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.

Q1-2022 Results

Conference Call Transcription

Paris, 28 April 2022

Presentation

Moderator

Ladies and gentlemen, welcome to the conference call for the presentation of Coface's results for the period ending 31 March 2022. As a reminder, this conference call is being recorded. Your hosts for today's call will be Xavier Durand, CEO, and Phalla Gervais, CFO.

Xavier DURAND, CEO, COFACE

Welcome to all of you on this first quarter report call.

As you have seen from the headline, it has been a really strong first quarter for Coface with EUR 66.2m of net income for the quarter. I think we are pleased with our turnover line as well, which is EUR 431m and up 12.8% at constant FX and perimeter. Within that you see our trade credit insurance premiums growing almost 15%, driven first by high client activity but also our record client retention at close to 95%. Pricing continues to be down. That's the trend that we've seen for the last nine months. We also continue to see double digit growth in our information business with strong momentum and I will make a few more comments along the way about what's going on there. Our loss ratio came in at 40.7%. Here, we have actually taken a further EUR 33m this quarter in terms of the cost of the government schemes. That brings the total cumulated cost to EUR 199m and we do not expect any further material impact from the government schemes going forward. This is going to be the last quarter where you're going to see our numbers skewed by that. So, without those one-off government costs, we would be at 30.4% in terms of the net loss ratio, bringing the net combined ratio to 67.3% and 55.3% if we exclude the public schemes. Another important feature here is our net cost ratio which is down 1.7 point to a record low of 26.6%, which reflects both operating leverage in the business and better reinsurance commissions. Net income at EUR 66.2m is a 17.5% increase from the first quarter of 2021. It brings the return on average tangible equity to 13.2% and we're happy obviously to confirm the dividend per share of EUR 1.50 which we'd already announced at the end of the year.

Before we go into the usual slides, I just want to take you through a little bit of the Ukraine/Russia risk story on page 5. Obviously, that's on everybody's minds. We highlighted on the last call that our exposures were below 1% of our total. You can see on the chart on the top right here that we went from EUR 4.8bn in total exposures on 28 February to EUR 2.6bn at the end of the quarter, which is 28 March, so a month later, a reduction of 46%. We've actually been very focused from the first day of this crisis on managing the existing exposure and reducing our risk. Just as a matter of background, about 80% of what we do in Russia is for large international clients, with most of them being Europeans. We've been focused on trying to reduce our exposures, collect the money on behalf of these clients and in the meantime we've suspended writing new business. What we see right now is that the Russian economy has actually been quite resilient. Payments have mostly continued to flow. There's been a flurry of sanctions and counter sanctions and we're addressing these in real time. It's a pretty complex environment to manage but I think we've been staying right on top of it. Our focus is really on maintaining debt collection and key risk capabilities while we right size the operations and, so far, the financial impact has been pretty limited. The main claims that we've seen have been related to sanctions as the Russian economy has proven pretty resilient. To reflect this in our accounting, you see the gross loss ratio in Central Europe coming in at 76.6% versus an average of 28.9% for the group, so that includes obviously some reserves that we put in there to take into account what's going on in this part of the world. So, we're focusing on continuing to drive our risk and exposures down.

With that I'm going to go through the usual slides that you're familiar with. On page 7, turnover growth stands at 12.8% and premiums are up 14.7%. Other revenues have increased 5.2%, which is really a mixture of business information sales, which are up 11%, and collection fees which are obviously still low because claims are low. In terms of the information business, we are continuing to invest with determination in this line of business, which we believe has got nice potential for us. Just in the course of this quarter, we've had some really nice commercial wins. We signed one of the key German auto manufacturers. We've been able to sign one of the largest rating agencies in the world. We've been able to sign one of the largest credit card insurers in the world and we've been able to sign one of the largest aircraft manufacturers in the world. So, we see that the value proposition is actually taking hold and you'll see some variation in the numbers quarter to quarter because this is still a young business, but we are continuing this double-digit growth story. The fees to earned premiums ratio is going down but with this level of risk it's not a surprise as the collection fees continue to be pretty low.

