

Q3 2019 Earnings Call

Company Participants

- Fernando Passos, Deputy CEO, Chief Financial Officer and Investor Relations Officer
- Jose Carlos Cardoso, Chief Executive Officer

Other Participants

- Henrique Navarro, Analyst

Presentation

Operator

Good morning, and welcome to IRB Brasil RE's 2019 Third Quarter Earnings Conference Call. Here with me today are Jose Carlos Cardoso, CEO; and Fernando Passos Deputy CEO, CFO and IRO. This conference call is being recorded. And participants will not be allowed to ask questions during the presentation. After the presentation, we'll open the question-and-answer session. (Operator Instructions).

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Mr. Jose Carlos Cardoso, CEO of IRB RE will now begin with presentation.

Jose Carlos Cardoso {BIO 20228447 <GO>}

Good morning, and thank you all for participating in our earnings conference call for the third quarter and nine months of 2019. I'll begin the presentation with the highlights of the period. Actually, we are very happy with our achievements during this year.

Our performance was recognized with the first place in the Premio Broadcast Empresas award, which assessed 190 publicly-held companies that trade shares on B3, the Sao Paulo stock exchange. In the same award, we were the highlight of Novo Mercado, as tripled our market value since we went public on July 31, 2017. As of September 30, IRB Brasil's market capitalization was BRL35.2 billion, compared to BRL8.5 billion on the IPO date, placing us among the world's ten largest reinsurers in market capitalization.

Regarding the performance our share, we can say they have performed very well, with a 39% appreciation in the first nine months of 2019, compared to a 19% rise in the Ibovespa. An important decision made by our shareholders was to approve the stock split, effective as of September 26, when each share was split into three, with no change in the capital stock. In September, we had 33,000 shareholders, a significant increase from the 17,000 shareholders we had in December 2018.

In October 2019, we renewed our retrocession contracts for 2020. During the negotiations, we managed to maintain essentially the same financial conditions as in 2019, and better general conditions. As a result, we expect the total retrocession cost to post a material reduction compared to 2018. This reduction in cost, and the maintenance of the coverage of reinsured amounts, was possible due to our good loss ratio history over the last four years, by the upgrade in our rating by A.M. Best, from A minus to A, on a global scale, as well as improved governance after we became a corporation.

Our results show we have been on a continuous growth track. In the first nine of 2019, the written premiums rose 22% compared to the same period of 2018, totaling BRL6.4 billion. The written premium abroad rose 36% to BRL2.8 billion. Our income rose 34% to BRL1.1 billion. Our return on average equity, ROAE, rose by 6 percentage points from 31% in the first nine months of 2018 to 37% in the first nine months of 2019.

Finally on November 6, 2018 the Board of Directors of IRB-Brasil Resseguros SA approved the payment of interest on capital, IOC, for the total gross amount of BRL198 million and gross value per share of BRL0.21 to be paid on December 5.

Now, our CFO Fernando Passos will continue the presentation, discussing further details of our results for the third quarter and the first nine months of 2019. Fernando, please.

Fernando Passos {BIO 20117537 <GO>}

Thank you, Cardoso. Good, morning everybody. I will begin on slide number three. Here you can see our net income and the return on average equity. The green graph to the left shows our net income increased by 29% from BRL305 million in the third quarter of 2018 to BRL393 in the third quarter of 2019. This result was driven by an increase of written

premium, increase of earned premium, better efficiency due to the reduction in the administrative expense ratio and the financial results. The return on average equity rose by 4 percentage points from 33% in that third quarter of 2018 to 37% in the third quarter of 2019.

On the following slides, we will discuss in detail the performances in the quarter. The slide number four shows the history of our overall written premium by quarter. In the third quarter, our written premium increased by 18% year-over-year, achieving BRL2.3 billion. In the third quarter written premium in Brazil increased by 10.5% year-over-year, achieving BRL1.3 billion. Written premium abroad achieved BRL999 million in the third quarter of 2019, an increase of almost 30% year-over-year. This growth of almost 30% was mainly due to the organic growth in the issue currency, that is dollar. As the weighted average variation of the exchange rate in the third quarter was of only 1% compared to the same quarter in 2018.

