Please note that the conference call was accompanied by a complementary presentation in PDF format available on the Group's website: http://www.coface.com/Investors, under the "Financial results and reports" section.

FY-2019 Results

Conference Call Transcription

Paris, 5 February 2020

Presentation

Moderator

Welcome to the conference call for the presentation of Coface's results for the period ending 31 December 2019. All participants are in listen-only mode. Later, we will conduct a question and answers session. As a reminder, this conference call is being recorded. Your hosts for today's conference will be Mr Xavier Durand, CEO and Mrs Carine Pichon, CFO.

Xavier DURAND, CEO, COFACE

Good evening everyone and thank you for calling. We are happy to report our 2019 full year numbers. As you know, this is an important milestone for Coface, as it is the final year of our Fit to Win plan. I am even happier to report that we are recording another strong quarter, which actually caps a record year. We are reporting a net income of EUR 146.7 million, which is up 20% from last year and is a record for Coface. Our turnover reached EUR 1,481 million year-to-date, up by 5.9% at constant FX and perimeter. Underlying that growth, trade credit insurance is growing at 7% at constant scope and FX for the year. Later in this presentation, you will see that the same trends we have seen over the recent quarters remain true. Client retention is at a record high, new business is growing again and all regions are contributing to growth.

It has also been a strong quarter on the loss side. You will see that our net loss ratio for the year improved by (0.1) point, to 45.0%. Our net combined ratio stands at 77.7%. The losses for the fourth quarter come in at 44.8%. We are continuing to see good past claims returns and we have maintained disciplined underwriting within a riskier environment.

The cost ratio is down by (1.8)%, to 32.7% (versus 34.5%). We have maintained our strategy of continuing to drive strong cost controls, while driving business growth and investments. This brings our combined ratio for the fourth quarter to 80.4%, which is one point lower than for the same period last year.

Of the net income of EUR 146.7 million, EUR 29.4 million was for the fourth quarter. If we exclude non-recurring items, that brings us quite close to the EUR 150 million mark, at EUR 149.2 million. The earnings per share are a record EUR 0.97, which is up 23% year-on-year, so we are close to the EUR 1 per share mark.

I am also happy to report that we have just signed an agreement to acquire a company in Norway called GIEK Kredittforsikring. This is a EUR 9 million premium, so it is not a big acquisition, but it gives us an entry into the Norwegian market where we were not present other than by doing business through Sweden or Denmark. This is an additional way for us to acquire a position in this significant market.

Going on to page 5 and continuing on the highlights, our solvency comes in at 190% and we are proposing a dividend of EUR 1 per share. The return on average tangible equity comes in at 8.9% and if we take out the exceptional, we are above the symbolic benchmark of 9%, at 9.1%. The solvency ratio obviously now includes the usage of the partial internal model. As you know, this was approved at the end of last year and we can now reflect this in our calculations. We have also introduced the new methodology for calculating solvency for our capital requirements for factoring. Again, there are no surprises here. We have translated the comfort scale that we had in the standard formula, which you will remember was 140% to 160% and with the same risk framework, the new target range comes in at 145% to 175%. Consistent with what we have been saying over the last few quarters, we have increased our retention, that is to say, we have decreased our recourse to reinsurance on the quota share down from 26% to 23% for 2020, and that is included in the solvency calculation.

We are continuing to return funds to shareholders and the EUR 1 per share dividend is a little over a 100% pay-out. I am also happy to give you a number for Fit to Win, as in total we have returned EUR 390 million to shareholders. I am also happy on a personal level, as the Board has just renewed my mandate for another four years. Clearly, it has been a great journey leading Coface through this deep turnaround and I am excited about all the things that are still lying in front of us. We will actually be talking about these during our next planned presentation, which will be on 25 February. I invite everybody to join us in Paris for that event.

