

Q2 2019 Earnings Call

Company Participants

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

Other Participants

- Mario Pierry, Analyst

Presentation

Operator

Good morning and welcome to IRB Brasil RE's 2019 Second 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 will open the question-and-answer session. (Operator Instructions) This presentation was prepared by IRB Brasil RE and shall not be considered as source of data for investments. This presentation may contain certain forward-looking statements and information related to the Company reflecting current views and/or expectations of the Company and its management concerning its performance, business and future events.

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

Jose Carlos Cardoso {BIO 20228447 <GO>}

Thank you all for participating in our earnings conference call for the second quarter and first half of 2019. I'll begin the presentation with the highlights of the first half of 2019. On July 31st, 2019 we celebrated our second year as a publicly held company. We are very happy with our achievements during this period. This first half of 2019 was another big step for IRB. In two years as a publicly held company, our market cap went up from BRL8.5 billion in July 2017 to over BRL30 billion in June 2019 with our shares appreciating 267% in the period. Given our stock's liquidity and traded volume, we have been listed in the capital markets major index; both the Ibovespa and IBrX100, MSCI, and FTSE. Our first big achievement refers to our ownership structure. We are now a full corporation. This increased the liquidity of our stock, driving governance improvement, and efficiency and agility in our decision-making process and approval.

These changes derived from two successful follow-on offerings. First, in February, the FGEDUC fund managed by Caixa raised BRL2.5 billion. Now in July, the Federal government and BB Seguros raised a further BRL7.4 billion bringing largest shareholders to our base, of which 71% is allocated in foreign investors. The Federal government and BB Seguros were able to sell their interest because the change in the Brazilian Private Insurance Board and SUSEP that allowed for publicly-held companies in the insurance and the reinsurance industry, which is our case to become a corporation with diluted controlling stock. In other words, we had became a corporation, which should make our decision process faster. However, without a controlling shareholder or block, we had to improve our governance such as by having committees made up of more senior members and extend the term of mandate of both the Board of Directors and the Executive Office to two years and beyond, adopt a succession plan to prepare our new future leaders.

Another highlight was the upgrade by specialized rating agency, A.M. Best, which raised our rating from A minus to A in a global scale. The upgrade by A.M. Best, which is the largest and oldest global rating agency in the insurance market, will enable us to do business with more international insurers since some of them requires an A rating from trade partners. We are also proud of the institutional investors recognition including Best CEO, Best CFO, Best Investor Relations Professional, Best IR Team, and Best IR program in the financial institution category. The awards came in a year when we dedicated our best efforts to the market with two follow-on offerings, our listing in the Ibovespa and our intense participation in national and international conference. We also ranked the second with website, analyst day, and best governance practice categories.

IRB was also the winner of the best listed companies ranked in the revelation category created by InfoMoney in partnership with Ibmecc and Economatica. The award reviewed the companies that went public in the last three years based on three criterias; profitability, stock performances, and corporate governance practice. Our results show we have been on a continuous growth track.

In the first half of 2019, written premiums rose 24% compared to the first half of 2018 totaling BRL4.1 billion. Another highlight was the international written premium, which grew 40% reaching BRL1.8 billion and our net income of BRL738.9 million represented an

increase of 37%. In terms of return on average equity, ROAE, there was an increase of 8 percentage points from 30% in the first half of 2018 to 38% in the first half of 2019.

Our CFO, Fernando Passos, will now continue the presentation discussing in further detail our results for the second quarter and the first half of 2019. Fernando, please.

Fernando Passos {BIO 20117537 <GO>}

Thank you, Cardoso. Good morning. I will begin on Slide Number 3. Here you can see our net income and return on average equity. The orange graph to the left show that our net income increased by 35% from BRL287 million in the second quarter of 2018 to BRL388 million in the second quarter of 2019. Return on average equity rose by 6 percentage points from 33% in the second quarter of 2018 to 39% this year. We had some relevant drivers that were important for us to achieve this 35% increase in net income during the second quarter of this year. First, a 22% growth in written premium, an 18% growth in earned premium, a 19% growth in underwriting results, and more efficiency with the reduction in administrative expenses ratio of the Company as percentage of earned premium. On the following slides, we will discuss in detail these figures.

