# Q2 2013 Earnings Call

## Company Participants

- Alain Lessard, SVP, Commercial Lines
- Charles Brindamour, CEO
- Dennis Westfall, VP, IR
- Mark Tullis, CFO, SVP
- Martin Beaulieu, SVP, Personal Lines
- Mathieu Lamy, SVP of Claims

## Other Participants

- Bryan Brown, Analyst
- Doug Young, Analyst
- Jeff Fenwick, Analyst
- Mario Mendonca, Analyst
- Paul Holden, Analyst
- Tom MacKinnon, Analyst

## Presentation

### Operator

Good morning, ladies and gentlemen. My name its Martina and I will be your conference operator today. At this time, I would like to welcome everyone to the Intact Financial Corp's Second Quarter earnings results conference call. All lines have been placed on mute to prevent any background noise. After the speakers remarks there will be a question-and-answer session. (Operator Instructions) I would now like to turn the call over to Dennis Westfall, VP Investor Relations. Please, go ahead.

### Dennis Westfall {BIO 15155973 <GO>}

Thanks, Martina and good morning everyone. A link to our live webcast and background information for the call is posted on our website at www.intactfc.com under the Investor Relations tab. As a reminder the slide presentation contains the disclaimer on forward-looking statements, which also applies to our discussion on the conference call today. Joining me today are Charles Brindamour, Chief Executive Officer; Mark Tullis, Chief Financial Officer; Martin Beaulieu, Senior Vice President, Personal Lines; Alain Lessard, Senior Vice President of Commercial Lines. And Mathieu Lamy, Senior Vice President of Claims. We will start the formal remarks from Charles and Mark followed by a Q&A session. Martin, Alain and Mathieu will be available to answer your questions during the Q&A session. With that I will ask Charles to now begin his remarks.

## Charles Brindamour {BIO 7012323 <GO>}

Thanks, Dennis. Good morning, everyone. Before getting into the Second Quarter's results, I want to first make a few comments about the events of the past six weeks. I can say without hesitation that the number and magnitude of catastrophic events that we've witnessed are unprecedented in my 21 years in the industry and with Intact.

The flooding in southern Alberta was unique not only because of the volume of water involved. But also because entire communities were devastated. The recovery effort will take months and even years for some areas. I'm confident, though, that we have the people and the expertise to be there for as long as it takes. Our promise is to get customers back to their normal lives and we're more committed than ever to doing that.

The tragedy in Lac Megantic is beyond anything I have seen before given its atrocious nature and devastating impact on the lives of many individuals and families in that community. Within a few hours of the accident, we had a fully functional mobile unit on-site and our people were there to help our customers in those trying times. Our thoughts are with these families. I was on-site in both these places and had the opportunity to see our people in action as they helped our customers.

I've been impressed by the speed of their response. But more importantly by the empathy that they have displayed in those difficult times. I want to thank our people on location, as well as across the country, who went beyond and above to respond to these and other events this summer. Despite the CAD0.92 per share in total losses from catastrophes, this morning we announced Second Quarter net operating income per share of CAD0.89. Our combined ratio of 97.5%. reflects the resilience of our business in light of these events.

Continued strong performance in automobile insurance and improvements in our expense ratio were the drivers behind the underwriting profit. From a topline perspective premium growth of 10% reflects the continued successful integration of Jevco, as well as solid organic growth. I'm pleased with our ability to leverage the Jevco products across our distribution platform. This has offset or more than offset the expected impact we have seen from re-underwriting parts of the acquired business, particularly, in commercial lines. Our earnings over the past years have generated an operating ROE of 14.4%. And a 9% increase in book value per share.

From a capital perspective we're comfortable with our MCT of 197% and expect to maintain it between 195% and 200% through the remainder of the year. The frequency of severe weather events in the past few weeks has made it clear to me that the sustainability of home insurance in its current form is being challenged. While we have made meaningful progress with underwriting profits on average over the past three years in that line of business, our approach needs to evolve further given the environment we face and will likely face in the coming years.

So while our 3,100 claims employees were focused on helping our customers, a special task force composed of folks from coast-to-coast busied themselves laying out a robust plan to be implemented in the coming weeks aimed at ensuring the sustainability of our offer in the coming years. The plan we have in mind will focus on ensuring customers have a better understanding of the risks they face and what they can do to better adapt to climate change.

We will further implement meaningful rate risk selection, as well as product actions. This issue is not one solely affecting the insurance industry. But rather society as a whole. And as such we will work and support communities across the country to raise awareness and help provide guidance as to how they can better protect themselves against the impact of extreme weather. We expect our plan to generate a minimum of 10 points of combined ratio improvement in that line of business.

Moving to automobile insurance, our view is largely unchanged from the First Quarter. We are operating in an environment where both competitors and regulators behave fairly rationally. And costs have been generally stable in the recent past. Understandably, Ontario has been a source of concerns with investors in the past few months. It has been a source of concern for my team and I, as well. But our view has not changed.

While it will be difficult to achieve, we continue to work with the government to bring cost reductions in the system to improve affordability for Ontarians. In their quest to achieve 15% reductions over time, the government understands that meaningful cost reduction measures will be critical to ensure availability of the product given the fact that the industry operates at breakeven at the moment. We will continue to work with the government and the Insurance Bureau of Canada to identify and quantify additional costs reduction measures.