Going to page 6, I just wanted to give everybody a perspective on what happened throughout the whole Fit to Win plan. We are happy to have met or exceeded all of our objectives for the period. I have listed here some of the key metrics we set out for guidance, including the return on average tangible equity which was negative in 2016 and is now around the 9% range. As a reminder, this includes 0.42% of capital optimisation and we set a target of 1%, which will now obviously be achieved with the capabilities that the internal model gives us. In terms of savings, we had set a benchmark to save EUR 30 million in 2018 and we have exceeded that. We are continuing to work on this, as we are not changing our strategy of saving costs everywhere we can, in infrastructure, purchasing, organisation, simplifying the business, digitising and lean, etc. We reinvest the money where we see it is necessary and as you are aware, we have reinvested most of that money into better risk management tools, better efficiency, better service, more technology and some growth initiatives in different parts of the business. Our solvency ratio has improved by 40 points in three years - or actually by 45 points in four years if the end of 2015 is included, when we were around the 145 level. The combined ratio is below the target of 83% that we set for the business through the cycle. Revenues have grown by about 9%. As a reminder, in 2016 and 2017, we had a lot of portfolio cleaning to do, which actually led to some attrition in the book. We reset the baseline for what our salespeople had to achieve, and we are happy that growth has now returned, following the different turnaround actions we have led. Finally, you are all aware of the approval of the internal model. I think it was a key element for us in delivering on this plan, because as you know, while we were doing this, the standard formula has actually evolved in the opposite direction and the requirements there have been less favourable. Therefore, it has been a good plan and we are happy with these numbers.

Before I wrap it up, I am going to take you through the usual pages. Turning to page 8, to talk a bit about growth, you see there is the 5.9% at constant FX and perimeter I was talking about. Underlying this, trade credit grew at 7%. Other revenues were up slightly at 0.6% and this includes both services such as information and debt collection, but also the factoring business revenues. As you know, we have been repositioning factoring for about a year. We have a new team on it, the good news is that growth from information, and services offset the still-negative growth on the factoring book. In terms of fees, they are growing but they are growing less than the premiums. Obviously, we are in a part of the cycle where the losses are actually pretty good and we have less collection fees, so there is nothing surprising here.

If we go to page 9, on the regions, I think the good news is that every region in the world is growing. Our biggest challenge for Fit to Win was to turnaround the growth in Western Europe and Northern Europe, which are the oldest, biggest and most stable markets for us. Western Europe comes in at 3.4%, which I think is a record for the last 10 years for Coface. This is driven by both new business and strong retention in France and the UK. Northern Europe shows a 1.5% headline that includes a drag from the factoring business, but if that is taken out, we are up 3%, which is again another record for the last 10 years in Germany and Northern Europe. Central Europe has been growing less than in prior years. We have undertaken restrictive actions on risk, in Poland in particular and I think we have been quite deliberate about this. We now also have the integrated PKZ business in these numbers, so less growth but you will see that the risk actually benefitted from these measures. Med and Africa continues to be steady in terms of growth, where both new business and activity remained pretty good. North America is growing again at 4%. Here, we are seeing much better retention and new business picking-up towards the second part of the year. In Asia Pacific, when you take out the one-offs that we had in 2018, the underlying growth for the region is about 10.8%, so not quite as spectacular as the 17.8% that you see here on the slide. However, the business is back on the growth track after we cleaned up the book and reset the baseline. Latin America shows pretty impressive growth at 24%. As a reminder to everyone, this is linked to some very large multinational contracts we signed back in 2018, which were fully in force in 2019 and where the proportion of Latin America was bigger than average. However, these are global contracts where we actually look at the profitability of that piece of business throughout the global P&L.

On page 10, you will find the usual breakdown of our growth numbers. There is a turnaround going on in terms of new production. The total number for the year is EUR 133 million, up EUR 17 million from where we were in 2018. It is also higher than 2017, so I think it confirms that the actions we have taken in terms of turning around, particularly for our mid-market segments, are working. Client retention continues to improve and at 91.6%, it is an absolute record for Coface. This shows the company is making progress in terms of servicing our clients. Price effects remain negative, which I think is quite natural given the loss ratios we are seeing. However, it is better, and we have been able to see some price gains, particularly in certain markets that were more volatile, and we will talk a bit more about that. Volume effect, after reaching a peak, which was in mid, or probably the beginning of 2018, has been constantly and consistently dropping, so the number for the last year is 2.8%. You are all aware of the slowdown of the global economy that has been ongoing since 2017 and I think that is what we are seeing here - so I am not expecting miracles here on that line given the current circumstances.

