Y 2012 Earnings Call

Company Participants

- Arthur Farme D'Amoed Neto, Executive Vice President of Control and Investor Relations
- Beto Trindade, Auto VP
- Eduardo Dal Ri, Vice President
- Gabriel Portela, Health VP
- Marcelo Mello, Investment VP
- Mauricio Lopes, Vice President
- Thomaz de Menezes, Chief Executive Officer
- Unidentified Speaker

Other Participants

- Eduardo Nishio, Analyst
- Marcelo Henriques, Analyst
- Rafael Frade, Analyst
- Unidentified Participant

Presentation

Operator

Good morning and thank you for standing by. Welcome to Sul America Conference Call to announce the results referring to the fourth quarter of 2012. Today with us we have, Mr. Thomaz Menezes, CEO; Arthur Farme, Controller VP and IRO, Mr. Gabriel Portella; Health and Dental VP, Mr. Carlos Alberto Trindade; Auto, Property and Casualty VP, Mr. Renato Terje [ph] Life and Pension VP; Mr. Marcelo Mello, Investment VP and Mr. Matias de Avila, Commercial VP.

We inform that this event is being recorded and all participants will be connected in listen-only mode during the presentation of the company. Next we are going to start a questions-and=answers session when further instructions will be provided. (Operator Instructions) A replay facility of this event will be available right after it ends for one week.

We are also going to have a live webcast with audio and slides, which can be accessed in the company's Investor Relations website at www.sulamerica.com.br/ri in the banner Webcast 4Q12 [ph]. The presentation will also be available for download from the webcast platform.

Before proceeding, we would like to clarify that statements made during this conference call pertaining to the business prospects for Sul America, operational and financial projections and targets, our beliefs and assumptions of the company's management and they are based on information currently available.

Forward-looking statements are not guarantee of performance. They involve risks, uncertainties and assumptions because they refer to future events and therefore they depend on circumstances that may or may not happen. Investors should understand that general economic conditions, industry conditions and non-operational factors may affect the future performance of Sul America that may lead to the results that are materially different from those expressed in such forward-looking statements.

Now I would like to turn over to Mr. Thomaz de Menezes, CEO who is going to start the presentation. Please, Mr. Menezes, you may start.

Thomaz de Menezes {BIO 16674464 <GO>}

Good morning, everyone, thank you very much for your participation. Before starting the call, I would like to highlight and invite you to the conference call we are going to have -- right afterwards, we are going to about the material effect that has just been published and we are going to open for questions and answers right after.

(inaudible) and the number for access will be the same as used by you in this call. During this call, we will be talking about the fourth quarter results and also for the year of 2012. The VPs here with me are Mr. Arthur Farme, IRO and Controller. We also have here with us the VPs, Gabriel Portella, Health and Dental; Carlos Infante Santos, VP and Property and Casualty and Renato Terje, Life and Pension and Marcelo Mello, Investment VP; in addition to, our Commercial VP, Matias de Avila and some other officers.

I would like you to look at slide number two so for us to see the main highlights of the year where company has had a very good performance in the fourth, which has greatly contributed to the great results of the year. 2012 was a special year because we were successful in reacting to the challenges that were posed to us and there were many.

For example, the global macroeconomic environment, which was weak and its consequences on the domestic Brazilian market. The reduction of interest rates faster and further than we had expected thereby, in fact, affecting our financial income, the high loss ratio and the higher use of our services and the environment that that was strongly competitive in auto insurance in addition to the reduction of cost of quality were important because it went down in 2012 then we eliminated it completely earlier this year, therefore, we have kept our path of growth with explicit volumes in our operations.

The growth in premiums (inaudible) has reached 12.5% in the year, which means a net reduction of R$1.2 billion of new premiums. The highlight was the increase of 17.8% in health and dental plan.

And therefore, the company was practically stable, if we compare year-on-year, which was good for us, considering the challenges that I have just mentioned.

