T R A N S C R I P T

Conference Call Transcript

H1-2016 Results

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Operator

Ladies and gentlemen, welcome to the Coface financial results conference call. At this time, all participants are in listen-only mode. We will then conduct a question and answer session. As a reminder, this conference call is being recorded. Your host for today's conference will be Mr. Xavier Durand, CEO of Coface, and Madame Carine Pichon, Group CFO.

I would like now to turn the call over to Mr Xavier Durand. Sir, you may now begin.

Xavier DURAND, CEO, Coface

Thank you very much and good evening to all. Thank you for joining us. Sorry for starting this call with a couple of minutes' delay, as we had more callers than usual.

One of the two things we want to do today is take you through our first half results. As you can see, they are completely in line with the announcement we made on 4th July. We want to take some time on this call to give you more colour on the risk numbers and the key drivers, as clearly it's something important. Then the second point is, as promised, we've been working hard on putting together our three-year strategic plan and we want to give you the highlights and discuss these. We call this plan "Fit to Win" and what we aim to do here is to build on our international presence to transform Coface into the most agile global trade credit partner in the industry. I'll take you through what this means.

I'll start with the highlights for the first half and move directly to page five. On this page you can see our net income is down for the first half, at € 26 million, of which € 3 million was in Q2. As we communicated previously, net income has been impacted by an increased loss ratio. Our turnover comes in at -5.7% versus the first half of last year and -3.4% excluding FX. We can pretty much see the same trends at play that we discussed in Q1, with price erosion in mature markets combined with the impact of the risk measures we've taken in emerging markets, as well as some lower client activity.

Our net combined ratio comes in at 92.2%, which is 90.8% excluding one-offs, for the first half. There are two components to this. Our net loss ratio, at 60.8% (which, as we explained, is driven by emerging-market claims), has developed more than expected and this has been combined with the effects of longer collection times in these countries. The key sectors affected are more or less the usual suspects: commodities, metals, chemistry, textiles and agriculture and we'll take you through this in a little more detail. Our net cost ratio comes in at 31.4% (30% excluding one-offs) - a result which reflects continued good cost control in the business, as you will see.

As we announced on July 4th, we continue to foresee a net loss ratio for the year of between 63 to 66%. We have had a lot of questions on solvency and, as you can see, it remained strong at 155%. This allows us to maintain the long-term 60% pay-out policy. In addition, we will propose an exceptional distribution of six cents a share for the year 2016.

With that, I'll move to page six, where we highlight some of the developments in the business during the first half. Starting with risk and portfolio management, as you know, we took some

strong actions in 2015. What we're doing this year is following up with more granular and segmented adjustments. We have reviewed our commercial and risk underwriting policies for the areas that are higher risk - and by that I mean trading, commodities and single risks, as already discussed during the Q1 call.

We're continuing to make risk adjustments in certain countries -those with the highest volatility or highest risks in our view, such as Brazil, China and more recently Turkey. We are also targeting key sectors with large exposures, or weaker credits, and once again these include chemicals, textiles, commodities and metals. We are also following the Brexit impacts closely. We see the short term impacts of this mainly being linked to the devaluation of the British pound, which is driving some hesitation from investors. We are also closely monitoring areas which are more linked to imports and less tied to exports, particularly in the construction sector. Moreover, there are likely to be protracted discussions which will take some time and the impacts of these will be more in the medium term.

There has been a lot of movement on the people side and you've probably seen the announcements on new people coming into the team. Thibault Surer has joined us, following 15 years as a partner at McKinsey and five years in private equity. He is taking on our business development and strategy. Valérie Brami has a long experience in managing operations, systems and operational efficiency during her years with PricewaterhouseCoopers, IBM and Allianz. She will be helped by Pierre-Emmanuel Albert, who comes from Tinubu Square, a company that began proposing integrated solutions for trade credit management in the IT space some 15 years ago and has been quite successful. As you know, we've also hired Thierry Croiset as our new group risk director. He comes from GE and we've worked together in the past. Bhupesh Gupta, also from GE, will join us in September to run our Asia-Pacific region. In addition, you're probably all aware that Thomas Jacquet is joining us from Exane, as the head of our investor relations group.

A word on the state guarantees transfer. As you know, the transfer has been postponed to the end of 2016, at the earliest. Quite frankly, this is driven by French state legal constraints, which require them to pass more acts of law at the end of the year. In the meantime, we're continuing to manage the activity and continuing to be paid by the State, as usual. We still anticipate a gain of €73.4 million before tax, which will be recorded at the effective date of transfer. At this point, the date of transfer is expected to be either at the end of 2016, or very early in 2017.