On page 8, you see the breakdown we usually show on growth by region and what you see here is a bit of the reverse situation compared to about a year ago when Western Europe was growing faster than the rest of the world. This is due to accounting differences and the way the contracts work and this time it's kind of reversed but it will normalise itself over time. So Western Europe is at 6%, and the rest of the region has posted double-digit growth. Northern Europe, Germany is at 13%, Central Europe at almost 22%, Med and Africa pretty steady at 11%, North America up double digits for the first time, Asia Pacific at 16%. Latin America is being driven again by increased hard and soft commodity prices and is at almost 35% growth.

On page 9, you see the usual breakdown of our new business and different components of growth. New business is back to where we were in the first quarter of 2019. It is in line with pre-COVID levels. We are taking a selective approach on growth given where the economy is. The retention rate is at an absolute record for us of almost 95%, so we have done really well there. There is a drop in pricing which is continuing in line with what we talked about over the course of the last few quarters. This basically offsets the growth and pricing that we've seen during COVID. Then there is the volume effect, which is the underlying client turnover trend, driven in good proportion by inflation, is up 4.4% and that is really helping the top line for us. So, as I said before we're a pretty good resilient business when it comes to operating in an inflationary environment.

Moving on to page 10, the gross loss ratio comes in at 28.9%. That is still below the mid cycle despite the Ukraine/Russia crisis. We are seeing continued normalisation. Frequency has been increasing since the middle of last year. The number of large losses is increasing but it is still below the cycle average. We have seen a pretty limited amount of claims related to Ukraine at this stage. We have not implemented any change in our reserving policy. We are opening the new vintage at 75.4% to reflect an environment that continues to be complicated, but you see the releases from the prior years are still at 49.1% just like last year. We do expect any potential risk linked to Russia and Ukraine to be more on the 2021 vintage than any other. We are continuing to see pretty strong releases from prior years at this stage in the cycle.

Page 11 details the loss ratio by region. You can see at the bottom the four largest and usually more stable markets performing pretty well. The loss ratio is 31.7% in Western Europe and just below 30% in Northern Europe. As I mentioned, in Central Europe we chose to book a little bit more reserves here. At 22%, Med and Africa is quite benign. Then at the top, you see the markets that are usually more volatile but which are very benign this time at 4% for North America, 1% for Latin America and 20% for Asia Pacific.

Page 12 tells pretty much the same story but quarter by quarter. There is really not that much news here from what I have just said, but you can see that we have had a pretty good story for many quarters in a row almost across the board except for the Central Europe situation which I just described. We are continuing to perform on the risk side.

On page 13, we go through the cost story. You see that our costs are up 10.6%. Part of this is external acquisition costs, which are growing as the turnover is growing. Internal costs are up as well. Our cost ratio before reinsurance is lower than the prior quarters but slightly higher than the first quarter of 2021. On the bottom right-hand side, the graph shows that we are getting about 0.3% of operating leverage so that's just the growth of the premiums, which is higher than the growth of the costs, but we are investing in the business information line and you see that's costing us 0.4% of cost ratio. Debt collection is below the cycle and still lower from last year is another 0.2%. Therefore, we end up the quarter at 31.6% before reinsurance. Putting that in perspective, in the first quarter of 2019 before the COVID crisis we were at 33.2%, so despite the fact that we're investing quite significantly in new things, we're still able to reduce the gross cost ratio. With that, I am going to turn it over as usual to Phalla to take you through the next few pages.

Phalla GERVAIS, Group CFO and Risk Director

Thanks, Xavier. So, on the reinsurance side, the result come down from -47 million to -56.7 million. In terms of the key drivers here, we start with the premium cession rate. The premium cession rate is down. Of course, we're sitting at less premiums than in Q1 last year. The public schemes stopped at the end of June 2021. In terms of cession rate, you can see -2.4%, which is what everybody notices. This is related to the fact that we have prior year positive development especially for years 2020 and 2021 and of course all the reserve release, part of which goes back to the external reinsurers and part of which also goes back to the government that put in place the public schemes.

