Q3 2013 Earnings Call

Company Participants

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

Other Participants

- Asim Imran, Analyst
- Mario Mendonca, Analyst
- Shubha Khan, Analyst
- Stephen Boland, Analyst
- Tom MacKinnon, Analyst

Presentation

Operator

Good morning. My name is Amy and I will be your conference operator today. At this time, I would like to welcome everyone to the Intact Financial Corporation Third Quarter 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 will now turn the call over to Mr. Dennis Westfall, VP of Investor Relations. You may begin.

Dennis Westfall {BIO 15155973 <GO>}

Thanks, Amy. Good morning everyone. Thank you for joining us on the call today. 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; Alain Lessard, Senior Vice President Commercial Lines; and Mathieu Lamy, Senior Vice President of Claims. We will start with formal remarks from Charles and Mark followed by a Q&A session. Martin, Alain. And Mathieu 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. Good morning everyone. Earlier today, we announced the Third Quarter net operating income per share of CAD0.41 despite reporting our first underwriting loss in the last 10 years, driven by extreme weather events. As we announced in September, cat losses from the early part of the quarter amounted to CAD1.52 per share.

From a topline perspective, premium growth of 6% reflects the continued successful integration of Jevco. September marked the first month of purely organic growth that we've reported in two years. Although growth slowed somewhat in the quarter, we believe our action plan can generate low to mid-single-digit growth in 2014.

Our earnings over the past year have generated an operating ROE of 12.7% and a 5% increase in book value per share. From a capital perspective, we are comfortable with our MCT of 199%. And expect it to remain relatively constant through year-end.

As we outlined on our last earnings call, the extreme weather events from the summer have made it clear that the sustainability of home insurance in its current form is being challenged. I indicated then that we must bring meaningful change to that line of business and established an objective of generating 10 points of combined ratio improvement over the next 24 months.

As we have shown in the past, we are quick to act when we feel the bottom line is under pressure. In fact, renewals effective November 1 now reflect our new pricing algorithm, which should lead to average rate increases in the low teens, varying by province.

But we cannot reach our objective with pricing alone. This fall, we began communicating our action plan with brokers from coast to coast. Our plan focuses on ensuring customers have a better understanding of the risks they face and what they can do to better adapt to climate change.

In the coming months, we will implement meaningful product changes, including higher deductibles as well as the introduction of sub-limits. We will also show separate pricing by peril to provide customers with a better sense of the cost of various types of coverage. At the same time, we will offer customers the option to reduce premiums through loss prevention discounts.

As I said, this issue is not one solely affecting the insurance industry. But rather society as a whole. And as such, we are continuing to work with the University of Waterloo to raise awareness amongst communities and to provide guidance as to how they can better protect themselves against the impact of extreme weather.

Moving to automobile insurance, we maintain our positive view on this line of business. 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 continues to be a source of concern with investors. But our view has not really changed.

The government has outlined its timetable for expected rate decreases overall. And it's really what we anticipated as the targeted rate reduction will be phased over a couple of years. What is important now is for the government to come out with the details for the cost portion of the cost and rate reduction strategy. I maintain the view that they understand the importance of meaningful cost reduction measures to ensure availability of the product, given the industry operates near breakeven at the moment.

We are encouraged that the government reaffirmed through legislation during the last quarter that Minor Injury Guidelines are indeed binding. And we continue to work with the government and the Insurance Bureau of Canada to identify additional cost reduction measures that would be effective in the coming years. We expect concrete measures to be announced in the near term.

We are pleased that the mediation backlog in Ontario has been fully assigned and is expected to be cleared by year-end. This really should help alleviate some of the inherent uncertainty in the system.

It's important to bear in mind, though, that a file is not necessarily closed after mediation as the insured could still choose to dispute the outcome in arbitration. Consequently, we have seen the number of arbitrations increase 68% at the industry level during the first eight months of 2013. Due to our proactive approach to managing our files and disputes, IFC's arbitration had increased only 3%. Beyond that, our view of the Ontario market is largely unchanged. And we feel strongly about our ability to grow and outperform in that market.

