Q3 2012 Earnings Call

Company Participants

- Alain Lessard, SVP, Commercial Lines
- Charles Brindamour, CEO
- Dennis Westfall, Vice President, IR
- Mark Tullis, SVP & CFO
- Martin Beaulieu, SVP, Personal Lines

Other Participants

- Andre Hardy, Analyst
- Bryan Brown, Analyst
- Doug Young, Analyst
- Mario Mendonca, Analyst
- Paul Holden, Analyst
- Tom MacKinnon, Analyst

Presentation

Operator

Good morning, ladies and gentlemen. My name is Ryan. And I will be your conference operator today. At this time, I would like to welcome everyone to the Third Quarter results conference call. All lines have been placed on mute in order 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 your Vice President of Investor Relations, Dennis Westfall.

Dennis Westfall {BIO 15155973 <GO>}

Thank you, Ryan. 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 a disclaimer on forward-looking statements which also applies to our discussion on the conference call today.

Here with me today are Charles Brindamour, Chief Executive Officer; Mark Tullis, Chief Financial Officer; Martin Beaulieu, Senior Vice President, Personal Lines; and Alain Lessard, Senior Vice President, Commercial Lines.

We will start with formal remarks from Charles and Mark, followed by a Q&A session. Martin and Alain will also be available to answer your questions during the Q&A session.

With that, I will ask Charles to begin his remarks.

Charles Brindamour {BIO 7012323 <GO>}

Thanks, Dennis. This morning we announced a Third Quarter net operating income of CAD122 million or CAD0.89 per share, despite incurring more than CAD1.00 a share in net losses from weather-related events. The CAD1.02 in losses from weather is comprised of CAD0.97 for July and August within our preannounced range of CAD0.85 to CAD1.00.

Overall, we reported a combined ratio of 95.9% as a very strong performance from our commercial lines businesses and solid underlying results in personal lines somewhat offset these weather-related losses.

Our 47% top line growth reflects the strong retention we've maintained on the AXA Canada portfolio and one month of premiums from our recent JEVCO acquisition. We continue to experience retention in the AXA book that is comparable to that of the Intact portfolio.

Our underwriting performance and steady investment income resulted in an operating ROE of 16.4%, while book value per share was up 10% from a year earlier.

Our outlook for the industry remains unchanged from a top-line perspective as recent industry results have played out largely as we anticipated. Going forward, we continue to expect mid single-digit overall growth for the industry and for personal property to be the primary driver of rate increases, reflecting the ongoing trend of severe weather patterns. The low interest rate environment should support our outlook and will likely lead to firmer conditions over time.

We expect an improvement in the industry combined ratio to be partially offset by a reduction in the level of investment income. The resulting industry ROE is likely to improve from 6% in 2011 to the upper single digits in 2012. We believe we'll continue to outperform the industry's ROE by more than 500 basis points in the periods to come.

Turning to Ontario auto, we continue to see the benefits of the reforms in our claims actions. Although the industry made some headway in reducing its mediation backlog, now down 5% from January, a meaningful backlog remains leading to uncertainty around the ultimate impact of these reports.

The Ontario regulator, FSCO, is proactive and is now in a position to substantially increase its capacity to handle mediations and arbitration. This should contribute to greater clarity throughout 2013. We expect our own mediation backlog, down 30% since the start of the year, to decrease at a faster pace than the industry in the coming months.

The industry's loss ratio in Ontario auto, the first half of 2012 improved by close to 10 points over 2011, largely reflecting the benefits of the reforms. Though improved, this still reflects a combined ratio of approximately 100%, indicating that a number of industry players continue to be in a loss position.

The recently-announced political changes in Ontario and the prorogation of the legislature creates uncertainty as to the timing of upcoming changes such as that of the definition of catastrophic impairment and other proposed measures from the anti-fraud task force.

I mentioned previously that these changes would influence the rate environment for 2013. Given the uncertainty around these changes and the improvement in the industry's results, we can expect industry premiums in Ontario to be up in the low single-digit range in 2013.

In personal property, benefits from past actions to improve results were more than offset by the elevated level of weather-related losses, resulting in a combined ratio of 119.8% in the quarter. On a year-to-date basis, our combined ratio is now 102.8% in personal property.

