

Q4 2018 Earnings Call

Company Participants

- Fernando Passos, Brasil Resseguros S.A.
- Jos   Carlos Cardoso, Brasil Resseguros S.A.

Other Participants

- Mario Lucio Pierry, MD

Presentation

Operator

Good morning. Welcome to IRB Brasil RE Earnings Conference Call. Here with me today are Jos   Carlos Cardoso, CEO; Fernando Passos, Deputy CEO and Financial and Investor Relations Vice President; and Sandra Matsumoto, Investor Relations Manager. This conference call is being recorded. (Operator Instructions) This presentation was prepared by IRB Brasil RE and shall not be considered as source of data of investments.

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Mr. Jos   Carlos Cardoso, CEO of IRB-Brasil RE will now begin the presentation.

Jos   Carlos Cardoso

Good morning, everyone. And thank you for participating in our earnings conference call relative to the Fourth Quarter and the fiscal year of 2018. We have been a publicly held company for over a year now. Actually, our IPO was held in July 2017 and our share gained the most value in 2018 among the companies in the IBrX 100 index of the 100 most

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actively traded and best representative stocks of the Brazilian stock market. Remembering early last year, IRB shares were quoted at BRL 32 and end 2018 at BRL 83, an impressive increase of 157%. Our market cap grew from BRL 10 billion in December 2017 to BRL 26 billion by the end of 2018. The delivery of these robust results for the eighth quarter in a row proves how resilient our performance is, even in a challenging scenarios. As you know, Brazil experienced low economic growth in 2018 with a estimated GDP rise of 1.3% only. But even in this less favorable scenario, our written premium rose 20% achieving BRL 7 billion in 2018. The market expects to see a more positive business environment in 2019, with the economy and the industry growing at a faster pace. So far in 2019, the industry activity points to a stronger rebound over the year, providing a basis for our perspective of employment in our businesses. More than positive expectations, we believe that our ability to anticipate the economy's moves, positioning our company to serve our clients in a distinguished manner. We are a key player in Brazil's reinsurance industry, market leaders and one of the top world's 10 reinsurers. Such a position inviting us to develop products and services that enable our prominence, making us the preferred choice for the clients. Therefore, technology and innovation are priority trends for our investments in efficiency gains.

As an example, one milestone on this area was the Innovation Day that was held in September 2018, with the goal of expanding even further the discussion of this key theme for the future of our business. The event was held in Rio de Janeiro and included starts-up accreditation, cocreation sessions and fresh talks with the top market professionals, in addition to connecting our employees through largest training. It reflects our commitment to renovate our business every day and to using digital and technological evolution as an analyze for meeting the needs of our clients.

Our extended result curve shows this is the right strategy. We are once more restructuring teams and investing in the best use of information technology because we believe talent and motivated people and innovation are the key for us to become more and more efficient, focused in value creation, which has been the core of our strategy since we joined the company. Efficiency and results are clearly the commitment we have been making to our stakeholders.

And this is not the end. We understand that our role within society is very important and goes beyond of this. Through our own initiatives and partnership with different institutions, we strive for improving several aspects of life in our society, developing responsible bonds with the world we live in and the people we engage with. We are proud to say that in the social front, we strive for promoting education, the health and quality of life of society in general. These initiatives are jointly worked with our employees and their respective families creating a feeling of commitment, dedication and belonging, thus enabling the fulfillment of the company's goals.

Now I would like to briefly comment on some of our highlights for the period, which Fernando will discuss in more details later. In 2018, we kept our growth history. We posted a growth -- in our written premium of 34% in the Fourth Quarter of 2018 and 20% for the full year of 2018. Our written premium in Brazil grew by 38% in the Fourth Quarter of 2018. Our written premium abroad also posted a growth of 29% in the same period, which confirms our right strategy of expanding our business abroad for the past few years.

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The underwriting result achieved BRL 358 million in the Fourth Quarter of 2018 and the financial results totaled BRL 145 million for the same period. In 2018, we continued to focus on increase in efficiency. In the Fourth Quarter of 2018, our administrative expenses as a percentage of the earned premium was only 4.1%, in line with the ratio reported for the Fourth Quarter of 2017. For the full year of 2018, the administrative expense ratio was 4.8%. Our net income for the Fourth Quarter of 2018 increased by 50%, achieving BRL 373 million. For the full year of 2018, net income reached an impressive BRL 1.2 billion, performing our initial goal of reaching a net income of BRL 1 billion, in line, as you remember, with our campaign we are all One Global Citizen. With this campaign, the entire company get together as a one single team to outperform such goal. Our shareholders should receive dividend and interest on capital of over BRL 800 million, or 75% of our reported net income for 2018. Please note that these proposed amounts will be submitted for the approval by the Shareholders' Meeting to be held in March this year.