This morning, we announced the upcoming launch of a telematics-based solution that will allow drivers in Quebec starting this year to save on their annual insurance premiums based on their driving behaviors. We expect to introduce a similar program to the Ontario market in early 2014 and two other provinces throughout next year. We believe this will allow us to attract and reward safe drivers with discounts based on their driving behaviors. And will also contribute to the Ontario government's policy objectives in the coming years.

When it comes to our outlook for the industry, we foresee low single-digit growth in the near term with upper single-digit growth in personal property. And low single-digit growth in personal auto and commercial lines. We continue to expect the current hard market conditions in personal property to accelerate meaningfully for the foreseeable future. We also expect firming conditions in approximately one-quarter of the commercial P&C industry in the near term. The low interest rate environment and elevated losses from catastrophes should support our growth outlook.

Turning to the industry's ROE, we do not expect the industry to reach its long-term average of 10% in 2013 largely due to the elevated cat activity which has already materialized.

Looking specifically at Intact Financial Corporation, we believe we will continue to outperform the industry's ROE by at least 500 basis points.

The benefits from our two most recent acquisitions are undeniable with growth and profitability metrics both exceeding initial expectations. Thanks to extraordinary efforts of our employees from coast to coast, integration efforts have gone very well and are now in the final stages. We remain on track to complete the system decommissioning of AXA in early 2014, with Jevco following shortly thereafter.

In conclusion, I believe the disciplined approach we take towards operating our business will continue to serve us well. I am confident that we will confront new challenges with the same level of transparency and 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 we will continue to outperform the industry and maintain our superior level of profitability.

And with that, I will turn the call to our CFO, Mark Tullis.

Mark Tullis {BIO 4180270 <GO>}

This morning, we reported Third Quarter results greatly impacted by previously announced cats. These losses added more than 15 points to our combined ratio, driving it above 100% for the first time since being a publicly traded company. However, despite the cat losses, we reported net operating income of CAD0.41 per share on the strength of our underlying performance. In fact, this quarter, we reported one of our strongest underlying loss ratios, which excludes cats and prior year development.

Personal property was hit especially hard by the cats. However, we reported a 7 point year-over-year improvement in the underlying results. Although we benefited from relatively good weather outside of the cats, the actions we have taken in this line of business over the past 12 to 18 months are also clearly bearing fruit. And we remain committed to operating our property business at or below a 95% combined ratio.

Part of our plan to improve results is via pricing, where we are taking meaningful rate actions. We realize that this might translate into some loss of units in the short-term. But we believe protecting the bottom line is essential. We are also on track to roll out new product features in the first part of next year.

Losses from cats also impacted our results in personal auto although to a lesser extent than in 2012. This quarter experienced CAD27 million of such losses, down from CAD45 million in Q3 of last year when hail, which hits auto harder, was a larger contributor to cat losses. Our 93% combined ratio was almost 2 points better than a year ago as favorable prior-year development was also quite healthy at CAD56 million.

On a year-to-date basis, our performance remains quite strong with a combined ratio of 91.4%. From a topline perspective, growth of 8% in the quarter reflects the addition of Jevco.

Growth in our commercial lines businesses was 4% versus Q3 of last year reflecting the addition of Jevco. This quarter, the combined ratio of 102.5% in commercial lines was significantly higher than a year ago, reflecting nearly CAD100 million of losses from cats. We continue to expect firmer conditions in commercial P&C, driven by industry groups that represent approximately 25% of the market.

Our expense ratio was higher than last year when we benefited both from a one-time release as well as from favorable timing of accruals. Also this quarter, the accruals, which tend to vary from quarter to quarter, went the other way.

Our net investment income of CAD104 million was 13% higher than a year ago, as we continue to benefit from reinvesting the additional assets from Jevco into our higher-yielding portfolio. Now that the Jevco assets have been fully integrated, we expect investment income will remain flat in the coming quarters, given the continuing low yield environment.

The combination of our underwriting loss and the impact of tax-free dividend income resulted in a negative effective tax rate this quarter. Our tax rate is always higher in quarters with more underwriting income and lower or negative in quarters with less underwriting income.

