

Conference Call Transcript

H1 2015 Results

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Operator (Audio begins in progress)

Ladies and gentlemen, welcome to the Coface results conference call. I now hand over to Mr. Jean-Marc PILLU, CEO of Coface. Sir, please go ahead.

Jean-Marc PILLU, CEO, Coface

Thank you very much. Good evening everybody. It is my pleasure to welcome you to the second quarter analysts call. As usual, I am with Carine Pichon, our Group CFO, to whom I shall give the floor within a few minutes. Today, in addition to our usual comments concerning Coface's business performance and P&L evaluation, we'll be able to give you information about our public guarantees activity in France - for which we have just concluded an agreement in principle today, with the French State.

Before that, let me say a few words about the world economic background which is, as you all know, a main driver of our business and performance. Please take a look at slide three, which gives you a quick summary of the situation. The situation is well summarised by the title, 'Slight recovery, although fragile and bearing risks' and the sub-title 'especially in emerging economies'.

If we take a closer look at the situation, what would be our assessment? Firstly, growth is robust in the US and is relying on well-oriented fundamentals. In the Eurozone, the recovery is gradual. We all know that the pace is different from one country to another - and that is without even counting Greece. However in emerging countries, the situation is more heterogeneous. Even if economic activity remains dynamic in some areas like Central Europe and emerging Asia (excluding China), the structural weaknesses that were already there are rising progressively among some of the emerging countries - and not the smallest ones - but countries such as Russia, Latin America (mainly Brazil) and China.

If we focus here and take a closer look at China, the context is deteriorating in both ways. Firstly, in the real economy, with the reshuffling of growth drivers from export and investment oriented sectors to internal consumption sectors, growth is decelerating. This has some consequences for the financial market, and especially on the stock market volatility.

In addition to these structural situations, falling commodity prices are affecting some of these countries, for example in Latin America, Africa and the Middle East.

This context is not new for us, as you may remember that we already mentioned it during previous quarterly calls in Q1 2015 and Q4 of last year. However this situation is more and more significant in order to understand the evolution of our figures. It's important to keep this in mind while you listen to Carine, to whom I give the floor to comment on the main features of our P&L.

Carine PICHON, Chief Financial Officer, Coface

Thank you Jean-Marc. Good evening everybody. For our figures, the main indicators are, as

usual, on page four. Turnover has increased for the first half year of 2015 by 5.1% and, at constant perimeter and FX, by 2.1%. This is even more if we focus on our premium, which growth is 6.8% and 2.8% at constant perimeter and FX. We have registered an operating income, excluding some restated items, of €104 million for this first half-year. This is based on a net combined ratio of 81.9%. This is higher, by just under four points, compared with the first half of 2014 and by around two points compared with the full year 2014. I will come back to this, with the main component being the loss ratio.

If we start with the commercial performance on premium I mentioned, there is a growth of 2.8%. This performance is based on new production, which is continuing to evolve at a sustainable level. The figure for this half-year is €76 million, compared with the first half of previous years, which were 66, 76 and 87. Last year was exceptional, but globally we are still at a sustainable level.

Client loyalty remains consistent. The retention rate for this semester is 89.1%. It was previously 90.6% in H1-2014 and 89.2% in H1-2013, so you see the trend is around 89 to 90% showing that clients are staying with us. In terms of prices, at -2.5 %, profitability and competitive pressure (and I will come back on some markets) continue to drive the price effect. It is more or less the same as in Q1, so we have the same trend. Concerning our clients' activity, the turnover of our own clients and the volume effect, you can see that there is a regain, but very, very gradual, with 1.9% compared to 1.6% in H1-2014. This is despite the slow pace of the global recovery expected this year. So that's the trend for premiums.

On page six, we can take a look at fees. We continued to grow, by 2.2% (0.2% at constant FX rates), with a ratio of fees above premium for this half-year at 12.1%. The turnover can also be looked at with a contrastive stance according to the regions, as you can see on page seven. We can see the same trends as in Q1. The increase in the Group's turnover is driven by emerging markets and North America. In Mediterranean and Africa, turnover grows by +16% at constant perimeter and FX, in Asia +8%, in Latin America almost +17% and in North America +4%. In these areas, the new commercial approach we have already had the opportunity to present and discuss with you, is producing results. In the more mature markets (let's point to Northern Europe and Western Europe), competition is clearly hard, with pressure on prices. The deployment of this commercial strategy is evolving and imposing a deep, structural change within the organisation. That is why the effects of these changes will only materialise over time.

