Q1 2018 Earnings Call

Company Participants

- Helge Leiro Baastad, Chief Executive Officer
- Janne Merethe Flessum, Head of Investor Relations, M&A and Capital Management
- Jostein Amdal, Chief Financial Officer and Executive Vice President for Finance

Other Participants

- Jan Erik Gjerland, Analyst
- Johan Ström, Analyst
- Jonny Urwin, Analyst
- Niccolò C. Dalla Palma, Analyst
- Steven Haywood, Analyst
- Vinit Malhotra, Analyst
- Wajahat Rizvi, Analyst
- Youdish Chicooree, Analyst

MANAGEMENT DISCUSSION SECTION

Operator

Good morning ladies and gentlemen and welcome to the Gjensidige Q1 2018 Results Presentation. Today's conference is being recorded. At this time, I would like to turn the conference over to Janne Flessum, Head of IR. Please go ahead.

Janne Merethe Flessum {BIO 19368607 <GO>}

Good morning and welcome to this first quarter presentation of Gjensidige. As always, we will have our CEO, Helge Leiro Baastad, running us through the highlights from the quarter before our CFO, Jostein Amdal, gives you the numbers in more detail. And, of course, we will have plenty of time for Q&A at the end.

So Helge, please.

Helge Leiro Baastad {BIO 5865247 <GO>}

Thank you, Janne. Good morning and welcome, everyone. 2018 has started off with a harsh winter with heavy snowfall and low temperatures. Several places in central areas of Norway reported up to three times high snow depth compared to normal levels, resulting in difficult driving conditions and heavy snow creating huge damages on buildings. This, together with volatile capital markets characterized the first quarter results.

As previously communicated weather conditions in the first quarters over the past few years have been relatively benign contributing to better results than we would normally expect for winter quarter in our region. Last time we had a really harsh winter was in 2010. So it's important to remember the seasonality we have in the Nordic region and there are strong variations in the Nordics, and Nordic weather conditions which this winter is clear reminder of.

Our results are summarized on page 2. Profit before tax amounted to NOK 727 million in the quarter. The underwriting result was for NOK 411 million, and the combined ratio was 93%. We had a premium growth of 5.7% and we managed to continue operating in a very cost efficient and lean way. Considering historical average claims levels, we estimate the weather-related deviation in the frequency claims level during the first quarter this year to be in the range of NOK 250 million to NOK 300 million, and even more if we compare with the first quarter last year which was benign weather-wise.

Large losses were also high compared with the first quarter last year partly due to the heavy snowfall. Demanding weather conditions primarily impacted the Norwegian business. We are happy to see our operations outside Norway deliver significantly improved results compared with the first quarter last year, despite weather also being more adverse in this region. The operations outside Norway contributed to a total of NOK 104 million to the group's underwriting results.

Looking aside of weather effects, the underlying inflation trend we had seen in motor insurance over some quarters now, continues into 2018. We had price measures in place and more are to come to higher and more frequent increases as our tariff system is set to be even more agile going forward.

The financial results came in at NOK 255 million, or NOK 203 million adjusted for nonrecurring items. We are satisfied with this result on our investments, considering the market volatility during the quarter. Annualized return on equity year-to-date was 9.3%.

The maps shown on page 3 illustrates both the difference in weather between winters 2018 and 2017 and also that they are quite extreme in opposite directions, with regards to long-term and medium snow depth. We encourage you to study the weather statistics every quarter as it is the highly relevant leading indicator for Nordic concerns.

Just to give a few examples of winter weather effects this quarter, we saw four times more damages year-to-date compared to the same period last year related to roofs collapsing due to heavy snow. At Oslo emergency ward, they have treated 30% more fractures so far this year compared to the same period last year. And we had an increase of more than 15% in the number of motor claims in Norway during the first quarter this year compared to the same period last year. Based on the large amounts of snow this winter, the Norwegian Water Resources and Energy Directorate sees a higher than normal risk of severe spring floods in Southern Norway. If such large floods occur, it should impact our second quarter 2018 results.

As the largest general insurance company in Norway, we see claims prevention as an important part of our mission. So as a precautionary measure, we are in the process of delivering pumping and drying equipment to the high risk areas for floods. This is the first time an insurance company in Norway takes this kind of large scale preventive measures.

Then moving on to page 4 and leaving the weather for now, I want to give you some examples of our agility in the customer interface, contributing to keeping up our strong competitive position. Time to market is of essence when developing the best digital customer experiences, which is one out of the three operational strategic priorities. The other two strategic priorities are related to analytics and people. All three are equally important to secure the position as the most customer-oriented insurance company in our region, and at the same time delivering on our financial target. We are continuously monitoring market trends and put strong efforts into introducing user friendly and cost-efficient customer interface solutions with high speed to market.

In order to succeed in this area, we are reliant on attracting employees with relevant competencies. We are competing with all industries that attract the best people, and I'm glad to see that Gjensidige is able to recruit highly skilled digital talents. Our attractiveness was confirmed when we received the national award as the industry's most attractive employer last year.