I'll now move on to page 8 and talk about the different aspects of the P&L. Turnover, as previously mentioned, is down 3.4% compared to the same period last year. If we exclude the one-off that we had in the first quarter (from the public guarantees), it's down by 3.1%. On the fees side, as you can see, the number is flat from last year. This is relatively good news in fact, as the fees to premium ratio is actually increasing and this reflects the work that we are putting in to driving fees – as this is more capital-efficient and a good hedge for the business.

On page 9, you can see the split by region. Pretty much the same forces are at play here as those discussed in the first quarter. In comparison to last year, Western Europe is down by about 10% and Northern Europe by around 5%. Both of these have been driven by increased price pressure and premium refunds, within an environment of competitive, more mature markets. Central Europe has continued to grow, at a steady rate of 2%. The Mediterranean and Africa region in general shows a rather contrasting picture to Spain and Italy, with the two countries being subject to the same kind of price pressures we're seeing in the rest of Western Europe, while the rest of the region is continuing to grow steadily. North America, up 5%, has been driven by the signature of a contract in North America through our global relationships in the rest of the world. Asia-Pacific, after several years of double-digit growth, is now slightly down. This reflects

the impact of a more selective strategy in terms of growth. The same thing is true for Latin America, where the headline number is down 7.8% on current terms, with the +14% translating the inflation that we have seen in these markets.

The following page outlines our commercial performance. As can be seen, new production is slightly down from last year, at €81 million. We're seeing a lower level of large deals at this point but the retention rate is high, at 90.2%, in line with the first quarter. So this is a good performance from the business on this aspect. We are continuing to see a negative price effect –in line with the first quarter but better than last year and we are starting to see some ability to price better in emerging markets. However, this will take some time and, as you know, the bulk of the business that we write is in mature markets, which are still under price pressures. The final aspect is relative to volume effect and we have seen a slowdown in terms of volumes of business from our client base across the board. More importantly, we are also seeing a decrease in some sectors. Once again, the usual suspects, such as commodities and metals have been hit recently.

Over the next five pages, I would like to spend some time to talk about the risk situation and some of the trends that we have observed that led to some of the announcements we made at the beginning of July. Focusing on emerging markets, on page 11 we describe the impact of two countries on two of our main markets – Brazil in Latin America and China in Asia. What we are faced with in Brazil, is a prolonged, quite deep recession, with GDP down almost 4% in 2015 and deteriorating by 3.4% this year. In China there has been a rise in corporate delinquency, which as can been seen from the chart, was relatively towards the end of last year - and we have reacted to this. So just to say, we are in a context where these markets are performing pretty well through the global financial crisis but are now being challenged a lot more than anticipated.

On the next page, we describe some of the measures that we've taken on exposures and they've been pretty significant. In Brazil our exposure has gone down by 55% over the last 18 months. There have been a couple of waves of actions. We are continuing to focus on the weaker credits and some sectors like metals, agro, and construction. If you look at some of these sectors, we've reduced our exposure by two and a half times, with metals for example. The same thing is true in China, but as we said, the rise in delinquencies came in later towards the end of last year, when you can see that we decreased our exposure by about 47%. We are continuing to work on a sector-by-sector basis, looking at the quality of credit in a much more detailed way.

On page 13, I would like to take you through how the losses develop for each one of our underwriting years. In this chart we show the years 2012, 2013, 2014, 2015 and the beginning of 2016, which is still preliminary. Two main things can be observed from this chart. The first is that the development of claims relating to 2014 and 2015 look like they will be higher than those related to 2012 and 2013 - and, importantly, they are coming in two or three quarters later than we've seen in the past. That is an important fact that we are incorporating into our accounting policies now. It also explains why we are opening the new vintages at higher levels of reserves than we did in the past. To put this into perspective, on page 14 we took the vintage year of 2014 as an example and we split the loss developments between three markets. We used France as an example of a mature market, with the other two being Brazil and China –where it can be seen that not only is the loss development much higher, but the peak is also reached at a much later point in time. This reflects the business practices of these markets, where payments take longer and our contractual terms are longer than they are in the Western world. So again, recognising this fully, both for the past and then anticipating what that means for the business we are writing this year, explains the adjustments that we've made in our accounting policies.

