DENIS KESSLER: “The world is on an economically bumpy road”

To coincide with the presentation of SCOR’s 2011-2013 strategic plan, Denis Kessler, the Group’s Chairman and Chief Executive Officer, discussed with “Les Echos” his feelings on the new economic order which is starting to emerge following three years of crisis.

Do you believe that the worst of the crisis has passed now?

Probably. But we are changing era. We are now on an economically bumpy road with obstacles of all kinds disturbing the system: liquidity shocks, monetary shocks, financial shocks, systemic risk, inflationary pressures, exchange rate volatility, etc. It is the end of the linear era with its continuous curves and clear trends. This new economy is very difficult to manage. By definition it is much more unstable. Now is the reign of the news flow, a succession of good and bad news used by each economic player in an attempt to verify whether their theory proves right. Globalisation only intensifies this type of economy. The problems in Greece have led to a sovereign debt crisis. The extensive fires in Russia are affecting the world’s agriculture. The floods in Pakistan are set to impact cotton prices.

Do you think that the cost of the crisis has been deferred?

Yes, although this varies from country to country. In the United States, a much larger proportion of the crisis has been dealt with than in Europe, where the necessary adjustments have been postponed considerably. The wait-and-see attitude is prevalent and we have not yet reached possible scenarios to end the crisis as we are still managing it on a political level. Admittedly, David Cameron, promising ten years of austerity in the United Kingdom, now seems to have grasped the extent of the situation. Our public and social structures are no longer suited to the emerging world and must be reformed. Government finances in many European countries are not “sustainable”. Social democracy on credit no longer works! We cannot distribute money that we do not have, thereby passing on the bill to future generations.

The executive power in France will have to change tack…

Economic revival, if it comes, is not enough alone to put our country back on the road to long-term growth, to restore our competitiveness and to improve our standard of living significantly. This is why long-term recovery from the crisis must involve historic structural reforms, such as the pension reform. We are lagging behind and must work twice as hard to catch up!
You often say that recovery from the crisis will herald the return of inflation. Do you still stand by this idea?

There is a high probability that the end of the crisis will be marked by an inflationary period. Moreover, the start of inflation can be observed in China and Brazil. The beginning of globalisation contributed to disinflation, but now it may well lead to inflation due to heightened competition for the planet’s resources (energy, raw materials, etc.). The Federal Reserve’s balance sheet has doubled since Lehman Brothers went under! To soak up the excess liquidity generated during the crisis, central banks will have to persuade banks to give them their surpluses. They will have to raise their key interest rates to provide greater profitability than that offered to financial institutions on the market. Therefore, the scenario of a considerable rise in interest rates is increasingly probable. Consequently, the cost of government debt will rise significantly and this will be passed onto the taxpayer if deficits are to be curbed. I cannot say when this will happen. Probably when recovery is at its peak. What is sure is that central banks and political decision-makers are facing a series of very painful dilemmas.

For some, a controlled return of inflation would not necessarily be a bad thing…

Inflation is an easy way out but comes with serious pernicious effects. Price stability is a priority for governments as it is essential for the production sector, investors and society as a whole.

Are you satisfied with the regulations created during the crisis?

Regulations are always one step behind crises. They should be voted in advance rather than as a curative measure. The problem today is that public risk management is not optimal. In the 21st century, governments will be judged on their ability to apply optimum risk management to anticipate all risks (technological, natural, financial, health and social, etc.), to prevent them and manage them should they occur. This is not impossible, as Canada demonstrates. The country boasts a remarkable management of the financial crisis. Regulations there anticipate such trends. The local regulator asks our subsidiary to provide tomorrow’s solvability ratio, not today’s or yesterday’s!

Over the next three years, the fifth reinsurance group in the world is aiming for average annual growth of 9% and improved profitability. The group wishes to continue its improvements by optimising its risk profile.