Finally, I close this slide stating we believe the results for 2018 in line within our guidance for the same indications we estimated for the year. Our guidance was revised in October 2018.

Fernando will now continue this presentation with more details on our results. I will be available to answer your questions later. Fernando, please.

Fernando Passos {BIO 20117537 <GO>}

Thank you, Cardoso. Good morning, everyone. I will begin the presentation on the Slide #3. Here, you can see our net income and the return on average equity. The orange graph to the left shows our net income increased by 49% from BRL 249 million in the Fourth Quarter of 2017 to BRL 373 million in the Fourth Quarter of 2018. The return on average equity was 40% in the Fourth Quarter of 2018, an increase of 11percentage points compared to the Fourth Quarter of 2017.

On the following slides, I will discuss the factor that drove the growth in the Fourth Quarter. On Slide #4, we show the history of our overall written premium by quarter. In the First Quarter of 2018, our written premium increased by 34% year-over-year, achieving BRL 1.7 billion, of which BRL 978 million were written premium in Brazil and BRL 703 million were written premium abroad. In the First Quarter of 2018, written premium in Brazil increased by 38% over the Fourth Quarter of 2017. This growth was due to our market share expansion in Brazil and also to the local markets growth. As the written premium abroad, the growth was only 29% in the Fourth Quarter of 2018. As Cardoso has already mentioned, the growth of our written premium abroad confirms our right expertise of expanding our business abroad for the past few years.

On Slide #5, we will talk about the dynamics of our retrocession cost. Our retrocession ratio was 36% in the Fourth Quarter of 2018, a reduction of 2percentage points compared to the 38% ratio reported in the Fourth Quarter of 2017, reflecting better negotiation and operating conditions proving our track record of a low loss ratio. Also, in addition to the reduction in the retrocession cost, we also had better operational terms as an example of the proper preparation with a reduction of our current maximum loss from \$20 million to a maximum loss of \$10 million.

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The Slide #6 shows our overall retained premium, which increased by 38% from BRL 783 million in the Fourth Quarter of 2017 to BRL 1.1 billion in the Fourth Quarter of 2018. This growth is driven by the expansion in written premium and the reduction in the retrocession ratio.

On Slide #7, the graph shows the historical constitution and reversal of the technical provisions were achieved through written premium. Historically, as you can see in 2015, in 2016 and also in 2017, the provisions were constituted in the first 3 quarters of the year, followed by a reversal in the Fourth Quarter of the year. I will mention that in previous quarters, over the policies' coverage term, depending on the performance of the business and the term of the risk to expire, this provision may be taken to earned premium and then, consequently, to the underwriting result, which is what happened in the Fourth Quarter of 2018 as we illustrated in the graph.

Now on Slide 8, you can see that our earned premium increased by 44% from BRL 993 million in the Fourth Quarter of 2017 to BRL 1.4 billion in the Fourth Quarter of 2018.

On Slide 9, you can see our loss ratio performance. Our loss ratio went up from 53% in the Fourth Quarter of 2017 to 57% in the Fourth Quarter of 2018. This increase of 4percentage points was driven by the addition of new contracts in the quarter followed by the increase in the constitution of the IBNR reserves. As you know, the retained claims income has 2 main items: the OCR, outstanding claims reserve, which reflects the claims effectively reported in the period; and the IBNR, incurred but not reported reserve, which is an actuarial reserve based on statistics to prevent future claim reports.

In the Fourth Quarter of 2018, the loss ratio measured by OCR, which reflects the claims reported in the period as I mentioned, corresponded to 46% of the earned premium, a reduction of 2percentage points compared to the 48% reported in the Fourth Quarter of 2017. On the other hand, the loss ratio measured by IBNR, which is a statistical provision of the management, corresponded to 14% of the earned premium in the Fourth Quarter of 2018, an increase of 7percentage points compared to the Fourth Quarter of 2017. In nominal terms, IBNR went from a net addition of BRL 65 million in the Fourth Quarter of 2017 to a net addition of BRL 196 million in the Fourth Quarter of 2018. This increase in the quarter, both in percentage and in nominal terms, has a main driver higher premiums in the period, since new contracts account for the IBNR on an aggregated basis.

