Q1 2012 Earnings Call

Company Participants

- Arthur Farme, EVP of Control and IR
- Gabriel Portella, Head of Health and Dental Operations

Other Participants

- Guilherme Assis, Analyst
- Marcelo Henriques, Analyst

Presentation

Operator

Good morning, ladies and gentlemen. At this time we would like to welcome everyone to SulAmerica's First Quarter 2012 earnings conference call. Today with us we have Mr. Arthur Farme, Executive Vice President of Control and Investor Relations. We would like to inform you that this event is being recorded and all participants will be in a listen-only mode during the Company's presentation.

After SulAmerica remarks are completed, there will be a question-and-answer session. At that time further instructions will be given.

(Operator Instructions) There will be a replay facility for one week. Today's live webcast, both audio and slideshow, may be accessed through the Company's Investor Relations website at www.sulamerica.com.br/ir. By clicking on the banner webcast 1Q12 the following presentation is also available to download on the webcast platform.

Before proceeding, let me mention that forward-looking statements are based on the beliefs and assumptions of SulAmerica's management and on information currently available to the Company. They involve risks, uncertainties, and assumptions because they relate to future events and therefore depend on circumstances that may or may not occur in the future.

Investors should understand that general economic conditions, industry conditions, and other operating factors could also affect the future results of SulAmerica, and could cause results to differ materially from those expressed in such forward-looking statements.

Now I'll turn the conference over to Arthur Farme who will start the presentation. Mr. Farme, you may begin the conference.

Arthur Farme {BIO 1845065 <GO>}

Thank you. Good morning, all and thank you for participation -- for participating in our call today. Today, I'm here with Mr. Carlos Alberto Trindade, General Manager of our Automobile and Property and Casualty units, as well as with Mr. Gabriel Portella, the Head of our Health and Dental Operations.

Both with me will comment on the results of SulAmerica SA for the First Quarter 2012. SulAmerica experienced another positive quarter, which we deem as reflecting the good performances in all of our business units, as well as our healthy financial income.

These good results, combined with the Company's willingness to accelerate processes, and improve our already excellent relationship with brokers lead us to believe that we are meeting our targets in 2012. We continue to invest in modernizing our systems, improving our main operational processes, helped in some cases by specialized consulting firms, and expand our network of C.A.S.A.s, those cost-sharing centers that will serve our insured in automobile risks as well as our branches throughout Brazil.

Moreover, we continue to invest in the development of our key personnel, which I think is the main pillar to support our growth in the upcoming years. We remind you that something that we have been mentioning in previous conference calls that though the Company has already reached the important milestones, there's much more to do.

We always --- create value for our shareholders, so this is our main goal to improve the value of the Company for our shareholders and to try and invest in strengthening our relationship with clients, brokers, and partners as well.

And we understand that this is what makes us the largest independent insurance Company in Brazil. And with those -- the brief opening comments, I will start the presentation itself, which will be followed as usual by a Q-and-A session.

So beginning on slide 2, we have a (dash) board with the Company's main performance indicators with total insurance premiums growing a strong 14.5% as shown here in the slides with the Group health being the highlight growing 26% in the quarter compared to 1Q 2011. Our combined ratio ended the quarter at 101.1%, so above the hundreds, mainly due to the loss ratio in automobile.

On the other hand, net financial income came 3% higher with the Company delivering an (impressive) yield of a 117.7% of the CDI, the Brazilian base rates. All in all, we think we delivered net income of a BRL112.8 million in the quarter, growing 10.6% compared to 1Q 2011.

Moving on slide 3, we have listed just a few of the highlights in the quarter and some subsequent events. So very quickly, the Board of Directors approved a new dividend policy to be adopted from 2013 onwards, including those based on the 2012 results, with a minimum payout of 30% of the annual adjusted net income, that is 20% more than the minimum mandatory dividend in Brazil, also maintaining the payment of dividend, quarterly dividends.

In February, we also redeemed our senior notes and issued a total of BRL500 million in debentures in the local market, in the domestic markets, paying CDI plus (1.15%). Sul America Investimentos, our investment management unit, just received the Best Fixed Income Award from Valor Economico, which we thought was a very relevant award for that business.