Turning to page 11, the loss ratio for the full-year, before reinsurance and including claims handling expenses, comes in at 43.4%. This is about 0.8% below where we were in 2018. On the quarterly split, I think we need to consider the number that takes out the facultative reinsurance business, basically contracts where we seek specific reinsurance for a risk that we do not necessarily want to keep on our books. The quarterly sequence continues to be pretty good, at 46.3%, 42.2%, 41.9%, 45.1% and 44.4% for the fourth quarter of 2019. This shows continued good risk performance, in what is a riskier economic environment. I will talk about this towards the end of this presentation. When you look at the sequence on the bottom right-hand side, you will see that we open the year at 73.1%, which is in the middle of the range where we were in prior years. However, we continue to see high recovery rates, at 32.2% for the year. I think this shows that the discipline we have put in place in terms of managing risk is continuing to pay-off.

On page 12, we show the split of the risk numbers by region. The four large, more stable markets are at the bottom of the page. The work we have put into controlling risk in Central Europe is paying-off. They had a year at 42.5%, which is much lower than the more or less 50% range they were in for the prior three years. Western Europe is very stable at 34.6% and very much in line with the past. Northern Europe, including mainly Germany, has actually made quite a bit of progress and comes in at just below 41%. Again, there has been a lot of work done on the risk side here. Med and Africa is very stable at 46.3%. The three more volatile markets that have created more headaches in the past are on the top line of the slide. North America had a pretty good year overall at 45.8% and I would say a strong year. As you may remember, we saw a bit of a blip in the third quarter, but the fourth quarter was actually pretty good. After the trough in 2018, Asia Pacific is coming back up and at a pretty good level. Latin America is by far the most challenging market. I think this is no surprise to anyone, as you are all aware of what has been happening in Argentina, while social movements in Chile have also significantly influenced risks. However, I think the performance was pretty good and excluding foreign exchange, which introduces a bit of noise into the numbers, we came in at 51.8% in 2018 and 53.4% in 2019. I would say we have benefited from very positive reactions from our teams in Latin America to some unpredictable events. I think this validates the strategy we have been trying to put in place over the last few years, to contain risks in different parts of the world.

Page 13 is on costs and you can see that in total they were up 2.3% for the year. Obviously, we get leverage since the growth for the top line is close to 6%. There is a bit of a surge in the fourth quarter and I just want to give you a bit of a walk through from the EUR 132 million we had in Q3, to the EUR 144 million we had in Q4. You may remember that we had a EUR 2 million exceptional good guy in Q3, so that obviously did not repeat itself. We had a EUR 2 million-profit share for employees, which is a bit of an exceptional here, as we ended the plan in the fourth quarter. There are EUR 1 million of additional costs in North America. This is the transfer from external acquisition costs (shown by the light blue line) into internal costs (shown by the dark blue line). So the top line is growing and you would expect our intermediation costs to grow - but we are buying out our distribution in the US to regain control and that continues to drive more costs. There is a EUR 1.6 million non-recurring VAT item. Then, we decided to accelerate some IT investments towards the end of the year, at EUR 3.7 million. That is in-line with the plan, but this plan was back-end loaded, so it was bigger this quarter than it is usually. In total, the cost ratio before reinsurance was EUR 35.9 million for the quarter. On the bottom right of the slide, we show how we come from 35.9% in 2018, to 34.4% for 2019, which is a 1.5% improvement. The bulk of that is really driven by the difference between the growth in the top line and the growth in costs without, as I said before, compromising in any way the investments we need to make in the business.

I will now turn it over to Carine.

Carine PICHON, Group CFO and Risk Director

Thank you, Xavier. Good evening everyone. Before I present the 2019 reinsurance results, just to let you know that we have decided to review the cession rate on the quota share for reinsurance, which has decreased from 26% in 2019, to 23% for 2020. This will start in January 2020 and as before, it will be split into two quota shares on a two-year period. Having said that, looking at the 2019 figures, which do not yet include this change, we continue to have quite similar cession rates from a premium point of view, at 28.6%. It was 28.7% in 2018, so it is quite stable. On the cession rate, we have ceded 26%, which corresponds to the actual 2019 quota share.