On page eight, we have the loss ratio evolution before reinsurance. As concerns the curve of the loss ratio, we have an increase which already started in Q4-2014 and Q1-2015, again present with a loss ratio, just for this quarter, of 52.8%. This is specifically mirroring what we have said and what we've seen, with increases in claims in some emerging countries. Now if I comment the same loss ratio, looking at what is coming from the previous year and what is coming from the estimation of the loss ratio of the current year: the loss ratio of the current year is 73.3%, so a little higher. This integrates what we have seen in terms of claims increases since more than six months, and also a decrease in the positive run-off, with 24.3%.

As concerns costs evolution, on page nine, there is a slight increase in expenses. Growth in expenses was 5.6% at current FX rate. Internal overheads grew by 2.8%, which needs to be compared once we have restated figures of the FX change evaluation. On the right hand side of this slide, internal costs grew by 1.2%. When compared with growth in premium of 2.8%, we are clearly continuing to control our internal costs. The increase in global expenses comes from the fact that we have higher external acquisition costs, due to higher premiums for emerging countries - markets which are far more intermediated than the mature ones.

As for reinsurance results, the cost of reinsurance is 26 million euros. It was 36 million euros in H1-2014 : so we have transferred larger risks and, with a higher loss ratio, we have transferred more risks to reinsurance. So here we benefit from a lower cost globally for this half-year.

This leads us to page 11 and the net combined ratio at 81.9%. The increase you can see of 2.8 percentage points on costs, comes from external acquisition costs, which are higher because we have more work in emerging markets, with 3.2 percentage points. The -0.4 corresponds to internal costs - so the cost ratio of internal costs is decreasing. It increased by 1.1 percentage point in terms of loss ratio. You can also see the quarterly result on the loss ratio, on the combined ratio and it's composition. I will come back to this, but we should be careful that loss ratio from one quarter to another could change.

Turning to investment income, on page 12, the result is 28.2 million euros, compared to 22.3 in H1-2014, so accounting yield is a little higher. We continue to be prudent and proactive in terms of our investment strategy. As you can see, a large part of our portfolio is based on bond activities, which is quite prudent and safe. The economic yield is 1.2% for this half-year.

Finally, on page 13, we see the impact of all these results and our return on average tangible equity. The return of average tangible equity is 8.7% for the six months, and 9% if we exclude restated items. You can see the growth coming mainly from the tax rate and higher financial results. Maybe something that I can point out, which is not in the slide but is in the press release, is that the IFS rating of Coface has recently been reconfirmed by Fitch as AA- and that Coface SA, the parent company, has been upgraded to A+.

So that's it for the results and now on to the public guarantees, which Jean-Marc will comment on.

Jean-Marc PILLU, CEO, Coface

Thank you Carine. So on state public guarantees in France, you may remember that during our Q1 call, we discussed the announcement made in February 2015 by the French Government about its examination of the possibility of transferring the French state public guarantees activity from Coface to Bpifrance Group, a state-owned banking body. Since then, the French state has discussed the various aspects of the project (opportunity, impact, compensation etc.) with Coface. All of these discussions finally led to a result today. The French Government announced that it has decided to implement the project and we negotiated and finalised an agreement in principle on various subjects - mainly on the financial terms of such a transfer. As you can imagine, it was our priority to settle this subject in order to know, and very quickly to inform you on, the positive and less positive impacts on Coface.

So that is what I am going to comment on now. I will start by saying that I really think that we have reached a fair deal, if you consider the main elements of the agreement in principle. Page 14 looks at the main financial components of the agreement. The French state has agreed on the principle of a payment of €77.2 million, at the date of the transfer (I will come back to this). This amount corresponds to a valuation of around €90 million - the difference being the transfer of net liabilities estimated at the end of last year at €12.5 million. So the gross profit of the operation, when confirmed, will be around €90 million.

I will now continue with the financial features. When we'll report this amount in our P&L, we shall have to post a write-off of around €17 million as an immediate consequence of this transfer. This means that the financial compensation (of €90 million minus €17 million, so roughly €73 million), will allow us to contribute to facing the loss margin of this contract of around €12 million and the

retained fixed costs of around €21 million on a 12-month basis, based on the 2014 figures.