We also released our 2011 annual report, again 100% on-line and for the fourth consecutive year, following all of the guidelines set forth by the GRI, the Global Reporting Initiative. Recently, we strengthened our commitment to sustainability overall, and signed the Global Compact, a United Nations initiative which seeks sustainable development for the global markets, encouraging companies to adopt corporate and social responsibility policies and practices.

Moving onto slide 4, as I mentioned before this comes back to premiums. We're growing 14.5% in the quarter and the pie chart on the right would show you that in the break-down, Health has accounted for 69% of our total premiums.

Moving on now to slide 5, the next slide, we have our Health and Dental insurance results. Briefly, insurance premiums in this quarter reached over BRL1.7 billion with Group health experienced health growth -- healthy growth, over 26% compared to 1Q '11.

In this case helped by a faster growth in the sales of new policies, the increase in the number of members in the portfolio, as well as high retention rates and price adjustments to this increase in portfolio.

Another highlight in the segment is the SME portfolio that has ended the quarter with 283,000 members, growing short of -- south of 30%, 29.3% in premiums compared to 1Q '11. The SME segment should continue to experience, we think, high growth of figures in the following years.

The (inaudible) insurance portfolio is also experiencing an expansion of growth rate. Total members almost doubled compared to 1Q '11, in this case reflecting both the integration of approximately 140,000 members from the acquisition of Dental PLAN, a specialized dental company, as well as the portfolio's organic growth to reach a total of 467,000 members at quarter end.

We'll continue to focus our attention in this case by taking advantage of cross-selling opportunities with existing health member portfolio. The total loss ratio shown on the upper right side of the slide was mostly impacted by the individual health insurance portfolio that increased 550 bps over 1Q '11, while the Group health portfolio has shown a slight improvement in this time.

According to the latest data published by AMS, the health care regulator, for the year-end 2011, SulAmerica grew 15.2%, whereas the market was growing at 13.4% making us one of the three largest groups in the Brazilian private health care market with 9.1% market share.

Moving on to slide six to address the Auto insurance business, in this segment we saw more a kind of contained growth in this quarter, 2.3% over 1Q '11, negatively impacted by the somewhat slowdown in the growth of new vehicles in the period, as well as market conditions that have prevailed so far.

We ended the quarter with close to 1.5 million insured vehicles in the portfolio, a 1.7% increase over 1Q '11. The chart on the upper right, we have the loss ratio in 1Q '11 and the increase of about 680 bps of 1Q '12 over 1Q '11. It's basically due to an improvement in the calculation methodology of our claims reserve with a one-time impact in the quarter.

This change affected the loss ratio in January 2012 at 81.8% as released by the regulator, but its effect should be diluted throughout the year. The loss ratio (in auto) was impacted by the higher frequency of theft and robbery, especially noticed in Brazil's largest cities.

Slide seven addresses the other P&C segments which carries a diverse portfolio which composition is illustrated in the bottom-right of the slide. Premiums in this segment saw a slight increase of 2.7% in the quarter, but the loss ratio improved I would say quite significantly decreasing 1,400 bps with 49% at quarter end mainly due to the improvement of the writing policy that we've been adopting, as well as some improvement in our pricing methodology. As a consequence gross margin in this line improved significantly to 33%, with an improvement of 1,950 basis points in the quarter.

Slide eight addresses our Life and Personal Accident businesses. In this case, premiums increased close to 13%. Then the loss ratio was stable at 52%, results -- in -- this line benefited mainly from the credit life insurance that we call the (presa) mutual line in Brazil, responsible for about 10.5% of this portfolio. Further break-down is shown on the chart on the bottom in the right of the slide.

On slide 9, we present our results for pension and VGBL, the life and savings component, accumulation component in which case contributions totaled BRL89 million in the quarter, and reserves were at BRL3.4 billion at quarter-end. VGBL piece of the reserves alone increased 22.5% totaling BRL780 million at the end of the quarter.