We believe that our actions over the past few years did, indeed, bring about 15 points of improvement for which they were intended. More recently, however, the impact from catastrophes has been higher than in the past, resulting in reported combined ratios that are higher than what is acceptable to us. Although we've experienced elevated losses from severe weather across the country, the situation has been most evident in Alberta.

We've talked about an expected run rate of Cats between CAD30 million and CAD40 million per quarter net of reinsurance in the past. Our approach to personal property now assumes that Cats will fall in the upper end of this range on an ongoing basis. As such, we will implement a number of actions and product changes, realizing that rate increases alone will not mitigate against losses from future catastrophe events.

We are committed to operating our personal property business at a combined ratio of 95% or lower. Should cats remain at the levels observed in the past couple of years, it will take up to 24 months for our actions to fully impact the bottom line.

Pricing conditions in commercial lines remain soft, especially on new business. But we maintain our focus. As a matter of fact, our retention remains strong. And we are experiencing low single-digit rate increases on renewals across the country for the third year in a row now.

Turning to our integration of AXA Canada, we are completing the renewal processing for personal lines and commercial lines. Specialty lines conversion is now underway and will proceed over the next 12 months. As such, I am very comfortable saying that our integration is on track. And I want to thank all our people from coast to coast for the hard work in ensuring that both our customers and brokers continue to receive top-notch service.

The addition of JEVCO enables us to strengthen our offer to brokers and customers by broadening our product offering into areas where we were underrepresented, primarily recreational vehicles, commercial and specialty lines. And non-standard auto insurance.

In planning for the JEVCO integration, a key principle was to ensure that there will be no disruption to the AXA integration nor to the high level of service we currently provide to brokers and customers.

As you know, we closed the JEVCO transaction in early September. And as of late last week, we begin renewing the JEVCO business on our own platform with effective dates of January 2013.

In conclusion, the resilience of our operating results was again illustrated as we recorded an operating ROE of 16.4%, despite severe weather. Given the quality of our operational platforms, the flexibility provided by our financial position and the additions of AXA Canada and JEVCO, we strongly believe we'll continue to outperform the industry and strengthen our position in the Canadian market.

With that, I will now turn the call over to our CFO, Mr. Tullis.

Mark Tullis {BIO 4180270 <GO>}

Thanks, Charles.

This morning we announced operating income of CAD0.89 per share, a strong result on the heels of the severe Calgary hailstorm. Despite elevated weather-related losses, an exceptional performance from our commercial lines business led to a combined ratio of 95.9%.

Our operating return on equity improved more than 2 points to 16.4%.

Slide eight and nine show results by line of business. In personal auto, premium growth was 36% year over year, reflecting the addition of AXA Canada and one month of JEVCO. As AXA had a larger proportion of lower-premium Quebec business, our unit growth was stronger than the premium growth. At 94.9%, our combined ratio was 8.5 points higher than last year's exceptional 86.4%, driven by a CAD39 million increase in Cat losses, less favorable prior-year claims development. And a CAD9 million increase in non-Cat weather-related losses.

In personal property, the Calgary hail storm contributed to an overall level of Cat losses of CAD81 million, resulting in an underwriting loss of CAD73 million and a combined ratio of 119.8% for the quarter, 102.8% year-to-date.

Because of the unacceptable recent results, we have established actions to be implemented in the first half of 2013 aimed at mitigating our exposure to catastrophic events. These actions are necessary steps to ensure that our property business operates consistently below a 95% combined ratio, even if topline growth is hindered in the near term.

AXA's contribution was, once again, most evident in our commercial lines business with premium growth at 78%. Commercial underwriting results were unusually strong with commercial auto at 77% and commercial P&C almost 19 points improved year over year to 81.4%. Results in commercial P&C tend to be volatile on a quarterly basis. And this particular quarter had several items in the right direction with elevated levels of favorable prior-year development, fewer cat losses and a lower-than-average level of large losses.

Our year-to-date general expense ratio was 10.3% compared to 11% in 2011. And the decrease is due both to AXA-related expense synergies, as well as the AXA business mix. This quarter the ratio was 9.1%, lower than the year-to-date figure due to the normal seasonality as well as timing.