A selection of many concepts and offerings we have launched in Norway very recently, are illustrated on the slide. Firstly, we have introduced intelligent inbound call routing making us able based on a sophisticated prediction model, to automatically route each customer to the service team with a relevant experience on the expected reason for the call. This gives a better customer experience and is more efficient for both the customer and us and contributes positively to the customer satisfaction.

Secondly, we have established a direct messaging system which is linked to each claims report. Customers having reported a claim can correspond directly with the claims handler, enabling efficient claims handling processes by making it easier for the customers to follow-up the progress and for the claims handler to provide updates or request input.

Thirdly, earlier this month, we launched an online mental health counseling service for our private customers over 18 years with child insurance or disability insurance. Customers are offered the web-based program for mental self-help which may either be an alternative to traditional therapy or an offer which may assist while waiting for a regular psychologist consultation, for which the waiting time may be several months. The program is developed by psychologists and services launched together with a start-up company.

Then moving on to our mobile solutions, a few weeks ago, we launched a brand-new digital concept for young customers to ensure that small ticket belonging by a travel insurance or have their claims handled. It takes us only five weeks from idea to launch of the concept via the (00:09:21) app and we are probably the first company to let the customers buy insurance through augmented reality. It has been very well received in the market.

We also launched a health and lifestyle app in November last year targeting customers between age 20 and 45. The customer receives health and lifestyle related advice, articles, activity tracking, and more. All to contribute to having a healthy lifestyle.

Then the final example is by far the largest initiative in the first quarter, a real estate, brokerage and property condition insurance. We want to create a better balance between sellers and buyers of homes, reduce the number of conflicts and make real estate transactions more predictable. We have introduced a new insurance product which guarantees the condition of the property. With this guarantee, real estate buyers get more better protection against seasoned effects (00:10:28) than they have today. We are the first insurer to offer this in the Norwegian market and believe this will become the gold standard going forward.

I will now let Jostein present the results in more detail.

Jostein Amdal {BIO 19939645 <GO>}

Thank you, Helge, and good morning, everybody. I will start on page 6 where you can see that the report, a profit before tax of NOK 727 million in the quarter. This is down compared to the profit reported for the first quarter last year driven by lower underwriting and financial results. Both the private and commercial segments in Norway were impacted by the regulated increase in claims. We estimate the weather-related deviation in claims compared to historical first quarter averages to approximate NOK 250 million to NOK 300 million. The difference is even larger compared to Q1 2017 which was particularly benign weather wise.

As announced earlier starting from this quarter, we will provide more insights in the Nordic results by reporting Sweden and Denmark separately. The underwriting results of Denmark of NOK 85 million rose considerably compared to the first quarter last year. Both the Sweden and Baltic segments contributed positively to the underwriting results, reflecting the ongoing restructuring programs.

The Pension business recorded stable profits of NOK 32 million. Retail Banking recorded a higher profits NOK 122 million mainly driven by portfolio growth. As mentioned, the financial results from our investment portfolio declined to NOK 255 million reflecting high volatility in the financial markets during the quarter.

Turning to page 7, premiums rose 5.7% compared with the first quarter of 2017, 4.2% adjusted for currency effects. All main product lines in the Private segment recorded higher premiums during the quarter. Premiums from the Commercial segment were up compared with last year following solid renewals for most product lines, particularly for motor, property, and liability. Sales initiative towards new sectors also generated positive contributions to premiums for the Commercial segment.

Premium growth in Denmark was driven by the Mølholm acquisition. Adjusting for this and currency effects, premiums were down compared with the last year due to the re-underwriting and general price adjustments in the commercial insurance lines. Current premiums for the private insurance lines in Denmark were up during the quarter.

Earned premiums in Sweden increased compared with Q1 2017 driven by the significant premium increases introduced in 2017. The Baltics have recorded lower premiums adjusting for currency. The decline was driven by portfolio restructuring and repricing activities aimed at improving profitability.

The development in the loss ratio is shown on page 8. Both large losses and frequency claims were up compared to the first quarter of last year. The harsh weather conditions in Norway negatively affected by frequency claims and impacted the loss ratio (00:13:38) percentage points more than expected based on historical averages.

Large losses were up 2 percentage points, partly due to the weather conditions in Norway. The run-off gains came in somewhat higher than the expected level of NOK 250 million per quarter and reducing the loss ratio by 1.5 percentage points compared with last year.

Frequency claims rose 5.9 percentage points, with motor and property in Norway significantly impacted by the weather conditions. The underlying motor concession (00:14:08) trend seen on some quarters now continued into 2018. In Norway, we now expect an inflation at around 6% over the next 12 to 24 months, slightly higher than before. This is due to the changes in our motor (00:14:22) claims bonus system which are expected to result in an increase in a number of smaller reported claims.