On page 15, as we do each quarter, we have set out our loss ratios by region. For the group as a whole, they come in at 61.9% for the first half of the year. The countries that are in the bottom are

still evolving pretty much at the levels we have seen historically, although they are higher than they were in Q1. Central Europe is at 46%, Western Europe at 39%, Northern Europe at 58% and the Mediterranean and Africa at 52%. Part of this return to normal is driven by the fact that, in these markets, we still have export policies relating to some of the emerging markets that we are exposed to. The three markets highlighted at the top of the page are those where we've seen the most volatility. In Latin America, the curve has actually come down to 60%. However there is a contrasting situation in this region, as some markets show good performance but Brazil is still at 105%. That's better than it used to be, but it's still high and it explains why we are continuing to work on Brazil. In Asia-Pacific, you can see the number coming in at 127%, which is better than it was last quarter. However I think it's early days and we are still awaiting the impact of the measures we took in 2015 to materialise through to the end of this year in the portfolio. In North America, we highlighted the large claims that we faced in Q1. To that we need to add the impact of export policies from North America into Latin America – which is a significant trade partner for this part of the world, so the number is coming in higher, at 86%.

With that, I'm going to turn it over to Carine, to take us through the second part of the presentation.

Carine PICHON, Chief Financial Officer, Coface

Thanks Xavier. Good evening, everybody. As you can see, the loss ratio for Q2 2016 is 70.1%. What is important to highlight is the loss ratio on the second part of the graph, of 59.6% for the first 6 months of this year. As you can see, there is an increase compared with the previous period. This comes first from the fact that we have less positive runoff coming from the re-estimation of the previous underwriting years. You can see that the figure is 14.1%, where previously it was between 20 and 25%. Clearly this results from the fact that we have received late notifications for claims on emerging markets and so we have less positive runoff than in the past. The second impact comes from the fact that we have readjusted our reserving policy to take this into account. The loss ratio for the current year is 73.7%. This also above what we are accustomed to having in our accounts when opening the year.

On page 17, which shows cost evolutions, it can be seen that expenses are decreasing in line with premiums. Globally, at the same exchange rate, we have a decrease of 2%, with internal costs down by 1.8%. Thanks to our cost controls, we have been able to achieve a stable net cost ratio (excluding the exceptional items we already disclosed in Q1 2016), leading to a 30% net cost ratio. This is very similar to the figure of 29.8% we reported for H1 2015.

Now for some comments on reinsurance, seen on page 18. The cost of reinsurance has decreased. The reinsurance result, which was - € 26 million for H1 2015, is + € 1 million for H1 2016. There are two effects which explain this difference. The first one is that we have registered one-off adjustments of around €14 million for this quarter, which we do not anticipate for the next quarter. The remaining difference comes from the fact that reinsurance is used to partially offset loss ratio deterioration, which explains the differentiation with H1 2015.

On page 19, net combined ratio for the first half of the year is 90.8%, with 97.7% for Q2. As can be seen by comparison with the previous period, the increase is mainly due to the loss ratio. You may remember that, on 4 July, we pre-announced a loss ratio for the quarter of around 67%. It is, in fact, 66.9%, compared with 55% for the first quarter of 2016.

As concerns our financial portfolio, on page 20, we continue to maintain a diversified and proactive investment strategy. Net investment income for H1 2016 was €24.6 million, down from €28.2 million for H1 2015. When you look at the gains on investment sales, H1 2015 showed a positive result of around €8 million. For this semester it's -€1.3 million. So if you adjust that, you

can see that the accounting yield on the average investment portfolio remains stable, at 1% for H1 2015 and around 0.9% for H1 2016.

Turning to page 21, solvency remains strong, with solvency cover under the Solvency II regime at 155%. At the end of last year, we published a ratio of 147%, so we have had an improvement. This is mainly driven by the decline in turnover which has led to reduced need for capital. We also published, for the first time, our comfort scale and our global policy dividends. As can be seen, as long as we are between 140% and 160%, we are within our target, which means that we have a dividend policy based on the 60% pay-out ratio. We continue to invest in business growth and we are maintaining our current investment risk appetite. If we fall under this ratio, to between 120 to 140%, we will increase our selectivity on growth initiatives and we may have some flexibility on the pay-out ratio. Solvency remains strong and for this reason we have decided to reconfirm and maintain the 60% pay ratio policy on a long term basis. On top of that, we are proposing an exceptional dividend of €0.06 per share, for the calendar year 2016.

On page 22, net income, as already discussed, is €25.6 million for this semester. There is a decrease in return on average tangible equity, down from around 8.5% for 2015, to 3.9% for the end of June. The main explanation for this is the technical result, meaning the increase in loss ratio. That concludes the global view on the results.