On the investment side, net investment income of CAD92 million in the Third Quarter was up 24% from a year ago due to the additional investments related to AXA Canada and one month of income from JEVCO, which contributed CAD2 million of income for the month on assets of approximately CAD1 billion. Declining yields continue to impact investment income. And aside from adding a full three months of contribution from JEVCO, we expect this trend to continue in the coming quarters.

Our financial position remains solid at the end of Q3 with a MCT of 201% and CAD598 million in excess capital, while our book value per share was up 10% from a year ago.

On the financing side, we successfully issued an additional CAD50 million of medium-term notes in response to strong investor demand. As a result of the conversion of the subscription receipts related to JEVCO into common shares, our debt-to-capital ratio is now 19.5%, slightly below our target of 20%.

The integration of AXA Canada continues to be on track. We remain comfortable with our target of CAD100 million in after-tax synergies and are on plan with a CAD45 million run rate thus far in 2012. We expect a CAD50 million run rate by the end of the year as occupancy savings and internalization of claims functions take hold. We are also on track with respect to restructuring and integration expenses.

The JEVCO transaction closed in early September. And as Charles mentioned, we've already begun renewing business on Intact systems. We expect the deal to be slightly accretive to net operating income per share in 2013.

Annual synergies amounting to CAD15 million after-tax are expected from a combination of external lost adjustment expense reductions, shared services savings, reinsurance and systems-related cost savings. We expect our run rate to be close to this level by the end of 2014.

In summary, we're pleased with the significant progress we have made to date on the AXA integration and look forward to similar success with the integration of the JEVCO business. We believe our solid financial position and disciplined approach to the business provide a strong foundation for continued growth.

With that, I'll turn the call back to Dennis.

Dennis Westfall {BIO 15155973 <GO>}

Thanks, Mark. Ryan, we are now ready to take questions.

Questions And Answers

Operator

(Operator Instructions) Andre Hardy, RBC Capital Markets.

Q - Andre Hardy

Two questions, the first is a quick one. The weather more in Ontario than anywhere else related to Sandy last week, what impact would that have had on the Company?

But my second question is a little more big picture and more important, I think. It's clear if you look at the quarter, that commercial lines did better than normal. And personal lines in home insurance did worse than normal. It's not clear from your commentary what you think about auto outside of potential for reserve releases. When you look at your profitability on an accident-year basis today in auto, are you satisfied with that. And are you trying to grow the top line as opposed to improve the combined ratio specific to auto insurance?

A - Mark Tullis {BIO 4180270 <GO>}

Andre, let me handle the Sandy question. We expect the impact to be fairly minimal on our results. As you know, we have a Cat threshold of CAD7.5 million. It may qualify as a Cat. But it wouldn't be much more than that.

A - Dennis Westfall {BIO 15155973 <GO>}

Alain, do you want to comment on automobile insurance?

A - Alain Lessard {BIO 17592535 <GO>}

And automobile insurance, we are positive about the perspective of that product. There is -- we're adequately priced in all provinces. We have a stability in all provinces. Ontario still has a bit of uncertainty due to the backlog and mediations and a few cases that have passed into the court system that are weakening the Cat definition. But overall, we are very positive about automobile.

A - Charles Brindamour {BIO 7012323 <GO>}

I think that is right, Andre. You see 94.9% combined ratio on that line of business for the quarter and 93% year-to-date. There is in the quarter about 6 points of Cats in the combined ratio. So I feel pretty good about the performance of automobile insurance. And we're certainly in a growth mindset in that line of business and every jurisdiction in Canada at this stage.

Q - Andre Hardy

That's very clear. Thank you.

Operator

Doug Young, TD Securities.

Q - Doug Young {BIO 5640851 <GO>}

Ontario auto, as well. Charles, you mentioned you are pretty confident you can lower your mediation backlog faster than the industry. I'm just curious what you are doing different than the industry to do so.

A - Charles Brindamour {BIO 7012323 <GO>}

Well if I just comment on the past nine months, I think that, as I've mentioned in my remarks, the industry's backlog is down 5; ours is down 30. At one of the main reasons why our backlog is down to a greater extent is that we have been, I think as far as FSCO is concerned. And it's been their comments to us, we have been way more aggressive than our peers in embracing some of the changes that they've brought to the process such as electronic schedulings of mediations and those sorts of things.

