 <GO>}

Thanks. So just to follow up on the (00:29:00) number then. So, I mean, it's a really good number and even adjusted for the experience variance like 16 points or so. So, I mean, is the message today that that's broadly sustainable, obviously, there'll be pluses and minuses in any given year? And then, secondly, what sorts of level of losses would be needed in 2019 to turn the P&C market? It feels like we're closer to the tipping point than we have been in recent years. Thank you.

A - Frieder Knüpling

On your first question, I think the one somewhat more favorable impact on operating in 2018 was the fact that the SGI has grown only by a very small amount. That's driven by improved risk return expectations for the business in 2019. We've placed our retrocession program on the P&C side early and the favorable conditions. We've seen good renewals. And given the much wider spreads at the end of 2018, we also expect a bit more divestment income on a market value basis.

So, of course, as the business grows, we can't expect our capital to remain flat forever. But having said this, improving the risk return profile and improving diversification of our business and keeping the growth of capital requirements under control and managing this is at the core of what we are doing. So that's something which, in the future, we'll also pay a lot of attention to it. (00:30:52).

With this exception, I don't think there's anything unusual about the operating impact and in particular, as I said, the own funds value creation was not unusual and in line with what we've generated in the past.

Q - Jonny Urwin {BIO 17445508 <GO>}

Thank you. Could you give us a normalized expectation just for where you think that (00:31:21) would run even if it's just a range? That'd be great.

A - Frieder Knüpling

Yeah. I don't think we can give that guidance. We all need, I think, a bit of a longer track record of those numbers. They are volatile. I mentioned new business as something which is very dependent on market conditions and which moves up and down. And you've also seen this on an MCV (00:31:48).

But then, the contribution from the in-force business is a bit more mechanical. That's mostly unwinding of discount and release of cost of capital and investment income on an expected basis. So, you should see less volatility in that regard.

Q - Jonny Urwin {BIO 17445508 <GO>}

Got it. Thank you.

A - Frieder Knüpling

And the other variances, I mean over a longer term period, they should average out to zero. But again, claims variances, assumption changes, and so on will lead to pluses and minuses over time so you'd need a somewhat longer time series to really make robust projections on this. But now with this in mind, I think you can take the numbers as a good starting point (00:32:45).

A - Denis Kessler {BIO 1498477 <GO>}

So on the P&C market dynamics?

A - Victor Peignet {BIO 6287211 <GO>}

Well, you need to look at it from three perspectives. The P&C market insurance, reinsurance, and retrocession. But my feeling is that we've got the losses already in the books. I mean, we've got the nat cat losses for sure with the last two years and don't forget that the 1/1 renewals were mostly European renewals, and Japan and U.S. are coming in April, June, July. So, I think we should see a reaction of the market as (00:33:21) built to the – in particular to the contracts that have been affected by losses.

As far as the man-made, I think we had our fair amount of losses as well and the market has started to react in insurance and in retrocession. So, you look at commercial and industrial lines, it's quite obvious and I cited the industry sectors that have been heavily affected by losses starting with energy and refining, in particular, mining and you've seen the losses recently in the press. It's in the large project, in particular, hydroelectric. Cyber has been in there as well. So, there are a certain number of industrial sectors that have been heavily affected, and those have started to react already and we see that in Business Solution (sic) [Solutions] (00:34:06), in particular, and we benefit from it.

And last, I would cite casualty in the U.S. where certain segments have been identified. And you can see the reserves strengthening in a number of them, commercial auto, in D&O (00:34:21), in med mal and related to hospitals, in particular. So, there are a number of segments in the market where you see that the reaction is already there. As I said, it's not sufficient, but we expect it to amplify as we pursue the next two renewal seasons in 2019.

Q - Jonny Urwin {BIO 17445508 <GO>}

Thank you very much.

Operator

We will now take our next question from Sami Taipalus from Goldman Sachs. Please go ahead.

Q - Sami Taipalus {BIO 17452234 <GO>}

Yeah. Hi. Thanks for taking my question. First one is again on the capital generation, actually. Is it possible to just break down the new business contribution a bit between P&C and Life just so we get a feel of it? That would be quite helpful.