In terms of financial income, in spite of a lower SELIC -- average SELIC, it was better than0 we expected, but, of course, we did not reach the same result that we had in 2011. But in terms of yield, we have had a return of 128.5 of the CDI and 114.1% of the CDI in the year. It's an important result driven by the good performance of our share portfolio. Our combined ratio also was better by 0.6 percentage points compared to 2011. In this manner, our net income went up 7.8%, which too was a very good result in a year with so many challenges.

Now, I turn it over to Arthur Farme to give you more details about the results for three years, and next, as usual, we are going to open for questions and answers. Arthur?

Arthur Farme D'Amoed Neto

Thank you so much. Good morning, everyone. We are going to start on slide number three, talking about health and dental. I think that before the numbers on the slide, we invested heavily in operations. There were many premiums focusing on controlling the loss ratio and risk and we also worked with our hospital network, selection of providers and we were more careful also in terms of logistics of this segment.

And so we, the management, think that these results are very good for the year of 2012. So, I think that our project insurance premiums grew 17.8%. We have added a significant share of new members, almost 100 -- 1000 new members who are included in our portfolio with a net profit -- with a net excess -- sorry, or some productivity in terms of policy that we have added during the year. And we have had very positive results. Obviously, everything that happened in health represents almost 70% of our revenue and this will really affect our consolidated results and that's why the company has had a very good performance, not just on the fourth quarter that we are focusing on, but in the whole of the year. We have a growth of slightly more than 17% in the fourth quarter. And then after everything we began year as a whole, we have had really very good growth in loss ratio.

It's interesting to show that because there is an effect of seasonality, we have seen this over the past years' fourth quarter again for different reasons has a budgetaries smaller than in other quarters. If we compare year-on-year, however, the numbers are practically the same, which -- in terms of frequency of utilization that were under pressure, we think that this is a good result and it's getting better in line with the next premium that we mentioned in the beginning and the margins were a consequence of the loss ratio because there is a risk in terms of -- that were significant, but we didn't really change our policy.

I think that we should -- we didn't mention yet so far, but we are seeing on the bars, the contribution of dental plans that a portfolio of dental plans grew considerably and has provided a positive contribution to our operations with important synergies, with the whole brand of the company, because we didn't yet have dental care and that it provides many very good opportunities in terms of offering dental cares in the new contracts. The brokers working with us more and more know about this opportunity and our offerings to our customers. And in the -- we are consolidating this dental segment. We should expect more in the future.

And now I am going to go through slide number four, talking about outlook. I think that throughout the year, we still have company dollar costs. I think the market in general, I would say, that the competition had a -- not a very rational behavior, especially, when comparing it with the context with the macro-economic context. There was a change in behavior and pricing directed through the margins and this was done earlier on. And the basic interest rates and all the sort of flow we have and everything dropped faster than the estimated average and the industry was positioned in terms of price due to the losses they were having in volume of reais in their own portfolios. In the fourth quarter, regarding the composition that compared to last year, we grew 3% year against year. This is what the market has indicated according to our policy to privilege results in the recovery of loss ratio, which is at the right-hand side on the top, we see a drop in the fourth quarter, as of the highest figure we had in the beginning of the year.

And this just confirms the trends that we had anticipated in which at the beginning of the quarter, we used the characteristic of the competitive environment both enabling this price composition and adequate adjustments, so they could be practiced in that year, we closed better than last year, especially due to the behavior of the fourth quarter, we can anticipate 2013 with better results in terms of volume and premiums and also due to the loss ratio behavior.

The margin, the gross margin, once again, is a consequence of the loss ratios and our sales policy in the case of (inaudible) there were a marginal improvement due to changes implemented and how we present the business to our customers in a positive way to achieve this margin.

Regarding the fleet, there is a slight drop more in the semester, than in the year, showing that the fourth quarter has shown some recovery anticipating like I said before, the beginning of 2013, with a better result regarding the average of 2012.