So that is definitely an area that has made a big difference for us and just being very proactive at dealing with the backlog and trying to settle before we end up in mediation.

So that's the first historic context.

Then prospectively, when I look at the pattern of FSCO scheduling mediations in the coming months, my sense in talking with FSCO is that we'll have a greater proportion of scheduled mediation than our peers, just by the nature of how we're positioned in terms of average date of these claims.

Q - Doug Young {BIO 5640851 <GO>}

Okay. Then just on Ontario auto as well, back to something Andre was mentioning, your current year combined ratio in auto did, by my calculations, deteriorate 2 points in the quarter. And I'm just wondering, is there something abnormal in there, or is there anything concerning?

A - Charles Brindamour {BIO 7012323 <GO>}

I think there's a number of things there and nothing much concerning, Doug. I think that there's a few -- a couple of points of prior development less than last year. But that being said, there's 2.5 points of prior-year development in automobile insurance, roughly, ballpark. So less prior-year development. But still a decent level of prior-year development.

There is in our view, year on year in that line of business, non-Cat weather-type effect, causing about CAD9 million worth of worst performance in automobile insurance. So nothing that I'm concerned about, Doug, on that front.

Q - Doug Young {BIO 5640851 <GO>}

There's nothing by province that is drastically different? Obviously this is a combined number. But I'm talking Alberta relative to Ontario or what -- there's nothing in there that sticks out to you as concerning, then?

A - Charles Brindamour {BIO 7012323 <GO>}

Well yes, when I look at -- well, not concerning but in terms of explaining the numbers, when I look at the frequency by province, Doug, we see that our frequency in Ontario and Quebec in the quarter was down, while our frequency in Alberto was up meaningfully 9%. And this talks to a certain extent probably of the non-Cat weather impact. But overall frequency in Alberta is up. And that's not something that over a three-month period you would necessarily become concerned about.

Q - Doug Young {BIO 5640851 <GO>}

Then just related to the definition of catastrophic claims, obviously I think the view was that that would be settled this fall. I'm going to assume that that is not necessarily the case any longer. But correct me if I'm wrong. And I know you mentioned it in your comments. Can you update us in terms of what your expectations are for that particular issue?

A - Charles Brindamour {BIO 7012323 <GO>}

Yes, I guess if we talk theory, the changes to the cat definition would not require necessarily legislative action because it can be dealt with through regulation. So in theory, the notion that the Parliament is prorogued is not necessarily in theory an impediment to the cat definition being ruled out.

In practice, the government is in a state of transition at this stage. And so to what extent will that move forward is where I certainly have a level of uncertainty. And I'm sure what your perspective would be here.

A - Martin Beaulieu {BIO 15316652 <GO>}

Now, I think we are in a wait-and-see mode at the moment.

A - Charles Brindamour {BIO 7012323 <GO>}

That is it.

A - Martin Beaulieu {BIO 15316652 <GO>}

We have no signs that this is not going to happen. But the timing I think is --.

A - Charles Brindamour {BIO 7012323 <GO>}

Yes. But I think we're just being pragmatic in looking at the fact that you have a transition in government that takes some will and courage to a certain extent even through regulation. So we are personally not counting on that at this stage when we think about the Ontario auto market. So that would be very good for Ontarians if that came true.

Q - Doug Young {BIO 5640851 <GO>}

Okay. And just lastly. And then I will re-queue, OSFI is obviously looking to increase capital requirements. And I think that's related to earthquake-related risk. But again, correct me if I'm wrong. And I know you mentioned in your release that you think there could be a slight negative impact. Can you quantify it at all what that impact might be from the changes coming in next year. And what changes are you making potentially to mitigate some of that impact?

A - Mark Tullis {BIO 4180270 <GO>}

Yes. So I think a couple of things. The big thing -- so nothing major in the near term. There are some issues with regard to changing the factor for the interest sensitivity factor, which will be graded in over a few years.

But again, that is going to be graded in over two years. We see a couple of points per quarter, nothing else being the same. I think it's important to point out on all this stuff, we plan for the changes. And so it's not -- it's hard to say exactly what that change in effect will have because we will take mitigating factors to offset to some degree.