Xavier DURAND, CEO, Coface

What I want to do from this point, is talk about our “Fit to Win” plan. If you turn to page 24, you can see that this plan is built around two key pillars. The first, which occupies most of the page here, is to improve the operational performance of the business, which is not yet where we want it to be today. The second pillar will be steering the business towards a more efficient capital model.

So let me start with pillar one, which is to position Coface as the most agile global trade credit partner in the industry. As you know, we have been a pioneer in global expansion and we are still seen today as the global leader in terms of trade credit, given our presence around the world. This is a strength that we want to build on. But what we want to do here, is bring our growth and our infrastructure in line with the reality of the risks that we are facing on the markets. So there are three main areas of transformation regarding pillar one.

Number one (box A), is to continue to strengthen our risk management and our information on the markets where we operate. You can clearly see here three points where we have been focussing and are continuing to do so. We are adapting our underwriting rules and our portfolio measures to the reality of the risks that we face in each one of our markets. Our plan will involve continuing to invest in select information and data management tools, to improve risk performance in the emerging markets. Then we are continuing to reinforce our teams and our expertise in the key areas where we want to operate. The whole idea here is to bring our risk infrastructure in line with the reality of these markets, where risks are greater than was probably previously understood. The benefits of this will be to return the business to a normalised loss ratio, in line with industry standards over the credit cycle.

The second area for transformation involves working on our operational efficiency and client services. We want to enhance our back-office and system capabilities for the benefit of our clients, in order to improve productivity. Our goal here is to completely offset the loss of the public guarantees, through cost savings, by 2018. For that, we need to continue to invest in key systems and technologies and drive workflow digitisation. This will not only drive better efficiency but also improve client services, in terms of response time, accuracy and ease-of-use. So really, it’s about adjusting our cost structures to the reality of the markets we operate in.

Thirdly, we are implementing a differentiated growth strategy which not only captures the value of our global presence, but also recognises the differences in the markets where we operate. We want to differentiate our growth strategies between the markets that are high risk and those that are more stable. Between the markets that are mature, versus those that have lower credit-insurance penetration and where the commercial effort is different. Furthermore, we want to segment our value proposition depending on the needs of our clients and the four key client groups - of small, medium and large global clients, as well as financial institutions – the latter being a different kind of client from the industrial companies we traditionally do export finance with.

Finally, we are continuing to drive fees and service revenues, as they are a good hedge against downturns in this industry. They are also very capital-efficient in terms of the profitability of the business. So this is not about growth for growth. This is about driving profitable growth over the long term – recognising that we are in markets that are very different from one another and that we need to take that into account.

The second pillar of the plan is our ambition to steer the business towards a more efficient model in terms of capital efficiency. What we want to do here, is to leverage the capabilities that we can gain from the reinsurance market in order to find a better, more efficient way to use our capital.

So I'm not going to say much more about this at this stage, but clearly, these two pillars constitute the core of what our "Fit to Win" plan is going to be for the years 2016 through to 2019. As you know, we expect to make a full presentation of this plan during an investor day, on September 22nd, in London. Hopefully, during this presentation, we will be able to give you a lot more colour, point by point, on each one of these items.

So these are the points we have today for discussion and from here I think we are ready to take questions.

Operator

Thank you. Ladies and gentlemen, if you wish to ask a question please press 0 and 1 on your telephone keypad.
We have our first question from Michael Huttner, from JP Morgan. Please go ahead.

Michael HUTTNER, JP Morgan

Thank you very much. On the sums here, regarding the 155%, I remember (maybe wrongly) from the call on the 5th that you indicated it would be flat, because although turnover (i.e. exposure) was down, the cost of risks (in other words volatility), is higher. The fact that it's up so much, seems to imply to me that you view the volatility as unchanged or underlying. That would be my first question. Is that right?

The second one is, within the increase in loss ratio, can you actually quantify a number? What is the actual cost of actual claims, versus the actions you've taken in terms of reserving? I didn't catch the reinsurance number. I'm not sure if you said 14 or 40 million of one-off benefits.

The last point is, if the deal to transfer the business out of the French state is delayed until 2017, does this mean you'll take a big restructuring charge in 2016 and then recognise the gain, which to my mind would be offset, in 2017? Thank you.

Xavier DURAND, CEO, Coface

I'll start maybe with the last part. We don't see the delay, (and I'm not sure if that was your question) in the public guarantees transfer as changing the amount of reserves that we need to take. There may be a timing difference. We are not going to delay the implementation of the plan, but the one-off gain from the sale of the public guarantees may come either in 2016, or in early 2017. So that's something we can't decide. I hope that's clear.