Here on Slide Number 4, we show the history of our overall written premium by quarter. In the second quarter, our written premium increased by 22% compared to the second quarter of 2018 achieving BRL2.4 billion. Written premium in Brazil increased by 14% in the second quarter of 2019, compared to the second quarter of 2018 achieving BRL1.4 billion, due to the growth of domestic market itself. This improvement was mainly due to the new contracts executed in the period, mainly in the oil and gas, property and life segments, following the economy's rebound.

On the other hand, written premium abroad increased by 35% in the second quarter of 2019 compared to the same period of last year achieving BRL975 million in the second quarter of 2019. This growth was sustained by our increased share in existing contracts and the weighted average appreciation of 6% of the dollar exchange rate in the second quarter of 2019, compared to the second quarter of 2018. Our expertise in international market is to seek business opportunities mostly in South America, focusing on business lines we specialize on, such as aviation, life, and agribusiness.

On slide number 5 we will talk about the dynamics of our retrocession cost. Our retrocession ratio remained stable at 28% in the second quarter of 2019 compared to the 27% ratio reported in the same period last year. Even with the premium reimbursement to the retrocessionaires, due to the use of retrocession protection in the period. As long as the premium 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 cost will show a greater reduction, since the retrocession contracts applicable to the year of 2019 have proportionally lower retrocession costs when compared to the previous years.

The slide 6 shows our written premium in the second provided of this year which increased by 20% when compared to the same period last year achieving BRL1.7 billion in

the second quarter of 2019. This growth was driven by the rise in the written premium in the period.

On Slide Number 7, the graph shows the historical figures of the constitution and reversal of technical provisions relative to written premium. You can see that in 2015, 2016, 2017 and 2018, the provisions were formed in the first three quarters of the year followed by an average reversal according to the historical numbers presented here. 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 the value from being taken prematurely toward net premiums and consequently to our underwriting results. Over the policies coverage term depending on the performance of the business and the term for the risks to expire, this provision maybe taken to earned premium and consequently to the underwriting result.

Now on Slide Number 8, we can see that our earned premium in the second quarter of 2019 increased by 18% when compared to the second quarter of 2018, achieving BRL1.4 billion in the second quarter of this year. This growth was driven by a higher premium written in the period. On slide number 9, we show our loss ratio performance. Our loss ratio went from 57% in the second quarter of 2018 to 53% in the second quarter of 2019. However, the loss ratio measured by OCR, Outstanding Claims Reserve went from 53% in the second quarter of 2018 to 65% in the second quarter of 2019. This growth was mainly driven by claims reported in the agribusiness segment, both in Brazil and abroad. So in nominal terms, the OCR, Outstanding Claims Reserve went from a net constitution of BRL622 million in the second quarter of 2018 to a net constitution of BRL900 million in the second quarter of 2019.

As we had largely mentioned during the fourth quarter of 2018 and the first quarter of 2019, this likely rise in claim reports would be materialized in the second quarter of 2019, being adequately and previously captured by the Company by using the IBNR Company, the incurred but not reported losses. Therefore the IBNR recorded a net constitution of BRL196 million in the fourth quarter of 2018 and a further net constitution of BRL67 million in the first quarter of 2019 achieving a total net constitution of BRL263 million in this six months.

Therefore now in the second quarter of 2019, IBNR recorded a reversal of BRL158 million due to the claim reports received by the Company in the second quarter of this year. And that were adequately registered as OCR in the second quarter of this year. We generated though the reversal of the correspondent IBNR, previously constituted at the time, given the development of the contracts. Our retrocession program proved to be effective this quarter, because it minimized more severe impacts on our retained loss ratio.

As you can see we recovered BRL515 million in claims from our retrocessionaires related to the quarter, compared to the recover of BRL156 million in the second quarter of 2018. According to the note number 25.4 to our financial statement as of June 30, it is worth noting that in the second quarter of 2019 there was a specifically reimbursement of a significant amount in the aviation segment according to the note number 25.2 to our financial statements as of June 3rd of this year. This specific reimbursement derives from an accident with a Brazilian airline company in 2007. But the amount retained by IRB in this

case was of less than 1% of the total claim amount paid at that time. So the same movement that caused a reimbursement revenue also generated and expanded the payment of the reimbursement to the retrocessionaires according to the note 25.4 to our financial statements. So the effect on our result is basically, almost zero.