A - Charles Brindamour {BIO 7012323 <GO>}

Yes and let me comment on the earthquake change that is being contemplated. There is sort of a draft on the table now that would start to look at what we call PMLs or probable maximum loss on a national basis as opposed to a local basis, which would effectively increase requirements either from a reinsurance point of view or from a capital point of view. And I'd like to make a few points on that.

The first point is that we tend to reinsure to a greater extent than our peers to start with.

Second of all, we don't think this proposed change makes sense. And therefore, it is subject of discussions at the moment with us -- so I'm not sure where this thing will end. But what I know, though, is that when OSFI lands on a framework, it will be implemented over a period of six or --

A - Alain Lessard {BIO 17592535 <GO>}

10 years.

A - Charles Brindamour {BIO 7012323 <GO>}

10 years, I think. There you go.

So that is the OSFI story. I would say though, that regardless of that, I've talked about our earthquake exposure and the fact that we spent way more on reinsurance last year to increase our reinsurance cover. We are proactively working on the West Coast to reduce our exposure through pricing and underwriting actions, regardless of where OSFI is going.

So when you put that in the mix, Doug, I'm not concerned about where the impact that the OSFI change might have on IFC, though I don't think these changes make complete sense at this stage. And that's why we're working with them to present a different perspective.

Q - Doug Young {BIO 5640851 <GO>}

Okay. Thank you.

Operator

Paul Holden, CIBC.

Q - Paul Holden {BIO 6328596 <GO>}

Two questions. I guess the first on commercial lines. Given the low combined ratios you are getting there, is there the potential to increase your market share both in commercial auto and commercial P&C, or does pricing on new policies sort of prohibit you from doing that?

A - Charles Brindamour {BIO 7012323 <GO>}

So I will let Alain take this one.

A - Alain Lessard {BIO 17592535 <GO>}

Well first, like Mark mentioned, we had a very good quarter on commercial lines. But pretty much everything went in the right direction being either prior development or large losses.

Basically, when you look at the past quarter, we've seen that those lines are fairly volatile, okay, moving from quarter to quarter anywhere between 80% to 100%, or in automobile anywhere 75% to 95%. So overall our view on the profitability of those lines has not changed because of this current quarter.

That being said, we're pushing the growth as much as we can. But the market currently is remaining very, very soft. We are able to push some rate increase on renewal. But on new business, the market is being very soft. In Canada, we're not seeing any of the rate increase we're seeing south of the border in the US and Canada. We are seeing either price levels being the same or slightly decreasing also on new business.

So because of that, we're keeping a very focused and disciplined approach to new business to maintain our profitability margin on these lines of business.

A - Charles Brindamour {BIO 7012323 <GO>}

Yes. These are great lines of business. And Alain talks about the quarterly volatility, absolutely. I think when you look at it year to date, nine months into the year, commercial auto is running at 81%; commercial P&C is running at 90%. Very healthy performance. The more we can grow in that market, the better.

Now our focus at the moment is clearly completing our integration where we have acquired substantial block of commercial lines business, in my view, at a very good time in the market. Our retention has been pretty good. And the upside for us here, post-integration, is to leverage the new product lines.

And so clearly to expand some of these specialty lines, the fact that we have a broader product than we had before the transaction across our distribution network is how Alain and the Intact Insurance team will grow their market share in a competitive new business environment.

I hope you agree with that, Alain.

Q - Paul Holden {BIO 6328596 <GO>}

One follow-up question to that perhaps then is, given the rate increases we're seeing in the US and the soft market in Canada, is there -- are there any specific factors you can point to between those two markets that explains the difference? And is it reasonable to expect that maybe the US is a leading indicator of what might happen in Canada eventually on the rate front?

A - Alain Lessard {BIO 17592535 <GO>}

Our understanding of the basic difference between the Canadian market and the US market is that the rate increase in the US is currently being driven much more by Worker's Compensation, which is a private line in most of the states in the US. While here in Canada, it is nationalized; it is government insurance. So that factor not being present in Canada has an important impact on the difference of behavior on both markets.

A - Charles Brindamour {BIO 7012323 <GO>}

I think just to put things in perspective with regards to the markets, I mean we are -- so new business in many sectors is really quite competitive.

That being said, the retention, you could comment on the retention, Alain, as well. And this will give people a sense of the fact that there is a way to do very good business in that market.