On page 15, this impacts the net combined ratio which, at 67.3%, is up from Q1 2021. Of note here is the fact that we have booked some reserves related to the Ukrainian crisis. This is one thing. But more importantly the 67.3% is distorted by the impact of the public schemes that we have absorbed this quarter and the impact is 12 points. Also of note is the net cost ratio of 26.6%, which is one of the lowest net cost ratio that we have seen at Coface thanks to the operating leverage but also thanks to the higher reinsurance commissions that we have been able to negotiate at the renewal in December 2021.

Let's move to the public schemes now on page 16. As I said, we took EUR 33m this quarter and the total pre-tax impact is EUR 199m since inception in 2020. We think that we have drawn the line here and booked everything behind us. With this, let's move to the financial portfolio.

As you can see on page 17, the strategic asset allocation has not changed much. The market value of those investment assets ended up at about EUR 3bn. There are a couple things to be highlighted here. We still have a very high amount of cash from our operating performance which is generating a lot of cash and we're also holding a pretty high amount of cash: EUR 423m to be paid as part of the dividend in a couple of weeks. What has to be highlighted as well is the equity hedges that we have put in place to allow to be quite efficient as you can see, contributed EUR 4.4m out of the EUR 12.2m in net investment income. As we are still holding a lot of cash, we will take advantage of the interest increase that is coming up.

As a result, our net income was very strong once again this quarter at EUR 66.2m with operating income up a little bit less than 21%, the tax rate was 27% and net income was up 17.5%.

If we move to the return on average tangible equity, I will start with the change in equity. Since December 2021, the net equity has slightly decreased from EUR 2.141bn to EUR 2.135bn. This was driven by the net income impact offset by the mark-to-market on the investment portfolio as the interest rate increased. The return on average tangible equity increased from 12.2% to 13.2%. The only driver here is of course our technical and financial results net of tax. With this, I'll hand back to Xavier.

Xavier DURAND

So, in terms of take away, I think we continue to be very focused on operating well. You see a few things here in this quarter. Double digit growth in TCI, mainly activity and retention. Double digit growth on the business information line. Operating income up almost 21% despite the fact that we've taken a further EUR 33m on the public schemes and that's going to be the end of it, and the Ukraine crisis reserves that I've just mentioned. We haven't changed our reserving policy. We continue to monitor the risk environment very carefully. I'm sure you're all aware that situation with Russia and Ukraine is quite volatile. It's creating shortages and potentially aggravating the energy and commodity prices that we've seen already go up. It's also probably going to create some inflation in the food supply areas. The sanctions against Russia are also going to continue to become increasingly complex from day to day. There's also as you're aware a COVID outbreak in China which is causing a series of lockdowns which themselves will have repercussions in terms of the supply chains, which themselves will have repercussions on solvencies of a number of companies. So, we are continuing to see risks out there which supports our idea of normalisation of risk. We're pleased to confirm a dividend per share of EUR 1.50. We continue to be focused on allocating capital efficiently. As I highlighted last time, our priorities are first core growth, and there's clearly some core growth going on, followed by acquisitions if we can find some, and then returning capital to shareholders, which we're doing with a EUR 1.50 dividend per share. That's the story for the quarter. A very short presentation I have to say because I think it's pretty straightforward and we are happy to take questions from anybody at this stage.

Q & A session

David BARMA (Exane BNP PARIBAS) Thank you. Good evening, everyone. My first question would be more broadly on the risk environment. It's pretty difficult to have a good view of the sector allocation and the changes there, but in this environment and given the inflationary risk, are you worried about some of your sector allocation, and have you started making sector changes within your risk budgets? Secondly, on capital, I know you typically don't disclose solvency in the interim publications but given the strong market movement here to date and the final effects from the public schemes, maybe you can give us an indication on where solvency stands versus the end of the year. And then lastly on single risk and sorry if I've missed that somewhere in your disclosure but can you remind us how big your single risk business is nowadays and what kind of actual risk you have in that bucket? Thank you.