We expect new regulations resulting from the budget to become available in early fall. These will likely lead to rate actions in the first part of 2014. We're pleased with the 50% reduction in mediation backlogs that the government has engineered so far in 2013. This is in my view another example of their focus on improving the environment. They expect the backlog to have disappeared by year-end. This should help alleviate some of the inherent uncertainty in the system. It's important to bear in mind, though, that the direct consequence of sharp reduction in mediations is an increase in arbitration.

So during the first four months of 2013, the number of industry arbitrations increased 37%. Now, due to our proactive approach to managing our files in dispute, IFC's arbitrations have increased only 7%. Beyond that, our view of the Ontario market is largely unchanged. We feel strongly about our ability to outperform in that market.

When it comes to our outlook for the industry, we foresee similar growth in the near-term to that of the past 12-months. However, we do expect the current hard market conditions in personal property to accelerate meaningfully for the foreseeable future. We continue to expect firming conditions in approximately one quarter of the commercial P & C industry in 2013. And we think that the low interest rate environment and the elevated losses from catastrophes should support our outlook.

Turning to the industry, we do not expect the industry to reach its long-term average of 10% in the next 12-months, largely due to the elevated CAT activity which has already materialized. Looking specifically at Intact Financial, we believe we will continue to outperform the industry's ROE by at least 500 basis points. Mark will provide updates on our integrations in a moment. But clearly we have made some good progress in the quarter. I continue to be impressed with our employees' dedication. And want to thank them for their hard work in ensuring our customers and brokers continue to receive top-notch service.

In conclusion, I believe the disciplined approach we take towards operating our business will continue to serve us well. I'm confident that we will confront new challenges with the same level of determination that has brought us to where we are today. Given the quality of our operations and the flexibility provided by our financial position, we believe that we'll continue to outperform the industry and defend our superior level of profitability. With that I'll turn the call over to our CFO, Mark Tullis.

## **Mark Tullis** {BIO 4180270 <GO>}

Thanks, Charles. Last month Southern Alberta experienced storms and flooding resulting in historic levels of damage to the homes, autos and businesses of our insureds in the Calgary and High River areas. Teams from Intact immediately went to work. The first day, we began to transform an industrial building on the north side of Calgary into a claims center with one hundred desks and computer connections as our offices in downtown Calgary were closed due to flooding.

Public transportation was shut down. So we chartered private buses so that our employees could go to work. We brought in claims staff from throughout Canada. And within three weeks we had visited and performed initial evaluations for virtually all of the claims. It will be months before everything is back to normal for the people of Alberta. But Intact moved quickly to help our insureds begin this process. We have shown the same response to the Toronto flooding and the tragedy in Lac Megantic.

Events like these separate world-class companies from the rest. And Intact has been up to the task. With this as a backdrop, today we announced Second Quarter underwriting income of CAD42 million with a combined ratio of 97.5%. Strong results in our auto lines of business. And strong property results outside of Alberta, particularly in Ontario, proved once again the advantage of diversification both geographically and by line of business. Both auto lines of business had combined ratios below 90% despite the elevated CAT losses.

Personal auto, in particular, had a strong quarter with a combined ratio of 87.2%. Our 14% growth in premiums reflects the addition of Jevco, as well as solid organic growth. The combined ratio in commercial auto remained excellent at 89.6%, although higher than last year's exceptional performance. Our personal property line of business has been most affected by the recent storms with a combined ratio almost 9 points higher than last year due to the CATs.

As Charles mentioned, we are committed to mitigating our CAT exposure for this line of business. And we're taking action on multiple fronts to build a sustainable product offering. Our actions will include product changes in risk selection, as well as additional rate increases starting on the fall on top of those already in the system. Our commercial P & C business also experienced elevated catastrophe losses amounting to CAD40 million in the quarter, which in conjunction with a higher level of large losses, led to a combined ratio of 108.2%. As with personal property, we are reviewing our product in underwriting in light of the new climate reality.

Our expense ratio at the total company level was 0.9 points improved versus 2012. This change was driven by a drop in variable commissions from the lower level of profitability in the quarter. And also from acquisition-related expense synergies. Our effective tax rate of 14.9% reflects a higher proportion of tax free dividend income relative to underwriting income, which was lower due to the CATs. Our net investment income of CAD102 million was up 7% from a year-ago. This was primarily due to additional investments from Jevco, a portion of which included dividend paying common shares.

Our market-based yield of 3.8% was up from 3.4% last quarter with the increase in yield due to the drop in market value of our investments driven by higher bond yields and weak Canadian equity markets. We expect the low interest rate environment to continue to weigh on our results in the near-term. And we expect second half net investment income to be similar to what we recorded in the first half of the year. Our financial position remains solid at the end of Second Quarter with CAD486 million in excess capital and book value per share 9% higher than a year-ago.

Our MCT decreased to 197% on the heels of the CAT losses, our share repurchases and market driven changes in other comprehensive income. We intend to manage our MCT to remain between 195% and 200% through the remainder of the year. Since introduction of our NCIB last quarter, we have purchased 1.8 million shares at an average price of CAD59.35. We will continue approach the NCIB opportunistically, dialing up or down, depending upon opportunities in the market, volatility in the environment and capital availability.

