# QBE Insurance Group Ltd Corporate Call

## Company Participants

- Inder Singh, Group CFO
- Patrick C. Regan, Group CEO & Executive Director

## Other Participants

- Andrew Buncombe, Insurance and Diversified Financials Analyst
- Ashley Dalziell, Equity Analyst
- Kieren Chidgey, Executive Director & Research Analyst
- Matthew Dunger, Research Analyst
- Siddharth Parameswaran, Research Analyst

## Presentation

### Operator

Thank you for standing by. Welcome to the QBE Insurance Group update. (Operator Instructions) I would now like to hand the conference over to Mr. Patrick Regan, CEO. Please go ahead.

### Patrick C. Regan {BIO 15131018 <GO>}

Good morning, everybody. Thanks for joining us today. We're just giving a very quick update today on the very unusual weather impact we've had this year on our crop results. As you are all aware, we've got what I think is a terrific crop insurance business, which had delivered an average 10-year combined ratio of around 90%. However, obviously, in any given year, that result can be significantly impacted by the weather. And unfortunately, that's been the case this year. You'll recall that in the first half of the half year, we highlighted that there was an especially wet spring in the U.S. that resulted really in 2 things, late planting of crops, particularly corn and soy across many of the states. And a large number of prevented planting claims where farmers couldn't plant their crops at all. And as a result of the half year, we booked the current accident year at 98% combined ratio for crop.

Now the late planting and the crops were more exposed to the potential of any adverse weather towards the end of the year. And that's been the case. The back end of the growing season included a significant amount of unusually early unseasonal cold weather, including very early bouts of sleet, frost and snow, which has contributed to now a material footfall in the crop yield.

Just to top things off, crop yields were also further impacted by significant amount of hail damage, particularly in the later part of the harvest season. So taking all that together, we now expect the crop business to have a current accident year combined operating ratio in the range of 107% to 109% for 2019, which on approximately $1.2 billion of net earned premium has about a 2% negative impact on the overall group combined ratio compared to that long-term average of 90%. Or relative to the 98% we booked at the half year, just about a 1% negative combined ratio impact. Smaller scale. But worth noting that the same bad weather also had a small impact on the loss ratios of some of the North American property portfolios.

So this means that we now expect the group's combined ratio could now be very slightly above the top end of our previously revised 2019 target range of 94.5% to 96.5%. Conversely, our 2019 investment performance remains on track to report a net investment return right at the upper end of our 2019 range of 3% to 3.5%. And more broadly, I continue to be very pleased with the direction of the business, including the levels of premium rate increases we're seeing right across the group and our outlook for underwriting margins.

Price momentum is indeed accelerated during 2019. And in the Third Quarter stand-alone, we achieved an average premium rate increase across the group of 7.5%, bringing the year-to-date rate increases to 5.5%. And indeed, strong rate momentum has continued so far in Q4.

We continue to see year-on-year improvement in our attritional loss ratios. Additionally, we've now finalized the placement of our 2020 reinsurance structure, which is very similar in structure to 2019.

And I believe we were the first global reinsurance program to be finalized. And to the same, our 2020 target combined operating range is now going to be 93.5% to 95.5%, reflecting our confidence in the outlook for the group.

I look forward to updating you all on further details of our full year 2019 results on February 17. Now happy to open up the call to a few questions. But we probably won't give a whole heap of more detail at this stage other than what was included in the release today.

So with that, I'll hand back to the operator to open up to questions, please.

## Questions And Answers

### Operator

(Operator Instructions) The next question comes from Andrew Buncombe of Macquarie Group.

### Q - Andrew Buncombe {BIO 19921333 <GO>}

Just a couple of questions from me, please. The first one, I'm just interested to understand how the combined ratio in the crop portfolio could get above 105%. My understanding was that TBA purchased reinsurance that attached at a state level at 105%. Then on top of that, you had commodities instruments. So can you just give us a bit of color on which line of defense failed this time, please?

## A - Patrick C. Regan {BIO 15131018 <GO>}

Okay, Inder, feel free to chip in here as well. The commodity -- as we talked through, Andrew, the issue this year has all been on the yield, not the price of the crops per se. So the commodity protection didn't really come into play. The reason for backstop reinsurance, the protection of crop result is just a bit higher than 105%. So that really kind of kicks in more at the 108% to 109%. So in really any circumstances, it's difficult for the result to get much worse than 108% or 109%. But it's that level rather than 105%. Anything you would add to that, Inder?

## A - Inder Singh {BIO 20594382 <GO>}

No. That's very safe path, I think, around that 109% is where effectively the backstop is fully effective.

## Q - Andrew Buncombe {BIO 19921333 <GO>}

Sure. Okay. That's great. Then the second question, please. From what we can see in the USDA data, it looks like harvests finished in October, if not early November, yet this announcement is coming out mid-December. Just interested to know why this announcement has taken so long? And how investors should be thinking about management reporting systems in the U.S.?