Our financial position remains solid at the end of the quarter with $515 million in excess capital and book value per share 5% higher than a year ago. Our estimated MCT improved slightly to 199% within the 195% to 205% range previously outlined. The ratio was helped by our earnings in the quarter, improved equity in capital markets. And a slowdown in our share buyback activity. In the absence of unusual events or growth opportunities, we anticipate in the near term our MCT will remain in the 195% to 205% range.

Acquisition synergies remain on track as our integration is near completion. Thought we are not yet done, I want to thank our employees for their hard work over the past two years. With the expertise they now have, we are even better positioned for future opportunities that may arise.

I believe that Intact continues to have a sustainable competitive advantage due to our disciplined approach and quality operations. As this summer has demonstrated, our employees have shown that they will work hard to provide our customers with world-class service even in the face of unprecedented levels of weather events.

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

Dennis Westfall {BIO 15155973 <GO>}

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

Questions And Answers

Operator

(Operator Instructions) Tom MacKinnon, BMO Capital.

Q - Tom MacKinnon {BIO 2430137 <GO>}

Thank you very much. Good morning. Two questions here, Charles. I wonder if you can elaborate first of all on what the tone has been like in terms the dialogue with the government on the cost reduction measures, kind of what you're looking for for implementation. And how you're prioritizing these. And I have a follow-up.

A - Charles Brindamour {BIO 7012323 <GO>}

I think, as I mentioned in my remarks, these guys really understand. I think they're constructive. And they know that cost reduction measures will be critical to ensure that the product is available in the market. I think there's been actually concrete measures that were implemented in August, actually, such as reaffirming that Minor Injury Guidelines are actually binding. And this was done through legislation, which, in my mind, will have a positive impact on the inflation in the system going forward, an important measure to strengthen the impact of the minor injury. We are working with them to provide concrete ideas that can have an impact in the short-term and that are compatible from a public policy objective to be rolled out in the short-term. And just to give you a bit of flavor, I'll ask Mathieu to share with you a number of the ideas that are currently on the table.

A - Mathieu Lamy {BIO 15207469 <GO>}

So I'm working with IBC. We've proposed a few items to the government. We are expecting antifraud or some of the recommendations by the antifraud task force measure to be implemented. We are expecting a review of the ADR process, the mediation process, to help simplify the process and make it more streamlined. Some recommendations were proposed in terms of the MIG guideline, in terms of pre-existing medical conditions, how are they are defined. So a series of measures to help on the cost side, on the Claims side.

A - Charles Brindamour {BIO 7012323 <GO>}

Thanks Mathieu. So Tom, my sense. And I have a fair bit of interactions with folks there, these guys want to do the right thing for Ontarians. I think it is a politically charged environment. But they are approaching the issue from the perspective of Ontarians and Ontario drivers. And I think they want to do the right thing. And so in my mind, people's intentions are well aligned. It is politically charged. I have described to investors that there is a base case scenario where I think we will see good symmetry between cost and rates. Then there are more adverse scenarios where there would be a disconnect between cost and rates. And as I've mentioned before, we have a number of measures that we are ready to act upon should we move in that scenario. But we are certainly not there at this stage.

Q - Tom MacKinnon {BIO 2430137 <GO>}

Okay. Thanks. Then on the telematics, what was the thinking behind the implementation of this? Presumably, it has some sort of a profit motive, or topline growth motive. I'm wondering if you could share what you think would be the impact of that as you continue to roll out this product, not just necessarily in Quebec but in some other provinces in 2014.

A - Charles Brindamour {BIO 7012323 <GO>}

I'll let Martin take that one, Tom.

A - Martin Beaulieu {BIO 15316652 <GO>}

Using telematics in fact is well aligned with what we are about. And that's leveraging our scale. And this is a way to segment even further with new information our pricing and our underwriting. So we are expecting margin expansion through this.

We don't have at the moment an exact impact because it will depend on how the claims side materializes versus these variables. We don't have a lot of data yet -- we anticipate the correlation but we don't have the exact data. And we are expecting as well that, through that segmentation, we will expand our growth in the market. And we are really aligning ourselves with what the Ontario government is trying to achieve, which is reward safe driving behaviors.