Continuing on to page 15, the net combined ratio stands at 77.7%. This is a decrease of 1.9% compared to 2018. Looking at each of the components, we have a stable loss ratio at 45%, which is a good result considering that the environment was more volatile than in 2018. Positive operating leverage helped us to decrease the net cost ratio by 1.8 point from 34.5% to 32.7%. It is also positive on a quarterly basis, falling from 81.4% in Q4 2018 on combined ratio, to 80.4% for Q4 2019. We continue to have a stable loss ratio, under control at 44.8%, within a riskier environment. Globally, the Q4 combined ratio is also below the though the cycle target, at 83%.

Page 16 presents the financial portfolio and results. With our EUR 2.8 billion of portfolio, we continue to focus on stability as much as possible. The accounting yield is quite stable, at 1.6%. This clearly reflects the fact that during 2019 we decided, and deployed, an increased allocation to real estate during the year, so this is a benefit we have for 2019. In our net investment income we have not only the results of the financial portfolio, but also the impact of the decisions we took from a strategic point of view to disinvest in Peru and to review our legal infrastructures in some countries, particularly in Africa. This led to some impairments in the net investment income and that is the reason for the decline.

The net income can be seen on page 17. You can see the split between current operating income and net income alone. There are some things to comment on that are new in Q4. On a yearly basis, we have investment and restructuring expenses of EUR 7.5 million. In particular, we have continued to try to find some efficiency measures and carry out some reorganisations. In Germany, we announced a new plan in Q4, which is why we have booked additional restructuring charges in that quarter. The tax rate is still 28%, which is in-line with what you have seen during the year and is better than 34% we reported for 2018.

On page 18, we have a view on return on average tangible equity. RoATE stands at 8.9%, up by 1.2 point compared with 2018. I will comment on the equity because you can see that it has increased from EUR 1.8 billion to EUR 1.9 billion. Knowing that we have distributed 100% of the result in 2019, the main explanation is the revaluation of our bonds portfolio. Following a decline in interest rates, our bonds have a higher value, as can be seen in the change in our equity. The return by itself rose from the 7.7% reported for 2018. Thanks to improvements in technical results - overall costs and loss control - we have a positive impact of 1.2 point. As concerns the financial results, as I mentioned, it was mainly impairments and some non-consolidated entities that led to minus 0.7 point. Improvement in tax rates contributed positively, by 0.5 point. The published RoATE result is 8.9%. Excluding some non-recurring items, it is effectively 9.1% for 2019.

As you are aware, we also comment on capital and balance sheets every six months, so I will go through this now. On page 20, we can see that the balance sheets continue to be solid. We continue to have very good ratings from Fitch and Moody's, which are key for our industry, as we need good ratings for our clients. On page 21, you will see our new comfort scale, which is the new method of calculating capital requirements based on the Partial Internal Model that was validated at the beginning of December. This range is now between 145% and 175% and the capital management principles remain completely unchanged. This framework helps to support the growth of Coface and obtain good ratings from rating agencies and that is the way it has been built.

On page 22, you can see the solvency evolution over time. Solvency has risen from 150% in 2016, to 190% in 2019 - so an improvement of around 40 points. It is interesting that we made a pro forma of this solvency ratio under the Partial Internal Model at the end of 2018, which would have made it 187%. At end of 2019 solvency stood at 190%, so it appears to be quite stable. However, if you look at the change in each variation, we have a decline in ratio coming from two effects. The first is that we need to support growth - and as a reminder, our growth on premiums is around 7%. We also need to finance the decision we took to reduce the cession rate from 26% to 23%, so it is already integrated into that valuation. We also benefit from a positive factoring evolution. A change of methodology led us to six points of improvement, as well as an improvement from own funds variation. I commented a moment ago that we have been affected by the revaluation of our bonds portfolio. All in, the ratio is stable and robust at 190%. For the first time, we are also presenting how this ratio would evolve in some stress cases. It continues to have low-sensitivity to market shocks, as that is the way we are managing our capital. If there is a either an interest rate increase or spread evolution by 100 basis points, or a 25% stock market decline, the impact on the solvency ratio is a maximum of six points. It is clear to see that we have low-sensitivity, but you will not be surprised to learn that we are still sensitive to a crisis scenario of 1/50 equivalent. This would mean that our ratio would decline to 169%, which is a decline of just over 20 points.