Slide 10, addresses our investment management unit, and in this case notice that the quarter ended with almost BRL23 billion in assets under management, with close to BRL5.3 billion of net increase over 1Q '11, some BRL3.2 billion just in the First Quarter of this year.

You'll notice that the component is basically growing more faster is that relates to third-party funds with a 41.1% increase in the same period. The asset management business of this investment management business generated results of BRL7.3 million in this quarter with an increase of 33.5% over 1Q '11 which was kind of helped by higher AUM and an increase of the allocation of assets to funds that would charge a higher management fees as a whole.

Slide 11 speaks about G&A which increased 40 bps compared to 1Q '11 as a ratio to retained premiums. This is basically due to personnel expenses and third-party expenses in this case, mainly related to investments in IT.

Slide 12 comes back with the percent of the combined ratio with the Company ending the quarter with 101.1%. This increase was mainly due to the high loss ratio in auto, an increase in G&A, and then also the level of loss ratio as seen in health as we noticed in the previous slides.

Slide 13 discloses our investments allocation and strategy. The upper half of the slide refers to those assets that are not linked to Life and pensions, so that's a total BRL5.1 billion and then here we're following basically an (ALM) approach to define the strategy that is on the left.

To the right you see that the Company is -- those investments are highly concentrated in government securities, some 22% over corporate credits and some 2% in variable income equities -- the equities basically markets. The yield of the portfolio not related to Life and pensions was at 117.7% in the quarter which given its composition was a very good yield we think.

Slide 14, we're concluding this part of the presentation summarizing our net income figures that came to BRL113 million in the quarter, up 10.6% over 1Q '11. ROAE end of 1Q '12 at 15.7% with an improvement of 20 bps over 1Q '11.

With this I will conclude this part of the presentation, and together with Carlos Alberto Trindade and Gabriel Portella, I'll be glad to take your questions. Thank you.

Questions And Answers

Operator

Ladies and gentlemen. we will now begin the Q-and-A session. (Operator Instructions) Guilherme Assis, Raymond James.

Q - Guilherme Assis {BIO 16143141 <GO>}

I have one question. It's regarding the sales in the affinity plan segment for health care. I understand you have -- you guys have very strong relationship and partnership with Qualicorp, and what we saw over the last quarter, that Qualicorp has signed other partnerships, one with (Amilpar) and another one with Bradesco a little longer ago. I'd like to know if these partnerships with Qualicorp could in any way affect your growth in the affinity plan segment and how have you been doing this specific segment over the past few months? That's my question. Thank you.

A - Gabriel Portella {BIO 18012687 <GO>}

Guilherme, this is Gabriel. Let me answer your question. Firstly, I think you have mentioned that we have a strong relationship with Qualicorp and other big brokers related to affinity. For sure, Qualicorp, one of the first that taken advantage of this affinity market and growth tied with SulAmerica and that's why SulAmerica has a strong presence in this market.

Remember that since 2009 the regulation shows and attract to the market new players, operators or administrators as main off of the companies that administrate those business. There are more than 70 registered in the AMS as an administrator. The recent movements was expected since 2009.

They take too long to come to the market to compete in the affinity segment. We are well prepared. We have a strong relationship not only with Qualicorp, but within the entire brokerage market and that we don't see any major problem with the competition. Competition, as you know, we have in all line of our business.

Q - Guilherme Assis {BIO 16143141 <GO>}

Okay. Can you give some color on how is the growth performing this year in the segment, the affinity segment?

A - Gabriel Portella {BIO 18012687 <GO>}

It's included on the Group plans. The Group plan was growth -- our growth was 26%, and then we include affinity and all segments in those growths.

Q - Guilherme Assis {BIO 16143141 <GO>}

Could you say like if the affinity segment is growing in-line with the Group as a whole, with the Group segment as a whole or is there any difference?

A - Gabriel Portella {BIO 18012687 <GO>}

I can see that even though with the competition we still continue to grow new sales in the affinity and SME and the Group plan as a whole.

Q - Guilherme Assis {BIO 16143141 <GO>}

Okay. Thank you, Portella. Thank you very much.

A - Gabriel Portella {BIO 18012687 <GO>}

Thank you.