A - Charles Brindamour {BIO 7012323 <GO>}

So Tom, this is a profit growth play that we're trying to achieve here. I think; will it move the needle in the short-term? Hard to tell. As far as I'm concerned, I think we have a plan that we are aiming for. I think we will be in a better position to clarify the impact that this will have in the coming 36 months, probably in six months from now, once we get a good sense of the take-up in terms of new business. And then what our existing clients actually choose to do. We will get first a picture in Quebec. We'll likely get a picture in Ontario in the first half this year. I think the rest of the country will see deployments for the rest of the year. It's something that we have been monitoring very closely for many years. I think, as I've mentioned before, we have made a conscious choice not to be the first ones with that. But we had agreed upon a few years back that as soon as somebody has output that, that within 6 to nine months we should be out and that's what we are announcing this morning.

Q - Tom MacKinnon {BIO 2430137 <GO>}

And are there any costs associated with starting up these efforts?

A - Martin Beaulieu {BIO 15316652 <GO>}

The startup costs are minimal. I would not consider this as substantial. There is a cost for the device. But this is something that those ongoing costs are really manageable within the way we are going to associate discounts to those behaviors.

A - Charles Brindamour {BIO 7012323 <GO>}

Reflected in how we price the offer.

Q - Tom MacKinnon {BIO 2430137 <GO>}

Okay. Thank you.

Operator

(Operator Instructions) Shubha Khan, National Bank Financial.

Q - Shubha Khan {BIO 16255963 <GO>}

Thanks. Good morning. Just on reserve development in personal auto, it's been quite strong for three quarters in a row now. I assume the most of that is coming from Ontario. And I also assume that you continue to reserve conservatively there, I guess because the environment remains uncertain.

My question is at what point would you be comfortable battling back that conservatism? Because judging by your comments it appears that the environment, at least with respect to bodily injury, for example, has been fairly stable for a few quarters now. And the impact of the 2010 reforms appear to be unfolding as expected. Your arbitration backlog is up only 3%. So I imagine that isn't generating too much uncertainty either. So when would you be comfortable dialing back that conservatism in personal auto?

A - Charles Brindamour {BIO 7012323 <GO>}

I'll let Mathieu explain his perspective on bodily injury, which is an important portion of our reserves and our IBNR. I think you are seeing healthy favorable development beyond and above our long-term average there. I think that it is fair to say that Ontario contributes to that. I think there's favorable development, as you can see, in the stat supplement for all accident years. So it's not all Ontario. And it's not all accident benefit or post reform-driven. That's the first point I will make.

The bulk of the favorable development that we observe in Ontario is driven by actual files that we close as opposed to meaningful changes in our thought process as to the degree of conservatism that is needed. There is still some uncertainty in the system which we take into account as we reserve. And I think BI in particular is one of those key elements. And I will let Mathieu comment on his perspective of the BI environment and why he thinks we should be cautious on that front.

A - Mathieu Lamy {BIO 15207469 <GO>}

We should be cautious. And we are cautious. We see an increase in the number of claims higher than pre-reform level. This was expected as some of the AB claims are transferred on the BI side. Although the increase that we see is less than our reform expectation, you have 2 to 2.5 years to submit a claim. And that claim may stay on average stay open for another two years. So we are looking at four or five years duration here. So that's why post-reform claims, we are not there yet. So that's why we need to remain cautious.

A - Charles Brindamour {BIO 7012323 <GO>}

Exactly. What we are seeing in the field, day in day out, are claims adjusters work is pretty good. I think at a high level we have to take into account what Mathieu has just mentioned and that's the basis on which we are reserving right now. And I think we're pretty comfortable with that position. And I think, as files close, then you see favorable reserve development at this stage. But no change in stance on our part.

Q - Shubha Khan {BIO 16255963 <GO>}

Okay. That's helpful. And if I could just switch gears quickly to commercial P&C, it looks like cat losses have been elevated through the summer. And you seem to suggest that this could result in firmer pricing over time. In the more immediate term, do these elevated cats provide the necessary impetus to reduce coverage or implement other sort of product tweaks similar to what you've been doing in personal property? Or in other words, do you intend -- or do you need to or intend to take actions (inaudible) in commercial P&C?

A - Charles Brindamour {BIO 7012323 <GO>}

So I think there's two elements to your question which are distinct. I think let's first go over what we think we need to do in a relationship with catastrophes on the product. And then we can maybe give you a broader sense of where we see the market heading and what we're seeing right now on the market and I'll ask Alain Lessard, SVP Commercial Lines, to share his perspective on that.