And also just on the assumption changes there, you've got a positive net number. But if I understood correctly, this number also includes nat cat losses, which I think maybe was minus €350 million maybe or something for the year. Can you just give us a bit more detail on what the positive moving parts are there?

And then my second question is on the reserve release. I think you've released about €100 million of reserves this year. Do you think that the reserve surplus is stable year-on-year? Thank you.

A - Frieder Knüpling

So, both Life and P&C have contributed to, I agree with you, the business. Contribution, we haven't splitted out at this point in time and virtually (00:35:57) what the developing market practice and appetite of readers, so this is going forward. So, we'll develop our disclosure in the future. Also, at this point, we're not providing a detailed split.

Sorry, on the variances, yes, you're right. Excess nat cat claims have gone into that, but we've had positive variances and developments from other parts of the P&C and Life portfolio so this has more than offset the P&C nat cat claims, but they are in there.

Q - Sami Taipalus {BIO 17452234 <GO>}

Is it possible to be just a little bit more specific on what those positive variances are?

A - Frieder Knüpling

They're really spread out across the portfolio. So, from other parts of the P&C portfolio and the Life business. So, as I said, it's spread out across the whole (00:36:57).

A - Denis Kessler {BIO 1498477 <GO>}

(00:36:59) on the reserve release.

A - Victor Peignet {BIO 6287211 <GO>}

Yeah. Also, I think this is totally consistent with what we've done all over the years when we have been hit by large natural catastrophe. And if you refer back to 2011 or 2012, you would find exactly then the same magnitude of reserve release that are totally consistent.

Secondly, I think €100 million needs to be put in perspective of an amount of net reserves, outstanding losses and IBNR of €11.5 billion for the division. So, I think not only we have positive development on recurring basis because we have kept the same prudent reserving (00:37:41), but this amount of release, while it's quite marginal compared to (00:37:47). So we believe (00:37:49-00:37:52), we believe that we are comfortably anticipate we have to do so (00:37:55).

Q - Sami Taipalus {BIO 17452234 <GO>}

Okay. But did the levels of surplus change over the year or was it stable or...

A - Victor Peignet {BIO 6287211 <GO>}

I think it has been – we have been unable this year to replenish the level of surplus. So we are basically in the same order of magnitude as we were at the end of last year.

Q - Sami Taipalus {BIO 17452234 <GO>}

Okay. Great. Thank you.

Operator

Our next question comes from Andrew Ritchie from Autonomous. Please go ahead.

Q - Andrew J. Ritchie {BIO 18731996 <GO>}

Hello? Hi. It's Andrew Ritchie here. I have two questions. First of all, for François, could you just give us a view on how you're thinking about credit risk right now. There's obviously been some spread widening in Q4. It's come back a bit in Q1, slightly more uncertainty on the credit environment. Maybe just talk about your new money deployment in light – and your current view on taking additional credit risk.

The second question, could you just clarify on the retro program, which I understand protected you a bit less given the nature of the 2018 losses? Was there any change in the structure of the retro program when you renewed it? I think you renewed it late in the year but before any sort of retro changes. But maybe just remind us on the broad structure and any significant changes. Thanks.

A - François de Varenne

So on your first question on the credit risk, so that's something we monitor carefully, having 49% of the portfolio exposed to corporate bond. We don't think we are at the end of credit cycle today, (00:39:41), if by – let's say if the records come out that this credit cycle is very long.

We have a specific focus today on the migration risk sitting in our portfolio, i.e., we monitor carefully the BBB bucket of corporate bond portfolio to minimize the risk of migration of (00:40:05) in the high-yield universe. So that's why we keep single A buyers in our corporate bond portfolio today. We purchased bonds. We purchase shorter duration BBB bonds to enhance the runoff capacity today and we decreased idiosyncratic exposure when bond redeemed (00:40:28).

A - Denis Kessler {BIO 1498477 <GO>}

In terms of the retro program, Victor (00:40:33).