Coming back to the schedule, or the agenda, we should keep in mind that this transfer is subject to a change in the law. As we have been empowered by the law for this business, the transfer can be only implemented if it is voted for by the Parliament. This should be done at the Budget Act at the end of the year. That is why you do not see any of these figures in the Q2 P&L we are presenting to you today.

The transfer itself should be done during the course of 2016. At this present time, we do not know the precise date. Coface will run the service on behalf of the French State, as we are still doing, and we will continue to receive remuneration.

Last but not least, it is clear that nothing will move before consultation with the works council. If and when the decision becomes official, what would be the impact on the following years? On page 14 you can see that the decision should reduce mechanically our RoATE by 1.4 percentage points on an annual basis. However this is a gross impact and Coface intends to limit, as much as possible, the impact of this transfer on its accounts. I am launching a study for an operational efficiency programme in order to do so.

I think, at this stage, this is all I can say on this deal, as we are coming to the end of our presentation. It's time to open the Q&A session, so operator, if you want to do so. Thank you very much.

Operator

Ladies and gentlemen, if you wish to ask a question, please press 01 on your telephone keypad. Thank you for holding until we have the first question.

We have a first question from Benoit PETRARQUE, Kepler Cheuvreux. Sir, please go ahead.

Benoit PETRARQUE, Kepler Cheuvreux

The first question will be on the impact of the state public guarantee going to the French State. I just wanted to clarify, because I see two amounts, €11.7 million and €20.8 million. It looks like you will lose, in terms of net P&L, €11.7 million, and that's the equivalent of 1.4% of return on intangible, is that correct? I also wanted to clarify that's on a net basis and could you also clarify how much revenue and expenses you will lose on this deal.

Coming back to the fair value, if I just do 73 million divided by 11.7, I get 6.2 times, which seems to be a bit low to me. Could you explain to us a bit how the fair value has been calculated?

Coming back on the price, you will get cash of, I think, about €77 million. What will you do with this cash? Will that be used to restructure the business? You mentioned the efficiency programme you might launch – or could that be paid to the shareholders as a kind of exceptional dividend at some stage maybe this year?

Coming back on the business, just looking at the macro trend you described in emerging markets, does that have any implication for your combined ratio target of close to 75%? It seems that the trend is moving up now and I was just wondering if there is any kind of risk that you will come back to on this target.

Finally, I was wondering what you were actually doing currently, looking at your risk exposure. I know you don't disclose it on a quarterly basis, but I see your competitor is actually trying to limit now its risk exposure. Do you see any similar trends, so trying to now start to maybe cut a little bit on exposures in emerging markets? Thank you.

Carine PICHON, Chief Financial Officer, Coface

Good evening Benoit, I will answer your questions. Let's start with the French public guarantee. Let me explain what will happen. Once the change in law has been made - let's make the assumption that it's before the end of the year - we will automatically book a profit of around €90 million (so positive) and then a write-off of €17 million. What do we mean by 'Write-off'? It's mainly the depreciation we have on some IT systems. So the net impact in 2015 is before tax. All the figures I will discuss are before tax.

The point is that once the transfer has been done, we will no longer have the revenue and we will no longer have some of the costs. People will move and dedicated IT will move but we will keep some costs that can't be transferred. An example is the rent of the building, which we will keep and we will lose the margins. That is why the global amount we will lose - or we will keep - is €11.7 million plus €20.8 million.

That is the summary on costs and that is what we have to work on. As you can see, it represents a decrease of return on equity of 1.4% on an annual basis. That is why we intend to (and will) launch an operational efficiency programme, to limit the impact of this transfer. That is the way it is calculated. The 1.4 spread is clearly the 11.7, plus 20.8, based on our equity.

Benoit PETRARQUE, Kepler Cheuvreux

But your pre-tax profit will only go down by €11.7 million.

Carine PICHON, Chief Financial Officer, Coface

Our pre-tax profit will decrease by 11.7, you're right, this is the margin we will lose, but we will retain fixed costs that we no longer invoice to the French state. That is why the global loss is 11.7 plus 20.8, so it's €32.5 million before tax, on an annual basis. So that's the correct amounts corresponding to 1.4 basis point of RoATE.