A - Alain Lessard {BIO 17592535 <GO>}

So if we look at -- the first thing when we are talking about commercial property is that we do provide flood coverage. We provide sewer backup and flood coverage. In general, if we look at our portfolio, roughly about 40% of our insured are insured for flood and sewer backup. So like you said, the summer event, either the rain in Ontario or the flood in Calgary, has led us to really reconsider some of the action there.

The first thing we are right now in the process of implementing is minimum deductible. We had variable minimum deductible between CAD10,000 and CAD25,000 varying by provinces. We are now in the process of harmonizing that, going to CAD25,000 everywhere.

We also have a measure where we don't offer flood coverage in flood recurring territory. And basically those two events right now we are reviewing those territories to see if there is somewhere we see more flood than we were expecting. So normally this will also have an impact on availability of coverage. And we are going to be reviewing our rates for flood and sewer backup in Q1 2014.

On the market, we have been I think pretty consistent since the beginning of the year saying that we were expecting firming conditions for about a quarter of the market, the market that was the worst performing. I think the flood, the event of the summer, is adding pressure. The renewal of the reinsurance that will be coming for some companies will also I guess adds some pressure, in addition to low interest rates. So we are now seeing I would say still a very healthy market in the sense that new business is really still competitive. But we are seeing more and more companies coming out with a profitability message on some classes of business and on some like flood and sewer backup where they are seeing and implementing underwriting rules.

So I would say right now, we were expecting firming conditions on about 25% of the market. I would say that we are slowly seeing those firming conditions emerge.

And if I look more on numbers side, we were pushing rate increase throughout the last few years, a small rate increase in renewal. And now we have been achieving like 1.9% rate increase on the First Quarter, about 2.3% in Quarter 2. And during the summer, we have kind of I would say reviewed our renewal strategy, pushing more rate increase on the underperforming segments. And now we are achieving 3% in Q3 on rate increase at renewal, going to 3.3% in the month of September. So we are seeing some traction in that movement. But it still slowly firming up. It's not like happening on every risk everywhere. But you know, the 25% we are seeing really firming condition gradually and we expect that to continue next year.

A - Charles Brindamour {BIO 7012323 <GO>}

You might comment -- I guess to judge the market, you might comment on what you're seeing in terms of retention and new business production and so on.

A - Alain Lessard {BIO 17592535 <GO>}

Yes. Like we said, we've increased our rates on new business in Q1. That had about no impact on our closing ratio. We are pushing a new rate increase in October.

On the renewal side, when we started pushing more rate increases during the summer, we saw a slight decrease in the renewal retention going from 86% to 85.5%. So we are applying something like 0.5 point to 1 point reduction in retention. But this is because we are pushing more rates on the underperforming segment.

Q - Shubha Khan {BIO 16255963 <GO>}

That's great. Thanks, I'll requeue.

Operator

Stephen Boland, GMP Securities.

Q - Stephen Boland {BIO 5546446 <GO>}

Good morning. A couple of questions. Just under the Minor Injury Guidelines, you said -- or you stated 55% of the industry claims are falling under the MIG. But your number is actually higher. So what are you doing differently than the industry to get I guess cost -- I guess contain costs under the MIG?

A - Martin Beaulieu {BIO 15316652 <GO>}

I'd say the reform expectation was 55%. We don't know for sure what the industry number is and we know our number and we are still experiencing above 55%. Hard to say what we are doing differently than the industry.

A - Charles Brindamour {BIO 7012323 <GO>}

Like I don't know what the others are actually doing. But I know that what we are doing translates in a meaningful loss ratio advantage in the market. And I think there is clearly a degree of proactivity on our side which is paying off. I mean the shorter a claim is open, the better for the client, the better for us. And that's the mindset that we are in here at this stage.

And when these reforms came out, we really embraced these things, not only with the reform. But you will recall, Stephen, that two years back, we said we will match the impact of the reforms with our own actions on top of the reforms. And I think it's our own actions on top of the reform that are really paying off for us at this stage.