In order to mitigate the expected claims inflation in motor insurance, we have implemented pricing measures and we'll continue with this going forward. Our planned average price increases in private motor in Norway, going forward, are now at least in line with the expected claims inflation. We will, however, need to balance price and volume configurations continuously. Bear also in mind that it takes 24 months from the initiation of price increases as these are reflected in the account. We are pleased to see positive development in the loss ratio in Denmark, Sweden and the Baltics and we are confident the positive development in these segments will continue.

Let's turn to page 9 for an overview of large losses. Total large losses amounted to NOK 225 million, somewhat lower than the expected level and corresponding to 3.8 percentage points on a combined ratio. The impact is 2 percentage points higher than the first quarter last year ago. And the commercial segments recorded a significant portion of large losses, NOK 118 million for the quarter, partially related to the heavy snowfall this winter.

Moving on to page 10 to comment the run-off gains. The runoff gains for the quarter came to NOK 340 million, higher than the current expected level of NOK 250 million. Random variations as well as adjustment of large loss provision explained the additional NOK 90 million of runoff gains. Our expectation remains that there will be approximately NOK 250 million per quarter in runoff gains for the rest of 2018. The run-off had a positive impact 5.8 percentage points on the combined ratio.

Let's turn to page 11. The cost ratio for the quarter was 15.3% reflecting continued good cost control. Cost ratio excluding the Baltics was 14.5%. The cost ratio in the Baltic segment is continuously improving due to ongoing restructuring efforts.

Page 12 illustrates highlights from Bank and Pension operations. Gross lending in the bank for the quarter was NOK 47 billion and measured by lending volumes, 75% of the Bank's customers are general insurance customers in Gjensidige. The majority of these lending volumes are related to mortgage and just a small portion to consumer finance loans. The bank reported a pre-tax profit of NOK 122 million in the first quarter and the improvement from the same period last year was driven by portfolio growth. Annualized return on equity amounted to 10%.

The Pension company recorded a profit before tax expense of NOK 32 million. Assets under management in the Pension operations amounted to NOK 29 billion. 70% of the customers in our Pension business are general insurance customers as well. Annualized return on equity amounted to 12.9%.

Moving on to the investment portfolio on page 13, the investment portfolio of NOK 56 billion yielded a return of 0.5% in the quarter, which we deem satisfactory considering high market volatility during the quarter. The result was positively impacted by NOK 52 million related to the sale of a Danish IT company, SDC (00:17:49). Asset allocation in the free portfolio reflected preparations for dividend and tax payments with adequate fund invested in money market instruments.

The match portfolio yielded a return of 0.7% on a portfolio of NOK 34 billion. A large part of the match portfolio consists of bonds at amortized costs which yielded a return of 1%. The running yield in this portfolio was 3.9% at the end of the quarter and the average reinvestment rate was close to 3%.

Unrealized excess value amounted to approximately NOK 1 billion. The free portfolio which amounts to NOK 22 billion yielded a return of 0.1% in the quarter. The return was generated by our investments in private equity funds and property offsetting the impact from weak equity and bond markets.

Last but not least, looking at our capital position of page 14. The capital position is still strong. In February, Gjensidige was granted an approval from the FSA (00:18:48) internal model to calculate the regulatory capital requirement. The approved model is more conservative than the model Gjensidige applied for. The FSA has specified some areas which have to be deferred, revalidated and documented to get an approval for Gjensidige original version of the model.

Gjensidige decided to accept the approval and we will continue our dialogue with the FSA. Same is to have the original version of the internal model approval. However, this will take time. The legal perspective (00:19:17) internal model. This gives a solvency margin of 159% while owned calibration of internal model gives us solvency margin of 171%. These solvency margins are calculated using book to reserves. (00:19:30) legal solvency margin should have been calculated using the best estimates. This would have resulted in solvency margins of 188% and 203% respectively.

Changes in the capital position from these two perspectives from last quarter are relatively small. Eligible capital increases mainly driven by retained earnings and lower technical provisions due to higher interest rates.

The capital requirement is stable from last quarter. We will continue to balance our capital structure in a disciplined way in order to support the target return on equity while at the same time allowing us some leeway for further bottlenecked decisions and stable dividends.

In the interim report, we have again discussed some of the uncertainties related to the capital position. Given the new tax proposal that has been launched, we assessed the likelihood of a taxation on the security provision as higher. This will reduce Solvency capital by approximately NOK 700 million, however, we expect the cash effects to stretch over the next 10 years.

I will then hand word back to Helge.

Helge Leiro Baastad {BIO 5865247 <GO>}

Thank you, Jostein. To sum up, we delivered results highly affected by the harsh winter weather and volatile financial markets in the first quarter. Looking past the winter, we experienced the overall good competitiveness and good progress in our operation overall and balancing cost efficiency measures with strategic investments is high on the agenda also during 2018. Over time, we still expect growth in line with nominal GDP growth and the combined ratio targets corridor is unchanged. Thank you.

We will now open for the Q&A session.

Janne Merethe Flessum {BIO 19368607 <GO>}

Operator, we are then ready for questions.