On the slide number five, we will talk about the dynamics of our retrocession ratio. Our retrocession ratio remained nearly stable at 22% in the third quarter of 2019, compared to the 21% ratio reported in the same period last year. As previously mentioned by Cardoso, we renewed our retrocession contracts for the full year of 2020 in October of this year. During the negotiations, we managed to maintain essentially the same financial conditions as in 2019, and to achieve improvements in the total cost of retrocession for 2020 with an expected material reduction year-over-year compare in 2020 with 2019.

As long as the premiums effectively written during the year of 2019 gain a greater proportion as a percentage of the company's total written premium. when compared to the premiums written in previous underwriting years, the company's retrocession costs will show a reduction, since the retrocession contracts applicable to the year of 2019 have, proportionally, lower retrocession costs when compared to the previous years.

As a result, the company has historically shown a significant reduction in its retrocession ratio. In 2017, the retrocession ratio went from 30% to 27% in 2018 and we believe that tendency will be maintained in 2019 and 2020, given that the company has already renegotiated its retrocession agreements.

Slide number six, shows our retained premium achieving BRL1.8 billion in the third quarter, up 16% year-over-year. On slide number seven, the graph shows the historical seasonality of the constitution and reversal of technical provisions relative to written premium. In 2015, 2016, 2017 and 2018 the provisions were constituted in the first three quarters of the year, followed by an average reversal according to this scenario in the fourth quarter.

It is important to remember that, the technical provision is used to retain values that are the result of an increase in our retained premium, in order to prevent all their value from being taken prematurely to earned premium and consequently to our underwriting result. Over the policies' coverage term, depending on the performance of the business and the term for the risks to expire, this provision may be taken to earned premium and, consequently, to the underwriting result.

On slide number eight, you can see that the earned premium achieved BRL1.4 billion in the third quarter, up 13% year-over-year. On the slide nine, we show our loss ratio performance. In the third quarter, the loss ratio went from 58% in the third quarter of 2018 to 52% in the same period in 2019. A reduction of 6.4 percentage point. However, measured by OCR, Outstanding Claims Reserve went from 44% in the third quarter of 2018 to 46% in the third quarter of 2019, mainly driven by claim reports in the agribusiness, reported both in Brazil and abroad. In nominal terms OCR went up from a net addition of BRL547 million in 2018 to a net addition of BRL650 million in the third quarter of 2019.

The loss ratio measured by IBNR corresponded to 6% of the earned premium in the third quarter of 2019. In nominal terms, IBNR went from a net addition of BRL184 million in the third quarter of 2018 to a net addition of BRL87 million in the third quarter of 2019. The net addition to IBNR was lower in the third quarter of 2019 year-over-year, because in the third quarter of 2018 there was a higher addition due to the prior research conducted by the company that indicated an increase in our loss ratio.

On slide 10, you can see our underwriting result rose 24% to BRL321 million in the third quarter of 2019, compared to BRL259 million in the third quarter of 2018. This growth was driven by the increase of 18% in written premium in the third quarter of 2019, which was a lot higher than the small rise in retained claims as a whole.

Slide 11 shows our administrative expense as a ratio of earned premium fell by 0.6 of a percentage point, down from 4.4% in the third quarter of 2018 to 3.9% in the third quarter of 2019. Our management's commitment to continue increasing our efficiency and improving our profitability continues to be the basis for our operations.

On slide 12, you can see our consolidated financial investments, including the parent company, subsidiaries and branches, achieving BRL239 million in the third quarter of 2019, versus BRL178 million in the third quarter of 2018. The consolidated performance of the management of financial assets of the parent company, subsidiaries and branches was 137% of the CDI in the third quarter of 2019. In the third quarter of 2019, the exclusive investment fund, IRB Multimercado had total assets of almost BRL1 billion. In the period, the fund's profitability was 348% of the CDI. This fund concentrated the company's investments in foreign exchange, equities and also indexed sovereign bonds, pre-fixed, and pegged to inflation plus coupon and other investments. The company's other financial resources were mainly invested in assets with profitability close to the Selic.