On page 23, we have the solvency capital details. Looking to the right of the slide, we can see that the 190% represents eligible own funds of EUR 2.2 billion. The breakdown of capital is mainly Tier 1 and Tier 2, with hybrid debt. We have a solvency-required capital of EUR 1.1 billion, which includes just over EUR 200 million for factoring activities. As previously mentioned, factoring required capital is now computed on standard methodology with all Basel 4 changes. This means 10.5% of risk-weighted assets.

Xavier DURAND

I am just going to wrap this up with a few comments on page 25, on where we are and the outlook. I think that Fit to Win has clearly met or exceeded all of its goals. We have really worked hard on the risk infrastructure. We have worked hard on service and efficiency. The cost base has been looked at in alignment with revenues. It is comforting to see that the business is back on a growth path, with better retention and the commercial momentum that we needed to offset the decrease in client activity that is happening. Net income is clearly at a record level, while profitability is very close to record levels. The balance sheet has been strengthened and you can see that solvency, at 190%, is strong.

The next step will be presenting our plan on 25 February. This will be based on the continuation of what we started three years ago, which is a deep cultural transformation of the business. I will come back to this. We are seeing this plan happen within a global economy that is growing at a slower pace. The way I would look at the economy is that since 2017, when we had a peak of synchronous growth between Europe, Asia and the US, things have been slowing down. I think we have been right and pretty clear about calling this out back in the middle of 2018, but we see this continuing this year.

There are a couple of underlying things to look at. First of all, debt levels around the world are pretty much at record levels, but this has been made quite painless by the fact that central banks have lowered interest rates. In parallel to all of this, we continue to see deep technology shifts impacting certain business areas. We can include here e-commerce, the energy transition and the advance of 5G, all of which will cause major transformations around the world. These deep transformations are impacting traditional players and continue to threaten their position. Then, because the global economy is growing at a slower pace, there is more fighting about who gets what share of the cake. This is actually taking place on a global scale. We are all aware of the increased trade tensions between the US and China. When you look at all the trade measures that have happened over the course of the last two years, there are over 1,000 a year. These measures are not only about the US and China, as they account for about a quarter of all these measures. Other countries have also been very active in protecting their markets.

The second phenomenon is that we are seeing more and more social movements within countries, in terms of how to split the pie. Last year was pretty impressive, with social movements in France, Hong Kong, Chile, Ecuador, Lebanon and Algeria. These events are very hard to predict, and I think they reinforce the importance of agility that we put forward when we put this plan together three years ago.

I think that the latest news about the health worries in China just compound this phenomenon. It is very hard to predict, but is certainly something we are watching very closely. This notion of agility is important and ties into our business culture. We have put together these cultural traits of being extremely customer-centric and I think you can see that in our client retention. We have expertise because our clients are here to buy our products and services. They are here to access the knowledge of our experts all over the world, our ability to monitor 70 million companies, our excellent data management systems and our latest technologies in analytics. There is great collaboration between our teams, because when something happens such as the movement in Chile, it is really our teams there who know what is going on. They are reading the papers, they speak the language, they are on-site and they understand the deep fabric of the economy. However, this team collaboration needs to be global, because our clients are global. So collaboration is the other key value we have put in place. Finally, we have to react quickly, sometimes with less than perfect information, but we do need to act and so this whole notion of accountability and courage is also at the heart of what we do. This cultural revolution that we started, making really deep changes in Coface over the last three years, is directly tied to our business model and I think it is well underway.

I just wanted to highlight a few things before opening it up to questions. As I said, we will be presenting our new plan on 25 February 2020 in Paris and you are all welcome to join us. We will be happy to answer questions as usual.

Q & A session

Thomas FOSSARD (HSBC) I have a couple of questions. The first one is related to the Solvency II ratio and the new model and maybe also related to the new comfort scale you are providing on slide 21, so there will be two sub-questions. Firstly, can you help us to understand why the range between the minimum and the maximum has increased from the previous case? Previously, I think you had 20 points and you now have 35 or 30 points. Also, could you help us understand what the 130% and 145% would mean if you were to reach these levels? Secondly, year-on-year, we have actually seen growth accelerating. I think that you have signalled that you were gradually more comfortable in getting this growth on-board. Could you help us to understand if there was anything special in the 6% or 7% top line growth you achieved in 2019? Or, to put it in a different way, will 6% or 7% growth be a realistic assumption for 2020?

