Q4 2017 Earnings Call

Company Participants

- Michael John Templeton Ford, Group Chief Financial Officer
- Patrick Charles Regan, Group Chief Executive Officer & Executive Director

Other Participants

- Andrew Buncombe, Analyst
- Ashley Dalziell, Analyst
- Brett Le Mesurier, Analyst
- Daniel P. Toohey, Analyst
- David Humphreys, Analyst
- James Coghill, Analyst
- Kieren Chidgey, Analyst
- Mark Hancock, Analyst
- Nigel Pittaway, Analyst
- Ross Curran, Analyst
- Toby Langley, Analyst

MANAGEMENT DISCUSSION SECTION

Patrick Charles Regan {BIO 15131018 <GO>}

Good morning, everybody, and welcome to our 2017 Full Year Results Presentation. Before I start, probably I should welcome a couple of people to the audience. We have David McMillan in the front row here, who's our new Group Chief Operating Officer, and obviously, Michael, who's our new Group Chief Financial Officer. In addition to talking you through the 2017 results, we're also going to take you through a little bit of our strategic agenda. We spent the last few months conducting a detailed review of the business and preparing our program for change, and I'll give you a few of the outline of that program in a minute.

Before I do that, let me give a little bit of color on 2017. The group recorded a combined ratio for 2017 of 104.1%. And as you know, our results as well as those of the broader global insurance industry were significantly impacted by unprecedented levels of global catastrophe events, with a total global catastrophe activity now estimated to be around $135 billion – Hurricanes Harvey, Irma, Maria, Mexican earthquakes, California wildfires, and closer to home Cyclone Debbie, and the December Australian storms, and all of that meant our overall cat claims increased and added 6 points to the group's combined ratio with North America and Equator particularly impacted. Excluding that excess cat cost, our combined ratio for 2017 would have been around 98%. After the reserve strengthening we booked at year-end, we saw a reduced level of positive prior year development at about $40 million for the year.

And touching quickly on some of the divisionals, which Michael will go into in a bit more detail in a moment. North America had a combined ratio of 109% with the results, obviously, heavily impacted by the weather events, which added 7% above our normal divisional cat allowances, and we also strengthened reserves across a few specific portfolios. Absent those two items, North America's combined ratio was approximately 98%.

Europe delivered a strong result with a combined ratio of 95% despite what's been challenging market conditions in the region for probably about the last five years and increased cat activity last year. In fact, Europe's combined ratio at 95%, I think, will in all likelihood be much lower than most of its London market competitors.

In ANZO, the remediation plans, cell review processes, and the focus on quality underwriting pricing and claims that we first implemented in the second half of 2016 and then throughout 2017 have further improved ANZO's performance. The division recorded a combined ratio of 92% with an attritional loss ratio, excluding LMI, now having improved by roughly 5% from the first half of 2016. We also strengthened the group PoA by half a point to 90%.

We delivered a good investment return of 3.2%, benefiting from both good tactical asset allocation and favorable market conditions. And despite the cat events, our capital position remains strong. Our PCA multiple of 1.64 and that's before the benefit to the LatAm sale and S&P capital close to AA level.

I did want to talk specifically about performance in Asia Pacific that I think can be best described as unacceptable. We saw significant losses on our Hong Kong workers' comp portfolio, particularly the construction book. We also strengthened reserves in the Hong Kong workers' comp portfolio. The attritional claims ratio was adversely impacted by increased frequency across a number of portfolios, including property in Hong Kong, Singapore and marine in Hong Kong, Singapore and Indonesia.

We also saw an increase in expenses, although in part due to the restructuring costs we took in the fourth quarter to take out a layer of regional costs. That said, our businesses in Asia are long established businesses and I believe we do have a realistic plan to improve performance there, and I'll come back to that in a moment.

On Latin America, as you will have seen from our announcement this morning, we have made the decision to exit Latin America, excluding Puerto Rico which will now become part of North America. And while we have a solid business in Argentina, we are subscale in a number of the other markets in Latin America, and we've made the decision that essentially we do not have a realistic plan to achieve an acceptable return in those markets.

The sale of LatAm to Zurich for $409 million is equivalent to approximately 1.4 times the book value or 2 times tangible book value excluding DTAs. And I think the deal represents very good chip (05:20) value for our shareholders. And this is consistent with our focus on simplifying the group, reducing risk and improving the consistency of our results.

Just on that, let me switch focus slightly and talk through our strategic agenda and priorities for 2018. As I commented earlier, over the last few months, we've been conducting a detailed review of the business. And let me start by saying, QBE has many strengths from which to build off. We clearly have some businesses with strong market positions that are performing well or indeed very well. We also have a number of areas where we can and need to improve.

On the back of the review, we have created a program that will drive performance with seven key elements to it: simplifying QBE by market and by product; our focus on the Brilliant Basics of underwriting, pricing and claims; driving performance improvement through our cell review process; further repositioning North America, building on the work that's already been done; remediating Asia and significantly improving performance there; building talent and creating a distinctive QBE culture; and building a QBE for the future and modernizing QBE.