In terms of prices, I will let you make the assumption, but we consider it a really fair agreement for both sides. We have had a lot of discussions with the French state and it was not always sure that we would have some compensation. So we have really struggled to achieve this, for the sake of our shareholders.

On your question as to what will we do with this amount, we will use it to finance part of the efficiency programme. We want decrease the impact of this event on the RoATE as much as possible, but it is clearly too early at this stage to give you more details. We will come back to you during the following months, to give you more information, once the plan has been clearly defined and evaluated.

You had a question on business and maybe on risk exposure? On business, in terms of evolution, -- what we have had in terms of loss ratio is confirming the trend we are seeing in emerging markets and have been discussing for over nine months. It is true that we don't disclose risk exposure, but you can imagine that on some risky sectors, in some risky countries, the exposure evolution is decreasing. This is not just for the quarter, but on a day-to-day monitoring level. So it

has decreased, because as I mentioned before, we already had these countries and sectors under scrutiny.

Benoit PETRARQUE, Kepler Cheuvreux

Sorry to come back on the 1.4%, but I don't understand how you calculated it. If I do the 69 times 2, for H1 times 2, minus €30 million, I get to something like 2 percentage points. I was just wondering how you calculate it.

Carine PICHON, Chief Financial Officer, Coface

Okay. Be careful in the equity to integrate the compensation.

Benoit PETRARQUE, Kepler Cheuvreux

Okay, so you write-off the €90 million in that...

Carine PICHON, Chief Financial Officer, Coface

In fact, we can come back, maybe within a year, to integrate the compensation and write-off in 2015.

Benoit PETRARQUE, Kepler Cheuvreux

Okay, and just to finalise, the €32 million you mentioned of loss, this is just pre-tax?

Carine PICHON, Chief Financial Officer, Coface

Yes, I confirm.

Benoit PETRARQUE, Kepler Cheuvreux

So that will be your €20 million net

Carine PICHON, Chief Financial Officer, Coface

Okay, it's not far.

Benoit PETRARQUE, Kepler Cheuvreux

Okay. Thank you

Carine PICHON, Chief Financial Officer, Coface

You're welcome.

Operator

We have another question from Michael Huttner from JP Morgan. Please, go ahead.

Michael HUTTNER, JP Morgan

Thank you. Just a couple of questions. You had, I think, 12.5%. Can you say something about your return on equity target for next year? And can you also say a little bit more where those losses came from and which geographies? Thank you.

Carine PICHON, Chief Financial Officer, Coface

On return on average tangible equity target, you're right Michael, it is a 12% in fact. It's just that you will have to integrate the impact of the French guarantee public procedure transfer. For the

other part of the business, it is too early for us to come back and to change that, as it's only one quarter's results, so we are continuing to monitor the risk. We have 18 months to continue to do the business and to meet our targets, so at this stage (except on the impact of the French state), there is no change on that.

Michael HUTTNER, JP Morgan

And just to understand where the losses came in this quarter?

Carine PICHON, Chief Financial Officer, Coface

The losses came mainly from the emerging markets we mentioned, as you can see in our results, some in Asia, some in Latin America and some in Russia. It's really mirroring the emerging deterioration in the countries I mentioned at the beginning of this call. In Europe the situation is good.

Michael HUTTNER, JP Morgan

Okay. Thank you very much.

Operator

We have a next question from Mr. Guilhem HORVATH, Exane BNP Paribas. Sir, please go ahead.

Guilhem HORVATH, Exane BNP Paribas

Good evening, all. My first question is on the public procedures. You mentioned an efficiency plan. I would like to know if you could give us a bit more colour on what you plan to do here, and do you actually expect to fully get the 1.4 points of return on equity that you're going to lose? And I will rephrase a little bit the questions from my colleagues. It's about both targets, return on equity and combined ratio. As the public procedures business was basically reducing your combined ratio, do you still plan to be able to achieve the combined ratio target you gave during the IPO? And jointly with that, the return on equity, which is very much linked because of technical profitability.

The second question is regarding a comparison I would make with your competitor, Euler Hermes. Yesterday they said that basically the claims frequency was going down for them but I understand that it's the opposite for you. Do you have some kind of explanation for that? What is your view on where it's coming from? Is it geography? I know that you're more exposed to emerging markets, but still I would appreciate a little bit more colour on that. Thanks.