Now, if we go to other property and casualty, the next slide, when we compare the quarter, there was a drop of more than 20%. This was due to the replacement policy. This is a little bit different from what we had last year. In this segment, many products did not participate in this and the transportation segment like marine as a whole and all the other segments that comprise the portfolio. Regarding the Massified, we had exceptional gains because we have brokers and buyers that work faster and we were able to have the growth in the portfolio. Our basis also regarding Auto that was important for the sales and this has positively contributed to the Massified segment and we were able to work well with these companies. We were more selective in the pricing policy. (Technical Difficulty). Obviously, the figures are very stable due to our operational efficiency in the market and I would like to highlight the fact that in 2012 we did not have an offer due to the contracts of service rendering that we couldn't have in 2011. And we kept assets at these levels and this represents an effort of the company so as to control its admin expenses in order to try to be competitive where it wants to be competitive more precisely in its relationship with brokers.

Now, on slide number 10, now we can see the combined ratio and because of loss ratio and also because of the improvement in our distribution policy and there is a slide -- and the next slide, it's about our investment strategy. And the top part you can see the funds that are not associated to the pension, the ex-pension [ph] and VGBL and the total portfolio below.

We also have a portfolio that is widely focused on fixed income and we have increased in 2012 significantly our -- the share yields equity, but the entire strategy and our location is fundamentally related to our policy of high yield. So the original guidance of our investment policy is precisely of a protection of assets -- of our partners in 2012. We've reformulated our investment policy and that we used in our company and we have also strengthened the relationship that we have with the manager that is part of our holding and the result of 114% of the CDI in the year is a very good result, especially for the type of growth that we've been having and what we do in our investments.

In real terms, we were expecting a smaller number especially because of our exposures, there is some possibility of pre-position, but this is something to compare more closely now in 2013 and 2012 and the distribution was basically what we had. In this manner, we end our presentation with the main things we wanted to mention to you in the first part of the conversation and now we are available for the Q&A session. Thank you all very much.

Unidentified Speaker

Thank you, Arthur. I would like to compliment the financial results of the company with some important piece of information. In 2012, we have invested heavily in operating efficiency, in IT and also in the improvement of systems that will help us to support, the growth of it is yet to come. We have restructured different areas in the company. We improved even further our processes, operating platforms, management systems, applications that provide support to businesses. We have new products and services. We have increased our physical expense and we have reached a brand of more than 100 units spread throughout the country.

We have also dealt with lots of serenity with the new regulation demands. We have delivered excellent results and especially, we kept the capacity of engaging people towards a common objective, which is to grow with profitability, controlling costs and seeking the best financial profitability within our risk policies. I would like to take the chance to thank everyone that was listening -- all of you listening to us. Since there is a large number of employees listening to our call, we would like to thank you all for participation, involvement and engagement.

Our company is made of people and it is in our DNA to have the commitment of more than 4,600 employees and also, the message to all investors, partners, and employees that we remain optimistic in terms of the prospects for the insurance, pension investment market and we are confident with the company's growth strategy for the next year.

Thank you very much for your attention and now we are open for questions and answers.

Questions And Answers

Operator

Thank you. Now we are going to start our Q&A session. (Operator Instructions) Now, our first question comes from Goldman Sachs.

Q - Unidentified Participant

Good morning, gentlemen. Thank you for -- congratulations on the strong results in the quarter. I have one question related to your performance. What can you tell us about the expenses with tax and the likelihood of recurrence and also in terms of personal insurance, so how it's been growing except for the recurring items?

A - Arthur Farme D'Amoed Neto

Thank you very much. So we have had an adjustment, which we've provisioned for lawsuit for the company to comply with IFRS. We were expecting now for kid we had a risk of variable income and that was possible and according to auditors, we have adjusted to IFRS and that has had a positive impact in some alliance and a negative impact on underlying. So that's why you see that variation in the income tax. And your other question about the size of our reserves in terms of life is about R$60 million, it's the reversal that we have had. Last year, we had an increase in about R$110 million, R$120 million built provisions and this year we have had the reversal, we adjusted our provision.

Q - Unidentified Participant

Okay, thank you very much. And then I will get back to you for more details. Now, in Health, there was really a very good improvement. Could you give us more details about what was seasonal, the recurrent factors and your forecast in terms of the recurring parts in terms of loss ratio in those lines since it is very heavily seasonal. So what should expect for this year and next year in terms of your forecast for a loss ratio in health?