Q&A

Operator

Okay. Thank you. We will take our first question today from Vinit Malhotra from Mediobanca. Please go ahead.

Q - Vinit Malhotra {BIO 16184491 <GO>}

Good morning. Thank you very much. Helge, just looking at (00:21:50) now its two quarters in a row we are hearing about the Norwegian winter and snowfall related affects coming outside the large loss. Have you explored or debated the possibility or some kind of a reinsurance solution for these kinds of frequency, some kind of an aggregate cover or something on to that affect, which could provide some relief from this volatility? So, that's the first question.

Second question is, on the solvency, I mean, I'm a bit surprised because I originally thought you are going to have a discussion with FSA to more align yourself or align – or to reduce the gap, let's say, between your understanding and their understanding. And I think now, you have stated that you were not bleeding (00:22:48) at all. How should we think about the target then because if the FSA is applying stricter rules, are you likely to change your target range if anything, because that will be important for us to understand the future plans (00:23:07)? Thank you.

A - Helge Leiro Baastad {BIO 5865247 <GO>}

Thank you for your question. I would pass actually both of them to Jostein. Just to remind you on the reinsurance policy we had, we have had that many years and it's based on more capital tool, protecting of the capital (00:23:27). Jostein, it seems has had discussion. I will actually pass both the questions to you, Jostein.

A - Jostein Amdal {BIO 19939645 <GO>}

Yeah. I don't think I'll comment on discussions we've had internally. Just to remind you that the reinsurance program is protecting ourself against events or things and losses. Natural perilous events of about NOK 200 million as one event will be protected. You have not – this is not natural perils as such. This is a weather that has affected many larger business and especially motor and property. And let's remember motor is not really a natural perilous business as such. It's just been more – a higher frequency of collisions or losses on the motor portfolio.

On the solvency position, we usually have an annual cycle where we discuss targets or buffer targets above this legal capital requirement each fall. We have – based on this theme, 120% to 175% buffer and for now that is standing.

Q - Vinit Malhotra {BIO 16184491 <GO>}

All right. Thank you very much.

Operator

Thank you. Our next question comes from Jonny Urwin from UBS. Please go ahead.

Q - Jonny Urwin {BIO 17445508 <GO>}

Hi there. Good morning. Just one question from me. So we've seen quite a lot of deterioration come through in the underlying loss ratio in recent quarters. And I understand the driver of that. Your claims inflation has run ahead of pricing. But you're saying today that planned price increases are in line with claims inflation, but I wondered, are already pricing for claims inflation now? And so we should expect more deterioration, but at least you stemmed the tide on the front book, or are you still in catch-up mode and you plan to catch up in the next – in the coming months? Thank you.

A - Jostein Amdal {BIO 19939645 <GO>}

I think I'll answer that. Price increases that are being affected and everything renewed now will be in line with claims inflation on average, and our plan price increases going forward be at least in line in claims inflation.

Q - Jonny Urwin {BIO 17445508 <GO>}

Okay. And can you give us an indication of what those are? I know on motor, you were flagging – it was around 5% claims inflation, wasn't it?

A - Jostein Amdal {BIO 19939645 <GO>}

Yeah. And (00:25:57) the same stat around 6% where the last kind of increase is due to the changes in the (00:26:04) system which makes it a bit, you can say, less publishing (00:26:09) if you have a smaller claim and expect that to have an impact on claims frequency in line with what we see a couple of our competitors have done and the price to catch – to mitigate that. So it's in a way for us, forecasted increase in the claims problem, it's not a problem as long as we are able to price it through and this is what we're doing now.

Q - Jonny Urwin {BIO 17445508 <GO>}

And I guess you're also saying in your commentary that the tariff model will be more dynamic going forward. So I guess the aim of that is to prevent this sort of situation arising again.

A - Jostein Amdal {BIO 19939645 <GO>}

That's two parts. That one is our ability to actually forecast against inflation and the second is when they see a change to implement the changes in the tariff. And it's the last part that's kind of always improved through the more agile tariff system but to be able for cost due to claims inflation, it's still based on competencies of the people that are closest to the business.

Q - Jonny Urwin {BIO 17445508 <GO>}

Great. Thanks, guys.

Operator

Thank you. Our next question comes from Niccolò Dalla Palma from Exane. Please go ahead.

Q - Niccolò C. Dalla Palma

Yes. Good morning. My first question is on the solvency targeting. So first, if you could confirm that the A rating target is now being dropped for good so that we – because I think we're not getting that information anymore. And secondly, related to that, if you were to go as low as 125% solvency on a legal perspective, would you be able to keep your single A rating? I would like to understand that.

And then a question on the taxes. So, there's a NOK 700 million impact to come through solvency. You mentioned there's a provision already taken. So is my understanding correct that when we look at reported profit, there will be no impact at all or will we see something in reported profit over time from the changes that we are seeing? Thank you.