We continue to make good progress on both of our integrations. For AXA Canada system shutdown is on schedule. We maintain our CAD100 million after-tax synergies target with a run rate at quarter end of CAD87 million. Most of the remaining synergies will coincide with final system shutdowns in early 2014. The impact on growth from cross-selling the Jevco product suite within our distribution platform remains better than expected, with the Second Quarter traditionally the strongest for Jevco.

We have completed our review of the rates and segmentation for nonstandard auto and motorcycles and are rewriting portions of the Jevco portfolio where required. Greater than expected synergies, primarily from claims, will enable us to reach our initial CAD15 million after-tax synergy estimate by the end of this year, a year earlier than previously expected. Our new after-tax Jevco synergy estimate is CAD23 million after-tax by the end of 2014.

The storm season is not over as we can see from the three small CATs of the past two weeks. And if necessary we will provide further guidance to the market later in the quarter. However, in this environment, I am particularly proud to work for a company that can respond so quickly when our clients need us most. Our people have responded professionally and with empathy for our clients during what has been a difficult summer for thousands of our customers. These challenging times best illustrate the resilience of our business, which along with our strong financial position, will enable us to take advantage of opportunities in the market and to bolster our long-term earnings potential.

Combined with our disciplined approach to the business, we have a strong foundation for continued profitable growth. With that I will turn the call back to Dennis.

## Dennis Westfall {BIO 15155973 <GO>}

Thanks, Mark. Martina, we are now ready to begin the question period.

# Questions And Answers

## Operator

Certainly. (Operator Instructions) Your first question comes from the line of Jeff Fenwick from Cormark Securities. Your line is open.

## Q - Jeff Fenwick {BIO 15350794 <GO>}

Hi. Good morning. Just wanted to start off today with a further discussion on the coming changes around the Ontario rate reductions. Charles, you gave a little color there about the process and perhaps a rough idea of the timeline. Can just describe, maybe in a little more color, what is it about the process here that's giving you some comfort that it's being done in an orderly fashion. And how have they gone about consulting with the industry to ensure that you really are going to get those cost reductions when they start to put through those rate reductions. And do you have a sense of -- is it 15%, you said it might be partially implemented the beginning of the year. So is there a timeline for rolling out the rate decreases, as well.

## A - Charles Brindamour {BIO 7012323 <GO>}

Yes. I think the government understands that this is a complex process, because you have to make changes in the system and, as such, I think very responsibly, they said we'll aim at 15%. And that will take place over a number of years. The budget that will be translated into regulations in early fall had a number of ingredients in there to tackle first portion of the rate reductions whether it's reinforcing the definition of minor injury, whether its regulation of clinics, tow trucks and so on, or a number of measures in there, which are really quite beneficial, I think. And will likely translate into rate impact. We will see what these regulations actually look like in the coming month or two. And following that we'll reflect that in our rates so as to have a commensurate impact on premium with the costs reduction measures that they're putting in place.

Now, the fact that it is an environment that is evolving, the fact that it is a complex environment really calls for a very tight cooperation between the industry and the government to find measures that will be effective at bringing affordability in the market. And there's been a lot of work between both parties. The Insurance Bureau of Canada has been very active on that file with the government. And the nature of these interactions and how constructive they've been gives me comfort that we're headed in the right direction there. But I think this is not a walk in the park. 15%, we have said it all along, is a big number and, therefore, that will take time to materialize. And I think we'll see a portion of that, I suspect, a fraction of that materialize in the coming year. But process so far has been good. I don't know, Martin, if you want to add to this.



## A - Martin Beaulieu {BIO 15316652 <GO>}

No. I think this is right in line with what I see in the relationship with FSCO and with the Ministry of Finance, where I think they want to do things right. They are expecting that within the next couple of months the process will be better defined. And that the rate reductions would start flowing. Not the 15%. But the Q1 of 2014 or so, that the market should start seeing rate reductions to reflect the costs.

## A - Charles Brindamour {BIO 7012323 <GO>}

Yes. We'll see what's in there. I think -- I mean these guys are smart and responsible in my view. And they understand the industry operates at the breakeven, at the moment. And they know that if costs reductions don't come along there will be an availability problem. And this is not an empty threat. I mean it happened eight years ago. They completely understand that. And I think they want to avoid that because that would be a much worse outcome for Ontarians. So I have great confidence in their leadership on that front.

## Q - Jeff Fenwick {BIO 15350794 <GO>}

Okay. Then maybe just a follow-up on that in terms of the where we are today and the Ontario market. And we saw TD, yesterday, take some additional strengthening and charge there mentioning some more recent developments in Ontario Auto. Is this something that is specific to TD. And do you feel like the strengthening you took last year is adjusting for, I guess, what perhaps they're seeing today?

## A - Charles Brindamour {BIO 7012323 <GO>}

You know, these guys are smart, they're disciplined. I think they're very good and when they notice or when they talk, I certainly pay attention. And I tried to see if there are parallels in our business. It's tough, though, from the outside to know exactly what they are talking about. I can tell you that we have been following the reforms that were effective in September 2010. We knew that bodily injury costs would increase by close to 25%. That's something we've talked about for two, three years now. And we, in September of 2010, increased our pricing, or certainly reflected that in our pricing assumptions, reflected that in our reserving assumptions. And as a result increased our reserves gradually over the past three years to reflect that assumption.