Xavier DURAND (CEO, Coface) I will start with the comfort scale. We have just taken the scale that you are familiar with (with the standard formula) and we have translated this, in terms of the statistical meaning of the scale, into the mathematical language of the Partial Internal Model. This means that the mean and range of the scale represent the same range of variation in risk events - or the probability of variation in risk events - and their impact on the solvency ratio. I think that the best way to read this is just to say it is the same scale, but the numbers have changed, because the methodology for counting has changed. So, you would see the same triggers, triggering the same events that we had before, on different scales.

In terms of the growth, as you know, there was a time when the company had to readjust its risk metrics, back in 2016 and 2017. We basically re-based the products we had to sell and the risk appetite that we were comfortable with. Then we set about turning around our sales organisation. You are right to point out that this is something that we hope is going to continue. However, the client activity that we enjoyed in 2017 and 2018 was exceptionally high and I do not think there is any way that this is going to continue to be the case within the current economic environment. This is no surprise because we are in a slowing economy and the clients that we serve around the world are not particularly seeing a lot of growth right now. I think it just makes sense.

David BARMA (Exane BNP Paribas) My first question is on reinsurance. Is the drop to 23% the first step you have negotiated as part of your bi-annual programmes? Are you planning to do more there, or are you comfortable with that level? Secondly, just as a follow-up on the previous question on the solvency comfort scale, you mentioned two reasons in your slides, but from your answer should we understand that the increased range does not reflect a changed view on the buffer you would want, given the macro conditions? Linked to that, you are at 190% after accounting for the change in reinsurance and you are still growing, but your capital consumption will be low going forward. On the M&A front, you have flagged many times in the past that the deals out there are quite similar to the one you have just announced today, in terms of scale. How should we read your current capital position versus your new comfort scale?

Xavier DURAND (CEO, Coface) On the capital position, I think we really have not changed our strategy here, or the way we think about the business. Our solvency has been strengthened and it is above the comfort scale we have just discussed. That is why this year we are again distributing 100%, actually a bit more than 100%, returning a dividend of EUR 1 per share to the shareholders. A few things happened, with obviously some growth in the underlying business, which pretty much translates directly into the growth of our capital solvency requirements. As you pointed out, if they become available, we will make some bolt-on acquisitions in a number of areas where we think we can actually benefit from a market, or from a scale standpoint, or in taking positions that we could not access from other markets. These things will basically be the way we see we are going to employ the capital at this stage.

Carine, do you want to talk about reinsurance?

Carine PICHON (CFO, Coface) On reinsurance, we have decreased from 26% to 23% and we will see what it will be for 2021 and the years to come. It seems to be a good basis for starting the first year of the new plan. So that is one of the targets as of today, knowing that it is already an exercise we are undertaking - to find the correct price for the capacity we buy. It is something we may adjust, but globally it seems to be a good base scenario.

Hadley COHEN (Deutsche Bank) Xavier, you talked about coronavirus but I was wondering if you have actually noticed any impact on the business from that yet? Secondly, I think within the investment result in the fourth quarter there were some negative hedging effects and I wondered if you could quantify those. I think I asked this question this time last year as well, but Carine I just want to make clear that the 190% solvency ratio is already adjusted for the EUR 1 dividend. So is it net of the dividend number? Finally, Xavier, I think you mentioned on the last quarter's call that up to that point you had achieved, I think, about 40 points of the planned 100 points capital optimisation within the Fit to Win strategy. Post this EUR 1 proposed dividend, I was just wondering where you think you after that?