Xavier DURAND (CEO, Coface) First of all, in terms of the risk environment, we're not looking at it just by sector, but by company, so you understand the way we look at the business is a mixture of sectors, the country, where companies are in the food chain or in the supply chains if you will, and so it's all about the details. You will tend to see that our sector allocations, when you look at the macro numbers, don't move that much over time, but what moves is the individual allocations that we make to this company or that company because in one sector you have very different situations. So, we are actively monitoring the risk, we're actively managing it. I think you're seeing it in the case of Russia but that's not the only case. We've been doing this now for years and we had to do it for COVID. So, the story continues for us. The fact that there's a little bit more risk in the market is not necessarily negative for this industry because as you know we've been operating at a very low level of risk for quite some time now. In terms of capital and solvency, we usually announce our solvency twice a year and we do not provide figures at each quarter but I think what I would say is we still expect to see pretty strong solvency at the end of this quarter because you see premiums coming in and so the premium component of that is actually pretty strong. So, we feel pretty good about our solvency. In terms of single risk…

Phalla GERVAIS (CFO and Risk Director, Coface) …it's a little bit above 1% of premium…

Xavier DURAND (CEO, Coface) …so, it's about 1% of what we do and, for those who might wonder, we actually do not have any aircraft. I guess the question is going to come up. We have looked at these deals. I spent some time on them and we turned them down, so we don't have any aircraft.

Phalla GERVAIS (CFO and Risk Director, Coface) and we have almost no exposure in single risk in Russia and Ukraine.

Xavier DURAND (CEO, Coface) So, I think that kind of closes that discussion. I hope that answers your questions.

Benoît VALLEAUX (Oddo BHF) Yes, good afternoon, thank you. A few questions on my side. Can you just tell us what has been the total group exposure at end March and what the evolution has been year-to-date? Second question is related to Russia. You gave us an update on your exposure at the end of March. What could the figure be more or less at the end of April? How has it changed over the past month? And maybe one question related to business information. You enjoyed 11% growth in Q1 which is still significant growth but it's going down a little bit compared to what you've seen over the last few years. So, what do you see as a potential growth rate over the next few years? I mean do you believe that a 15% to 20% CAGR is achievable? I don't know how you see this percent compared to your potential growth in the future. Thank you.

Xavier DURAND (CEO, Coface) Let me let me start with this last question and I'll turn it to Phalla for the other two. So, in terms of BI, we grew 11% in Q1. I'll just point you to last year when we had 9% in Q1, so it's a little bit better than last year. We ended last year at 18% total growth I think so I wouldn't read too much into one set of numbers for the quarter. We do not provide forward looking statements, but this is an area that we continue to significantly invest in.

Phalla GERVAIS (CFO and Risk Director, Coface) We're not disclosing much but in terms of total exposure today, you can count on low single digit growth in total exposure. On Russia, as of the end of April obviously the exposure is going down as you can see. We'll probably be somewhere well below EUR 2bn.

Thomas FOSSARD (HSBC) Good evening, everyone. I've got a couple of questions. The first one would be related to the Russia provision. Can you please quantify how much it is in order to avoid a debate on this? The numbers could be useful. The second question would be regarding your comment about a trend toward normalisation. I think that this is your message today that the war so far is not creating too much of an issue but potentially accelerating the return to a more normal claims environment. On this path toward a more normalised claims environment, can you tell us a bit about the acceleration, so the second derivative that you've been mentioning regarding frequency and severity of the losses? I mean how has it changed since the start of the year? And also, could you remind us of what a normalised combined ratio is now for Coface, given that you explained that you had a lot of operating leverage accumulated over the past two or three years. Can you refresh our minds about what this means in terms of overall number? Thank you.