A - Victor Peignet {BIO 6287211 <GO>}

Yeah. On the retro, there was no change of structure in the retro program. We discussed, as I commented, a question of the loss activity we had this year, you see that that's kind of an in-between scenario between benign and severe. And we have a pretty unusual feature, which is four blocks of losses. One Japanese block, one U.S. wind, one U.S. fire, and one rest of the world. And each block is in between €150 million to €200 million for our shares net of our proportional retrocession, which mean that with this in-between scenario, we are relatively high in terms of net combined ratio points, but we are not high enough to activate our aggregate and our – or even retrocession.

So basically, as I commented, on what we get this year is mostly proportional retrocession that is being activated. But this scenario, we knew about it and we have modeled it year-after-year, but this is a scenario that we consider as totally manageable and we prove it. Our combined ratio is below 100%. It's pretty unusual to have a loss activity that is so evenly well spread over five different blocks of event.

A - Denis Kessler {BIO 1498477 <GO>}

And you could give us the contribution of retro in 2017 and (00:42:04) that shows the pattern of claims.

A - Victor Peignet {BIO 6287211 <GO>}

Different, yeah. In...

A - Denis Kessler {BIO 1498477 <GO>}

The processing program (00:42:10) (00:42:12).

A - Victor Peignet {BIO 6287211 <GO>}

Yeah. In 2017, we had two major losses. The first two of the HIM (00:42:19) SIRI. So we had two big losses and we had others. Two big, activated and non-proportional. And the sum of the total was enough to active our aggregate policy.

So, we had non-proportional recovery on top of proportional. This meant that we had 50% recovery in all basically made of 30% proportional, 20% non-prop this year, but we are missing the 20% non-prop because we don't reach the per event and aggregate total by which our non-proportional retrocession would be triggered. (00:42:55)

Q - Andrew J. Ritchie {BIO 18731996 <GO>}

I guess the (00:42:58) I guess the positive being you didn't - because you didn't burn a large part of your retro in 2018 then that would have enhanced your ability to renew it on decent terms?

A - Victor Peignet {BIO 6287211 <GO>}

Well, I think you can see the glass half empty or half full. It's quite obvious to me that if 2019 is a normal year, we are going to come for renewal of our retrocession in a very favorable situation, whereby, I mean, we would not have activated our non-profit 2018. If 2019 is a reasonable year, well, then, yes, we could expect to be able to renew our retrocession with a lot of continuity, as always, plus a very good track record in comparison to the rest definitely.

Q - Andrew J. Ritchie {BIO 18731996 <GO>}

Okay. Thank you very much.

Operator

We will now take our next question from Vinit Malhotra from Mediobanca. Please go ahead.

Q - Vinit Malhotra {BIO 16184491 <GO>}

Hello? Hello. This is Vinit from Mediobanca. Am I on? But I don't - actually it's not clear. Ian, shall I go on?

A - Ian Kelly {BIO 19976646 <GO>}

Yes. Go ahead, Vinit.

Operator

Your line is now open.

Q - Vinit Malhotra {BIO 16184491 <GO>}

Yeah. Sorry. Sorry. Okay. So, I'm try to stick to two questions. I have few numbers of things (00:44:11) here. Just starting with the (00:44:17) in the fourth quarter. Victor, are you able to point out - you mentioned large losses in refining, infrastructure, mining. How much of this is coming from SBS? Are you able to give us some guidance on that just - and if that is very material again, then is there any plan on managing that risk? So that's the first question.

Second question is just on the investment line in the fourth quarter. I think the fair value line item has registered one of the strongest quarterly loss move (00:45:02) at €24 million that I have seen in many years. Is there some special item there?

And if I could just squeeze in, on the investment return outlook, it's a bit subdued compared to previous years. Is that because the - you're deemphasizing realized gains? So that's my two questions. Thank you very much.

A - Denis Kessler {BIO 1498477 <GO>}

Victor?

A - Victor Peignet {BIO 6287211 <GO>}

Yeah. Morning, Vinit.

Q - Vinit Malhotra {BIO 16184491 <GO>}

Hi.