A - Jostein Amdal {BIO 19939645 <GO>}

Okay. First, we'll not talk to A rating target. It is still important, as we have explained earlier and that we have an A rating for some segments, especially on the Corporate business, for the Bank, for the (00:28:31), and also on the reinsurance side. So, there are several commercial reasons for keeping an A rating, and we still have that as our financial target.

Whether we'll be able to keep an A rating at 125%, one of the reasons why we dropped reporting the number from the S&P model is that it's just one part of the basis that S&P uses for giving us a rating. And we don't have a specific view on kind of the bottom level of solvency margin that should support an A rating. That's more up to us and our communication with S&P.

When we have a range of 125% to 175%, the middle point there is 150%, which is kind of a reasonable starting point where we think we should capitalize over time. But as the previous – or one of the previous questions asked, it depends a bit on the conservative reports to build into the model ourselves. So, we'll take all these things into consideration when we set the target.

Q - Niccolò C. Dalla Palma

That's clear.

A - Jostein Amdal {BIO 19939645 <GO>}

The tax (00:29:28) security question, you're perfectly right, there is no effect on the P&L. It's a paid tax that increases but also that this has a solvency capital effect. This deferred tax that we have on our books before this change if it is occurring, plus, deemed as kind of a perpetual tax, deferred tax liability and now it's done more immediately paid and then it will need to be subtracted from the solvency calculations in our interpretation.

Q - Niccolò C. Dalla Palma

Okay. Thank you so much.

Operator

Thank you. Our next question comes from Youdish Chicooree from Autonomous Research.

Q - Youdish Chicooree {BIO 17430923 <GO>}

Good afternoon – good morning, everyone. Thank you for taking my question. I've just got one question, and again it's on the motor claims inflation in Norway. So you've increased your inflation expectation by around 1 percentage point to around 6% today. So, I'm wondering whether the objective there is to actually stabilize underlying profitability in motor in 12, 20 months' time, or are you happy for underlying profitability to decrease because other parts of your portfolio are actually performing quite well, especially your international operations. And if you look at the headline ratios you are reporting excluding whether, they are still solid in other parts of your business.

A - Helge Leiro Baastad {BIO 5865247 <GO>}

You are correct. The expected inflation now is 6% up from 5%. And as Jostein said, all our price initiatives this year will meet and at least meet this claims inflation expectation going forward. So measures are taken to increase prices to meet that claims inflation. We expect, however, prices to increase, as I said, even more going forward to compensate for this claims inflation. So, we are not happy to, over time, to reduce the profitability in motor in Norway. But as we also have said it has been claims inflation since end of 2016 to 2017 and we will not catch up with that development. But going forward, we will need the claims inflationary price initiatives.

Q - Youdish Chicooree {BIO 17430923 <GO>}

Okay. Understood. Thank you very much.

Operator

Thank you. Our next question comes from Steven Haywood from HSBC.

Q - Steven Haywood {BIO 15743259 <GO>}

Good morning, everyone. I've got a couple of questions please. You mentioned that the winter has been about NOK 250 million to NOK 300 million higher than the average on the weather claims in Q1. Can you tell us what exactly has been the average winter claims in Q1 over the last several years?

And then on your tax regulatory changes you mentioned that there's another potential change coming through that could have a NOK 0.2 billion to NOK 0.6 billion impact. Could you just describe this further? Give us a bit more detail and let us know whether this is a one-off or could be a yearly impact on tax.

And then finally, you're introducing a new property insurance, property condition insurance, apologies. Now, is this similar to the Danish change of ownership insurance? What sort of premiums do you expect to receive in this new line of business and what is the take-up so far? Thank you.

A - Helge Leiro Baastad {BIO 5865247 <GO>}

It's really hard to be very concrete on what the average winter and it's especially in Norway. I guess they have that wind more or less in Sweden as well, but it's different as you know in Denmark. Last really harsh winter we experienced was in 2010. And that was a different kind though. It was related to temperature and freeze. And I think we also, at that time and that was the significantly lower premium volume, communicated around NOK 360 million related to that harsh winter.

It was since 2011, 2012 until this winter, it has been very benign and very mild. So if you compare the winter effects in 2018 to 2017, you are comparing a very harsh winter with a very benign winter. I guess the normal should be somewhere in between. But it's hard to actually be very concrete on that going forward. As I communicated, this winter started very early, and it still snow not – up in the mountains, its huge amount of snow and it has been very volatile. So this is extraordinary harsh winter. We do not expect that kind of winter as usual with going forward.

A - Jostein Amdal {BIO 19939645 <GO>}

On the tax question, there are two other items in there in addition to the security provision. And one part is the so-called Norwegian Guarantee provision privy in our books, has set aside as a deferred tax liability. And that might not be the correct way. So one of the possible outcomes of the taxation is that there will not be a tax liability (00:35:25) so it's a positive. (00:35:28) suggested a possibility of increasing the amount of products, that's included in the Norwegian Guarantee arrangement. Then a guarantee arrangement for customers in non-life insurance sector, which does not exists in most places in Europe. And this capital is not included in solvency capital in our perspective which, in a way, represents some kind of an upside for us as well. That changes now.