Operator

Marcelo Henriques, BTG Pactual.

Q - Marcelo Henriques {BIO 17385475 <GO>}

My question is more related to the ROE of the Company. I mean, we should expect the Second Quarter is also usually is a weak quarter for you guys as well. So once again this year you will be relying too much on the balance of the second half, on the results of the second half.

And if we do like a year-over-year comparison against the second half last year, interest rates should be roughly like 200 basis points, 250 basis points below the second-half of last year. So this means that loss ratio improvement and efficiency will be even more crucial this second-half as it was the second-half of last year, and the fact that you also retain more capital because now you're paying 30% dividend payout instead of 40%, how confident are you that you can keep at least the ROE that was achieved 2011 and how confident are you that in the second-half, you would have this important recovery so you can deliver better ROE than we are seeing right now?

A - Gabriel Portella {BIO 18012687 <GO>}

I guess overall, as you know, the second-half there's some advantageous for the loss ratio basically. And the improvement in the overall environment or the competitive environment given the conditions, especially those macroeconomic conditions, namely a reduction in the interest rates should foster a more rational competitive environment especially in automobile.

So first of all, the impact that we mentioned in our loss ratio in Auto should be diluted across the year as it is not a recurring event. Secondly, we believe that, as I mentioned, the competitive conditions should improve if the interest rate still maintains its downwards trend.

Health is also improving. Q2 usually benefits from an improvement in loss ratio. Q3 should see the new cycle, the new pricing, re-pricing cycle in effect, and Q4 has a positive seasonal behavior. So those factors should contribute to the improvement in the ROE for the Company as a whole in 2012.

We're maintaining the same level of excess capital that we had last year. So in this respect, this is not a factor that would maybe explain a change in the ROE. There's no -- say, no capital commitment nor any utilization foreseeable in the near term. So this is the way we're looking at the year from now on. I'm not sure if I covered all your points.

Q - Marcelo Henriques {BIO 17385475 <GO>}

I think you did. Now just like even if you consider the improvement in the second-half of the loss ratio, and I mean, I would expect that it should be even more of an improvement -- the improvement needs to be higher than it was the case in the second-half of 2011 which was pretty significant for you to compensate the lower interest rate, unless of course you continue to perform quite well on the financial results which is something that -- but I think -- but that's my basically doubt.

And since you are paying less dividends, shareholder's equity should increase more. That's why you hurt a little bit, not that much, but you hurt a little bit the ROE of the Company. So I was just wondering with this dynamics how you could post a similar ROE of 2011? I think that was my -- that's my doubt here.

A - Gabriel Portella {BIO 18012687 <GO>}

I guess we -- even if it's going to be possible, it's doable. We're reducing from 50% to 30% the payout.

We think it's advisable and sustainable as a policy without a term in itself. So if you remember the other part that was prevailing up until this year, we had a three-year plan we have announced and that would be for us for three years.

Now as we have announced 30% which is 20% higher than the minimum, we have not that much reduced. What are the conditions? The macroeconomic conditions, the regulatory environment, not a change, we should be in a position to maintain this level going forward.

There could be some capital requirements so some increase in capital requirements, (say of) 13 or 14 in case the insurance regulators were to finalize the regulation of those risk factors. They have not been dealt with yet and that would require more capital and that's one of the reasons we've been maintaining such a level of excess capital in the Company.

Q - Marcelo Henriques {BIO 17385475 <GO>}

Okay. Thank you. Thank you very much.

A - Gabriel Portella {BIO 18012687 <GO>}

Thank you.

A - Arthur Farme {BIO 1845065 <GO>}

Thank you.

Operator

(Operator Instructions) This concludes today's Question-and-Answer session. I would like to invite Mr. Farme to proceed with his closing statement. Please go ahead, sir.

A - Arthur Farme {BIO 1845065 <GO>}

Well thank you for those participating and the questions you've made which helped us in delivering better information for you. The Company is available here, the Investor Relations unit, as well as the whole of the management. Thank you. And we'll talk next time. Bye-bye.

Operator

That does conclude the SulAmerica's audio conference for today. Thank you very much for your participation and have a good day.