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FY-2017 Guidance

Conference Call Transcription

Paris, 28 September 2017

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Presentation

Carine Pichon, Chief Financial & Risk Officer - Coface

Thank you and good morning everybody. You will have seen that we published a press release this morning, explaining that we have decided to improve our full-year guidance for our loss ratio after reinsurance to below 54%. This represents an improvement of 4 percentage points compared to the most recent guidance given in July. This is clearly thanks to the effects of our investments last year, within the framework of the *Fit to Win* plan. These investments have been focused on our risk infrastructure and on enhancing information – particularly in the regions such as emerging markets where we were suffering losses. This is also thanks to the current improving global economic environment, as growth in all large regions is in a positive momentum.

This 54% for the full year, as of today, means that for the second half of the year our net loss ratio guidance is below 50%.

I would be happy to take any questions you may have around the new guidance we are providing this morning.

Questions and Answers (Q&A)

Michael Huttner, J. P. Morgan

This is lovely news, thank you. I was just wondering two things. When do you think you will be in a position to review your through-the-cycle guidance: the 83%? At the moment, the ratios are improving so fast, that it looks as if that could be the next step. The other thing is on costs. Apparently, on the press release there was a mention that there might be more investment in growth. Can you talk a little bit about that, what that might do to the cost ratio and how much you might invest?

Carine Pichon

On your first question, Michael, where we are exactly in terms of guidance for the plan, we said that we want to reach an 83% combined ratio across the cycle. This morning's news does not change this. We said last year that we need on average between 18 months to two years to see the full effects of our measures. On top of that, we have an economic environment that is clearly better oriented. You may have seen that yesterday we published an update of our country ratings and sector assessments. Once again, during this quarter, all of the revised country and sector risk assessments have been upgraded. This is another signal that, in terms of cycles, we are in a better position than we were in previous months. We are not changing our mid- or long-term guidance, which is to provide an 83% combined ratio across the cycle.

I will also link this with your second question. It is very important to make good investments. The investments we have made this year have started to strengthen our risk management and information capacities - for example, in terms of information quality and better tools. We have hired additional analysts in risk-sensitive countries and reinforced our underwriting processes. As well as upgrading and enhancing risk management locally, we have also done so at head office level. These investments should continue to have a positive effect on our loss ratio. Globally, when you look at the combined ratio, it was a good trade-off to invest a little more in costs in order to see the benefits in loss ratio. Clearly, our strategy is to create value. Therefore, we will continue to invest in value-creating measures throughout the period, so that we can improve our agility and ability to face changes in economic situations of local markets and agility in the way we serve our clients, as it is also very important to create value on a mid and long-term basis.



Michael Huttner

There is no figure for that, this extra investment in agility?

Carine Pichon

No, there is no change compared with what we said last year. We are following exactly the same momentum and framework and we will continue on that basis.

Michael Huttner

The 83% in the mid to long term and you mentioned 18 months to two years, it sounds as if you might reach it more quickly. Can you comment on that?

Carine Pichon

As you know, in credit insurance the market and the volatility around the cycle can change quite quickly and significantly from one year to another. I think here there is the effect of the measures we have taken, plus the fact that we are supported by a global economic environment which is clearly more positive compared to what it was last year or even at the beginning of this year.

Benoît Pétrarque, Kepler Cheuvreux

Two questions on my side. I will just come back, not on the 54% guidance, but on the 50% guidance for H2. Is that a level we could see in 2018 in the current environment? Clearly 50% is quite a low figure and I was wondering if it was something that you think could continue? When we try to split the 83% combined ratio guidance, I think you said in the past that it was roughly 53% loss, 30% cost (which might not be the exact split). This 53% is 50% now, so can we say that we are in a phase in the cycle now, where we are actually below the average loss ratio? Are you in a better than average cycle right now, from an economic point of view?

Carine Pichon

Concerning your first question, we said that we plan to have an 83% combined ratio but we never specified a dedicated mid-term guidance for our loss ratio and cost ratio. The reason for this is that the improvement in terms of loss ratio is a direct result of decisions and strategies. Sometimes it is better to invest and have more cost ratio, so that we can have a lower loss ratio. That is why we want to keep this agility in terms of the way that Coface is managed, to create value. At the end of the day, profitability is based on the global combined ratio (in this case 83%), not just on one specific ratio.

We believe that as long as we invest to create value, it is a good strategy and that is what we did that last year by investing in risk and information. This was the first pillar of the *Fit to Win* plan. It was a success as we can now see the positive effects. It is a strategy that we will continue over the coming months.

In answer to your question about where exactly we are in the cycle, it is always difficult to have a mid or long-term view on whether it will improve or deteriorate. However, it is clear that we are benefitting from a better situation than a few months ago. We will have the opportunity to discuss this with you again during the next quarterly call and I think that month by month we will probably have more to share with you on where we think we see the future.