So it's very hard for me to judge but these guys are smart, they're disciplined and I pay attention to what they say. So we're pretty confident with what we have done. And, quite frankly, we have not noticed on the bodily injury front meaningful changes in the environment. We have seen an increase in litigation over time. Maybe not yet at the level of what we expected and what we're reserving for. But it is early and, therefore, we remain cautious on that front, both in pricing and in reserving.

## Q - Jeff Fenwick {BIO 15350794 <GO>}

Okay. Thank you very much.

## Operator

Your next question comes from the line of Paul Holden from CBIC. Your line is open.

## Q - Paul Holden {BIO 6328596 <GO>}

Thank you. Good morning.

## A - Charles Brindamour {BIO 7012323 <GO>}

Good morning, Paul.

## Q - Paul Holden {BIO 6328596 <GO>}

Within your results you mentioned on the personal auto side, that the core loss ratio picked up year-over-year. And that was due to an increase in severity, which I think you quantified at 6% year-over-year. So curious what's driving that severity if it's not BI.

## A - Charles Brindamour {BIO 7012323 <GO>}

Want to take that, Martin?

## A - Martin Beaulieu {BIO 15316652 <GO>}

Well when we look at the severity in the quarter, it's increasing 6% versus last year. We don't see any trends in litigation or in patterns that would lead us to believe that there is a trend there. When we look at the last three or four years, we noticed that this is a fairly stable severity level. We had a small adjustment last year that decreased somewhat the severity in that quarter so this is -- we're not concerned by what we're seeing in this particular quarter.

## A - Charles Brindamour {BIO 7012323 <GO>}

Yes. I think current accident year deteriorated by a couple of points, driven by severity increase. And we have seen that in a number of jurisdictions here. You know, Alberta was up a bit, Ontario was up a bit and as Martin said, the denominator might have been a bit understated. So not an area of concern. And Paul given the noise in the environment I can tell you that Mathieu and myself have spent time with people in the field to make sure that we were not missing anything from a trend point of view either in AB, either in BI Ontario, either in BI Alberta. So there is activity but not -- not much different from what we anticipated. I don't know, Mathieu, if there is anything you want to add there.

## A - Mathieu Lamy {BIO 15207469 <GO>}

No. I think in Q2 our view remains unchanged on the benefit of the reform in BI and in AB.

## Q - Paul Holden {BIO 6328596 <GO>}

Okay. So if I'm understanding the answer correctly, then, we should not expect to see that same type of 6% cost inflation in future quarters? Is that the correct way to interpret that?

## A - Charles Brindamour {BIO 7012323 <GO>}

Yes. I think that's that is the right way to interpret that. You know, I think we talked about 6%. We probably should talk about the fact that there's drift that's offsetting that, as well. And that's in part why the current accident year is not up 6%. It's actually up 1.5% or 1.6%.

## Q - Paul Holden {BIO 6328596 <GO>}

Okay. Then in terms of Alberta, the Rate Board approved the 5% increase for mandatory coverage, effective, I guess, in November of this year. Would you anticipate that you will be taking all five points of that?

## A - Charles Brindamour {BIO 7012323 <GO>}

Yes.

## Q - Paul Holden {BIO 6328596 <GO>}

Yes. Okay. Then in that case do you anticipate that that 5 point increase is sufficient to offset cost inflation, or is there other actions you might have to take with optional coverage?

## A - Martin Beaulieu {BIO 15316652 <GO>}

Well the 5% on the mandatory coverages was against the -- an indication by both the board actuary and the IBC actuary of low teens. So we don't see this as being the full remedy to rates--

## A - Charles Brindamour {BIO 7012323 <GO>}

Or the industry.

## A - Martin Beaulieu {BIO 15316652 <GO>}

-- or the industry. So there will be activity, also, on the optional side of the product where, as you know, the rate approval process is not that stringent.

## Q - Paul Holden {BIO 6328596 <GO>}

Great. And final question is with respect to reinstatement premiums. There was a fairly meaningful number in Q2 and anticipate there will be something in Q3, as well. Any way you can quantify what the number may be in Q3 for us. And remind us if there's any kind of limit on the number of times you can reinstate your reinsurance coverage in a given year.

## A - Mark Tullis {BIO 4180270 <GO>}

Yes. So the premium -- there's actual a separate premium for each layer of coverage. And since the event in Q2 was larger than the individual events in Q3, the reinstatement effect will be smaller. We're maybe looking at sort of half the level in Q3. So far assuming there's not another major event as what we looked at in Q2.

## Q - Paul Holden {BIO 6328596 <GO>}

Okay. That's all the questions I had.

## A - Charles Brindamour {BIO 7012323 <GO>}

Thanks, Paul.

## Operator

Your next question comes from line of Doug Young from TD Securities. Your line is now open.

## Q - Doug Young {BIO 5640851 <GO>}

Good morning.

## A - Charles Brindamour {BIO 7012323 <GO>}

Morning, Doug.

## Q - Doug Young {BIO 5640851 <GO>}

First question just -- Charles, in your descriptions of the first question, the question around the Ontario Auto. And how you see it unfolding. It sounded like. And correct me if I'm wrong, you think that the costs mitigation items will be determined first and adopted first and then the rate reductions will take place. Is that how you see it unfolding? Did I hear that properly?