Xavier DURAND (CEO, Coface) The answer to the quick easy question on 190% is "yes", it does include the dividend. That is the methodology we have to follow for calculating solvency. I will let Carine answer the other questions, but let me talk about the virus. Obviously, as you know, it is something that is pretty recent. It is literally developing by the day. I think the measures that China and some other countries are now taking are pretty extraordinary compared to anything we have seen in the past. The first thing I will tell you is that it is bigger and will have more impact than the crisis that happened in 2003 and 2004 with the SARS epidemic. It is bigger because the measures that governments have taken are stronger. However, the question is whether it is going to last and at this stage, I think it is anybody's guess and very hard to make any forecast. We could be completely wrong. We had our country risk conference yesterday, with four experts debating on China and what is going to happen in 2020. We had all sorts of forecasts and they were all different. Some said that such quarantine measures will actually have a huge effect and this virus could go away pretty quickly. Others said this is the biggest epidemic that we have seen in years and the effects will be profound and long lasting. We do not know but I can tell you that it is too early for anything to be seen in the numbers, because obviously payment delays are longer than the time this thing has been around - and as you know, parts of China have more or less been put on vacation. It is too early to see anything in the numbers or to have a very definitive view of where this is going. The things I have said before remain true. People in the business are watching this very carefully, the teams are on it and we are going to manage this like we managed the other events that have happened over the course of the last year around the world.

Carine PICHON (CFO, Coface) I will start with capital. You say that we have returned 42 basis points of the 100 basis points that were targeted, but I would say that after distributing a little more than 100% of our results in 2019, it will be more like 60 basis points. We will discuss the rest with you on 25 February.

In terms of net investment income, you are right to say that we have had a small increase in our hedging costs. As you know, we do hedge our equity book, mainly to avoid big shocks, but also to register capital requirements on that class of asset. That is why hedging costs did show a slight increase in Q4.

Thomas FOSSARD (HSBC) I have two additional questions. The first one is related to coronavirus. I understand that it is still early, but it seems that this is already leading to a pretty significant slump in commodities. If I remember correctly, in previous years you had some issues related to commodity traders. Could you help us understand how your exposure to these businesses may have changed over time? Beyond that, have you already taken some precautionary measures in some geographies or industries, which you believe, could be more significantly exposed to what is happening? My second question is slightly technical. On the 23% cession ratio, is that the writing year cession ratio – in other words not what you are expecting it to be on the financial year basis for 2020? Also, I think you have two quota shares, one of which renews each year? When are we going to effectively reach the 23% on a financial calendar year? Thirdly, on the costs, perhaps we will have more information on this on 25 February, but you have been cutting costs massively ahead of your initial expectations. How much further do you believe you will go beyond the current level? Are you reaching a point where things are going to be a bit more difficult and maybe additional investment will have a slightly bigger impact on your P&L going forward?

Xavier DURAND (CEO, Coface) Let me start with the virus. You are right to point out that there has been some impact on commodities, particularly oil. However, it is not nearly as brutal as what happened in 2015. If I recall correctly, we had oil at USD 110 going down to around USD 40. This time, we have USD 60 going to down to something like USD 55, which is roughly a 10% loss. So the magnitudes are not the same. The other thing I would tell you is that cutting the commodity trading business was a big part of what we did in 2016 and 2017, so I believe our exposure is now much lower than it was then. In terms of other industries and other measures, of course we are monitoring these, but it is still very early days. The key here for us is to be selective in what we do. I would just mention that China makes up about 2.6% of our overall exposures - and that includes everything in China. The province that is being touched is a much smaller piece of that, just to give you some perspective.

Let me say a few words about the costs. You are right to point out that when you start on a cost-cutting programme of course you get the low-hanging fruits and once they are picked it gets harder, because you have got to climb higher in the tree and there is not an infinite supply of them. That is true, but it is does not mean that we are not going to keep trying. The other thing is that we have been making disciplined, steady and continued investments - not just to deliver short-term results, but also investing in what we believe is key to drive this business forward. I have consistently mentioned risk controls, compliance, services, technologies, processes and growth. I think the mixture of all these different ingredients has actually worked. We are walking a pretty fine line between all of these different constraints and we do not intend to change this way of thinking. The fruits are harder to get, but I also think that the investment has to be commensurate. The other thing I would mention is that some of the investments we had to make initially will not have to be repeated - so that is true on both sides.

I will let Carine talk about the cession rate.