Michael HUTTNER, JP Morgan

So technically it means that if the restructuring is as big as the guarantee, which had been my initial assumption, you could, in theory, report a loss this year. Is that right?

Carine PICHON, Chief Financial Officer, Coface

Sorry, it was difficult to hear you Michael. There are two scenarios. One is that the transfer is effectively completed in 2016 and then we will have the gains. In any case, in 2016 we will have the restructuring provision for this. The second option could be that we still have the provision for restructuring in 2016. In any case, the State does not want to delay the implementation of the plan because (we're) expecting a lot of benefit from it. Then, effectively, if the transfer is validated in early 2017, we may have a gain on this. I think that answers your question. Up to that date, we will continue to have the revenues and margins we register from these activities.

On reinsurance, maybe I could come back on this in more detail, as there is a specific one-off for this quarter. As you know, we have a quota-share of 20% with our reinsurers. This means that we cede our premiums and our claims. It happened that, during an audit, we forgot to declare some collection costs on our claims to our reinsurer. We discussed this with them and they agreed to take this on board. The full adjustment for the reinsurer's share of these costs is €13.8 million, which has been booked into Q2 2016. That is why there is a positive adjustment for this quarter, but we do not anticipate that it will be repeated in Q3 and Q4.

Michael HUTTNER, JP Morgan

Okay. And the other two questions? The 155%, and the actual claims versus reserving?

Carine PICHON, Chief Financial Officer, Coface

So on reserving (if I understood your question correctly), what we have done is that we have taken on board the fact that we have had claims notifications which arrived later (if you look at the claims curve, compared to what it used to be in the past). So the first thing is that we have had to take on board these claims, which is why it was the level of run-off is at a lower extent than in the past. The second is because we are seeing changes in terms for portfolios from emerging markets. We have decided to adjust for the opening year and this adjustment means that we have 73.7% for the underwriting year of 2016, compared with previous years, which were more between 70 to 72%.

Michael HUTTNER, JP Morgan

And if I think about the foregone profit that I had expected in Q2, versus the one you have reported, how much of this difference is 'double reserving' and how much is actual claims?

Carine PICHON, Chief Financial Officer, Coface

The calculation is around 50/50.

Michael HUTTNER, JP Morgan

50/50. Excellent. Thank you. And the final point was the 155%. I had understood that you initially expected solvency to be more or less stable – but it's actually up. It sounds to me that you're not expecting this volatility in results to persist, which is why you haven't included it in your numbers going forward.

Carine PICHON, Chief Financial Officer, Coface

In fact, in terms of volatility, what is new is on the loss side. I don't think there is any volatility on the other lines of the P&L. It is just a question of loss.
As regards to Solvency, we didn't publish the Solvency ratio at the end of the last quarter, but last publication was on an annual basis, at 147%. On the 4th of July we said that the solvency ratio should not be an issue and that is why we are publishing it now, as we have the actual and final figure, at 155%. The way the standard model is built, let's say, is quite significantly driven by turnover: when you have higher growth you need more capital. Because of the decline in our turnover, in fact we have had a positive effect on the cover ratio. That's why we have a figure of 155%.

Michael HUTTNER, JP Morgan

I remember now what was said at the 4th July conference call - that the required capital base is partly driven by stress and that the stress is partly linked to your future expectations – and also the volatility – of your losses, and this has actually gone up. So, the reason I'm labouring this point and I apologise if it seems I'm labouring it, is it implies that in your own internal thinking, you do not see any volatility going forward now.

Carine PICHON, Chief Financial Officer, Coface

No. Maybe we were not clear enough on 4th July, so it's important that we clarify it now. In fact, there are two main components which have an effect on the solvency ratio. The first is clearly the loss ratio, which is why we provided you, at the end of the year, with the sensitivity tests and relative loss ratios. As a reminder, we said that we would be at 120% if we were to replicate the 2008 crisis, which was a level of loss ratio of more than 100%. We are far from 100% as of today. We have an effect of loss, but because we have reinsurance and we have put into place all of our capital management tools, we know how to manage that. In addition to that, there is also the fact that when you have growth in turnover, you need more capital – and when you have a decline, you need less capital. So you have here these two effects, which, all in all, are positive.

Michael HUTTNER, JP Morgan

Excellent, super. Thank you so much.

Operator

Thank you, sir. Next question is from Thomas Fossard from HSBC. Please go ahead.