## A - Charles Brindamour {BIO 7012323 <GO>}

Yes. I think the framework for the cost reduction will, I suspect, will be laid out in the regulations and I haven't seen the regulations yet. I'm speculating to a certain extent. But that's the objective of translating the budget in regulations. And once we see that we will reflect that in pricing. I think the pricing exercise will likely be an exercise, as well, of making sure that the assumptions we're making about the impact of the reforms of September of 2010 are in line with the reality, as we see it today. You know, that's the other element that I think will be part of that process. But, indeed, as I've said before, I think the costs reductions are a critical part of how one gets to premium reductions.

## Q - Doug Young {BIO 5640851 <GO>}

Okay. And just wanted to go in a different direction away from auto. I'm sure you'll get lots more questions. But on the commercial P&C side there was an increase in the number of large losses. And I just want to dig in a little bit further in what you're seeing, because this isn't the First Quarter where you have had an increase in large losses. And just can you give us a little more color on that?

## A - Alain Lessard {BIO 17592535 <GO>}

Okay. Well if you look at the large losses, we first of all, I would say we're not seeing rights now any trend. And I can look at, let's say, the last six quarters as an example. Q1 and Q4 of 2012, we had higher large losses than on average. Q2 and Q3 were very weak in terms of large losses. And this year Q1 was below average slightly. And Q2 was slightly above average. And on top of that the kind of losses we're seeing in the Second Quarter are coming from marine business, or a little bit of surety business, which is different than what we have experienced in the past in 2012. So basically, there's no trends. There's a lot of fluctuation. But the level we are seeing, right now, on a direct basis is still within expected normal variation in terms of large losses.

## A - Charles Brindamour {BIO 7012323 <GO>}

But I will tell you, Doug, even though Alain does not necessarily see a pattern, we're looking at these losses, one by one, to see if there's anything in our risk selection process, in our pricing process. And so on, that needs to be tightened trying to learn as much as we can out of that. So we don't take these lightly even though they're not a trend as far as Alain is concerned.

## Q - Doug Young {BIO 5640851 <GO>}

Okay. And I just wanted to go. And I know I've asked this question before and it sounds like the way you described the personal property changes, there's been a lot of changes to the product over the last few years. Sounds like you're going to lean further into the product, make substantial changes in that product. And you've had many discussions with the government around, obviously, the issues that have materialized for the industry. Has there been -- have you been approached, at all, or has there been any discussion with the government or the regulator about more tightly regulating this product?

## A - Charles Brindamour {BIO 7012323 <GO>}

I would say that our interactions with the government -- we often have been the ones approaching the government to let them know of the evolution we saw in the weather patterns. And the implications this had on availability and potentially affordability, more so than the government is coming to us and saying "we intend to do something there." I think we want to make sure they understand sort of costs pressure that took place over time. There's been, in particular in Alberta, ongoing dialogue with the superintendent on the home insurance front, as they understand that Alberta is the province that has been the most impacted on home insurance in the past few years with natural occurrences. I don't think it is the intention of regulators to own that problem at this stage. But there's certainly a dialogue there, even though this product is not regulated.

## Q - Doug Young {BIO 5640851 <GO>}

Okay. It doesn't seem like there's any additional further push at this point.

## A - Charles Brindamour {BIO 7012323 <GO>}

No. I think the thing will need to be very careful about this that if the reaction to these storms is too abrupt. And you end up with meaningful availability issues in a number much markets, well, then you you call to a certain extent for greater supervision and I trust my competitors to understand that. But overall, there's no sense that I have that there's an intention to regulate that product at this stage. Definitely the intention is to cooperate and make sure the awareness is pretty high across the country.

## Q - Doug Young {BIO 5640851 <GO>}

Okay. Then just, Mark, I just want to clarify. You talk about the MCT being negatively impacted by six point from CAT. But yet I mean you were profitable in the quarter. I'm just trying to understand how the CATs -- was there a change in your reserve requirements as a result of the CATs?

## A - Mark Tullis {BIO 4180270 <GO>}

Sure. Okay. So I think on the slide we talked about seven points of MCT due to elevated CAT losses. What that consists of, if you take the net costs of the CATs in the quarter, net of tax which is CAD123 million. And just reduce the available capital by the CAD123 million that costs six points of MCT. Now we also had to set up those reserves. And so then we have to hold capital on the reserves. That is how you get the extra point. So the six is just mathematically the costs the MCT, cash out the door, the extra 1% is capital we have to hold on the reserves. That's how you get to the seven. You are correct. We are earning other underwriting income. And we are paying dividends and we are doing other normal things.

So I think if you look on Slide 13, in the deck where we do the sort of abbreviated reconciliation, the intent here was just to show the unusual items in the quarter. So the unusual items being the CAT losses, the share repurchase and the movement in the OCI. The normal stuff, like the normal underwriting income and dividends and stuff, we didn't include that.

## Q - Doug Young {BIO 5640851 <GO>}

Okay. All right. Thank you very much.

## A - Charles Brindamour {BIO 7012323 <GO>}

You're welcome.

## Operator

Your next question comes from the line of Tom MacKinnon from BMO Capital Markets. Your line is now open.

## Q - Tom MacKinnon {BIO 2430137 <GO>}

Yes. Thank you. Good morning.

## A - Charles Brindamour {BIO 7012323 <GO>}

Good morning, Tom.

## Q - Tom MacKinnon {BIO 2430137 <GO>}

I've got a couple questions. The first one is when you pre-announced. And I got on the call late so you might -- maybe I missed this, when you pre-announced, I think you had CAD0.92 in terms of --

## A - Mark Tullis {BIO 4180270 <GO>}

Yes.