SCOR has just presented its new 2011-2013 strategic plan to the financial community. What assessment can you make of your eight years at the helm of the Group?
Everything has changed at SCOR! Its legal status, its governance, structures, organisation and policy subscription. The only thing that has remained unchanged is its name! When I arrived in November 2002, the company was on the brink of bankruptcy. It had recorded losses of €455 million. We are now in our 23rd consecutive quarter in profit. We have got through the crisis by pursuing our development programme. In seven years, shareholders’ equity has been multiplied by seven. Premium income has increased from €2.4 billion in 2005 to €6.4 billion in 2009. Over the last three years, we have paid out €466 million in dividends to our shareholders and have strengthened our net assets by €600 million.

**Do you consider SCOR’s competitive position to be satisfactory today?**

We are one of the few financial institutions whose ratings have risen during the crisis. SCOR currently boasts excellent positions on the reinsurance markets. Our debt ratio has dropped from 46% in 2004 to 11% today and is among the lowest ratios in the (re)insurance market, affording us considerable financial flexibility.

**And yet your market listing has dropped...**

It is true that we are currently listed around €17 per share, for net assets of over €23. All securities are undervalued as is typical in times of crisis due to investors attaching little worth to intangible assets. I am convinced that the market will recognise SCOR’s value. Our market valuation, which fell under the €500 million mark in November 2002, is around €3.2 billion today! Furthermore, SCOR’s listing has been one of the most stable during the crisis period, as demonstrated by the low volatility of our shares.

**Tell us about the Group’s new roadmap.**

Our new plan has been christened “Strong Momentum”. Our aim is to successfully increase both our “mass” and “speed”, in a context where one is usually achieved to the detriment of the other. To do this, we intend to make improvements within the Group by optimising our risk profile.

**What does this imply in terms of figures?**

We want to provide our clients with a level of security that corresponds to an AA rating and reach a return on equity greater than 1000 basis points at a risk-free rate during the cycle. We are confident that we can achieve growth of 9% per year over the next three years, including 5% growth in our existing activities, for which we recorded growth of 4.4% per annum since the start of the crisis. By bringing about a diversification of insurers’ portfolio of reinsurers, Solvency II will be beneficial for medium-scale players such as SCOR.
Are you planning to position the Group on new risks?

Out of the 9% of annual growth, 4% will come from around a dozen initiatives, four in life reinsurance, six in non-life and one in asset management. For example, we would like to expand our life reinsurance business to Australia as we forecast strong development potential there, and to make inroads into the British life expectancy market, for which demand is high. Our catastrophe programme is currently focused on Europe and Japan and we plan to adjust it slightly to better suit the United States. We are also planning to create cat bonds for well-informed investors with a view to sharing our expertise.

Is external growth on the horizon?

If you look at Revios in 2006, Converium in 2007 and XL Re Life in 2009, you can see that we have a good track record when it comes to acquisitions and integration. We have indisputable principles concerning external growth that require compliance from all projects. “Strong Momentum” is not based on acquisitions.

Are you going to make changes to your financial management?

Our new asset allocation is consistent with the interest rate and inflation shocks we anticipate. We have strengthened our real estate assets, shares and private bonds and we are shedding public bonds and cash flow. As the probability of the bond bubble bursting increases, part of our bonds are inflation-indexed and our portfolio continues to favour short-term bonds. €4.5 billion in financial cash flow will be reinvested in the next three years according to the new rate scale. Should there be no inflation or bond crisis, our strategy will not have cost us very much, and if there is, it will make a significant difference.

Your appointment comes to an end in April 2011. Are you planning to stand again for election?

The decision will be made by the Board of Directors, based on shareholders’ wishes. I am not alone in supporting the new plan; SCOR’s Board of Directors and Executive Committee are just as involved. I feel that I have fulfilled my assignment to turn around and redevelop SCOR. I like my job and the company that we have created. We’ll have to wait until next April to find out what comes next!

Interview by Nicolas Barré, Laurent Thévenin, Géraldine Vial and François Vidal