A - Alain Lessard {BIO 17592535 <GO>}

Where basically the retention we have and that's the good thing -- we're experiencing the same retention on the AXA and the Intact portfolio. And if we look at our retention this year premium-wise compared to last year, the retention is up by slightly a point or a little bit around a point in terms of our retention. And we know that the impact on the retention on our growth is much more important than the new business because it gears directly to the portfolio and, on top of that retention, our risks that we have underwritten over the past that we know and for which we have all the information to make the right underwriting.

So focusing on the retention is one way to grow our portfolio right now. And we're quite pleased with what we're seeing.

The new business, like I mentioned and like Charles mentioned, is very much difficult, okay? It varies sector by sector. Some of the sectors we're basically doing a little bit better. But overall there is an appetite in the Canadian market to grow the commercial line business. And that translates in our competitors being very active and going for new business.

A - Charles Brindamour {BIO 7012323 <GO>}

Yes. So no change from where we were before. We're still trying to get rate increases on renewals -- third year in a row now of low single-digit rate increase. And this shows to a certain extent in the strong performance of these two lines of business.

Q - Paul Holden {BIO 6328596 <GO>}

And final question would be related to distribution income. It seems to have become a little bit harder for us to model since the AXA acquisition. Maybe was thinking that Q2 would be a better run rate number. But now we've seen it come down substantially quarter over quarter. Maybe you can provide some comments to help us figure out how we should forecast that going forward?

A - Mark Tullis {BIO 4180270 <GO>}

Sure. And this is a small line of which there does tend to be a lot of volatility. Included in here is income from organizations where we don't fully control some of the timing of how they produce things. It's where we have partial ownership and they produce their own things. So there tends to be a little volatility on how the income is recognized.

I would say if you look at the distribution revenues, the CAD23 million we reported last quarter, is more indicative of an ongoing run rate. I think you should choose view the CAD12 million -- a little bit of timing there as there was timing in Q1 when we reported the CAD32 million. And I would look at the CAD23 million in Q2 as more what the current run rate is, hopefully growing in the future as we continue to grow our distribution relationships.

Q - Paul Holden {BIO 6328596 <GO>}

Good. Thank you.

Operator

Tom MacKinnon, BMO Capital.

Q - Tom MacKinnon {BIO 2430137 <GO>}

Just going back to some of the synergies that we talked, I think we had said we had CAD100 million in after-tax synergies from the AXA deal. You may have mentioned it in the call. But where are we in terms of how much more incrementally would be realized from that?

Then I thought you mentioned on the call some of the annual synergies you expect from the JEVCO deal as well.

A - Mark Tullis {BIO 4180270 <GO>}

Sure. So let me take that one. So yes, we are -- and these are after-tax numbers. So we are looking for CAD100 million of after-tax on AXA. We still have that as a view.

Our view is we will be at CAD50 million at the end of the year. We are at a CAD45 million run rate currently. The reason for the increase from the CAD45 million to the CAD50 million is two things. One, we will incur some occupancy savings as we move some people, primarily in Montreal, into the AXA offices at 2020 University. We can get some occupancy savings there.

The other thing is, on the claim side, we've been internalizing some of the claims expenses. It takes a while to actually realize the savings because the cases actually have to turn over to be handled internally. And we expect to receive some savings found that in Q4, as well.

Then the other CAD50 million of savings will occur throughout next year from a continuation of that sort of thing but primarily from system savings. Once we have converted all the business onto the Intact system, we can begin to shut down legal entities and actually turn off systems. And that is where we get a big synergistic savings.

A - Charles Brindamour {BIO 7012323 <GO>}

Yes and I think next year also a meaningful upside coming on the loss adjustment expense side as well.

A - Mark Tullis {BIO 4180270 <GO>}

Correct.

Q - Tom MacKinnon {BIO 2430137 <GO>}

And the JEVCO?

A - Mark Tullis {BIO 4180270 <GO>}

Yes. We're looking at about CAD15 million of --

Q - Tom MacKinnon {BIO 2430137 <GO>}

5-0?

A - Mark Tullis {BIO 4180270 <GO>}

Pardon?

Q - Tom MacKinnon {BIO 2430137 <GO>}

5-0?