Carine PICHON, Chief Financial Officer, Coface

Guilhem, for the first two questions I would have the same answer. The agreement with the state has just been signed, so it's really too early for us, but we will come back and inform you more, as Jean-Marc has told you, on the efficiency plan. When we do so, we will be able to tell you how the 1.4 points could tend to be offset by the efficiency plan. It is really too early. I prefer to come back with figures when they have been reviewed. We will then be able to give you more colour and explain how we intend to operate and implement this efficiency plan. It's the same answer for RoATE and the combined ratio, because you're right, that will have an impact on both indicators.

For Euler Hermes, it is very difficult to comment specifically on the results of competitors, as we can't comment on their operations and continual monitoring of business.

Guilhem HORVATH, Exane BNP Paribas

Okay, I get that. Just on the outlook, do you expect the claims frequency to go on like that in the coming quarters, or do you expect some kind of stabilisation?

Jean-Marc PILLU, CEO, Coface

Maybe I will take the floor on these two subjects to complete what Carine just said. Firstly, on the efficiency plan, let me remind you that during the past four, nearly five years, we have succeeded in reducing our internal costs, and this has been again confirmed with the publication of these latest Q2 results. So, an additional efficiency plan - compared with what we have already succeeded in doing as a permanent effort over the last few years - is not something we can yet determine, design and put figures on.

So, it needs time. It's not a question of not answering or not wishing to answer your question. We will answer your question. We will see if this will be during the Q3 or the Q4 call. As you know, we do not like to talk about things before they are precise and we have a certain degree of confidence that we will implement them.

That is why we are not giving you the figures today. We have just finished the negotiation of the agreement in principle with the state, and the implementation of the transfer with all of the necessary features to put in force is in front of us, not behind us.

In addition to this, we cannot even tell you how long our contract with the state will be extended to during 2016. So, you can see why today we are not able, for very technical reasons, while wishing to be as transparent as possible, to reply to your question on the combined ratio target, or in terms of RoATE, which is roughly the equivalent.

To summarise, what we know today is that in gross terms, this transfer would make us lose 1.4 points of RoATE on an annual basis. We also know that we will spend some days, weeks and months, continuing with the business for the French treasury next year. We don't know how long for, as we have not yet studied with Bpifrance the duration of the transfer process. The actual date of the transfer of the activity will impact the date of the extended contract with the state. This, in turn, will have a higher or lower impact on our combined ratio and RoATE for next year.

What we know in addition, is that we want – I want – to launch an additional efficiency programme. I want to strengthen the daily efforts we have been making for the last four years in order to keep internal costs growing at a slower pace than turnover. I want to launch an additional study – not only in France, but also in other Coface countries – to see what I can do in order to contribute to a kind of compensation towards the impact of the fixed cost remaining at Coface's charge and the margin loss equivalent of a little more than €30 million in gross terms (around €20 million net terms), for the years to come, including 2016, when the business will leave Coface.

I will progressively be more precise. Probably, before the end of the year, I will be able to give you and the investors a quantitative answer concerning the efficiency programme, which will include the forecasted cost decrease to be created by this plan, the speed at which we should be able to find the necessary decrease and the terms of additional provision, financed by the net profit of the immediate write-off that we will receive if and when the transfer is done.

So, in addition to these three elements you see that have an impact on the answer to your question to 12% RoATE or 75% combined ratio targets, there is the evolution of the economy.

And today, while we are talking, we are – as Carine said – one and a half years from the time in question. You can see how quickly the world is moving and how quickly we are moving. As you can see through the results of the past years, we are proactive and we anticipate crises in these countries. We continue to strongly monitor risks, even if we cannot avoid them in a moving world and a moving business, especially from one quarter to the next. It's really too soon to tell you anything about the potential impact of the evolution of our risk monitoring, with regards to the evolution of the economy for the next year.

To be more precise maybe on this question of frequency of claims and volume, etc., you need to bear in mind that in our business, the reason why we don't publish (especially quarterly) macro figures, such as exposure and number of claims, is because they do not give the right feeling about how our business is managed, the evolution of claims, and subsequently the loss ratio from one quarter to the next. As already explained during the IPO and our previous calls, the loss ratio we publish is very often impacted by very precise situations concerning specific countries or specific sectors. These specific situations may explain 100% of the evolution, even if in terms of percentage of number of claims and percentage of exposure, they do not automatically correspond to the same proportion of the big macro figures at the Coface level.