Thomas Fossard, HSBC

I have two questions. On the 54% guidance on a full-year basis, can you give some clarity on what reserve releases we should expect on a full year basis and for H2? Are you seeing the benefits of maybe having been very cautious in terms of closing the accounts over the past two years and there is now this positive



effect coming back into the reported loss ratio in 2017? The second question is related to the strategy of Coface going forward. Clearly a major turnaround has been achieved in the underwriting profitability and in 2017 the environment is pretty good on the economic side, as you just described. Does that mean that we should expect Coface to be looking to gradually increase its risk exposure and seek a bit more growth going forward?

Carine Pichon

I will start with your second question on strategy. Our strategy has not changed since a year ago and we are continuing to focus on profitable underwriting, by granting limits at the correct price. We have not decided that we need to increase risk globally. What is important, is to continue to have a granular view of risk, as we put into place last year, on a per sector and per country basis. There is no change in this respect. We keep in mind that there may always be a spot in some sector or area, rather than look at the environment as something that is just globally positive. We will continue to support our clients and adapt our growth strategy to each market environment. This is very important and that is clearly the strategy that we will continue. We will follow what happens in each sector and each country.

To answer your first question, the way we calculate and estimate reserves is by following the rules which we put into place several years ago and there is no change in this respect. Last year, when we were facing difficulties in emerging markets, we had to issue a profit warning. This was also because claims declarations were being made later in emerging markets than we normally see in advanced markets. These uncertainties also led to a reassessment of our reserve levels.

In terms of what we are seeing today in Asia, Latin America and, to some extent North America (for some sectors and for US exporters to Latin America), the number of claims has decreased. There is therefore less volatility and uncertainty, which is important. We can also see that we had some major claims in North America last year - the like of which we have not had to book in this year. In addition, the recovery rate is improving for previous claims of this size. All in all, the uncertainties and volatility of last year, particularly those seen in H1 2016, have improved. That is why we have reviewed our target, which is linked to global improvements in this and past two underwriting years. In our Q3 announcement on 25 October, we will be giving you the split in change in loss ratios between what comes from prior years and the current underwriting year. It is clear that the improvements we are seeing mainly concern these 2015 and 2016 underwriting years.

Thomas Fossard

I would just like to come back to the first question and the top line growth expected for next year. Listening to what you have just said, should we expect Coface to stabilise its premium income in 2018 (compared to what you will achieve on a full-year basis in 2017), or should we expect small single digit growth?

Carine Pichon

We are not providing guidance on turnover, as we believe that what is more important is to create value and profitability. We are committed to a level of profitability and a return on equity. We will see on the 25 October where we will be in terms of turnover. We will also give an update on the different components of this evolution.

Hadley Cohen, Deutsche Bank

Most of my questions have already been answered, but just a couple of points of clarification please. I just want to make sure that the four-point upgrade that you are making on the net loss ratio is also a four-point net upgrade to the combined ratio. That is, for this year there are no offsetting factors on costs that you are seeing - or have you? Secondly, your guidance is below 50% for the second half of the year. We are actually only half way through the second half of the year, which implicitly suggests that Q3 is very, very strong and arguably in the mid-40s. Firstly, is it a fair assumption? And secondly, as that would be your best



quarter for several years, I was just wondering if there are any one-off items that we should be aware of, or anything like that, or if it is just down to normal business?

Carine Pichon

On your first question, we have only upgraded our loss ratio – we are not announcing anything new on costs, but we are continuing to invest. I do not have any other comments in this respect.

I am not sure I completely understood your second question but you are right - what we are saying for H2 is that we now have a guidance of below 50% for our loss ratio - which is clearly good. This is our base assumption and there are no specific major one-offs that we have included in this target.

Hadley Cohen

Essentially, my question was that we are only half way through the second half of the year, so there are still three months of the year to go. You are guiding to below 50% for the whole of the second half. As you do not yet know what the numbers are going to be for the fourth quarter, this presumably means that you have got a very, very strong third quarter. I was just wondering if there was anything within this third quarter that we should be aware of?

Carine Pichon

No, as of today these are our best assumptions, goals and targets. As I said, this is supported by a lower number of claims for the moment, by improvements in debt collection rates and the outlook for the market within the global economic environment. These are the bases for the review and today's upgrade for the end of the year.

Hadley Cohen

Just coming back to an earlier question, why can't we regard this below 50% as a more sustainable level into 2018?

Carine Pichon

I cannot comment on this for the moment.