And the second part is natural perils capital where we have not satisfied deferred tax liability in our accounts on the assumptions that the tax on this natural perils capital is never going to materialize because as long as we continue writing property business, we'll continue to have this natural perils capital in our balance sheet.

The (00:36:18) assumed taxation of profit on natural perils business going forward and there's a small possibility that might change the weight needs to be existing account, i.e., setting up a deferred tax liability and that's being debated. And there's, I would say, a very small probability that we'll also have a contagious effect on the solvency capital. But in regard, as I said, that's really unlikely.

A - Helge Leiro Baastad {BIO 5865247 <GO>}

Of a brokerage company. We launched this Gjensidige brokerage company in February, and it's a combination actually of a completely new insurance product in the Norwegian market. It's a five-year risk product. We have looked, of course, and we are involved in this kind of business in Denmark.

In Norway, it has been a completely different situation. It has been (00:37:28) products for the seller and it has been more or less all the insurance companies and a small niche player called (00:37:35) just been insured, just insured their buyers. So what we have done here we have created a completely new taxation of properties. We have launched a very digital brokerage company and we have introduced a completely new risk product for both sellers and buyers. It has been some learnings from Denmark but it's not the same product that's in Denmark. It's a completely new concept in the Norwegian market and it has been very well received and we believe that you will see a change actually in this market going forward where you will see all the insurance companies following us on this with a completely new combined insurance product for buyers and sellers.

Q - Steven Haywood {BIO 15743259 <GO>}

Okay. That's great. Thank you very much.

Operator

Thank you. Our next question comes from Jan Erik Gjerland from ABG. Please go ahead.

Q - Jan Erik Gjerland {BIO 5346031 <GO>}

Good morning. It's Jan Erik from ABG. I just had two questions. The first one is a follow-up on the large – the premiums on the property side and the competition. I saw that you compete head-on-head with Protector. And on the premium side, how much do you really think this could be adding to your private lines in Norway.

And the second part is on the price and premium increases in general. On the private side you may have some further competition from the banks, et cetera, DnB. While on the Commercial side, it might be easier as Tryg has said that they are willing to give up business. But just wanted you to tell us about the competitive picture, both on the new property side and also on the general side. Thank you.

A - Helge Leiro Baastad {BIO 5865247 <GO>}

Thank you, Jan Erik. (00:39:33) handle the property insurance concept. So far, it's very limited. This will take time. We will not compete head-on-head with Protector. It's a completely new type of product. It's a (00:39:47) risk product. It's a combined – as I said, combined insurance product composed of sellers and buyers.

Through the brokerage company and this new insurance product, we believe this will be positive for all the traditional home and content insurance products. So this is the initiative to secure that they have more dynamics in their home and content process. It's a new product. That will take time. And it's not directly in competition with the Protector's (00:40:26) product.

Q - Jan Erik Gjerland {BIO 5346031 <GO>}

Okay.

A - Jostein Amdal {BIO 19939645 <GO>}

In terms of competitive situation in private, in general, and in commercial in Norway, I think so far, we've managed to keep our position very well. If you look at market shares and so, we are fairly stable. So the picture there hasn't really changed that much over the last couple of years. It's been quite (00:40:51) have been more aggressive one from their stable and so our main competitors have been losing and (00:40:58) is stable.

It's hard to predict what's going to happen going forward, but we think that most of these players will have to prioritize profits before volume and will have seen (00:41:11) the same way as we have done. We haven't listened to their results yet and I don't think probably they have started yet either. And but you see as a 35% player, I think it's a safe bet that they will have to see more the same effects as we have and need to price accordingly. So I don't really foresee a business short- to medium-term changes in the competitive position.

In terms of commercial, our results, as you have seen, are (00:41:40) the pressure, and we've seen that – we communicated that they all really focus on profitability. And it's always – it's more of a (00:41:49) account that is in the higher end of that Commercial segment, and it remains to be seen what really happens when the customers are on tender. But we at least prioritize profitability of volume with margin here.

A - Helge Leiro Baastad {BIO 5865247 <GO>}

Just to add, we had the Capital Markets Day back in 2014, and we talked about 1% to 2% claims inflation. What we are talking about today is 6%. It's not just structural changes. Electric car, hybrid cars, leasing is a completely more dominant concept now compared to what we saw some few years behind us. We, as you had heard, we will increase prices with higher price increases going forward compared to what we have done. We are market leader. We will do this and as we have said several times, profitability before market share. If this reduce volume a bit, we are prepared to take that as well.

We think we have to increase prices to meet a completely new high volume motor insurance market in Norway with significantly higher claims inflation, and the signal is that we are in the mood of higher price increases going forward with more frequent due to the new tariff system, more agile.