That's why it's useless, I think, to publish and to comment on these kinds of big figures, which are not really significant. But the evolution of the loss ratio from those specific countries we are currently talking about is under strict scrutiny.

Talking about the countries, what are the main countries? We mentioned LatAm, where the usual suspect is Brazil. If you come back to our previous quarterly discussion, you or one of your colleagues, asked a question specifically about Brazil. It's true that it's economy is decelerating more and more. There is a difficult structural situation in Brazil, and the country has been a concern for us for the past two or three quarters, since the end of last year.

We have other subjects concerning Latin America, but more on certain sectors. I don't want to talk too much about the sectors on this call, because it would be too long, but here again, it's not adequate to generalise. Our business is to focus, in a surgical manner, on the sectors and the countries where we have things to do. Another country I could mention is Russia, which you may remember we talked about last quarter and the quarter before: things are improving but it remains a country on which we keep a close eye.

Then you have China, which we talked about last quarter. I gave you China as an example of a country where, from a macro point of view, things are moving, but not in the right direction. This is especially the case in some sectors, including building and construction, textiles and metals. This has an impact on many other countries, because, for example, when China slows down, building and construction slows down, which means that the consumption of metals slows down. When investment slows down, less metal is needed from other countries such as Brazil and Chile. China is a concern, not only for us, but also for others. Just looking at the evolution of the financial situation in the equity market gives a proof of that.

We also mentioned Turkey and South Africa. Things are going positively in these countries, and I can tell you that call after call, quarter after quarter, the list of countries will change. The countries we are discussing today will become less important in terms of claims monitoring for Coface, while other countries will appear.

The figures we delivered during the last four or five years have been delivered under exactly the

same context as the one we are seeing today. This shows some quarterly evolution : starting I think at least for 2013, 2014 and the two quarters of 2015, you have the loss ratio quarter by quarter. You may have felt that we delivered good results while our loss ratio, quarter by quarter, was evolving in a narrow range. A range I could estimate of between zero to five points.

What we see today is exactly what I am describing and is in line with what we have seen over the past years. It's true there is a kind of progressive transfer from a European crisis to, let's say, a kind of multi-local crisis in emerging economies. This is very short, but that's how I could summarise the situation we have been going over the last two or three quarters.

Operator, do we have other questions?

Operator

Yes, sir. We have three other questions. We have another question from Hadley Cohen from Deutsche Bank. Sir, please go ahead.

Hadley COHEN, Deutsche Banks

Hi. Good evening, everyone, and thanks for taking my questions. Three points of clarification, please. Firstly, just on the retained fixed costs. Carine, I didn't quite hear what you were saying. Can you just explain what these relate to? I'm trying to get an understanding of one, why they're so big, and two, how easy it would be to remove some of those costs?

The second question is on the €11.7 million lost margin. I appreciate that's probably in line with what other people would have expected. That, to me, suggests that the profitability of the French State contract was weaker than the overall Group, which suggests to me that the underlying combined ratio for the rest of the Group, now that this contract is gone, should be better. Is that fair?

And then my final question relates to this efficiency plan. Would you have looked to implement this efficiency programme if you hadn't lost the French contract, and if not, why not? Thanks.

Jean-Marc PILLU, CEO, Coface

I will answer the beginning of your question, as Carine already answered some of them. What do we mean by fixed costs, I think your question is retained fixed costs?

We are talking about a business which was at the origin of Coface. Coface was created in 1946 for this business. It progressively extended its turnover by far, by developing its own credit insurance in such a way that it now corresponds to 96% of our turnover.

When we talk about public guarantees, we are talking about a contract of €59.9 million in 2014. This business was – how could I say, nicely integrated with our main business which accounts for the 96%. Furthermore, this integration benefitted both parties – the French State and Coface. It's the exact consequence of the term derived from the Greek word, synergies. It is exactly what happens when you make external acquisitions. You pay a certain price, which is the price of the autonomous business, but you are ready to pay this price because you consider that you will integrate this business properly and that your global business will benefit from fixed costs being mutualised and being optimised, not only on your former business but on the business that you just acquired.