Q - Stephen Boland {BIO 5546446 <GO>}

Okay. Second question, on your home insurance and the changes that you're being proactive on, sub-limits, higher deductible, rewording of policies, again how much more -- I presume all the industry is moving to contain costs here. Where would you say you are in terms of are you being more aggressive than the industry?

And I guess my point is if you are being more aggressive than the industry, is there a chance here that you end up losing more business as you're increasing rates a lot faster than the competitors and you lose premium?

A - Charles Brindamour {BIO 7012323 <GO>}

Yes. Well we don't look at what happened in the past two or three years as freak occurrences. And I don't think that many of the players are in that mindset. I think that the sense I am getting is people are waiting to see what we are doing. Now our colors are becoming increasingly clear because we are actually taking actions. But there's no doubt in my mind.

I am in Alberta this morning with the team here. We are sitting here in Calgary, met lots of brokers in the past couple of days. And it's very clear that we are ahead of everybody else on these things.

And there is a risk that units will suffer. There's no doubt about that. I think the industry will follow. I don't know when. And at this stage, it's tough to be a leader. But that's what it's all about. We're doing what we think is right. And we will live with the consequences there.

So there might be pressure on the unit front. But it's not something we are overly concerned about.

I think what we are concerned about is making sure that, A, we have a product that is sustainable, B, that clients understand and have incentives to make sure that the product remains affordable for them. And C, that the brokers and the employees are well equipped to explain why changes are taking place and why it's important for these changes to take place.

I think the coming six to nine months will be very demanding on our troops. I think it is creating additional work for brokers; there's no doubt about it. But you know, it's really important for us to do this.

I think it's also important to understand, Stephen, that we are not spreading with a broad brush, I forget what the expression is in English. But we are taking a segmented approach here in the area -- in the areas where the risk is actually the highest. And so it's not as if there was risk on all units I think. The segments where we are acting are segments where we feel that it's not sustainable at this stage.

And so I think if you look at our big financial objectives, which is ROE outperformance and growth in operating income per share, we are very comfortable with the actions that we are taking so that it will contribute to those two objectives.

Q - Stephen Boland {BIO 5546446 <GO>}

Okay. Thanks.

Operator

(Operator Instructions) Mario Mendonca, TD Securities.

Q - Mario Mendonca {BIO 2450557 <GO>}

Just a couple of quick questions. First, on telematics, do you see any potential that, to the extent it becomes widespread, Intact's sort of informational advantages could deteriorate somewhat? Is that something that is possible, or do you maintain those advantages?

A - Charles Brindamour {BIO 7012323 <GO>}

I think that's why it's important to be out there quickly, first point.

Second point, I'll take you back to Ontario which in my view is the province where we have the most constraints when it comes to pricing and segmentation. And we have one trillion price points. And we have a team, an R&D team, that is not sitting on their hands at the moment. They are working on the next two, three ideas to keep segmentation advantage.

So you know I think we will see what the take-up is, Mario, on telematics to assess that point. But I would think there's lots beside telematics that contributes to a segmentation advantage. And our folks are not sitting on their hands.

The other thing is that, with telematics, there is what you do and what you price for. And then there's the data you collect that you are actually not using. And for me, that adds a lot of value from a segmentation point of view. And given our size, our ability to match this data with claims experience and obtain credibility on that I think is much greater than everybody else in the market. And so I think there is actually an opportunity there on the segmentation front beyond and above what the program is doing today.

A - Martin Beaulieu {BIO 15316652 <GO>}

And I would say to the contrary of is there a potential that we would lose some of our advantage, I think it's further advantage for us because our larger database are going to allow us to slice and dice this new information faster than most and have credible information to apply this in our segmentation techniques. So I am very upbeat when it comes to that new way of doing business.

Q - Mario Mendonca {BIO 2450557 <GO>}

But it's fair to say we won't have a good answer on this for probably several years.

Like whether it narrowed the gap or not?

A - Charles Brindamour {BIO 7012323 <GO>}

Yes. I think the take-up rate and the amount of data we'll be able to collect, we will get a sense in the coming six months I think. Then based on that, we will assess where we can take this. It's something we will talk about at the Investors Day as well, give you a bit more color on that. But it is indeed fair to say that it will take a bit of time before we get full clarity on that. But certainly an avenue that could provide a segmentation advantage over time.