A - Victor Peignet {BIO 6287211 <GO>}

Actually, just to be quite clear, my point was to say that the market has been hit by series of large man-made in different sectors and the sectors I mentioned are refining in the energy side, aluminium, mining, large construction project - hydroelectric, in particular - and cyber.

If I look at where we've been affected, we've been essentially affected ourselves in refining. We have three large losses in onshore energy, and we have one large property loss. But we've not been affected massively on aluminium, we've not been massively - unaffected on mining. We've escaped the problem of large construction project, in particular the hydroelectric dams, and we've escaped the large cyber.

So what I meant is that if I look at the market position and our position, the fact that we've been selective, the fact also that (00:46:36) has a principal of underwriting for years and years and years, SBS has always given priority to balance of the portfolio by avoiding to have peaks in share acceptances, while we've been able to absorb, to a very large extent, the few large losses that you had during the year, hence, the excellent normalized that we are able to pull out despite the fact that the year is heavy man-made loss activity here.

Q - Vinit Malhotra {BIO 16184491 <GO>}

And I'm sorry...

A - Victor Peignet {BIO 6287211 <GO>}

I don't think we have to change anything in our underwriting. We just have to continue it, and then we have to benefit of the strengthening of the market and probably the rectifications of certain clauses that have deviated over the years. That is going to happen and is already happening. We see that in different sectors that have been loss-affected.

Q - Vinit Malhotra {BIO 16184491 <GO>}

Sure. And the €130 million, Victor, you mentioned on page 15, is that – that's an early figure, but are you able to point out a quarterly fourth quarter figure or it's not very relevant?

A - Victor Peignet {BIO 6287211 <GO>}

Oh, the €130 million is the total amount of nat cat losses in excess of €3 million each that we have sustained during the entire year. The larger ones in this €130 million is Frederick, the European storm, which stands at – it's about €30 million, I believe.

Q - Vinit Malhotra {BIO 16184491 <GO>}

Okay. Thanks, Victor. Thank you.

A - Victor Peignet {BIO 6287211 <GO>}

€26 million, exactly. So you've got this one at €26 million, and then we've got a lot of them which are probably corresponding to higher activity of severe convective storms that we have seen everywhere in the world. I mean tornado, flash floods, hail storms, as the one we had in Sydney just before the end of the year.

Q - Vinit Malhotra {BIO 16184491 <GO>}

Yeah. Thank you.

A - François de Varenne

Vinit on your first question on the fair value impact in Q4, so that's good. That's the average of finance, €24 million, (00:48:43) in Q4 in fair value. 2018 return on invested assets was indeed slightly impacted by the equity market downturn that happened in Q4 and especially the negative market development within our convertible bond portfolio, which is accounted under fair value through P&L. And also a lower-than-expected capital gain on the disposal of the large equity co-investments.

Normalized for this volatility in Q4, our return on invested assets would have been of 3% for the full year 2018, so comfortably in the upper part of the 2.5%-3.2% range of Vision in Action.

For your second question, the outlook for 2019, as long as the full Vision in Action plan is concerned, I confirm that the average return on invested assets over the entire strategic plan will be in the upper part of the 2.5%-3.2% range which should be close to 3%. Please note also that since the beginning of Vision in Action, the quality of the financial contribution has significantly improved with an income yield of 2% in 2016 and expected at 2.5% next year.

So with the guidance for next year of 2.7% up to 3%, I include capital gain. If you look at unrealized gain portfolio at the end of 2018, we still have a significant buffer of gain, especially coming from the real estate portfolio and capital gains from (00:50:23) in 2019 and probably the following year.

Q - Vinit Malhotra {BIO 16184491 <GO>}

Okay. Thank you.

Operator

We will now take our next question from Thomas Fossard from HSBC. Your line is open. Please go ahead.

Q - Thomas Fossard {BIO 1941215 <GO>}

Yes. Good morning, everyone. Two question on my side. First one would be for Victor and that will be I guess my last question for Victor. Just wanted to come back on the Californian wildfires. So you had in 2017 €105 million of income losses, 2018 €143 million. I mean any change in the underwriting or in terms of (00:51:18) exposure for 2019? Because at this stage, it's difficult to see why there will be no (00:51:27) again of this type of losses in 2019. So did that trigger any change in the way you were approaching the business there? That would be the first question.