For the fiscal year of 2018, the loss ratio went from 59% in 2017 to 56% in 2018, a reduction of 3percentage points year-over-year. This reduction is due to the lower loss ratio measured by OCR, which corresponded to 48% of earned premium. The loss ratio measured by the IBNR remained fairly stable around 9% in the fiscal year of 2018 compared to the reported in 2017.

On Slide 10, we talk about our underwriting results. The underwriting results achieved BRL 358 million, an increase of 37% in the Fourth Quarter of 2018 compared to the same period of the last year. For the fiscal year of 2018, the underwriting results achieved BRL 1.2 billion, an increase of 43% compared to the fiscal year of 2017. The combined effect of

growth in written premium and improvement in our loss ratio was the key driver to the robust drive in our underwriting results.

Slide 11 shows our administrative expense as a percentage of earned premium was 4.1% in the Fourth Quarter of 2018, fairly in line with the Fourth Quarter of 2017. In the fiscal year, the administrative expense ratio went from 5.5% in 2017 to 4.8% in 2018. This reduction was in line with our guidance reported for the fiscal year of 2018, which projected the ratio between 4.8% and 5.2%. Such performance confirms our management's commitment to increase efficiency and improve our profitability.

The Slide 12 shows the performance of our financial and real estate investment. Our consolidated financial investment achieved BRL 135 million in the Fourth Quarter of 2018 versus BRL 155 million reported for the Fourth Quarter of 2017. The consolidated performance in reals of the management of the financial assets of the parent company and subsidiaries and branches was 139% of the CDI in the Fourth Quarter of 2018 versus 128% of the CDI in the Fourth Quarter of 2017, an improvement of 11percentage points.

In the Fourth Quarter of 2018, the fixed income investment fund denominated IRB Brazil Absoluto, managed by IRB, had total assets, excluding the government bonds, of BRL 2.8 billion, corresponding to 42% of our financial assets portfolio. In the period, the fund's profitability was 252% of CDI. In the fiscal year of 2018, the profitability of the IRB Absoluto was 124% of the CDI. I would like to highlight that the investors can see the performance of the IRB Absoluto on a daily basis in the Bloomberg system.

Our own portfolio had assets amounting to BRL 3.8 billion at the end of 2018. And the most important asset group was the fixed government bonds. The average daily balance of the financial investment portfolio, excluding the real estate portfolio, was around BRL 6 billion for the fiscal year of 2018. Our consolidated financial investments achieved BRL 629 million in the fiscal year of 2018. The consolidated performance in reals of the management of financial assets of the parent company and subsidiaries and branches was 141% of the CDI for the fiscal year of 2018 versus 131% of the CDI posted in 2017, an improvement of 10percentage points.

The graph to the right shows the breakdown of our portfolio by the end of December. Most of portfolio remains allocated to fixed income.

Before I close this presentation, I want to discuss our expectations on Slide #3 (sic) (13), that is our guidance for the full year of 2019 according to the material fact we disclosed to the market yesterday. We expect a growth of 17% to 24% in our written premium in 2019 compared to 2018. We also estimate an extended combined ratio ranging from 69% to 73%, in line with the guidance disclosed in 2018. Regarding our administrative efficiency, we expect to report an administrative expense as a ratio of earned premium ranging from 4.6% to 5.2%.

And now Cardoso will make his closing remarks. Cardoso, please?

José Carlos Cardoso

Thank you, Fernando. Well I would like to thank you once again for your interest in our company. We are extremely proud of the results achieved in 2018 and confident that, in 2019, with our hard work and dedication, we'll once again exceed our goals. The company has already prepared itself to capture the positive expectations that are foreseen for the market's current scenario in 2019, which will allow us to position ourselves differently. The next few cycles of both 2019 and 2020 are already starting with a solid foundation built to date and pave the way for an even greater growth. In the year that IRB completes eight years of its foundation, I remain committed to the management of the company, always focusing on generating value, on efficiency, on the sustainability of our results and promoting social inclusion.

And now I'll close our presentation. And we open for questions and answers. Thank you very much.

Questions And Answers

Operator

(Operator Instructions) Our first question comes from Mario Pierry from Bank of America.