Thomas FOSSARD, HSBC

Good evening. I've got several questions. The first one is related to the chart you presented on slide 14. I'm surprised that you're seeing a negative evolution in claims on the 2014 underwriting year. I can understand it is taking a longer time for you to get full recognition of claims certifications, but still, it looks like you're recognising a different claims pattern, almost two and a half years after the business has been returned. This seems to be really, really long. So, I was wondering if this was linked to any lower recoveries that you're getting on this business, and that you have adjusted your recovery expectations for some of these emerging

markets? Otherwise, I'm still a bit confused on why this is coming so late, when we know that you're writing two third of your business at the start of the year. So that is the first question.

The second question is, that I wanted to better understand your full-year net loss guidance of 63% to 66%, compared to what you reported in the first half, at 60.8%. Just to better understand, where is the deterioration you're pointing to coming from? Why is that and which region would that be coming from?

The last question is on the dividends. So, you're still confirming the 60% pay-out ratio. Could you remind us if this is based on the underlying, or if the 60% is potentially net of any exceptional restructuring costs? Also, potentially, if you get the exceptional gains from the guarantee transfer, would that also be paid to shareholders, or is this below the line? The other thing is, that on the special dividend, looking at your comfort level, I'm not quite sure why you're paying out a special dividend right now. On the chart it looks like any special dividend will be for when a level of over 160% is reached. So does this mean that you are expecting to be above 160% towards the year-end? Could you clarify this point? Thank you.

Xavier DURAND, CEO, Coface

I'll take the first question on the claims delay here, on page 14, which I commented upon earlier. So, I think you've got a conjunction of factors when it comes to emerging markets. One is that when we write business, we write it all through the year, including up to December of the year 2014. So we're a year and a half on at this stage, not two and a half.

The second thing is that the payment delays in these markets are longer. It's just traditionally the way business practices function in these parts of the world. You also have commercial contracts which may have longer periods than in Western Europe. And then finally, yes, you are right, there is an impact from the fact that claims are taking longer to be recovered once they have been registered. So it is the accumulation of all these impacts that makes a major difference, if you will, between emerging and mature markets, when it comes to driving these delays. This is also why we're seeing something different today, from what we've experienced in the past.

I'll turn it over to Carine to talk about the question concerning the outlook for the year-end.

Carine PICHON, Chief Financial Officer, Coface

Concerning the outlook, your question is accurate, we are currently at 60.8%. Mathematically, if we say that we will be at between 63% to 66% for the full year, it's because we anticipate an increased loss. This is, however, clearly not the case. It is just because of a reinsurance one-off we had in the quarter. If I exclude the one-off we had in Q2, it means that we will have a net combined ratio of a little less than 64%. So that is the reason why. We said between 63% to 66%, as there is always a kind of uncertainty on the loss side. That is why we prefer to take a range in terms of forecast.

On the dividend point, I think your question was what do we plan for the end of the year as a basis for the 60% pay-out ratio? Clearly, on capital management, our position is that we will distribute all excess of capital we think we have. This means that, for the end of the year, all provisioning will be financed by the gain on sale, and any other complementarity which remains will be on the basis of the 60% pay-out ratio. So we will distribute on the basis of the net result, including these exceptional or extraordinary events. The reason why we decided to announce an extra dividend of €0.06 per share is because, based on our calculations, we think that on top of that, we have the capacity to deliver and to give more dividends. That is the policy that we want to

have from a capital point of view. As long as we have the correct level of solvency in the comfort scale we have presented, then we will give it back to the market and to our investors. There is no reason why we should keep it on board.

Thomas FOSSARD, HSBC

Okay, if I may come back. So, Carine, a strict 60% pay-out policy. So without special dividend, which part of the range will it be in?

Carine PICHON, Chief Financial Officer, Coface

We cannot give you the net result for the end of the year but we will give you more information on the 22nd September. This will be important for the end of the year, as it will include the restructuring provisions we plan to have for 2016. This is something we need to integrate and communicate, both to the market and internally. So everything will be clearer on 22nd September

Thomas FOSSARD, HSBC

Okay, thank you.

Operator

Thank you, sir. The next question is from Benoit Petrarque from Kepler Chevreux. Please go ahead.

Benoit Petrarque, Kepler Chevreux

Yes, good evening. Just a couple of questions on my side. The first one was on the transformation plan. So you plan to invest quite a lot in improving risk management, improving data management and invest in different tools – and obviously new management. How much impact do you expect this will have on the cost ratio? Do you think it could be a significant amount over time? I was wondering because, during the IPO, the pitch was really based on the fact that risk management had already improved and there had been no other thoughts on improving quality data. So what went wrong, in your opinion? Do you think the group focussed on the wrong sectors, or the wrong countries? I'm actually trying to understand why, so far, it went so wrong.