In this slide 10, in order to illustrate better about the IBNR provisions, we prepared this graph in which we demonstrate the dynamic of the constitution and result of the IBNR component over the last three quarters and the year-on-year comparison with corresponding quarters. This graph shows exactly what we said in the previous slide that is, in the second quarter of 2019, IBNR recorded a reversal of BRL158 million due to the claims report we received in the second quarter and that were recorded by OCR in the period that generated a reversal of the corresponding IBNR previously constituted at the time, even the development of the contract. As you can see, the loss ratio measured by IBNR for the last three quarters is a recurring 3% when we considered a total net IBNR constitution for the last three quarters compared to the overall premium earned in the period.

On the Slide 11, we will talk about our underwriting results. The underwriting results achieved BRL354 million in the second quarter of 2019, an increase of 19% when compared to BRL296 million achieved in the second quarter of 2018. This growth was driven by the increase of 22% in written premium, which was higher than the rise in retained claims. The Slide 12 shows our administrative expense as a percentage of earned premium, which remained stable at 5% in the second quarter of 2019. Such performance confirms our commitment to increase the efficiency and to improve profitability.

On the Slide 13, you can see our consolidated financial investments, including the parent Company subsidiaries and branches achieving BRL184 million in the second quarter of 2019 compared to BRL177 million in the second quarter of 2018. The consolidated performance of the management on financial assets of the parent Company subsidiaries and branches was 121% of the CDI in the second quarter of 2019. In the second quarter of 2019, the exclusive fixed income investment fund IRB absolute had total assets, sovereign bonds of almost BRL3 billion.

The period, the fund's profitability was of 1.71% or 112% of the CDI. IRB's portfolio had assets of BRL2.8 billion as of June 30 of this year. And the most important asset group was fixed sovereign bonds. The average daily balance of the financial investment portfolio, except for the real estate portfolio was almost BRL6 billion in the second quarter of 2019.

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

Jose Carlos Cardoso {BIO 20228447 <GO>}

Thank you, Fernando. Before I close my presentation on the slide 14, we want to discuss our guidance for the full year of 2019, just to remind you given the last two follow on offers, one in February and the other one in July of 2018, our Board of Directors decided at an extraordinary meeting to discontinue the disclosure of the guidance for 2019. At the

FINAL

same time, the Board of Directors also delegated to the executive officers, the decision of analyzing the possibility of resuming the guidance disclosure. Therefore on August 5th, the executive officers decided to resume the disclosure of our guidance in the material fact seeded in the CBM [ph] yesterday. (inaudible) increased its estimated related written premium growth compared to the year of 2018.

The previous estimation was a growth of 17% to 24% in written premium compared to the year of 2018 and now the estimate is a growth of 20% to 27% in written premium compared to 2018 confirming our expectation of a premium growth of 2019. The other indicators remain as the same or in other words, an amplified combined ratio, ranging from 69% to 73% and our administrative expense as a ratio of earned premium ranging from 4.6% to 5.2%.

I also highlight two other events that we consider significant for the Company's growth in the coming years which we announced yesterday night. The partnership with C6 Bank, a digital bank and the signing of a subscription for B3i in which IRB will be partnering with a major global insurers and reinsurers to develop insurtech projects. The operating reinsurance agreement with the C6 Bank and its affiliates provides that IRB will be the leading reinsurer on the credit life insurance business generated on C6 platform for a period of 10 years proportionally with IRB reinsurer with 85% of the business generated and the insurance with 15% retention.

The agreement also set rights for IRB on a similar basis to the credit life Insurance segment for other business lines except for health, auto and dental lines. The deal does not include payments by IRB beyond the reinsurance commissions on a market base. This deal is part of IRB Brasil RE's wider strategy to sign partnerships with Brazilian and South America Fintechs with value propositions similar to the Company. The other highlight is the partnership with B3i. The B3i is one of the main global technology development initiatives for the insurance and the reinsurance segment, including the registration of this transaction through a Blockchain platform.