Carine PICHON (CFO, Coface) Thomas, you are right. On reinsurance, the 23% is related to the 2020 underwriting year. However, what we have done is to keep an alignment between both treaties and we have also renewed the other reinsurance treaty by anticipation. The 23% is split into two quota shares, one which will finish at the end of this year and one which will finish at the end of 2021. That means that the impact on the financial year will be in proportion to the premiums that are underwritten in 2020. As you know, we still have 2019 premiums, which are 26%.

Thomas FOSSARD (HSBC) On the financial year, the 23% is to be expected for the end of 2021?

Carine PICHON (CFO, Coface) The full effect on 2021, but significant impact on in 2020.

Rahul PAREKH (JP Morgan) What is your outlook on Western Europe with Brexit now happening and what is your view on rising insolvencies for the next couple of years? There were some impairments due to Peru and some other entities. I was just wondering if there was any goodwill or impairment risks to come over the next year? Finally, do you look at reinsurance as a factor to offset the slowing economy - or is it something that you continue to look at even if the economic outlook changes?

Xavier DURAND (CEO, Coface) Let me talk about the reinsurance question. There are two parts to our reinsurance programme, one is a quota share and the other is an excess of loss type of policy, which is there for risk mitigation purposes. We are not changing this second part, which has been very constant over time. What we are changing is the quota share - that is how much of the business we retain and how much we cede to reinsurers. This is something we adjusted upwards, back in 2016. The reason we did this was to start to get some capital optimisation. Our cost to capital at the time was not as strong as our friends in the reinsurance industry. Things have changed a little bit since then and that is why we are taking the reverse route here.

In terms of Western Europe, Brexit started four years ago and literally weeks after that happened, we saw impacts on the British economy. I would say that the UK was lucky because they started Brexit at the peak of the cycle, so they did not really feel it that much for the first few years. Nevertheless, construction and retail slowed and there were some pretty visible bankruptcies in the retail, construction and food and beverage spaces. Since then, it has been continuously slow and I think over the last two years we have seen insolvencies in the UK rise by about 17%. If you contrast this with France, where insolvencies dropped 4% last year, this is a pretty significant impact. We expect insolvencies in the UK to continue to rise. I think what has happened with them getting out of the EU has not actually changed anything this year and we are in the same situation we were a year ago. However, what is now in front of us is that they have to cut a deal somehow with Europe and we do not know anything more about it now than we did a year ago in terms of where it is going, or if it will be a hard or soft Brexit. For me, in terms of our business, there has not really been much change in terms of this milestone of leaving Europe, except that we now know that they are going to have to cut a deal, or find a way to go forward.

In terms of Western Europe, I think we are going to see the same trends we saw last year play-out again this year. We have a slowing European economy and although France has actually been doing pretty well, Germany has been slow and probably the slowest in a long time. There is a sort of two-speed economy and I do not think we can expect any change in these trends in the short-term. The industrial space has been hit, including the automobile industry among others and we are not going to see a turnaround in the very short-term. Carine, do you want to talk about Peru?

Carine PICHON (CFO, Coface) Concerning impairment, it is not impairment on goodwill, it is impairment on the shares we had in the Peruvian entity. We could see that the way we were operating with this entity was not positive and could not be profitable in the years to come. That is why we reviewed our structure in Peru and decided to liquidate the company, while continuing to support our clients from Chile because it would be more profitable in the future. It is difficult to say if there will be any other similar decisions in the future but let us say that we do not anticipate it at this stage. If it were the case, we would have put a note in the P&L.

Xavier DURAND (CEO, Coface) I think we are past the hour and we usually keep these calls to about an hour. I think the interesting thing about this call is that we are just a couple of weeks away from our new plan. Again, I invite everybody to join us in Paris for the Investor Day that we are going to have. Obviously, this will focus on talking about where we go from here and there will probably be more questions that we will address. I want to thank everybody for joining this call.

(End of transcript)

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FINANCIAL CALENDAR 2020 (subject to change)
Investor Day: 25 February 2020 (Paris)
Q1-2020 results: 23 April 2020 (after market close)
Annual General Shareholders' Meeting 2019: 14 May 2020
H1-2020 results: 29 July 2020 (after market close)
9M-2020 results: 29 October 2020 (after market close)

FINANCIAL INFORMATION
This press release, 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 S1-2019 and our 2018 Registration Document.

Coface: for trade - Building business together

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