And the second question, which is I guess a more strategic one, looking at the way the group is deploying the capital at the present time, Life versus Non-Life, you're still significantly overweight also balanced, but overweight Life business, and actually, the growth in Life keeps going up. And how do you feel about this slight higher exposure to Life at a time where maybe the P/C market is starting to show some signs of stabilization. So any current thinking about how to maybe rebalance the group or is it time to rebalance the group now towards P&C in order to capture maybe the next five years leg? Thank you.

A - Denis Kessler {BIO 1498477 <GO>}

Victor.

A - Victor Peignet {BIO 6287211 <GO>}

Well, we've done a lot of studies on wildfire in California as you may imagine. We already changed our pricing after the year 2017, but we don't have any model at the moment that is really operational, but we have started to, well, work on deterministic scenarios last year, which has led us to revise our pricing upwards and has caused us to have to leave certain contracts at the end of last year. Well, this year, well, we are doing additional work to try to come out with recalibration of our models and we have launched a project to come up with our own model by the end of this year.

What has got to be understood is the wildfire of this year, as we can see them at the moment with what we have. And we've done extensive reviews of PCS figures and we have had discussion with the model provider on one of the few model (00:53:39) that exist for wildfires in California. But we believe that you are talking on the Camp Wildfire this year, our return period, well above 50 years. Somewhere between 50 and 100 year which is much, much higher than the return period of what we had last year. This fire is a much, much higher size. So if you look at the distribution of the heat for us between the two of them, the camp is really sticking out as the one that has impacted us the most.

So I think we are doing studies on that. We hope to improve again our underwriting. I don't think we have anything wrong in our underwriting. I think the size of this loss was massive. It remains that, well, we have to recalibrate our model and we have to make sure that wherever we underwrite contract with exposures, we are getting those exposure calibrated, assessed and priced for. And that's what we are doing not only in California but in other areas, Canada in particular.

A - Denis Kessler {BIO 1498477 <GO>}

So we don't invest (00:54:50) anymore in the companies producing (00:54:53). Mark, about the balance (00:54:57)?

A - Mark Kociancic {BIO 17852409 <GO>}

Yeah. So for the second question, we do have a 40/60 split in premium in terms of P&C and Life. But when you look at the required capital and this is on slide 13 of the deck you received, now you can see that the required capital is fairly balanced between the two.

Nonetheless, when the group does its annual planning and more importantly our next three-year strategic plan, this is something where we assess all lines of business. Geographic basis for the best contribution to the value creation and the strategic franchise development of the group, so that's something you'll probably hear a bit more of in September on our IR Day. But again, the split in the capital requirements really isn't that different.

Q - Thomas Fossard {BIO 1941215 <GO>}

Mark, I fully understand that. But I mean also contrast in terms of maybe what looks to be a stabilization of a five, six years soft market environment. And keeping in mind that last time you grew externally on the P&C side, which Converium was also, I would say, back to times where markets on the P&C side were a bit more, I would say, stronger than it has been over the past five years. I mean did that triggers any strategic thinking and conscious of the timing in the cycle currently?

A - Mark Kociancic {BIO 17852409 <GO>}

Oh, we're always prepared to allocate additional capital to areas of our business geographically in lines that are going to produce more. That's a clear point. It's something we were prepared to do in the first quarter of 2017. It didn't really materialize. But there's no issue with that. Just more broadly speaking, I would say outside of U.S. mortality, there's really very limited limitations on where we would want to grow and that includes investment risk, life risk and P&C risk.

Q - Thomas Fossard {BIO 1941215 <GO>}

Okay. Thank you.

Operator

We will now take our next question from Frank Kopfinger from Deutsche Bank. Please go ahead. Your line is open.

Q - Frank Kopfinger {BIO 16342277 <GO>}

Good morning, everybody. I have two questions. My first question is on the €200 million one-off. Given that we are halfway through Q1, any thoughts you can already share by now of what you are going to do with the €200 million? And then secondly, on the tax rate for 2019, in 2018, the tax rate even if I adjust for the U.S. tax effect had been pretty high. So any view on where tax rate should go in 2019?