A - Unidentified Speaker

I am going to ask Gabriel Portela, our Health VP, to answer your question with more details.

A - Gabriel Portela

Can you hear me?

A - Unidentified Speaker

Yes, you can answer.

A - Gabriel Portela

If we analyze the frequency and the average cost at the end of the year, we had a drastic drop. All the measures that we took from the first quarter on, in terms of costs, we were talking about the revenue, reflected not only in the increase of costs, but also in the frequency of use. I think that this year, we were able to practice all the measures that we had in place to revert the strength that we had in the second quarter, so that at the end of the year, we could get to the right figures.

Basically, our methodology, the reserves depend on these measures, and at the end of the year, as I said, the seasonality is more favorable. We got to the end of the year in a much better condition than in previous years, with very positive trends. And this is the good meaning of the word with a better balance. And throughout the year, all our actions in risk managements have given positive results, not only positive results, but also due to the speed that we were able to carry them out.

Q - Unidentified Participant

Gabriel, if you could highlight. I think that you have a target, right, regarding the loss ratio. So there is an interval of 67, 81 [ph]. Is there any target for 2013 and 2014 in which you expect that the health loss ratio will be affected?

A - Gabriel Portela

I don't know if I heard your question well, but, anyway, I'll try to answer that. I think the interval that you mentioned and the behavior of the portfolio, it has a lower level than that of the dental area, but in terms of the individual ones composed with the group ones and the interval that you mentioned, I think is adequate.

Q - Unidentified Participant

Thank you.

Operator

Our next question comes from Mr. Marcelo Henriques from BTG Pactual. Sir, you can ask your question.

Q - Marcelo Henriques {BIO 17385475 <GO>}

Good morning. I have two questions. One is a follow-up to better understand the basis of 2012 and generalizing [ph] 2013, it is the variability of the gross margin that you have. It's approximately R$360 million, 70, 80 points of this gross margin variation. I think it's R$100 million less. And the variation of the technical provision in 2011 was less. 2012 was another 30, so approximately 200. And this variation of the premium explains your gross margin. I'm asking this because I would like to better understand this technical provision and also in the part of people, so I would like to know what has been happening in the previous years, 300, 400.

I just want to understand the basis for 2013, understanding there is some volatility. If we can take 2012 as the recurrent margin or what happened in 2011 could be considered as recurrent?

A - Arthur Farme D'Amoed Neto

I might not have all the details here, but in general, the Auto did not grow so much. If you see the part of Health and this movement that you've just noticed and asked about, I think that when we compare the previous year with the current year, part of this comes from the auto behavior. Marginally, we have the impact of the legal issues and this affected the results as a whole.

Without going into further details here, later on we can give you these details regarding the Auto behavior. As you saw it did not grow so much. We had a lower impact. I thought there would be a faster growth in terms of that and also that was the expectation and this would generate more variability. All the segments, Auto and the other risks, as we get back to our normal speed at 24% in two years, a little bit more than that. We will see the effects that you highlighted working in the opposite way. But we can see any kind of movement that would be very significant in relation to life now.

Q - Marcelo Henriques {BIO 17385475 <GO>}

And I have a follow-up question. Can you give us any consensus for life in 2013? Is it for 450 million, 460 million? So there is a drop in the group insurance throughout time, but for 2013, are there any expectations of increase of our ROI as compared to 2012 due to all the trends that you have been analyzing for 2013, will it be kept at this level? Or should we expect any kind of decrease or increase for that?

A - Arthur Farme D'Amoed Neto

At this moment, the expectation is to maintain it. I don't know what would be the final net profit. It depends on the interest rate range and how prices will behave for autos. We will continue to collect the results from our attitude in terms of claims. I think we will be less conditioned to competition and we will have space to adjust premiums. But it's important that we will have an important contribution from the claim management and health. Regarding auto, if we do have space in the first weeks or months, we might have better results than what we are anticipating right now.