I'll give you a little bit of a flavor of each of those elements now. And while we do have many high performing businesses at QBE, we do need to further simplify our business, reduce risk and reduce volatility. And we'll do this by ensuring we only operate in markets and products where we have a good market position and a realistic plan that can deliver an acceptable return. Let me be clear, the vast majority of our portfolios will meet this threshold test. This is not about a wholesale reduction of the size of QBE beyond exiting Latin America, and Latin America is a major step forward to simplifying QBE. And our focus now will be more on certain products and portfolios than it will be on exiting countries.

To give you a few examples, we've stopped writing construction workers' comp business in Hong Kong, we've significantly refocused and reduced the marine business in Indonesia exiting, for example, the tugs and barges segment. And as we mentioned earlier, in December, we announced we entered into an agreement for the sale of QBE Thailand.

Number two, Brilliant Basics. It's fair to say we will be forensically focusing on what I call Brilliant Basics. It is imperative that the basics of insurance, of underwriting, pricing and claims are performed not just at consistently high standard but brilliantly. Don't get me wrong, we have got some real areas of expertise to build off here.

To ensure all of this happens, I have established a new Brilliant Basics program of work aimed at delivering a consistent excellence in our underwriting, pricing and claims everywhere that we do business. I'll give you a few examples. It's certainly nothing like the whole program, but a few examples of the work we're doing.

On underwriting, for example, we've developed a set of global underwriting standards that are being implemented across the whole of QBE. This could, for example, refine how underwriting authorities are earned, how peer audits are conducted, how product committees work in countries, product guidelines and indeed delegated authority frameworks.

We are, of course, hiring a new Group Chief Underwriting Officer, who, amongst other things, will ensure the full implementation of underwriting Brilliant Basics. In the meantime, Richard Pryce, our European CEO, has been leading this initial implementation and doing fantastic work for me driving this program forward.

For pricing Brilliant Basics, we've developed a customized pricing tool, customized pricing assessment tool that we call PAT that we're using to rank and assess all of our pricing models across the world, and we're working through a systematic program to deploy the best available pricing models. Now, sometimes this will be about using new data, sometimes it'll be about updating the models more frequently, sometimes using a greater amount of data analytics or indeed introducing machine learning into the pricing tools. And sometimes this will involve using a globally consistent pricing tool for something like commercial property.

On claims, we've previously mentioned we already have a global claims transformation program that made significant claims savings to-date. And we do believe there's further savings achievable in 2018. Claims Brilliant Basics will incorporate this program and expand it and we'll be implementing claims global standards and this will involve enhancing our use of supply chain techniques, embedding data analytics deeply in our claims processes, redesigning some of the critical core claims handling processes and better claims MI (10:32).

I've spoken to all of you about the cell review process we established in ANZO some 18 months or so ago that I think has been one of the key tools of our improvement there, and it's fair to say it's a much more mature process today than when we started it. It is a pretty intense and forensic process. We broke the Australian business down into roughly 50 sub-business units or cells as we call them, and regularly reviewed in great detail their underwriting improvement plans, specifically charting the underwriting, pricing and claims actions to drive improvement. And this is done with the head of claims, the head of pricing, and the head of actuarial in the room to verify those actions by set (11:17). This might include new hazard code approaches, price changes by customer segment, or specific claims actions.

These are then quantified and rigorously tracked by cell. And this creates a very thorough operating rhythm that will combine fact-based discussions with obviously a focus on tracking our Brilliant Basic initiatives, but ultimately, it's about driving a higher degree of accountability around our underwriting performance, but it's also about showcasing where we've got some real areas of expertise.

One of the key elements of our group strategy is ensuring North America performs at a similar level to Europe and ANZO and, as such, we've designed a piece of work aimed at further repositioning our North American business. Core elements of this are first and foremost, obviously, delivering the 2018 plan and fully implementing that cell review process; secondly, deeply embedding Brilliant Basic fundamentals across the division and all product lines; third, further simplifying the operating model there, simplifying our IT platforms there and taking out cost; and as we've done all of that, further refining the portfolio.

As you can see from the chart, we've significantly changed the North American portfolio over the last four years. We shrunk our program business down for more profitable core. We completely exited Mortgage & Lender Services and we've grown our Specialty business. And the next phase will grow and build on that by defining specific industry verticals and underwriting capabilities that allow us to selectively grow in corporate and Specialty portfolios. On the other side, we will also be reviewing our position in personal lines, which probably means exiting some of the smaller parts there, for example, the independent agents business, where we don't have scale or competitive advantage.

On Asia, previously mentioned, we need a lot of work to do to improve our results in Asia. And again, this falls into three pretty obvious categories: putting in place a comprehensive program of performance improvement plans, rebuilding Brilliant Basics across the region and reducing cost. We've identified 18 portfolios that are significantly underperforming and need specific profit improvement plans. And you can see the total of those up there on the chart, for example, Hong Kong workers' comp, Hong Kong marine, Singapore marine, accident and health. And you can see the premium we're writing there has already started to reduce in the second half of 2017. Specific actions we've taken include obviously rate increases; a reduction in the high hazard indexes – and again, you can see that's starting to get some traction; and significantly reducing certain subsegments of business.