A - Charles Brindamour {BIO 7012323 <GO>}

1-5.

A - Mark Tullis {BIO 4180270 <GO>}

1-5.

Q - Tom MacKinnon {BIO 2430137 <GO>}

Okay, good.

A - Mark Tullis {BIO 4180270 <GO>}

Sorry. CAD15 million of after-tax savings. Again, we expect to achieve that run rate by the end of 2014. And again, it's the same sort of process. We have to convert the business over to our systems and shut off the systems is where we get a lot of the savings there.

A - Charles Brindamour {BIO 7012323 <GO>}

Yes. And we will report on the progress on the CAD15 million next quarter --

A - Mark Tullis {BIO 4180270 <GO>}

Yes, every quarter.

A - Charles Brindamour {BIO 7012323 <GO>}

Because, as you know, we closed in late Q3, early September.

Q - Tom MacKinnon {BIO 2430137 <GO>}

And is there anything you can say about supply chain benefits? I know that when you had an increase with respect to when you bought AXA, you hand to end up buying some more reinsurance. In the end, you said, well, okay, that will be probably be offset by increases in terms of earnings associated with supply chain benefits. What's in the pipe for that. And how can we -- I suspect as you continue to get bigger, there's got to be some benefits from supply chain. Is there anyway we can -- how are we supposed to think about that?

A - Charles Brindamour {BIO 7012323 <GO>}

Well I think that it's pretty clear that the supply chain benefit that comes from applying our deals on the new claims or on the AXA claims more than offsets the additional cost of reinsurance, which was CAD15 million. And I would say that this was toward the end of Q2. This is true at the end of Q3.

Additional upside, of course, comes when you use your full size to negotiate supply chain arrangements that will take place in the coming years. And my advice to better understand that is to come at the Investors Day because we'll spend some time precisely on that topic to give a bit more clarity there and talk about some of the levers that we intend to pull.

Q - Tom MacKinnon {BIO 2430137 <GO>}

Sounds good. Thanks.

Operator

Mario Mendonca, Canaccord Genuity.

Q - Mario Mendonca {BIO 2450557 <GO>}

You've reduced your backlog by around 30% in Ontario. And the backlog has been reduced across the industry. Has there been any indication on the direction of the mediation or arbitration whether it would be more favorable to the industry or to the claimants?

A - Charles Brindamour {BIO 7012323 <GO>}

The bulk of the backlog reduction that has taken place to date was on pre-reform claims. And therefore, with respect to reforms per se, I expect that in the early part of 2013 we'll get a better sense from the mediation output there.

A - Martin Beaulieu {BIO 15316652 <GO>}

And that is true. The bulk of mediations are pre-reform. And in arbitration there have been none that are post-reform as of yet.

Q - Mario Mendonca {BIO 2450557 <GO>}

So in the very few, your message thus then is still too early to tell.

A - Charles Brindamour {BIO 7012323 <GO>}

Well we don't change our view based on what we've seen to date, Mario.

Q - Mario Mendonca {BIO 2450557 <GO>}

Understand. The second question is, I've never heard you refer to non-Cat weather-related losses before. You may have. I just don't recall hearing that. And maybe you can help me understand, what do you mean by non-Cat weather-related and personal auto? I'm not suggesting that -- sorry, in personal property -- I'm not suggesting that everything is weather-related in personal property. But wouldn't the vast majority the weather-related?

A - Charles Brindamour {BIO 7012323 <GO>}

Yes, I think we're talking of weather occurrences where the cumulative loss is less than CAD7.5 million. Like we define Cat when a natural occurrence exceeds CAD7.5 million.

A - Mark Tullis {BIO 4180270 <GO>}

So when there is an event that occurs, we set up a Cat code in our system and we track it. We don't know until the claims come in, whether the event will actually generate claims over CAD7.5 million. If it does, we categorize it as a Cat; if it comes in at CAD5 million or CAD4 million or CAD6 million or whatever, it is not categorized as a Cat. But it is still associated with an event.

Q - Mario Mendonca {BIO 2450557 <GO>}

So the trigger then is it has to be classified as an event first.

A - Mark Tullis {BIO 4180270 <GO>}

Correct.