A - Denis Kessler {BIO 1498477 <GO>}

Mark on the first question.

A - Mark Kociancic {BIO 17852409 <GO>}

Yeah. So the tax rate was elevated in 2018 at 34%, approximately 34%, and that was heavily influenced by the U.S. tax reform charge of €68 million, which we saw as a onetime event. If you normalize it for the U.S. tax reform charge, we're slightly above 21% in the group for effective tax rate. So that's in the range of the 22% to 24% ETR that we would expect through normal volatility.

There could be a little bit of friction in 2019 with respect to the U.S. base erosion anti-avoidance (sic) [anti-abuse] (00:58:45) tax as we still are waiting for potentially guidance from U.S. Treasury on how the BEAT will be calculated. But I wouldn't expect that to be very significant. So I think our original guidance of 22% to 24% holds, and probably a little bit more pressure on the downside or a lower tax rate, I should say, given the favorable change in rates that have happened in the U.S. and that assumes a normal distribution of geographic profitability.

On the first point, the 3SE merger benefits. So the merger is well on track. We're very happy with where we are right now and we expect it to be formally completed on March 31 with retroactive date to Jan 1. And we expect the benefit to be upwards of close to €200 million, but we have not made any decisions on what to do with this risk margin benefit that we'll get under Solvency II. That's probably something that we will approach in the strategic plan, which will be unveiled in September during our Investors Day presentation.

Q - Frank Kopfinger {BIO 16342277 <GO>}

Thank you.

Operator

We will now take our next question from Vinit Malhotra from Mediobanca. Please go ahead. Your line is open.

Q - Vinit Malhotra {BIO 16184491 <GO>}

Yes. Thank you. Thanks for the follow-up on, just some non-numbers topics please. Vinit, Mediobanca again, sorry. So, Denis, there was a media article I read a few days ago that SCOR wants to be a consolidator or views itself as a consolidator. Are you able to comment on what kind of lines you would be thinking about where you feel that you would like to grow for that? The first question.

Second question just quickly, on this normalized ROE, it's now three years in a row, so literally most of this plan where it's above the target substantially so or maybe at least 100 bps. Which bit is in your view the surprise versus the target 800-plus five-year risk-free (01:01:06), if anything? Thank you.

A - Denis Kessler {BIO 1498477 <GO>}

Mark?

A - Mark Kociancic {BIO 17852409 <GO>}

I want to make sure I understand your last question, Vinit. You were asking which business was a surprise versus the (01:01:22)?

Q - Vinit Malhotra {BIO 16184491 <GO>}

Or driver, sir. Yeah, I mean we've seen 10.1%, 9.4% and even the previous year was 9.5%. So we are consistently above target which is good news. I'm just wondering where is this in your view the good news coming from? It's just a very small – I mean if there's nothing that is striking then that will stick. I'm curious (01:01:41) to see something is standing up here.

A - Mark Kociancic {BIO 17852409 <GO>}

Yeah. We have enjoyed, for example in 2017, we enjoyed a very nice return on invested assets. It was probably stronger currently at the upper end of our guidance or (01:01:58) the market. P&C remains very resilient so take a look at the combined ratio. That's better than the assumptions we've put in Vision in Action. We had a 95%, 96% combined ratio and we are outperforming that the first two to three years of the plan thus far and then Life continues to be quite stable for us. So it's been quite a strong performance across the board for us I would say in all three areas.

A - Denis Kessler {BIO 1498477 <GO>}

On the first question, Vinit. We look at – always say if you want to understand what we do today and what we are going to do tomorrow, the best is to look at what we did in the past because one of the certainly characteristic of the group is to be highly consistent over time. So we made acquisitions for the last 10 years, 11 years, even before, reviews in (01:03:01) Life and then Converium and then we made (01:03:06) portfolio and some more the small acquisitions. So the group has been able to make acquisitions over the last 11 years.