When you loose business – let's use this expression - it is the exact opposite. You have disynergies. You have disynergies because your fixed costs are no more covered partially by the contract which is disappearing. Some examples of this are very easy to understand, for instance all the support functions surrounding this business. When we talk about the support functions, we are talking about IT, not the ones dedicated specifically to this business which will leave Coface, but the additional IT costs such as accounting software and the specific hardware on which the public guarantees were running. Carine also mentioned the example of the premises. There was an optimisation of the premises inside the Coface building, which will less be the case now.

All of these fixed costs amount to the €20.8 million that we mentioned. There are two complementary ways to cover these fixed costs. One is to sign additional contracts, which we will continue to keep on doing the maximum to achieve. We would have signed contracts whatever the situation of the public guarantee case would have been. Anyway, the more we sign contracts, the more we will cover fixed costs.

An additional way is to try to decrease these fixed costs, other fixed costs and any other kind of costs within the Group - especially, but not only in France. That is what the efficiency programme is for. You asked the question would we have implemented this programme if this had not have happened? Yes, for sure, but maybe not in the same way. Probably concerning the planning of implementation and the provisions to be made. We will see what amount of provision we'll have to make this year.

So probably, yes. You know the management spirit of Coface and we would have done it. It's only the way which will change, that is to say through an accelerated process with corresponding provisions to be made. We will do it in another, quicker way than we would have done, had this public guarantees case not been happening

I don't remember if you had other questions, sorry?

Hadley COHEN, Deutsche Banks

Yes, sorry. The other question was just on the €11.7 million. The margin by my calculations implies a weaker margin than at the overall Group level. Maybe I'm working it out wrong, but if that's the case then it suggests that the residual business now this contract has gone should have a better combined ratio anyway. Is that fair?

Carine PICHON, Chief Financial Officer, Coface

The €11.7 million of margin, if I've understand your question, was integrated in the cost ratio. So once it disappears, it will have a direct impact on cost ratio. I don't know if that was your question, but that's what I understood.

Jean-Marc PILLU, CEO, Coface

Everything being equal on the cost ratio, allows us to say that if we don't implement any efficiency plan, the impact would be (on a 12 months basis) 1.4 percentage points.

As concerns your question about the profitability of the business as compared to the global profitability of Coface, I don't think I will make the calculation here, but you have everything now to make the calculation. You may calculate the net margin rate by dividing 11.5 by €60 million of turnover, in gross terms. In net terms you can divide around 7.6 by the same turnover. That was for the full cost margin. If you want to calculate the marginal cost margin you can add to the €11.5

million, the €20.8 million of fixed costs which were financially amortised by the contract. And in this case the margin is higher.

It's very difficult to precisely answer the question. On the question of profitability, it is always about what do you take into account? A short view or a more medium- or long-term view? I will let you make your own reasoning, considering our cost ratio on all the global costs of Coface. It varies depending on the angle from which you are looking.

Hadley COHEN, Deutsche Banks

Okay. Thank you very much.

Jean-Marc PILLU, CEO, Coface

Other questions, operator?

Operator

Yes, we have another question from Thomas Fossard from HSBC. Sir, please go ahead.

Thomas FOSSARD, HSBC

Yes, good evening, three questions. The first one please, Jean-Marc, is are you today officially and maybe temporarily dropping the 12% return on the TNAV target?

The second question will be on the cost efficiency programme. If you have to offset the €30 million costs, if I compare that to your admin costs on a full year basis which are currently €217 million, will that imply that you have to cut costs by 10%, or a bit more than 10% right now in order to make up the 1.4 percentage point of loss in return?

The third question will be on claims deterioration. You see coming back to the chart on page eight, obviously the only way is up in terms of loss ratio deterioration. And what is linked to the erosion of margins linked to prices? What is linked to the deterioration of frequency and what is linked to potentially mid-size random claims you may have incurred in Q2 only? Thank you.

Jean-Marc PILLU, CEO, Coface

Thomas, maybe I will answer the two questions, as you named me. However you will be disappointed because I have the feeling that I already tried to answer as best as possible, the first question about the 12% RoATE target. It's not the time to answer in detailed commentary on the various components, as today I shall not be more precise. It's not because of unwillingness, but rather a question of possibility.