Q - Mario Mendonca {BIO 2450557 <GO>}

Going to personal auto for a moment, the claims ratio, the current-year claims ratio, it is up now I think it's five consecutive quarters. There have been very good explanations in the past. Is there any particular thing you would point to this quarter that would drive the year-over-year increase in the current-year claims ratio in personal auto?

A - Charles Brindamour {BIO 7012323 <GO>}

The current accident year claims ratio is up 1.9 points, basically year-over-year. And I'll let Martin give his perspective on that.

A - Martin Beaulieu {BIO 15316652 <GO>}

Most of that deterioration we are seeing is coming from the seasonal nature of the Jevco portfolio, which was not present last year at that time in our numbers. And bringing it this year in our numbers, motorcycle seasonality is during the summer. These are larger claims that you see coming in. This comes also with an offset with respect to the average premium going up. But since the seasonality in Q3 of motorcycles is higher, this is what is most of the explanation for the increased experience.

A - Mark Tullis {BIO 4180270 <GO>}

I think the thing to keep in mind is we book the premium for that ratably throughout the year. But we incur the bulk of the claims in the summer because people drive the motorcycles less in the winter. So this is a new seasonality that's been added that we didn't have before Jevco.

Q - Mario Mendonca {BIO 2450557 <GO>}

And Jevco wasn't around 12 months ago. And that's why seasonality (multiple speakers).

A - Mark Tullis {BIO 4180270 <GO>}

Exactly Right.

Q - Mario Mendonca {BIO 2450557 <GO>}

Okay. Then is there any connection, can we draw any inferences from this year-over-year increase in the current-year claims ratio? And acknowledging that this was maybe perhaps a special quarter, is there anything we can take from that in relation to the very strong reserve development? Is there a connection there? For example, if we continue to see year-over-year deterioration in the core claims ratio or the current-year claims ratio, does it say anything about the future insofar as development is concerned? Or are these two really independent in you thinking?

A - Charles Brindamour {BIO 7012323 <GO>}

The stronger reserve development you're seeing is largely driven by field activity where we actually settle claims. So you could argue that if the world didn't change and the field activity continued as is, as we observe it, you could argue that the current accident year loss ratio might be overstated. I think we look at it. And we are seeing the field activity is great. But there's been a number of changes in Ontario in particular which lead us to remain cautious. So I would not infer at this point, Mario, that the current accident year loss ratio might be overstated because we are seeing in previous accident years favorable or greater favorable development this year. I remain cautious on that front.

Q - Mario Mendonca {BIO 2450557 <GO>}

I'm not sure which direction to go, whether to call the current year overstated or just expect that the reserve development will eventually fade, because it feels like one of those two things is going to happen. It's sort of hard to say.

A - Charles Brindamour {BIO 7012323 <GO>}

You know, one should not -- if you take a very long-term perspective, you should think about favorable reserve development in line with sort of guidance we have given in the past, 3 to 4 points. I think it's no surprise that reserve development has been more favorable than the long run average in the past few years, because we have taken a cautious stance.

So should one expect reserve development to move towards 3% to 4% over time? I think so. Will it be the case in the coming 12 to 24 months? Not clear to me. If the reforms remain effective, we might see favorable development in that sort of order.

Q - Mario Mendonca {BIO 2450557 <GO>}

Okay. I'll try to be quick with Mark. The impairment on the callable preferred shares, you called it one-time in nature. Can you just provide a little color on what's going on there?

A - Mark Tullis {BIO 4180270 <GO>}

Sure. So we bought preferred shares a number of years ago at a premium. And when they changed the capital rules for the banks, they are now more apt to be called earlier. So our expectation is now many of these preferred shares that we bought at a premium may be called in 2014.

So what happens on a market basis is the market values tend to move down toward the call price. But the way IFRS works is you don't do the write-off until you pass a bright line test. So when the market value gets below a certain point, it triggers an impairment. So it's not a credit driven impairment. It's an impairment driven by the fact that we bought at a premium. There have to be -- the price we paid for it was based upon being called. So economically this is not an economic impairment. It's an accounting driven thing caused by the fact that we bought at a premium. And we've passed the bright line which causes it to be written off. The reason it's one-time in nature is we can model this out and we know there's not going to be significant more of these in the future.