I cannot ensure that we will have higher profits than we had in 2012. But this should not be seen as any surprise. Some of you know that, but especially due to the way that the financial results have with insurers. And the other element of the situation is our tax level and the administrative expenses, we did all the investments necessary to work on the infrastructure of the company. But we want to maintain our yield at the appropriate levels. And this due to the environment we've been living in. I said something [ph] not to tell you really -- not to address the profit that you mentioned, I don't want to ensure extraordinary profits in relation to the risks we have in 2012.

Q - Marcelo Henriques {BIO 17385475 <GO>}

Okay, thank you. Just one last question. Well, the performance was really exceptional and there is a flow for capture. Are you seeing like this year or last year? And do you think you will be able to keep your asset results at the same speed as in 2013?

A - Arthur Farme D'Amoed Neto

I am going to ask Marcelo Mello to answer your question. But I would like to emphasize that assets are part of our growth strategy. I think that this 15 [ph] history of asset management has proven to be a right strategy and we have high expectations for the contribution of asset management not just part of our portfolio, but also in terms of the management of third party portfolios and according to what Marcelo has established. Marcelo?

A - Marcelo Mello {BIO 21963995 <GO>}

Thank you for your question. As Arthur said, about asset management what we've been doing a long time, we have been giving more and more resources to this company. And it's very clear, especially in terms of our performance and what we can expect for 2013 is a continuing growth. Like we saw this year, we've seen investors increasing their allocation in stock market.

As our position is quite competitive with compared to the market, I think that we can believe that customers will increase their allocations. So we also need to take into account that as we grow and we increase our market share, the contribution of the business will have a more significant contribution to the whole of the operation. So what we should expect is a positive scenario, but slightly more volatile in terms of scenario because the volume that we charge its performance has been increasing.

I think that we should highlight that SulAmerica Investimentos has a customer of portfolio that is very much concentrated on a given segment that was very positive. This is a segment that has a goal that is way above what is paid and they are naturally investors of SulAmerica Investimentos and they make their allocations and we get to sell other products to them.

Q - Unidentified Participant

Thank you very much for your answer.

Operator

Our next question comes from Mr. Eduardo Nishio from Brasil Plural. You may proceed.

Q - Eduardo Nishio {BIO 15333200 <GO>}

Good morning, everyone, thank you very much for the opportunity. I had joined the call slightly late. I would like to understand the transaction of the company in terms of changing in (inaudible) what did you change?

A - Marcelo Mello {BIO 21963995 <GO>}

The transaction between the family and ING. This is Marcelo. We made an announcement in the beginning of the call. We are going to address this issue right after this call and you can use the same number, if you don't mind. Thank you very much.

Operator

Our next question comes from Mr. Rafael Frade from Bradesco. You may proceed.

Q - Rafael Frade {BIO 16621076 <GO>}

Good morning, everyone. I would just like to go back to health, as Gabriel could comment looking into 2013, 2012, we saw the performance more or less in terms of the price adjustment that you have in middle of the year contributed to an improvement making in loss ratio. But last year, you were caught by surprise in terms of your adjustments by the medical inflation and I think you talked a lot about all your claim management measures that you've been implementing.

But if you could give us more or less scenario within the medical inflation going up in a generalized way, and so what's your perception, the adjustments that you made in 2012 and the other changes that you implemented, should they complement for us not to see such a sharp change of performance in different quarters as we saw in 2012?

And the second question, could Portela, please tell us about the competition scenario in automobile? So you said that you're focused on profitability and the competitors on the market as a whole. Could you give us an update? Do you still see the market like that or are there competitors that are slightly more aggressive? Could you give us your opinion?

A - Unidentified Speaker

Well, first I'll let Portela talk about health and then we'll talk about auto.

A - Gabriel Portela

Hi, again. Can you hear me well? I think that we had two main directions, new sales and revenues and we had a lot of presence and lots of synergies in the work with brokers, and we have new customers.

In terms of the fee, we sold more than in previous years and we are also having different prices and we tried to reach a balance in loss ratio. We had new policies and we had a recovery with the adjustment, even though we tried.