Xavier DURAND (CEO, Coface) On the normalisation, I've said that we had a surge in insolvencies in the first two quarters of 2020 when COVID started. Then the government poured money all over the economy and we reached a trough in insolvencies in June 2021. And since then, we've seen what I call the normalisation going on. We thought it might have been a bit faster than what happened. The government schemes were extended and there was less volatility than we probably anticipated, but it is happening, and I think that's the message we've been consistently giving you since June last year. So, I think the war is accelerating or creating another set of things that are going to create more activity. I think COVID continues in Asia so whatever the event is that's out there, there's something that's going to happen that we anticipate is going to create some return to normalcy. So that's what I call normalisation – it's something we expected, something we're not really surprised about. You never know where it's going to come from, but I think there's nothing here that comes out of the scenario that we have defined for ourselves or the things that we expected to see. In terms of the combined ratio for Coface, I think we have a four-year plan. We've given you a target. I have no reason to change that target today. What we're focused on doing quite frankly is just running the company as well as we can quarter by quarter, month by month, day by day literally when it comes to some situations and that's what we do. So, I'll have to refer you to that plan.

Phalla GERVAIS (CFO and Risk Director, Coface) We haven't changed our reserving policy, so basically the way that we look at things is that in the numbers that we presented, the loss ratio related to Central Europe is up at 76.6% and this provides for the situation in Russia. So, this would be the worst loss ratio level that we have booked for Russia.

Xavier DURAND (CEO, Coface) Frankly, this is a situation that's still ongoing, so it'll have to be updated on a quarterly basis. We don't know everything. I don't think anybody does by the way. So, we took a view which includes some IBNR at this stage and I think we'll have to play it by ear.

Moderator

There are no further questions. If I hand the call back to the speaker for any closing remarks.

Xavier DURAND (CEO, Coface) No other questions? This may be the shortest call I've done at Coface. I'll take it as a good sign or maybe there were fewer participants or maybe the story's clearer. Anyway, no need to torture everybody. We will obviously be here to answer any further questions and we will meet again in July for the second-quarter results. On that call we'll be updating everything else like solvency and exposures and all that good stuff. And thank you very much for attending tonight.

(End of transcript)

CONTACTS

ANALYSTS / INVESTORS

Thomas JACQUET: +33 1 49 02 12 58 – thomas.jacquet@coface.com
Benoît CHASTEL: +33 1 49 02 22 28 – benoit.chastel@coface.com

FINANCIAL CALENDAR 2021/2022
(subject to change)

Annual General Shareholders' Meeting 2021: 17 May 2022
H1-2022 results: 28 July 2022 (after market close)
9M-2022 results: 27 October 2022 (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 S1-2021 and our 2021 Universal Registration Document (see part 3.7 "Key financial performance indicators")

COFACE: FOR TRADE

With more than 75 years of experience and the most extensive international network, Coface is a leader in trade credit insurance and adjacent specialty services, including Factoring, Single Risk insurance, Bonding and Information services. Coface's experts work to the beat of the global economy, helping ~50,000 clients build successful, growing, and dynamic businesses across the world. Coface helps companies in their credit decisions. The Group's services and solutions strengthen their ability to sell by protecting them against the risks of non-payment in their domestic and export markets. In 2021, Coface employed ~4,538 people and registered a turnover of €1.57 billion.

www.coface.com

COFACE SA is quoted in Compartment A of Euronext Paris

Code ISIN: FR0010667147 / Mnémonique : COFA

n

declarations featured in this press release may contain forecasts that notably relate to future events, trends, projects or targets. By nature, these forecasts include identified or unidentified risks and uncertainties, and may be affected by many factors likely to give rise to a significant discrepancy between the real results and those stated in these declarations. Please refer to chapter 5 "Main risk factors and their management within the Group" of the Coface Group's 2021 Universal Registration Document filed with AMF on 6 April 2022 under the number D.22-0244 in order to obtain a description of certain major factors, risks and uncertainties likely to influence the Coface Group's businesses. The Coface Group disclaims any intention or obligation to publish an update of these forecasts, or provide new information on future events or any other circumstance.