Our investment portfolio was reduced as at September of this year compared to December of last year, mainly due to the payment of dividends in April of this year and the material volume of payment of claims, with immediate cash effect, but whose recovery from reinsurers does not occur simultaneously, following specific bases of retrocession contracts. Furthermore, it is important to mention that with the Selic rate at its lowest historical level, we have prioritized the negotiation of contractual conditions that provide us better conditions on payment of claims by accelerating such payments, benefiting the claims interest line.

It should be noted that, during the third quarter of 2019, we completed the transfer of the management of exclusive funds previously managed by IRB to IRB Asset Management.

Now I will ask Cardoso to proceed to his closing remarks.

Jose Carlos Cardoso {BIO 20228447 <GO>}

Thanks, Fernando. Before I close this presentation, on the slide 13, I want to discuss our expectations for the fiscal year of 2019 and what we have achieved so far.

Relative to the guidance disclosed by the company on August 5, I'd like to point out the following aspects. The written premium rose 21.5% in the first nine months of 2019, in line with the estimate of 20% to 27% for the year. The amplified combined ratio for the first nine months of 2019, achieved 70.5% which is within the range of 69% to 73% for 2019. And the administrative expense ratio although is slightly better than we forecast of 4.6% to 5.2% is in line with the company's expectations for the fiscal year of 2019.

The company's outlook remains positive. We have already recorded an improvement in our operations in the oil and gas sector. And large construction works are expected to be resumed along with the privatizations and the approval of the new regulatory framework for bids in Brazil, increasing the guarantee for public works and the momentum of the large risk portfolio.

A new opportunity has just opened up with a new Private Insurance Superintendence, Susep, standard that determines annual policies are no longer mandatory, making room for other offer of products that can last months, days, hours, minutes or even with no determined term. Such flexibility should create innovative businesses that we are ready for.

We now close our presentation and open the question-and-answer session. Thank you all.

Questions And Answers

Operator

Thank you. The floor is opened for questions from investors and analysts. (Operator Instructions) Our first question comes from Henrique Navarro, Santander.

Q - Henrique Navarro {BIO 16188960 <GO>}

Hi. Good morning Cardoso and Passos. Thank you for the opportunity. Well, if I read the guidance and you have been in line so far with the guidance -- within the guidance range. And if I translate this guidance to a net income for the year. I would reach -- my number is BRL1.6 billion for the year and this number is pretty much the same number that you can find in Bloomberg Consensus. But the problem with this number is that, after the third quarter we might need a sizable increase in the net income for the fourth quarter in order

to reach this number. So my question to you is, is there any risk of you missing the guidance for the full year of 2019? Thank you.

A - Fernando Passos {BIO 20117537 <GO>}

Thank you, Navarro. Thank you for the question. We are completely committed and absolutely comfortable that we will deliver the guidance that we reported. So, no risk from our point of deal.

A - Jose Carlos Cardoso {BIO 20228447 <GO>}

Henrique, listen, every time there we see an opportunity to look at our guidance, you voluntary did it. At this time, we see, again, absolutely comfortable with the numbers that you published last quarter and we see no reasons for any changes to change this situation. Therefore, the administration of the company remain fully committed to deliver the guidance that you provided last quarter without any concern about it.

Operator

This concludes the question-and-answer session. At this time, I would like to return the floor back to Mr. Jose Carlos Cardoso for any closing remarks.

A - Jose Carlos Cardoso {BIO 20228447 <GO>}

Thank you all for participating and for your interest in learning more and discussing our results and vision of the future. I invite you all to participate in our Investors Meeting on November 26, in Sao Paulo where we talk about the business perspectives. Thank you very much and have a great day.

Operator

Thank you. This does concludes today's presentation. You may disconnect your line at this time and have a nice day.

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