Then it will be on the average size of claims, which is increasing. You have a higher share of high claims. Do you think this is a trend? Do you see this deteriorating further in 2016 and potentially in 2017? I'm just trying to understand why. In which conditions are you seeing higher claims? Is it because of recessions in emerging markets, or something like that?

Also, coming back to the question from Thomas, it's not fully clear to me why it takes so long to recover on the years 2014 and 2015 in emerging markets? Is there an issue on the assumptions that were made on recoveries? Or, is it a more lengthy process to recover money in emerging markets? Why does it take so long? What went wrong there? Thanks.

Xavier DURAND, CEO, Coface

Okay, let me start with the question on the investments. So yes, we plan to reinvest in the business and continue to strengthen our tools. This is connected with systems and also sometimes with just adding people in certain parts of the process. It has to do with digitisation and things of that nature. Now, I realise that there will be investments that are tied to this. Part of this is P&L and part will be investments that will get amortised as usual and over a longer period of time. So again, we'll give you some flavour and much more detail on the 22nd September, but clearly it will be a mix of effects.

When it comes to risk management and what was said the IPO, I think that what is new here, is that we're faced with something new, which is a rise in claims. You could call it a crisis, or a risk increase, in emerging markets. They are showing different characteristics from what the business has seen in the past – as I would say that, during the global financial crisis, the crisis was mainly driven in the US and then moved over to Europe. But if you think of Asia, for example, it was untouched during that time. So I think what the business is realising, is that the type of risk volatility – the nature of the risk and how it moves - is different. Obviously the information we have now is different from what was thought at the time. So that's why we're adjusting both the risk capabilities and the growth strategies to what I call the reality of what's out there. Once again, this is a new phenomenon, as the business hasn't been exposed to these risks in these markets before. And that's the whole idea of the plan here.

Carine, you want to talk about the other two?

Carine PICHON, Chief Financial Officer, Coface

If I may come back to slide 13 and the reason we now have later claims. If, for example you look at the curves for the underwriting year 2014 to, let's say the end of Q2 year 2, we would have thought at that time that the crisis would be more or less in line with what we saw in 2013, with a loss ratio of 50%. From today's viewpoint we can now see that we received later certification of claims and lower recovery rates. This led to the fact that the curve moved and, as you can see, has continued to rise, up to the point where the delivery rate is now two and a half years later on. So that's clearly something that is new and the reason why we have readjusted our reserving policy, to take that on board.

For the case of above average-sized claims, you asked whether it was a trend? It's clear that we have seen have higher losses, and specifically in the US, in claims of above €500k. That is why we have also taken some measures to readjust on large exposures in some specific sectors.

Benoit Petrarque, Kepler Chevreux

Okay, great, thank you very much.

Operator

Thank you, sir. Next and last question is from Guilhem Horvath from Exane BNP Paribas. Please go ahead.

Guilhem HORVATH, Exane BNP Paribas

Yes, thanks for taking my questions. The first question is on the loss ratios. If I compute the loss ratios per region, I think you have quite an impressive improvement in Asia Pacific and in Latin America. Can you confirm that I'm not completely wrong? And quite a deterioration in the other markets? I'd like to understand what, in the mature markets, is coming from the export rates, and what is coming from the underlying profitability? What's the proportion there?

My second question is about the plan you presented. I think if you look at slide 24, you want to cut quite a lot of the costs, or at least adjust to the market. On slide 6, you say you reinforced the management team. So isn't that a little bit contradictory? Because this comes at a cost, right? I can only congratulate you for the hirings you've been making, but should we expect you to cut quite a lot of head count - elsewhere in your other services maybe?

And lastly on solvency. You spoke about standard formula and you spoke about reinsurance but I

don't think you spoke about internal model approval. I think it's quite an important element, because if you compare your consumption in terms of capital with Euler Hermes, I think you consume something like a little bit more than 30% for the same type of business. Isn't there quite a lot of upside coming from internal approval and where are you in terms of negotiations with the regulator? Do you still expect to get this model approved at some point? Thanks very much.

Xavier DURAND, CEO, Coface

Okay, let me start with the cost question. So, clearly we have an ambition to improve the operational efficiency of the business, which is a multi-faceted plan. I mean, it's looking at a broad number of things. Again, I'm not going to describe them here, but we will do that on 22nd September. It's technology, it's cost, it's process, it's a whole bunch of things. So yes, it is a significant improvement in operating efficiency.