Q - Mario Mendonca {BIO 2450557 <GO>}

That was the nature of the question, why it was you felt it would only be one-time. I suppose that was the answer.

A - Mark Tullis {BIO 4180270 <GO>}

It's because when we bought them, this is the quarter when they pass that bright line.

Q - Mario Mendonca {BIO 2450557 <GO>}

Got it. And can you give us like how large that was?

A - Mark Tullis {BIO 4180270 <GO>}

Sure. It was CAD17 million this quarter. And I would expect nothing significant in future quarters.

Q - Mario Mendonca {BIO 2450557 <GO>}

Thank you.

Operator

Asim Imran, Macquarie.

Q - Asim Imran {BIO 18416793 <GO>}

Thank you. Good morning. With respect to your plan for delivering a 10 point improvement in the personal property combined ratio, is there any way you can guide us to whether a majority of it will come from the low teens rate increase or would it be more from the product improvements?

A - Charles Brindamour {BIO 7012323 <GO>}

I think there's three angles to think about in the coming 24 months. There's pricing, there's product. And there's claims. I think that we frontloaded our actions in pricing because that's the easiest first step you can do. And the increase in pricing actions on top of what was in place already could explain two-thirds of that. We think that the remaining portion will come from product.

We think there's a fair bit of upside in claims as well. I think putting our finger on how much claims is worth is not clear at this stage. And I'll let Mathieu maybe talk about some of the things we're doing in claims on that front. But out of 10 points, I think there would be a good two-thirds coming from rates within 24 months.

A - Mathieu Lamy {BIO 15207469 <GO>}

On claims, we are focusing on the part of it that is going to come to improve our execution at Cat time. We've increased our resources that (inaudible) internally so we think that has -- is a place to improve the expense of managing the claims as a customer service aspect to it, an improvement on that. And certainly a control on indemnity, because we have IFC eyes on the scope of the claims. So this is certainly one aspect we continue to have activity on the supply chain side of things. Like you said, it's difficult to measure exactly how it's going to bear in terms of exact percentage. But we are certainly active on that front.

A - Charles Brindamour {BIO 7012323 <GO>}

Yes. And I would say that when I think about claims, the one where there's a fair bit of upside in my mind is the control point you talked about where we are much tighter in the appraisal process to make sure that we are not being taken advantage of in periods where lots of claims need to be appraised. So we really boosted our troops and our efforts on that front, have done a what we call a leakage study after the hailstorm last year and figured out that there was upside for us to increase our control. We had prepared to roll out that plan in may. And we had an opportunity to execute on it with a vengeance to a certain extent, given the summer we've had. But a fair bit of it left to be deployed in the coming years. Hopefully, we won't have as many opportunities to use it. But we are preparing for the worst.

A - Martin Beaulieu {BIO 15316652 <GO>}

On the claims front, we are introducing the notion of settling roof on the basis of the age of that roof in Alberta. So that's hail-related, that measure. So that's going to take a chunk out of those settlements.

And in addition to price, product. And claims, I think the one thing that's difficult to quantify but where our actions are focused is trying to make people in society change behavior towards climate change. And this is something that needs to happen to put the equilibrium in the system. And many of our actions are geared towards education and prevention. But also even when the product is changing, we are giving people opportunities to change behavior therein and improve the overall scheme.

A - Charles Brindamour {BIO 7012323 <GO>}

So we've done a very good job giving you a very long answer to a small question. The answer is two-thirds from rate for sure.

Q - Asim Imran {BIO 18416793 <GO>}

Great, thank you.

Operator

(Operator Instructions) There are no further questions on the phone line. I turn the call back over to the presenters.

A - Dennis Westfall {BIO 15155973 <GO>}

Thank you, everyone, for participating. Webcast will be archived on our website for one year. A telephone replay will be available at 3 p.m. today until Wednesday, November 13. And a transcript will be made available on our website. Please note we'll be hosting our annual Investor Day in Toronto on November 27 and our Fourth Quarter and year-end results for 2013 will be released on February 5.

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

Operator

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