As concerns the potential impact of the operational efficiency programme, you are totally free to make your own assumptions, but here again I don't want to enter into this game of assumptions - as it would not look professional to you. As I just told you, we have just launched a study in order to be able to better answer this question. For the remainder of your questions, especially question three, I give the floor to Carine.

Carine PICHON, Chief Financial Officer, Coface

Yes. Thomas, just on your calculation, maybe just have in mind if we have a look at 2014 administrative expenses, it was €551 million. This is because you mentioned that it means a 10% decrease in costs, but I don't think it's true. On the basis of the full year it was €551 million. So you can see that the decrease is set to be lower.

In terms of claims and your last remark, what we have seen really in the countries we mentioned, is not really severity. It's not a question of one or two large claims. We would have told you if it had been a large claim in one country, in one sector. So it's not a claim, it's a global situation. In some countries I mentioned and also in some sectors, it's the mix between frequency and average, middle-sized claims. So not one big claim but a higher number multiplied by a higher cost per claim. So it's more middle-sized.

Jean-Marc PILLU, CEO, Coface

Operator, is there a question?

Operator

Yes, we have two more questions. We have a question from Michael Huttner from JP Morgan.

Michael HUTTNER, JP Morgan

Lovely, thank you so much. It was just a very quick follow-up question. When you mentioned the compensations from the French State, you said they were all pre-tax. So I was wondering what the impact would be net of tax.

Carine PICHON, Chief Financial Officer, Coface

The impact is a French tax rate. I don't know what the French tax rate will be next year, so I am cautious. But let's take a range of around 33, 32.

Michael HUTTNER, JP Morgan

Brilliant. That's very helpful. Thank you.

Jean-Marc PILLU, CEO, Coface

One last question?

Operator

Yes, we have one last question from Frank Kopfinger from Commerzbank. Sir, please go ahead.

Frank KOPFINGER, Commerzbank

Yes, good evening. Thank you for taking the question. My first question is on your net cost ratio for the Q2 standalone basis, on slide 11. Can you comment on why not only the claims but also the costs significantly went up in Q2? My second question is on your investment income for Q2. The question is whether there are any extraordinary negative items reflected there, because I would have expected that net investment income in Q2 is up further, as you have share of equities. And we saw also from other peers some seasonality from dividend income here.

Carine PICHON, Chief Financial Officer, Coface

On the net cost ratio, if we come back on page 11, you have the curve of the cost ratio. Just to mention the point that it is not internal costs. If you look at the trend quarter by quarter, we are decreasing internal costs. It's really on acquisition costs and maybe a technical comment between Q1 and Q2. Be careful. It was the case last year, if you compare Q1 and Q2 2014, we have a seasonality effect on fees. And you can see it really when you look at the detail of the fees at the end of the presentation. We have more fees which are more involved in the first quarter than in the second one. If you compare, we have around a €7 million difference. So knowing that the cost

ratio is not only expenses, because these expenses are offset by the fees, so from one quarter to another, if the fees are lower, the cost ratio is higher. So just be careful of this technical point from one quarter to the next.

For investment income, we have €28.2 million - so higher than last year and not very far from one quarter to the next. Maybe what I can mention is that we have, at this six months stage, gains on sales of equity and bonds. Maybe just to say that in this respect we decided to crystallise, and to take the profits on bonds just before the increase in the bond market. So that's why we have posted, for this first half year again, with global equity plus bonds at around €7 million. It was €3 million first-half year 2014. So, on that point I think we have fixed revenue and it was quite well done.

Frank KOPFINGER, Commerzbank

Okay, thanks.

Jean-Marc PILLU, CEO, Coface

Okay. Thank you. So, operator, as it was the last question I think it's time to close the call. And so I would like to thank you very much for attending and also, as usual, for the quality of your questions. I wish you a nice evening and a nice summer. We will see you again on the next call for Q3. Good bye.

Operator

Ladies and gentlemen, this concludes the conference call. Thank you all for your participation. You may now disconnect.

(End of Conference Call)

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FINANCIAL CALENDAR 2015

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This transcript, as well as Coface SA's integral regulatory information, consolidated accounts and H1 analyst presentation, can be found on the Group's website: <http://www.coface.com/Investors>

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