Q - Jan Erik Gjerland {BIO 5346031 <GO>}

Thank you. Just one follow-up on the commercial side, is it so that you have seen any more foreign competition, if you, well, think about the typical Nordic ones? Or is it so that they are still not apparently here on the commercial side and large corporate side?

A - Helge Leiro Baastad {BIO 5865247 <GO>}

It's the same as we have had all the years (00:43:45). And the texture in some segments and that's actually the competition.

Q - Jan Erik Gjerland {BIO 5346031 <GO>}

Okay. Finally, just remind us on the flooding. Last time it was a big flooding in Norway, that was 1995 and you were not listed, but you were definitely an insurance company. Could you just give us as example of how damaging that was to staff and what has happened on preconditions measured down in the past? As you said, you have already done some stuff to prevent the flooding to happen or not to happen, but just to make the damages less damaging for you. So what have you done and how was 1995 compared to what you see today?

A - Helge Leiro Baastad {BIO 5865247 <GO>}

1995, that's the biggest one. We had also a flood back in 2011. It was quite significant. Just to remind you, the figures in 2011, the industry estimates back in 2011 was NOK 200 million, and we had around NOK 65 million. That was in 2011. In 1995, do we have figures from 1995? It's a question mark here. No?

Q - Jan Erik Gjerland {BIO 5346031 <GO>}

Okay.

A - Helge Leiro Baastad {BIO 5865247 <GO>}

Denmark, it was 1.6%, Jan Erik, back in 1995.

Q - Jan Erik Gjerland {BIO 5346031 <GO>}

I think that's adjusted to today's nominal Kroner value.

A - Jostein Amdal {BIO 19939645 <GO>}

Yeah, that's adjusted?

A - Helge Leiro Baastad {BIO 5865247 <GO>}

Okay, yeah. So NOK 1.6 billion for the total market. And the last flood we have recently was in 2011 and that was the market damage, NOK 200 million.

Q - Jan Erik Gjerland {BIO 5346031 <GO>}

Okay. Perfect. Thanks a lot for your time.

Operator

Thank you. Our next question comes from Johan Ström from Carnegie.

Q - Johan Ström

Hi. Good morning, guys. So first of all, on the claims inflation, you're thinking – can you just confirm that the uptick from 5% to 6% on motor claims inflation was driven by the changes on the bonus system.

And then secondly, on your capital position, the uncertainty related to the PIM model and maybe a little bit on the tax side has reduced the solvency uncertainties. So, how should we think about unutilized NOK 1.5 billion to NOK 1.9 billion of subordinated loan capacity? Well, how do you see the market for potentially utilizing some of that now?

A - Jostein Amdal {BIO 19939645 <GO>}

I'll start...

A - Helge Leiro Baastad {BIO 5865247 <GO>}

Address all?

A - Jostein Amdal {BIO 19939645 <GO>}

Yes, it's due to the no exchange and no transfer, no system, so that's easy. In terms of uncertainty related to them, the Partial Internal Model, as we have said, we kind of disagree with the assumptions made by the FSA to utilize, for instance, the correlation from the standard formula between market risk and then (00:46:43) discussed we are forced to do. But decided against to kind of complaining and not accepting model. We all respect the model and that's (00:46:53). And then we'll continue our work over time with FSA and with internally, with our documentation.

But we are able to get more of them – of our internal model approved. And for internal purposes, as we present to you, these are our own calibration of the internal model with a slightly higher solvency margin. What we implemented now is some of these requirements from the FSA, and then as we say in the report, during 2018, there are also a number of smaller changes we need to do, with everything else equal, will reduce the solvency margin by 10 percentage points at year-end. But then, of course, we also work at the same time with our own model and to prove it and discuss with the FSA whether you can get anything changed there. But that will take time as (00:47:42).

The uncertainties created by the tax hearing in Norway, we think it's highly likely that the NOK 0.7 billion (00:47:54) solvency due the security provision and that will occur. We also think it's fairly unlikely that they will have a negative effect from the taxation of the natural perils capital. We think that is really very unlikely because the natural perils capital stays with the company as long as it's a going concern. Only if we close for business will that come to taxation, hopefully that is (00:48:21) and then there is no present value of the said tax bill.

And then, there finally was the guarantee provision, as I also took earlier question, there is both upside and downside to the changes there. But from our solvency perspective, it's more of an upside than a downside, I think.

The final question was on the unutilized capacity for subordinate debt namely then Tier 1 debt. We see as you do, that the market is fairly positive with those kind of (00:48:57) now. They (00:48:59), that's a spread of 250 basis points. So we follow that market and try to evaluate the possibilities there, weighed on a continuous basis.

Q - Johan Ström

Okay. Thank you.

Operator

Thank you. Our next question comes from Wajahat Rizvi from Deutsche Bank. Please go ahead.

Q - Wajahat Rizvi {BIO 19928187 <GO>}

Hi. Good morning, everyone. Wajahat Rizvi from Deutsche Bank. Can I ask the question again actually on solvency margins? So, on Partial Internal Model basis, you're looking at your solvency ratio range of 125% to 175%, though on average, let's say you're 150%. After this 10 percentage point impact that you have highlighted, you will be almost at that level. Then on top of that, you have highlighted that EIOPA stress test changes may impact your solvency negatively by 5 points. And then you have this ongoing drag from the tax charge, which you have also highlighted.