Now, when it comes to recruiting people, I think to drive such a transformation, you need good people. You need to bring in some skills that are different from the skills that the business has and to complement the strengths of the business with some others. So to me, it's actually in line in order to engineer a transformation like this. There is a cost involved with this, but I think it's a worthy investment and it's part of what we need to do in order to drive the change. So, you know, we have our eyes open on that point.

When it comes to capital efficiency, I think the way we look at this is, we think that in the short term and medium term, we see an opportunity. We will strive to get the most that we can out of opportunities coming out of reinsurance. I think we see the internal model discussion as more of a long-term discussion. I think there's quite a lot of work that still needs to be done on that. We probably see a focus on managing the way we leverage the capabilities and opportunities offered in the reinsurance market as a more short- to medium-term opportunity than the internal model.

Guilhem HORVATH, Exane BNP Paribas

Should we expect you to cede a lot more business reinsurance through a much larger quota share? Is this the type of business you're speaking about here?

Carine PICHON, Chief Financial Officer, Coface

It could be an option. We'll give you more details on 22nd September, Guilhem. It is something which has already been done on the market, so it's not particularly exceptional. We are going more into detail in order to have the correct scheme and we'll come back to you for sure.

Xavier DURAND, CEO, Coface

Yes, we will provide more colour on this. But again it's a dual plan. It's improving the operational performance of the business and then finding ways to make it more capital-efficient. Again, I think when it comes to the internal model, there's more work required here and it's going to take more time. So I think we'll have to look at this more as a long-term question.

Carine, do you want to talk about the loss ratios per region?

Carine PICHON, Chief Financial Officer, Coface

On the loss ratio per region, you asked us where the increase in loss ratio in emerging markets comes from between Q2 and Q1. We have mentioned North America and its exports, which are linked to a higher level of claims. We can also give the example of Brazilian exports for clients which are located in the US. As a reminder, we also said in Q1 that in Western Europe, we were

at kind of an abnormal loss ratio at 11%, so we have a readjustment. This doesn't mean that we are worried about what is happening in the region because, as you can see, it's still good on H1. It is under 30%, which means that the situation is clearly under control, but you have the small effect of some adjustments

Guilhem HORVATH, Exane BNP Paribas

Just to come back on that, my calculation gives me a Western Europe combined ratio of 102.8% in Q2. Is this correct?

Carine PICHON, Chief Financial Officer, Coface

For combined ratio, I don't know, but on page 28, for Western Europe, I see that the loss ratio is 69%. But as I said, we need to be careful in case there is a readjustment - as in Q2, where we had an increase. However, I think what is more important is to look at the trend on each one under 30%.

Xavier DURAND, CEO, Coface

Yes, I think there could be some quarter volatility. There is a page in the presentation with the details.

Carine PICHON, Chief Financial Officer, Coface

28.

Xavier DURAND, CEO, Coface

Page 28. You'll see the numbers which were quoted in Q1 and the numbers that we see in Q2.

Guilhem HORVATH, Exane BNP Paribas

Are the regions the clients' regions, or is it the –

Carine PICHON, Chief Financial Officer, Coface

Yes.

Xavier DURAND, CEO, Coface

Yes, this is the clients. You are right to point this out. As I said that on the call earlier, in the mix of what we insure, say, in a country like France or in Germany, there is some business that is linked to exports in other parts of the world. This mix varies by region and this is pretty much in line with normal trading patterns you would find for the global economy in that part of the world. So it's like an intertwined web of exports and local business. So there is an effect of emerging markets everywhere – although it is stronger, for example, with North America and Latin America, than it is in other parts of the world.

Guilhem HORVATH, Exane BNP Paribas

Okay, that's good. Thanks.

Operator

Thanks. We have no further questions.

Xavier DURAND, CEO, Coface

Thank you very much. We very much appreciate everybody calling in. Obviously the next point for us will be the 22nd September presentation. Have a good evening, everybody.

Operator

Ladies and gentlemen, this concludes today's conference call. Thank you all for attending. You may now disconnect.

(End of Conference Call)

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T R A N S C R I P T

CONTACTS

MEDIA

Monica COULL
T. +33 (0)1 49 02 25 01
monica.coull@coface.com

Maria KRELLENSTEIN
T. +33 (0)1 49 02 16 29
maria.krellenstein@coface.com

ANALYSTS / INVESTORS

Cécile COMBEAU
T. +33 (0)1 49 02 22 94
investors@coface.com

FINANCIAL CALENDAR 2016

September 22 2016: Investors' Day (London)

November 3 2016: publication of 9M-2016 results

FINANCIAL INFORMATION

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