The rule is the following that the policy for acquisition for exogenous growth: We check if the acquisition is in line with the targets of the plan that we pursue at the time. So this acquisition accelerate the plan? Fine. This acquisition make us deviate from the plan? No. It's very simple and since it's a plan with profitability and solvency targets, we really check that the acquisition is fully in line with what we said we would do when we launched the plan. And may I say that looking backwards, it seems those acquisitions have been successful and indeed accelerated the development of the group without deviating the track that we decided to follow.

So that's the philosophy and the practice (01:04:07). And I said in an interview – by the way, it's the only interview I gave for months (01:04:13) that I'd rather be a consolidator than a prey, it means that it's true that SCOR values the fact that we're independent company. We are Tier 1 reinsurer. The fact that (01:04:29) freedom that we are responsible and accountable for everything we do, the fact that we decided on the track and our plan is it's a lot of value for our clients, it's a lot of value for the franchise.

Our clients know that we are the deciders of last resort. Our clients know that when we sign a treaty, when we sign a contract, we're going to deliver, we're going to stick to our price, whatever the outcome of the contract. So it's absolutely fundamental. If we want to remain a Tier 1 reinsurer to show that we are the deciders of last resort. For that, of course, we have values and support of our shareholders.

So we look at the opportunities. It's the whole (01:05:18) fiduciary duty of any CEO and any executive committee in the world to look at the potential developments and that's what we do, make reviews and we decide to go further on the (01:05:36), those reviews lead to the conclusions that I just said, absolutely in line with the objectives of the group. So nothing new.

Our last point, we've been able throughout the last seven years to combine quite nicely exogenous growth and endogenous growth. When we make an acquisition, it's not at the – most of the time, at the expense of the endogenous growth. So we've been able to grow with our own resources. And in the meantime, we make acquisitions and integrate those acquisitions in quite an optimal way. It's almost seamless. So I think this is a recipe and we're going to continue to use this recipe in the years to come. So we are really on track.

The next plan will give you the new objectives we're going to set and the ways and means to reach those objectives but there will be certainly continuity in the acquisition policy that was stated quite a few years ago (01:06:39) the last more than 10 years (01:06:44).

Q - Vinit Malhotra {BIO 16184491 <GO>}

Thank you.

Operator

There are no further questions in the queue. I would now like to turn the call back to Ian for any additional or closing remarks.

A - [05HFRJ-E Denis Kessler]

Maybe before Ian takes the floor, we feel good and it's nice. It looks like a advertising campaign. We feel good. But we feel good. I think we check everything in this company with the board yesterday and (01:07:23) committees to strategy, audit, risk, so on and so on. And we looked at the fundamentals of the group and I really believe with a conviction that the group is at good shape. I mean we grow and we demonstrate that year after year in a quite homogeneous way, part of the world where we want to expand.

We are profitable and we have a good technical profitability. We absorb volatility and finally, we maintain a high level of solvency (01:08:02) the fundamentals of the group. So in a world, which is more uncertain and more demanding than before, notably due to the U.S. tax reform or the Brexit case or whatever, the IFRS 17 and the other (01:08:12) developments that are taking place, and again, we prepare and we anticipate. (01:08:16)

This is the last meeting where Victor Peignet will take part. He is planning to apply for retirement after years and years and years of an incredible contribution to the group, traveling about four or five times around the world per year, absorbing an incredible number of (01:08:43) quite emotional (01:08:46) which is around the table to see Victor leaving. But I want to just to pay tribute to Victor for everything he's brought to the group, which is absolutely exceptional (01:08:59) and we wish you the best, Victor. Thank you for your contribution.

A - Ian Kelly {BIO 19976646 <GO>}

Thank you. Thank you, Denis. So thank you very much, everybody, for attending this conference call and please don't hesitate to call us should you require any further information. Just to remind you, we do have our Analyst Roundtable call at 5:00 PM GMT, 6:00 PM Europe in our local offices. So hopefully see you later on. Thanks a lot and have a nice day.

Operator

Thank you. That will conclude today's conference call. Thank you for your participation. Ladies and gentlemen, you may now disconnect.