## A - Patrick C. Regan {BIO 15131018 <GO>}

Andrew, I think, on that one, the harvest has been later this year for all the reasons we said. Then the slow on from, obviously, after the harvest comes out of the ground, you then got the actual kind of notification of claims. Everything is a bit later this year because the crops went in the ground this year later. Actually, at the end of October, there was quite a bit of harvest that haven't been completed on some of the key states. So the % harvested by -- in places like North Dakota, Minnesota, South Dakota was still relatively immature at the end of October. Then, obviously, once they harvest, they go through the process of making the claims, lodging the claims, all of that.

## Q - Andrew Buncombe {BIO 19921333 <GO>}

So that makes sense. Then just one more from me, please. Just interested in the 2019 combined operating ratio, it seems like all the big moving parts have now been -- well, they were excluded from the definition previously in terms of crop and LMI. Just maybe you could give us a bit of color on what was left remaining inside the rest of that definition? I appreciate that there is the U.S. property portfolio. But what else was there that's caused that '19 number to slip up to the top end, please?

## A - Patrick C. Regan {BIO 15131018 <GO>}

Really, it's impacted crop. So as I mentioned, to do a $1.2 billion of net earned premium, if you're kind of close to 20 points above your long-term average, I mean, that's getting up to not quite $250 million of underwriting impact. But close to $250 million of underwriting impact. And even compared to where we booked it at the half year, it's well over a point. So that's quite far to '19. Then -- and seasonally, that is slightly higher in cat load in the second half versus first half. But that's the best time expected.



## A - Inder Singh {BIO 20594382 <GO>}

Andrew, you might be reading footnote 2, which references actually the attritional claims ratio, which excludes LMI and excludes crop. That doesn't reference to combined ratio.

## Operator

The next question comes from Matthew Dunger of Bank of America.

## Q - Matthew Dunger {BIO 20863237 <GO>}

Could I just ask you, in terms of the FY '20 guidance, the 93.5% to 95.5%, what are you factoring in for the combined ratio for the crop business?

## A - Patrick C. Regan {BIO 15131018 <GO>}

Yes. A good question. So that will be back towards the long-term average. So we reconcile it being close to 90%. It will be around that number.

## Q - Matthew Dunger {BIO 20863237 <GO>}

Okay. And if I back out -- if I back out the crop losses this year, is it fair to say that we've been looking at a combined ratio around 95%?

## A - Patrick C. Regan {BIO 15131018 <GO>}

Obviously, there's various different kind of ons and offs in the year. We had -- we were slightly light on cat in the first half. Broadly, yes, I mean, the difference between this year's crop performance and our long-term average of 90% is about 2 points on the group combined.



## Q - Matthew Dunger {BIO 20863237 <GO>}

Okay. And are you able to talk to the composition of the large risk versus the catastrophe claims in the second half? Because I think we saw low catastrophes and high large risk claims in the first half. Are you able to give us some color on what's happened in the second...

## A - Patrick C. Regan {BIO 15131018 <GO>}

Yes. We're probably getting, Matthew, into the kind of detail we'll share more with you in February. I would say second half cat has been more in line with the allowances. We were slightly light on cat in the first half, as you mentioned. Second half due to various things, Hurricane Dorian, et cetera, we'll be kind of closer to our allowances.

## Operator

The next question comes from Siddharth Parameswaran of JPMorgan.

## Q - Siddharth Parameswaran {BIO 15037291 <GO>}

Patrick, a couple of questions, if I can. Firstly, just on the combined ratio guidance for this year. Are there any issues that you've seen in terms of claims inflation that some peers, particularly in the U.S.. And to some extent in the U.K. have highlighted? If you could just maybe tell us if there's any allowance for any reserve adjustments or the like in your numbers? And whether you're seeing any of those trends?

## A - Patrick C. Regan {BIO 15131018 <GO>}

So is there anything factored into our numbers on that? No, not particularly, Sid. For a couple of reasons, we'd like to think that we've repositioned some of our books away from some of the areas that's got the most social inflation. We're not completely immune. We do have some financial lines. But we recut our U.S. book of business to be much smaller ticket, thus we've avoided some of the heat and light on U.S. financial lines without all these financial lines really to speak of. So you will see -- if you have the detail of all of our reserve in front, you would see elements of that. But it's offset with a relatively small element. And it's offset by good guys. So there's nothing net-net that gets factored into the numbers we've given you today, nothing that we needed to.

## Q - Siddharth Parameswaran {BIO 15037291 <GO>}

Okay. Then if I could just delve into guidance for next year. I mean you mentioned there that one way of thinking about this result is that if we strip out the impact of crop, looking at an underlying figure of 95%. But you're guiding not much of an improvement into next year despite flagging very strong rate momentum. So could you just give us some idea of what might be holding back the improvement in that combined ratio? I mean 0.5% improvement is quite modest versus the kinds of rate increases that you're flagging 5.5% plus?