So, I'm just wondering if we capture all of these things, you will be below the mid-point of your appetite range. Would you need to change your dividend philosophy or raise capital or do anything to shore it up or move back in the upper end of the range? Or you are happy to operate bit more flexibly around the middle of this appetite range? Thank you.

A - Jostein Amdal {BIO 19939645 <GO>}

I'll start at the back end of your question that we're happy to be and operate flexibly within that range. We don't see that these uncertainties will have any effect on our ordinary dividend capacity. So, no.

And the first part on the, yes, as we've said, there are 10 percentage points that effect if everything is implemented. And we think that the NOK 700 million is likely to go through when the parliament decides finally on the new tax (00:51:00). But we do think that the other changes are likely to go through. Remember also, as we're now past what is historically the most – this is easily the most negative quarter for us and then new build up accumulated retained earnings over the next three quarters.

Q - Wajahat Rizvi {BIO 19928187 <GO>}

And can I just ask a follow up on this EOPA comment you have made, the changes, stress parameters for interest rate risk. So, as I understand, that is on Standard Formula and given that you have moved to Partial Internal Model, I would have thought you would have no impact from that change. So why is change to Standard Formula also hitting your Partial Internal Model?

A - Jostein Amdal {BIO 19939645 <GO>}

That's a very good question. And because we are on the Partial Internal Model on the non-life insurance business, but with also our pension business and that is on the Standard Formula. And that is affected. That's why we have these numbers.

Q - Wajahat Rizvi {BIO 19928187 <GO>}

Okay. So, the pension business is still on Standard Formula?

A - Jostein Amdal {BIO 19939645 <GO>}

Yeah. I mean, we don't have any plans here to change into Internal Model for that part of the business for some time.

Q - Wajahat Rizvi {BIO 19928187 <GO>}

Okay. Fine. Thank you.

Operator

Thank you. Our next question comes from (00:52:17). Please go ahead.

Hi. Just two questions for me. The first question is going to be on the guidance. If I understand correctly, the guidance is not changing. But doing the math around and the adjustments for the weather and for the release, the reserve release, the quarter was basically combined with 95% versus 92% last year, so a 300 bps move. That's the first question. Is the math correct on that?

And the second question is going to be how do we reconcile those numbers with an intact guidance, given that investment income is as well under pressure and the P&C side has seen combined going up by 890 bps. So, I'm just trying to reconcile the numbers and see how if we think about that guidance being intact and also the fact that the reserve release have gone up, how should we anticipate that going forward? I think it's been the highest quarter almost over the last few years on this side. So, thanks for reconciling the two sides of the equation here.

A - Jostein Amdal {BIO 19939645 <GO>}

In terms of runoff, I don't really remember if that's the highest level, but our runoff guidance here is that we do expect, based on planned reserve releases from intensified – that was in the reserves of NOK 250 million or NOK 1 billion a year approximately. As we're working on the balance sheet item of more than NOK 30 billion, there's some natural volatility around that. In the first quarter, as I said, there is kind of one large (00:54:12) estimate as previous reduced and display some (00:54:15) normal volatility in the reserve situation which explains the NOK 90 million on top of the NOK 250 million. Our guidance is the same thing going forward. You should expect around NOK 250 million a quarter with some volatility around that – nature of the business.

In terms of guidance, we don't have a short-term guidance. We only have long-term financial targets and they remain the same and we believe that they are perfectly achievable with the metrics that we have in place. NOK 90 million to NOK 93 million excluding runoff, NOK 86 million, NOK 89 million given the current runoff guidance.

And then...

Q - Operator

Just on the runoffs, if we can have a bit of – is there any reason of this increase, maybe this is because that's we are talking about NOK 340 million, so 5.8% versus 4.3% last year. How should we think about it going forward?

A - Jostein Amdal {BIO 19939645 <GO>}

It's NOK 340 million versus NOK 250 million, which is kind of the deviation from the guidance. This NOK 90 million, I just explained is partly due to kind of one large loss provision that has been reduced, and partly has some normal volatility around this. As explained, this balance sheet item is more than NOK 30 billion with estimates going 20, 30 years into the future, it's naturally somewhat volatile.

Q - Operator

Okay. Thank you.

Thank you. There no further questions left in the queue. I'll hand the conference back over to your host for any additional remarks.

A - Janne Merethe Flessum {BIO 19368607 <GO>}

Okay. Thank you for participating, everybody. Just reminding you of the roadshows we're doing this quarter to London, Copenhagen, Paris, and Edinburgh. We hope to see you there and hope to see you also in London tomorrow in the Analyst presentation there. Thank you and goodbye.

Operator

That will conclude today's conference call. Thank you for your participation. You may now disconnect.