## Q - Tom MacKinnon {BIO 2430137 <GO>}

What I would call CAT hits. And then there's CAD0.79 in the quarter. So what's the difference in there?

## A - Mark Tullis {BIO 4180270 <GO>}

CAD0.79 is Calgary only. CAD0.92 is Calgary plus the other CATs in the quarter.

## Q - Tom MacKinnon {BIO 2430137 <GO>}

Yes. But I think the CATs in the quarter, don't they just sum up to the -- the CATs that you noted in the quarter were they -- did they all sum up just to the CAD0.79, or did they sum to the CAD0.92, or is there something different in tax rates? I can take this offline but --

## A - Dennis Westfall {BIO 15155973 <GO>}

I can quickly walk you through. The CAD136 million is the current year CAT level. You add to that the CAD31 million reinstatement premiums that we talked about earlier gets you to CAD167 million, about a 26 and a half point tax rate. And there's a 133 million shares in the quarter gets you to the CAD0.92. Calgary was CAD105 million after-tax which is CAD0.79 a share.

## A - Mark Tullis {BIO 4180270 <GO>}

Yes, I think it's the reinstatement premium.

## Q - Tom MacKinnon {BIO 2430137 <GO>}

Okay. That's probably it, then. Okay. Great. Okay. Thanks. Now, the second was have you quantified, maybe I missed this. Did you quantify the -- some of the action you're going to be taking in terms of tightening terms and price hikes with respect to personal property? Did you -- are you able to quantify what the improvement would be to the combined ratio in this. And over what time we might be able to get it?

## A - Charles Brindamour {BIO 7012323 <GO>}

Ten points.

## Q - Tom MacKinnon {BIO 2430137 <GO>}

Okay. Then over what time we'd be able to get that?

## A - Charles Brindamour {BIO 7012323 <GO>}

Look, we're taking actions will start in the coming weeks taking effect this fall. As you know, the renewal process, you need 60 days, really, to put that in the machine and send the renewals out. So that will start -- when we think about our action planning, there's two phases. There's an immediate phase that will start this fall. And then there's a broader product and offer phase. So to speak, that will start in Q1-2014. These are meant to take effect in the coming 12 to 24 months.

## Q - Tom MacKinnon {BIO 2430137 <GO>}

Okay. And this would all be on ex-prior year and year ex-CAT basis, ten points.

## A - Charles Brindamour {BIO 7012323 <GO>}

Well no, not ex CAT. I think that's the key.

## Q - Tom MacKinnon {BIO 2430137 <GO>}

Well assuming you had a normal level of CATs. But I guess we just -- the issue is we don't know what a normal level of CATs is.

## A - Charles Brindamour {BIO 7012323 <GO>}

Tom, if you look at the past three years the non-CAT combined ratio was improved dramatically. I would say 15 points, in fact, steady. Very clear. So what we're after now. And what we've been after in the past 12 to 18 is to tame the consequences of CAT, the levels of CATs. And the volatility that this creates so that our ability to run the business at 95% is not hampered by CATs every three years, basically.

And so we're taking an action on, a number of actions on a number of fronts to achieve that. The difference between this time and previous action plan is we're going coast-to-coast with these actions. You know, our approach has perils-driven depending on the province in the past. You know, focus on hail in Alberta. And so on. Now, we're saying, "You know what? Who knows where hail will happen next? Who knows where a flood will happen next?" We're going coast-to-coast with deep changes in our offer, as well as pricing. And that's starting this fall. .

## Q - Tom MacKinnon {BIO 2430137 <GO>}

Okay. I guess I could paraphrase that, that if you like to think of these events as being sporadic. And I don't know, one in a hundred, or ten in a thousand; however, you want to look at them do we actually you're going to limit some of the variants. But if of you have what would be a normal level of CATs. And that's really hard to define, then you would probably find your accident year ex-CAT loss ratio improve. Am safe in saying that?

## A - Charles Brindamour {BIO 7012323 <GO>}

That may be. I think if we say this year for instance is a freak year, because things came at us from everywhere at the same time. One should not expect to see that every year. First thing we're saying is that we're trying to protect our offer in every region, in every business, to mitigate the impact of those sort of events. Now, when that doesn't happen, or when you have a normal level of CAT, in theory, your results should be better, because you're protecting yourself against events that will materialize once in a while.

## Q - Tom MacKinnon {BIO 2430137 <GO>}

And given that the personal property, this is all just in personal property. And I guess given that it's about 25% of the business, we should probably see a two to three point -- that would translates just into a two to three point improvement over the Company, overall, I guess.

## A - Charles Brindamour {BIO 7012323 <GO>}

I think that's a fair statement. Then I think you need to ask yourself do I think that the CAT levels, going forward, will be higher than they've been in the past given what we've seen this summer, you know. And I think it's early for us to make a call there. But it's not early for us to protect our business in that regards.

## Q - Tom MacKinnon {BIO 2430137 <GO>}

Appreciate that and I think that's being proactive. With respect to commercial, I think I'm seeing firming in 25% of the industry. Can you elaborate that? Is that certain parts that you're seeing it in. And how are you positioned in those segments. Then you did talk about taking some action in terms of commercial and product offerings. If you can elaborate a little bit on that and want -- how that might improve your accident ratios, ex-CAT, for the commercial lines.