## A - Patrick C. Regan {BIO 15131018 <GO>}

Yes. I think, actually, it was Matthew who said the underlying was 95% rather than 85% if I could. So look, in terms of -- so there's probably a 2-point difference between this year's crop result and our expectation of the long-term average crop result and indeed what we plan to do. Equally, we'll end this year. But really in the first half, due to the first half a bit light on what we would normally expect cat. So when we would plan on our capital for next year, that will be a little bit higher than we will end up recording for 2019. So that probably pushes you up a little bit. We have seen good rate increases. Obviously, we're not -- what's holding us back? Nothing in particular, no, we feel good about our program of work. We feel good about turning -- we've got a reasonable track record now. We're turning the rate increases into improved attritional. We think still there is more gas in the tank now. We've -- obviously, Second Quarter a bit heavy attritional loss ratios over the last couple of years. But we still think there's more that we can do on that. So there's nothing in particular that I would highlight that would be quite holding us back next year, other than we're just announcing today, we're at the top end of our range or slightly over for 2019.

So that's the nature of these kind of ranges, as nothing is going to happen in running the business.

## Q - Siddharth Parameswaran {BIO 15037291 <GO>}

Yes. Okay. And just, sorry, one final question for me. Just the 2.5% to 3% target range for investment returns for next year. Could you just give us some idea of what you're assuming, perhaps, at the bottom end in terms of rate cuts around the world? And also just -- maybe just some idea of whether there's any change in the risk mix of your portfolio in that guidance?

## A - Patrick C. Regan {BIO 15131018 <GO>}

Inder, why don't you take one that for us?

## A - Inder Singh {BIO 20594382 <GO>}

Yes, sure. Thanks. Look, I think what we're assuming is broadly a rate environment in line with what we're seeing today. There's some very modest repositioning of the portfolio, nothing material to call out. And the year-on-year change is largely flowing through the lower risk-free rate environment that we're in relative to where we were last year. Loss ratio modestly extending the duration.

## Q - Siddharth Parameswaran {BIO 15037291 <GO>}

No further rate cuts?

## A - Inder Singh {BIO 20594382 <GO>}

No, effectively, we're sort of following the current curves, we're not expecting a material step-down from that.

## Operator

Your next question comes from Ashley Dalziell of Goldman Sachs.

## Q - Ashley Dalziell {BIO 20853789 <GO>}

Just another question on the outlook for the investment return. Are you able to perhaps frame how the running yield is looking in the second half of '19? I think in the first half of '19, you said it was maybe around 1.6. And just following on from that, you touched on mix briefly. But should we assume the 2020 guidance is predicated on sort of sitting at about 15% growth assets, i.e., the top of your range?

## A - Inder Singh {BIO 20594382 <GO>}

Yes. Look, I think the running yield was bumped around a little bit when we announced the first half result in August, it hasn't markedly shifted from that sort of mid-1s level. Then there isn't really any change we're flagging in terms of our appetite on growth assets as we shift into next year.

## Q - Ashley Dalziell {BIO 20853789 <GO>}

Okay. Then just a second question, just thinking about the combined guidance into '20 and just the placement of the 2020 reinsurance program year-over-year, does that represent any sort of headwind to the combined ratio?

## A - Patrick C. Regan {BIO 15131018 <GO>}

Just a slight one, actually. I mean, as you have been following that, generally, the market for reinsurance rates is nothing like the price increases we're seeing on the primary side. So 50% of the structure was already placed in 2019. So it's slight. But not material.

## Operator

(Operator Instructions) Your next question comes from Kieren Chidgey of UBS.

## Q - Kieren Chidgey {BIO 7268946 <GO>}

Most of my questions have been answered. But maybe just one on top line with rate momentum picking up, I think, you said 7.5% perhaps in the Third Quarter. You're at the point now where you think unit accounts sort of can be fairly flat across the group and sort of how should we -- or how are you thinking about top line growth into next year?

## A - Patrick C. Regan {BIO 15131018 <GO>}

Yes, look, it's an interesting question. So whilst I'd like to think that we've -- we're building up a little bit of track record of improving our attritional loss ratios, we haven't been able to do that and grow top line in line with rate. As you remember, the first half, we were, obviously up 5% on rate and up 3% on volume. So I think we'd like to at least get sort of even of if we're up 5% on rate, get to up 5% on volume as well. Then maybe over time, obviously, grow. Kind of no reason in why we shouldn't do. We're not really in the repositioning, reunderwriting of the portfolios. With areas, there are more areas we should look to grow, than probably there is little to shrink. So with that being ahead of the top, hopefully, we can do a little bit better on that in 2020.

## Operator

I will now hand back to Mr. Regan for closing remarks.

## A - Patrick C. Regan {BIO 15131018 <GO>}

I appreciate everybody jumping on the call at short notice with us. And we look forward to give you all further detail on the full year results in February. Thank you.