In terms of the revenue, as you've seen, we have other measurements that contributed positively. On the side of cost, some actions that we implemented, but they were more directed to materials and medication and the other ones we're focused the most on. And I think that the one that provided the greatest benefit in terms of cost, as we already have a lot to do in this area when we have positive expectations, we have a great opportunity in terms of having improvements. So in a nutshell, the trend is for us to control costs and we compare that to the general scenario. And in terms of specific actions that we are implementing so as to manage, but also to offset the ascending curve of the average cost that we see in our portfolio.

The scenario is not really positive in terms of the market, but it is positive for Sul America because of the more intense actions that we have been implementing, not just in terms of claim management, but also we have had health management actions that we really increased in 2012, our actions towards case management and other actions. So we've taken several measures in addition to other specific measures to reduce loss ratio.

Q - Rafael Frade {BIO 16621076 <GO>}

Just a follow-up. You see these prospects in terms of the whole market, do you think that the market will continue to have a need of high adjustments in 2013 and do you agree with that?

A - Gabriel Portela

I think that we still do not have a position. It's not just based on past experience, but also future expectations for the medical and health industry. And this will affect adjustments. Of course, we are expecting to continue having such strong products that we were able to offer last year. And considering the results, we have expectations of increasing costs in 2013.

Q - Rafael Frade {BIO 16621076 <GO>}

Thank you.

A - Mauricio Lopes {BIO 21675846 <GO>}

Before turning it over to Beto to talk about auto, just one point in terms of illustrating what our expectations for 2013. What we saw last year is the acceleration of inflation that we corrected through pricing in 2012. We identified the actions in terms of claim management and what we've been seeing is a stabilization in these rates, which may provide us some relief in a cycle that is going to start in the second half of 2013. So you're still going to see pressures, but we are still going to see some seasonality, but less than last year. So now, Beto, could you talk about competition in the auto segment?

A - Beto Trindade

Thank you, Rafael. I think that if you have had a chance of following up gross margins and align that with interest rates, that is related to prices that we have had last year. And we are having this policy of favoring profitability and obviously our competition strategy is still going on, and numbers have shown a good performance during the year.

Loss ratios have been going down. And as you can see in the curve in the chart, and we are going to have the consolidation of these results especially in terms of the gross margin that is also going to be affected. It will drop. And then, we are favoring results and we are managing our fleet and also the portfolio. And it is a quite interesting position that we will announce to you every quarter.

So the market, yes, more fully aware, more concerned with profitability on the whole and this is being reflected in pricing and you can see that in the competition in the auto segment and it is also reflected in our competition and also the adjustments that we are going to have. So I think it's a quite positive cycle and we are preparing ourselves for that and we will be able to reap the fruit of everything that we've been preparing. Our Auto Director is also taking part in all events in the market, and Eduardo would like to compliment.

A - Eduardo Dal Ri

Thank you, Beto. Just to illustrate what Trindade is saying, we regulate and we try to see our competitiveness and we are seeing brokers giving increase of insurance companies, the whole main differentiation is through pricing when this type of insurance company when they raise their prices and as we have done our homework in terms of price increase along 2012, we can see that brokers seeing our brand and our product as more attractive again within our this -- in respect verifies that instantly online which is the number of estimates and hope that we give to our customers and something that had not happened in previous year.

Q - Rafael Frade {BIO 16621076 <GO>}

Thank you, Eduardo.

A - Eduardo Dal Ri

Thank you.

Operator

Our questions and answer session has now ended. Now I would like to turn it over to Mr. Thomaz Menezes for his final remarks. Please, Mr. Menezes, you may proceed.

A - Thomaz de Menezes {BIO 16674464 <GO>}

Well, once again, I would like to thank all participation interest and questions that you have made to the company. And usual about myself and my team and Arthur, we are all available to give you more details whenever you need. And I would like to emphasize our commitment of growing with profitability as you've seen we have invested greatly in the company almost in all areas of the company and I am sure that we have closed the year much better structured and prepared to take advantage of the opportunities that our country and our industry will offer.

So I would like to thank you all for your questions and thank you very much.

Operator

Thank you. Sul America's conference call has now ended. We thank you all for your participation and have a good day.