The subscription of 8.93% of the B3i [ph] shares position, putting IRB as the only company in Latin America, alongside the leading global companies operations. The interest of B3i's share capital we allow IRB RE to have the right to appoint a member to the Company's Board of Directors with a relevant involvement in B3i's strategic guidance. B3i currently has nine Board members.

In addition to the recent highlights mentioned, the outlook is encouraging, especially due to the following facts. The increase in the subsidy announced by the federal government to help farmers pay the rural insurance for an amount that reached BRL1 billion in 2019, 2020 season. The amount available in the last season was BRL371 million. The second aspect privatization transactions by the Brazilian government involving, airports, highways, railways and ports which lead the acquirers to contract more robust insurance and reinsurance policy than those contracted by state-owned enterprise. And ongoing process to choose partners for the bank assurance business, which could pave the way for new operations for insurers and reinsurers in Brazil. Finally, our nearly 380 employees remain fully committed to the challenged targets, but the ones that can be met or even

exceeded even more, because all employees participate in our profit sharing program, which is linked to meeting 100% of the target.

We now close our presentations and open the questions-and-answer session. Thank you, all.

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Questions And Answers

Operator

Thank you. The floor is now open for questions from investors and analysts. (Operator Instruction) Our first question comes from Mario Pierry, Bank of America. Please Mr. Mario.

Q - Mario Pierry {BIO 1505554 <GO>}

Good morning, everybody. Congratulations on the quarter. Let me ask you two questions if I may. The first one, we noticed that you've maintained your amplified combined ratio guidance unchanged, but my understanding is that before you were working on the Selic rate of 6% at the end of the year and now I think you're working with 5%. So, if you can explain to us a little bit why you think that your results are not going to be volatile with the Selic rate or maybe you're seeing better operating trends than you were expecting before? And the second question is related to this upgrade from A.M. Best that you mentioned at the beginning. If you can be a little bit more specific on how that can help your premium growth in the future. Thank you.

A - Fernando Passos {BIO 20117537 <GO>}

Hello, Mario. Good morning. I'm going to talk about the amplified combined ratio and Cardoso will talk about the A.M Best upgrade. In fact when we reported our guidance on February of this year, specifically the guidance for the amplified combined ratio that considers the underwriting results as well as the invested results, we were competing at Selic at the end of the year of 6%. Now we reported again the same guidance for the amplified combined ratio, but we are considering Selic at the end of the year of 5% and we are comfortable to keep the same guidance that we were considering before due to the dealers due to the new fees we have, performance fee of our underwriting side. So in fact, the figures we have now -- the expectations we have now to the underwriting reserves was enough to offset the parallel decrease in Selic and we keep the amplified combined net ratio guidance. As you know, we increased our guidance for written premiums growth from a range of 17% to 24% to a new range of 20% to 27% and again we are comfortable to report this new guidance due to the figures we have up until now during this year. Cardoso?

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

Well, thanks for your question. Regarding the upgrading in terms of we received from A.M. Best, it might affect us positively in some aspects that I'm going to try to explain to you. First of all is with respect to the image of the company, become a company rated by A.M. Best, that is the most important rating agency we have in the market, that allow us to enter in the -- in a very selected group of the major reinsurance players in the world. So,

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this is a clear indication of the credibility of our Company and this is something that certainly is going to benefit us in terms of gaining new markets, increasing our share also in existing insurance companies. It's important to mention to you that we have some companies that put some cap in terms of lease exposure we had according to the rating of the reinsurers.

So in the moment that we -- with regards to this increase in our rate will allow us to increase our shares in those companies that we had net cap presenting us to increasing our lines. Secondly, other important aspect is the fact that being A rated allow us to enter also to do business in insurance companies that have this kind of impairments in their guidelines according to the rating of the trade partners might have. Therefore, especially in respect to some multinational insurance companies where this is really looked -- score is monitored closely, we expect to be benefit of this upgrade.

Q - Mario Pierry {BIO 1505554 <GO>}

Thank you.

Operator

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

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

One more time, thank you all for participating and for your interest in learning more and discussing our results and vision of the future. We will meet you again in November for our third quarter earnings conference call. Thank you very much. Have a great day.

Operator

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

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