Q - Mario Lucio Pierry {BIO 1505554 <GO>}

I am going to ask you 2 questions. The first one is related to your premium growth guidance that you're providing us, 17% to 24%. If you can -- I was thinking of a breakdown of what you are expecting to grow in Brazil or in the international? Also rates guidance is relatively stable or -- the midpoint of your guidance is stable with what you posted in 2018. So I'm trying to understand why it will be higher? If you can provide to us some of the macro forecasts that you have behind your guidance as well related to Selic rates and also to GDP growth. So that's the first question. Second question is related to your ability to continue to gain market share and premium. Given that you are running already I think about 45% market share, you have an ROE of about 40%. How competitive do you think this industry is going to get in Brazil or maybe there are enough barriers that we won't see that many new entrants being aggressive? Also, as part of this question, if you could talk about your capital position and your ability to grow -- to continue to grow at this fast pace and maintain the 75% payout ratio?

A - Fernando Passos {BIO 20117537 <GO>}

(technical difficulty)

written premium growth and Cardoso will talk a little bit about market share. In general terms, reinsurance is linked with the GDP growth, especially when we talk about the part of GDP linked to the investment and also the part of GDP linked to the price of the real estate market, okay? In general terms, we're seeing the premium growth in Brazil in a level much higher than the historical level of the last four years. So we're seeing the premium in Brazil growing faster than during the last years. Of course, we have also seen some risk involved with the macroeconomic overview, especially linked to the pension

plan reforms. So we think our guidance in general terms reflects an (upward lead) of the (country's) GDP growth. But also can be linked to the approval of the pension plan reforms and other important reforms that we have to implement here in Brazil. Now Cardoso will talk a little bit about the market share.

A - JosÃ© Carlos Cardoso

Mario, thanks for participating in this call. Well first of all I believe it's important to mention that market share for us is a consequence, it's not our target. Our target has been to provide good results, to bring good results for the company to our investors. However, to do this, it's necessary to provide a high quality of services to the insurance community. And we will use one of our strong points. Remember that IRB is one of the few reinsurers in South America, in Latin America, that operate in all lines of business. These start to become to be one of our differentiation in comparison to our peers. Then bearing this in mind, future entrants here will create a new model of -- to do reinsurance, to provide reinsurance. Our -- this model means that we do not provide a capacity in the reinsurance line per line, this is something that is over. When providing capacity we have to provide a full range of capacity for all lines of business. And this has been truly well accepted by our clients because in one stop, they can buy all types of reinsurance they need. In addition to that, we arbitrage because it's quite natural that in one company, they have some lines that are performing well which are extremely attractive for the whole reinsurance companies. And there are other lines that are not very attractive, they're losing money, that -- which ones are rejected by their insurance company. In our case, we provide a full package for all lines. I mean for good lines and for bad lines. And when we provide the capacity for these lines that are performing below what we expect, we complement our service, providing them training, showing them where they are losing money, providing them guidelines, a full range of services that is going to help them to sort out the problem and to bring good lines of business to the profession to get stability again. Therefore, with all of these actions, we have seen that the clients are starting to approaching us in a very different way. They really are searching for us in order to build this full achievement from our side. It's not only capacity, it's much more service. And we think that while providing services, we are honestly speaking, we have become more invisible because we have been key team in property, engineering, agriculture, rice, aviation. And to look at the ramp of the market, they don't have full dedicated team for each and every line. Therefore, with all of these range of services and products because we know we are the only ones developing new products here in Brazil, products extremely adapted to the Brazilian needs, to the South American needs. We are the only one that can provide it quickly because the team is there, underwriters, the experts, the all of them are located here. These make an addition. This is why the gain in our market share has been gradual and a natural consequence of the service, the parts of service that we have been providing to the market. Fernando, if you can...

A - Fernando Passos {BIO 20117537 <GO>}

Mario, talking a little bit about the dividend payout ratio, in general terms, we have around BRL 3.5 billion in regulatory capital. And the required capital for the company according to the Solvency II rules is only around BRL 900 million. So we have almost 5x the required capital. It is enough to sustain our dividend payout of 75% according to our capital plan for a long period and also sustain the growth perspective of the company. So we don't see any change in our dividend payout in a short time.

Operator

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

A - Jos   Carlos Cardoso

Thank you, all once again for trust in our company. I count on your presence at our earnings conference call for the First Quarter of 2019 scheduled for early May 2019. Thank you very much. Have a nice weekend.

Operator

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

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