## A - Charles Brindamour {BIO 7012323 <GO>}

I'll ask Alain take this one, because it's focused on that.

## A - Alain Lessard {BIO 17592535 <GO>}

Okay. Thank you very much, Charles. So just rephrasing what we're seeing is we expect the market to firm up on what we see as being 25% of the market, which is the worst part of the market, underperforming. And that's coming from discussion and everything that those classes are underperforming all over the market. If I talk, specifically, about what we did at Intact, we did in the Second Quarter increase. And I would say mid-teen -- by mid-teen digit, you know. Those classes of business, that 25%. So we did increase the new business. But what we saw at the same time on this was a drop in our closing ratio. The closing ratio is how often when we get a quote are we successful.

So basically, like a mid-teen increase over that 25% of the book translated in like 2.0-3.5% increase on new business. And we saw the closing ratio drop by 2%. So that tells us that currently there's still, at that point, there was still a very competitive market. There was still plentiful capacity. So we're not seeing it turn immediately. What we're going to be starting. And what we're starting in August, is to do similar situation on our renewal book of business. So starting to push significant increase or important increase on the same classes of business.

We'll have a better view with what's happening at the end of the Third Quarter. We'll have a better view on how successful we were, what will be the -- what will that happen on the retention ratio. But at the same time, what we saw with the catastrophe or the events in the last few weeks, either Calgary or Toronto, these are additional, I would say, pressure point on the industry to a little bit sober up the level of competition. And re-question the underwriting and the situation on those line of business. And that builds against the confidence that we will see in the next, probably, quarter the market start to turn but it's difficult to predict exactly when.

## A - Charles Brindamour {BIO 7012323 <GO>}

So bottom-line, Alain, is that we're pushing on a quarter of the portfolio double-digit rate increases.

## A - Alain Lessard {BIO 17592535 <GO>}

Yes.

## A - Charles Brindamour {BIO 7012323 <GO>}

We'll -- we did that at new business; now we'll do that at renewal. You know that we're getting a couple of points of rate increases, already, in our portfolio. So what is happening in the market with these changes should help that situation. But I think the point that Alain is making is that we've seen some compression in our closing ratio by taking those bold moves on the quarter. So there's change. We expect the environment will bring additional change and we're pretty focused at the moment.

## Q - Tom MacKinnon {BIO 2430137 <GO>}

Okay . Thanks for that color. Then one final one for Mark. I'm trying to look at how much the MCT would go up, quarter over quarter, on a -- if everything was kind of normal and you didn't have any AOCI noise, quarter over quarter. Obviously, that quarter will never happen. But what would be the normal run-rate of the MCT? I assume it would have to go up a little bit.

## A - Mark Tullis {BIO 4180270 <GO>}

Yes I would say if there was no noise. And it was a typical quarter, maybe a couple -- one or two points up, something like that.

## Q - Tom MacKinnon {BIO 2430137 <GO>}

One or two points up, quarter-over-quarter.

## A - Mark Tullis {BIO 4180270 <GO>}

But obviously, there would be seasonality. We would pay out more cash in Q1. So there's kind of more of a drop from Q1 to Q2.

## Q - Tom MacKinnon {BIO 2430137 <GO>}

Yes.

## A - Mark Tullis {BIO 4180270 <GO>}

It varies from quarter to quarter. But if you looked at it over the course of the year it might be six points or something like that.

## Q - Tom MacKinnon {BIO 2430137 <GO>}

That's great. Thank you.

## Operator

(Operator Instructions) Your next question comes from the line of Mario Mendonca from Canaccord Genuity. Your line is now open.

## Q - Mario Mendonca {BIO 2450557 <GO>}

Good morning.

## A - Charles Brindamour {BIO 7012323 <GO>}

Good morning, Mario.

## Q - Mario Mendonca {BIO 2450557 <GO>}

A quick question. Charles, you referred to not really seeing any trends in personal in current year claims ratios or that core claim ratios. But over the last four quarters we have seen a year-over-year increase in that core claims ratio. So what I'm trying to understand here is with four consecutive quarters under your belt of an increase, what gives you confidence in saying that there isn't some sort of trend emerging here?

## A - Charles Brindamour {BIO 7012323 <GO>}

When you look at -- so we're talking personal auto?

## Q - Mario Mendonca {BIO 2450557 <GO>}

Right.

## A - Charles Brindamour {BIO 7012323 <GO>}

When you look at first six months of 2013 versus first six months of 2012, you're seeing very mild frequency increase, a little more than a point. You're seeing mild severity increase of a couple of points, which is not too far from the drift in the value of the insured car pool.

## Q - Mario Mendonca {BIO 2450557 <GO>}

Yes.

## A - Charles Brindamour {BIO 7012323 <GO>}

I think the other thing that one needs to take into account is the areas where we have seen movement, we're pricing for it. So I think what we're seeing is -- we're not seeing anything new or anything that was not anticipated emerging in the market at the moment.

## Q - Mario Mendonca {BIO 2450557 <GO>}

Okay. So if this were to persist, if the core claims ratio were to increase year-over-year for another say 12 months, what would that then indicate? That there -- pricing increases would be necessary or you need to do more on the costs front? Because, presumably, this can't go on for too much longer before it becomes a problem.

## A - Charles Brindamour {BIO 7012323 <GO>}

No. Fair enough. I think that's exactly what this would mean, that one would need to reflect that trend in pricing so as to insure that, once you know it is a trend, that you're actually pricing for it.