Guilhem Horvath, Exane BNP Paribas

I have two questions. The first is going back to the improvements in the current underwriting year. I would like to better understand where these improvements come from. You explained about the normalisation of emerging markets and other elements, but are there also improvements coming from the mature markets? If so, what is your view on this, because these markets are already quite profitable and one could argue that at some point the profitability there should deteriorate? What is your outlook on this? I am a bit surprised to see a four point improvement to the net loss ratio just two months after the previous guidance improvement. What was the reason for upgrading the guidance by only three points in H1 and then coming back again so early to upgrade by an additional four points? The second question is on reinsurance. I am guessing that you are currently negotiating with your reinsurers for the renewal of your quota share and excess of loss treaties. My question regards quota share. What could be the impact of these improvements on profitability for your terms and conditions - and potentially your cession rates to reinsurers? Can you also update us on the current discussions and how it went in Monte Carlo? Are these discussions already well-advanced, or are you still in negotiations?



Carine Pichon

I will start with your last question on reinsurance. You are correct that we are continuing discussions with reinsurers, specifically in Monte Carlo. I think the reinsurers are happy with the improvements we were able to show in our loss ratio and we are having positive discussions with them. I would just like to remind you that last year, during the renewals for the underwriting year 2017, they played fairly with us. They have worked with us for a long time and we were even able to improve our reinsurance conditions. They trusted our capacity to recover our loss ratio, because they trusted the *Fit to Win* plan.

Guilhem Horvath

That is true, but now it is fact and it is always better to show that.

Carine Pichon

Exactly. As I say, it is good news, because we have proven to them that we can deliver on what we say we will do. We are now in discussions with them, but for the moment I cannot say too much more. They can see that we have made improvements to the loss ratio and we are in discussions around that.

Guilhem Horvath

Just a quick follow-up on this one, because I still do not totally understand how the commission ratio evolves in relation to improved profitability. Last year, I think you had something like 37% of commission ratio, if I am correct? Shouldn't this improve because you have a better loss ratio?

Carine Pichon

I think this is a similar question to the one you raised earlier, on what we are doing with new terms and conditions with the market. We are discussing the improvements in the loss ratio and how it can be translated into better terms and conditions. As I mentioned, we already had very good terms and conditions last year. We obtained lower prices for reinsurance (by comparison with previous years) and we were in a crisis, with issues in emerging markets. This also means that reinsurers trust our capacity to recover and they pay a commission which reflects that. We will now see what the improvements in terms and conditions will be compared to last year. It is too early to say, as Monte Carlo was only at the beginning of September and the negotiations may take up to the end of the year. When we know more for sure, we will be keeping you updated. But for the moment we are discussing with them, and I will come back to you on that topic.

Your other question was on where the improvements in loss ratio were coming from. In terms of the trends, the improvements are clearly coming from the areas where we were suffering losses last year – North America, Asia Pacific and Latin America. We have started to see improvements in these three areas over the last two quarters. We are continuing to see positive evolutions in these regions and a continuing level of good profitability in the more mature markets. This has led us to improve our guidance. We are also seeing a global improvement in terms of frequencies of claims.

You asked me why we did not revise our guidance even more in July. There were still uncertainties when we reviewed our guidance in July – more so than we now have in September. When we saw the new figures we had in terms of claims and debt collection rates, as we have a little less uncertainty, we decided to review our guidance again.

Michael Huttner

This is also on reinsurance. Thank you for this extra opportunity and really well done for this nice announcement. On reinsurance, you have this plan to improve return on equity with the help of more efficient reinsurance and the use of capital, etc. How is that progressing, because you were in Monte Carlo so are presumably now beginning to look at that in detail?



Carine Pichon

I am sorry, Michael, I understood the first part of your question, but not the second. Could you repeat it please?

Michael Huttner

You have a plan to improve return on equity with the help of reinsurance, by roughly one point by 2019. I am assuming that you have started discussions around this topic? I just wondered how these are progressing?

Carine Pichon

You are right, we reconfirmed this target and we are working with reinsurers. We told you last year that we will do it on a step-by-step basis - also because it is better to discuss this with the reinsurers when the situation is improving. Last year we took the first step by increasing our quota share. I think the good news that we are seeing this morning will also help in this respect, by showing a good balance between the cost of equity and the cost of reinsurance. That is what we are working with. It is progressing in line with our expectations and we will give an update in Q4 on capital, as we do every semester

Operator

We have no more questions. Ms Pichon will make the final remarks.

Carine Pichon

Thank you for very much for being here this morning. Coface is clearly in line with its Fit to Win plan and the upgraded guidance we have given you this morning is clear proof that we are delivering on what we planned last year. I look forward to commenting on the Q3 results on 25 October and to continuing our discussions.

(End of transcript)



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FINANCIAL CALENDAR 2017 (subject to change)

9M-2017 results: 25 October 2017, after market close

FINANCIAL INFORMATION

This transcript, as well as COFACE SA's integral regulatory information, can be found on the Group's website:

<http://www.coface.com/Investors>

For regulated information on Alternative Performance Measures (APM), please refer to our Interim Financial report for the first half 2017 and the 2016 Registration document.

About Coface

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