Q - Mario Mendonca {BIO 2450557 <GO>}

An event would be what? Just super-heavy rain storms or hail?

A - Mark Tullis {BIO 4180270 <GO>}

A hailstorm, that sort of event.

Q - Mario Mendonca {BIO 2450557 <GO>}

Okay. Then finally. And forgive me if you've already answered this question, on integration expenses, they came in a little higher than I would have expected. Can you give us some outlook for the next couple of quarters and how you expect integration expenses to play out?

A - Mark Tullis {BIO 4180270 <GO>}

Sure. On the AXA side, we've given guidance that it would come in more or less at the level of one-year pretax savings. To date, we are proximately CAD129 million. I think we're looking at coming in at the end of the year in the CAD160 million range, perhaps a little more in next year. But that is what we're looking at.

Q - Mario Mendonca {BIO 2450557 <GO>}

Then JEVCO?

A - Mark Tullis {BIO 4180270 <GO>}

JEVCO, I think you could think in terms of a bit larger envelope than 1 times the savings. Because some of the things we have to do, like converting systems, are the same, take the same amount of expense. But we have fewer policies to put them over. So I think you'd look at it a bit larger as a percentage as the cost savings there.

Q - Mario Mendonca {BIO 2450557 <GO>}

Okay. Thank you very much.

Operator

Bryan Brown, Macquarie.

Q - Bryan Brown {BIO 16358540 <GO>}

Just a couple of quarters we've seen some of your competitors aggressively cut their rates in Ontario auto. And I just wanted to know if you saw this as a concern?

A - Charles Brindamour {BIO 7012323 <GO>}

Martin, do you want to comment on that?

A - Martin Beaulieu {BIO 15316652 <GO>}

Yes. Well I think you are probably referring specifically to one player that has reduced rates by high single digits. That player has done that over a number of quarters. And that player in itself was reporting better results than the industry for the past three, four years. So that is not a concern with respect to our competitive potential in the future because when we look at the industry as a whole, we think that the industry still has to continue to adjust by 5 to 10 points. That doesn't create a concern for me at this stage.

A - Charles Brindamour {BIO 7012323 <GO>}

Sure. Same here.

Q - Bryan Brown {BIO 16358540 <GO>}

Okay. Thanks. And just one last question. In terms of expenses, the commissions and the general expenses were quite low this quarter. And I just wanted to know your view on sustainability of the decrease.

A - Mark Tullis {BIO 4180270 <GO>}

Yes. That's a good question. On the general expense side, I think it's a couple of things. So if you look at our year-to-date general expense ratio, it is in the 10.3% range compared with 11% last year. And I would consider the difference between the 10.3% and the 11% to be sustainable. A little more than half of that due to synergies on account of the AXA business coming in. Some of it due to business mix with AXA creating different general expense levels.

If you look at the quarter, it came in at 9.1% versus our year-to-date of 10.3%. I would not consider that sustainable.

I think if you look at the last few years, last year through three quarters, our expense ratio was at 11%. And Q3 it came in at 10.4%. And if you look at 2010, Q3 came in about 50 basis points lower than the full-year expense ratio. So there seems to be a bit of a pattern where we spend a little bit less maybe in the summer months than we do in the rest of the year. So I think you saw some of that this year, plus maybe a bit of timing on top of that.

On the commission side, again, I would view the quarter-by-quarter variations. There's been no change in the commission arrangements. We tend to have timing of CPC or contingent profit commission. So when we, say, have a really good Q1 because of the weather, we tend to see a little bit more accrued, when we see a little more weather-related events in Q3, maybe a little less accrued there.

So I wouldn't view that as a sustainable thing. It's more of it related to the performance of the business and maybe a bit of timing.

A - Charles Brindamour {BIO 7012323 <GO>}

Yes. Think what is sustainable in the improvement and the expense ratio is the synergies.

Q - Bryan Brown {BIO 16358540 <GO>}

Okay. Great. That is it for me. Thanks.

Operator

We have no further questions at this time.

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 p.m. today until Wednesday, November 14. The transcript will also be made available on our website.

Please note that we will be hosting our annual Investor Day in Toronto on November 20. And our Fourth Quarter and year-end results for 2012 will be released on February 6.

That concludes our conference call. Thank you. And have a good day.

Operator

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