## Q - Mario Mendonca {BIO 2450557 <GO>}

But you just -- I guess, you're saying you're just not there yet.

## A - Charles Brindamour {BIO 7012323 <GO>}

Well I think, Mario, if we look at the areas that we have talked about in the past six to nine months. Alberta was one of the areas where we said, "You know what? We are seeing things that are different than what we anticipated as a result of number of court decisions. And so on on the BI front." We did reserve adjustment in Q4 and we have taken rate and we will take rate the second time as a result. So you know there are a number of areas where rate actions are being taken, number of areas where costs actions are being taken, to react to the things that we have observed in the past 12 months.

## Q - Mario Mendonca {BIO 2450557 <GO>}

Another question then. The mediation cases are down, significantly and obviously, arbitration is up. Have you learned anything from the mediation, or early arbitration, that tells you, that informs your call on reserve development? Have you learned anything new?

## A - Mathieu Lamy {BIO 15207469 <GO>}

Not learned anything new. I would say it sort of declines or removes some uncertainty the fact that the backlog is down. But I think it's largely unfold as we were expecting.

## A - Charles Brindamour {BIO 7012323 <GO>}

Yes.

## Q - Mario Mendonca {BIO 2450557 <GO>}

Okay that's important. Then finally, for Mark, on buybacks. The MCT, below 200, you're giving us some comfort here that it will be between 195% and 200% what I'm not sure about is has the Company repurchased stock in the past when the MCT is below 200%? Would that be and unusual thing.

## A - Mark Tullis {BIO 4180270 <GO>}

So we -- I would say it wouldn't be unusual if we buy it below 200%. I think what we intend to do is manage the MCT level between the 195% and 200% range. And share buyback is sort of one of the variables in that determination.

## Q - Mario Mendonca {BIO 2450557 <GO>}

So does that necessarily mean that buybacks have to sort of cool it for a little while, because the buybacks in this quarter would have taken the, I think the -- in your presentation I think you said it's five points.

## A - Mark Tullis {BIO 4180270 <GO>}

Correct.

## Q - Mario Mendonca {BIO 2450557 <GO>}

Does that necessarily. And if you're adding, as you described to Tom in answering his question, you're adding say two a quarter, doesn't that necessarily mean the buyback has to be a fair bit smaller or not at all in the near-term?

## A - Mark Tullis {BIO 4180270 <GO>}

I think there's a lot of variables in a lot of levels including to what happens to OCI; what happens to underwriting some other levels there. You know, one of the levers is what we do with the buyback.

## Q - Mario Mendonca {BIO 2450557 <GO>}

Okay. Thank you.

## Operator

Your final question comes from the line of Bryan Brown from Macquarie Capital. Your line is now open.

## Q - Bryan Brown {BIO 16358540 <GO>}

Thanks. Just two quick questions. The first one for investment income. I saw that increased, sequentially, by about 6%, while the market-based yield declined by about 20 basis points. Could you explain the decrease, or the increase, sorry, in the investment income?

## A - Mark Tullis {BIO 4180270 <GO>}

Sure. So I think the market-based yield was up. If you look -- I think the best way to look at that is quarter-over-quarter. So it was 3.4 last quarters and 3.8 last quarter. The -- and so -- and that's a bit of an odd calculation because it's our -- what we -- the income we earn divided by the market value of the asset. So the reason for that increase, that it went from 3.4 to 3.8 is the market value of the assets went down due to the increase in interest rates and the decline in market value of the share portfolio. I think the best way to look at this is, in my comments I gave the advice that we expect investment income to remain relatively the same the second half of the year as the first half the year. I think, because as the market values go up and down, it's going to impact the market-based yield but not really so much impact the investment income.

## Q - Bryan Brown {BIO 16358540 <GO>}

Okay. Thanks. And just one last one. In personal auto, for the last two quarters we have seen some pretty large prior claims development. And if you could explain what's driving that.

## A - Charles Brindamour {BIO 7012323 <GO>}

You want to take this Mark or --

## A - Mark Tullis {BIO 4180270 <GO>}

You know, we've seen about 5.5% favorable development in our relationship with premium anyways. And the -- in the Second Quarter. A little more than that year-to-date. And we've seen favorable development in automobile insurance across many of the jurisdictions in which we operate would be my first sort of perspective. We have seen some of it in Ontario automobile. I think that I've mentioned before that in Ontario automobile, we're seeing probably more development in the field, favorable development in the field, than what we let flow through, because we want to be conservative here. It's still early in the game. There's still uncertainty and so we are seeing that across jurisdiction. Clearly, we're seeing some in Ontario. But I do believe that we remain conservative despite the fact that there is favorable development in that province.

## Q - Bryan Brown {BIO 16358540 <GO>}

Okay. Thank you. That's it for me.

## Operator

You have no further questions in queue. I turn the call back to Mr. Westfall for closing remarks.

## A - Dennis Westfall {BIO 15155973 <GO>}

Thank you, everyone for participating. The Webcast will be archived on our website for one year. The telephone replay will be available at 2:00 PM until Wednesday, August the 7th. The replay number is 1-855-859-2056. And the passcode is 11292411. A transcript will also be made available on our website. Please note that our Third Quarters results will be released on November 6th. Thanks and have a great day.

## Operator

This concludes today's conference call. You may now disconnect.