In addition, underwriting appetites and authorities have been reset and sometimes completely centralized. The program is somewhat similar to the program we implemented in Australia, but probably different and a little more complex. And it will take some time to fully fix Asia, although I do think we'll make significant progress in 2018.

I think I'm confident that the areas we've just spoken about are the right plan and focus for QBE for the near term. But I'm equally passionate about building a QBE to thrive in the future. To be successful in the future as well as having underwriting discipline, we also need to be innovative, more customer-focused, invest in our talent, have a distinctive culture and have a clear technology road map embracing digital. So most of our time will go on areas one to five I've just outlined. We will also be accelerating some work in these areas as well.

On culture, we'll roll out a new target culture built around our seven cultural dimensions of accountability, being technically excellent, being fast-paced, being decisive and courageous, putting team first, being customer-oriented and being diverse and inclusive. This made a big difference to us in the ANZO business, and I'm hoping it will make a similarly big difference to us across the whole group. On innovation, we made two very successful investments in short-term partners last year. We'll be looking to make more of those this year.

On customer focus, we need to increase our customer-centricity overall, but specifically in our claims process. And on operational efficiency, I do think there is significant scope for automation there. And David, obviously, one of his primary tasks as our new COO is to look at where we have specific efficiency opportunities, and we'll come back to you on that in due course. More on all of these areas as we go through 2018.

With that, I will now hand over to Michael to take you through a little more of the financial detail.

Michael John Templeton Ford {BIO 17494941 <GO>}

Thanks, Pat, and good morning, everyone. I'm delighted to be here today to deliver the QBE year-end results. I'd like to start by taking you through a few key items that relate to the group's results. It's important to note that the results reflected in this slide, with the exception of the last three items, have been adjusted to exclude the material items that distort the group's performance. And these adjustments are as outlined in our 23rd of January market announcement. And as Pat highlighted, the final result is broadly in line with that announcement.

And just to remind you, as we discussed in January, we booked a $700 million noncash impairment charge relating to the North American goodwill. Secondly, the results were impacted by $230 million write-down of deferred tax assets in North America and that's following the recent change in tax rates there. The results have been adjusted for Ogden in the UK, and finally the loss portfolio transfer that we've just completed at the end of the year to reinsure the U.S. commercial auto liabilities. And that's only had a very small impact on the overall ratios.

Now moving through the adjusted results, the group achieved 0.5% growth in GWP and 7% NEP growth on a constant currency basis. And it was pleasing to see we achieved over 2% in overall premium rate momentum for the year-end, largely due to the average rate increases in ANZO of around 5% as well as improvements in pricing conditions in North America and Europe. And that's despite the market environments remaining highly competitive.

As Pat outlined earlier, the group recorded a combined operating ratio of 104.1%, excluding the impact from the change in risk-free rates. And there were two key factors that contributed to the deterioration. The significant cat activity and weather-related items in 2017 have resulted in a net cost of large risk and cat claims of $1.3 billion or around 14.6% of NEP. This added approximately 6% to the group's combined operating ratio.

We strengthened reserves around $110 million in the second half of 2017, largely in our long-tail casualty lines in our Assumed Re business in North America. And in Asia Pacific, we increased reserves in our Hong Kong workers' compensation portfolio. Prior accident year claims development was favorable for the full year amounting to $37 million and inclusive of that second half reserve strengthening.

So turning to a couple of the other items, the statutory net loss for the year was $1.2 billion. The group's tax rate was distorted by the tax losses in North America, coupled with losses in Equator Re impacted by those significant cat losses. We will pay a final dividend of AUD 0.04 per share resulting in a full year dividend of AUD 0.26, down from the AUD 0.54 paid in 2016.

Turning now to the divisional results and this slide shows the overall divisional results comprising our combined operating ratio of 104.1%. As Pat has already run through Asia Pacific and Latin America, I will provide an update on North America, Equator Re, Europe and Australia and New Zealand.

So as you can see in the waterfall, North America's combined operating ratio of 109% was impacted by two key components. The record catastrophe activity and severe weather events added around 7% above the normal allowances to the ratio. We also specifically strengthened reserves in North America mainly in casualty in Assumed Re, management liability, accident and health, and a now-terminated specialty program. Excluding these items, North America's adjusted combined operating ratio was around 98%.

Furthermore, during 2017, we completed a further loss portfolio transfer of discontinued programs to mitigate the risk of substantial adverse claims development. Together with the LPT undertaken in 2016, we've removed in excess of $850 million of potentially volatile claims liabilities from our balance sheet. The LPTs, coupled with a further $114 million of reserve strengthening, provide us with a strong foundation for improved profitability and reduced earnings volatility as we head into 2018.

Equator Re, and as you know, this bridges the gap between the group's risk appetite and local risk appetites. As you would expect, as our internal reinsurance vehicle, the severity of catastrophe activities heavily impacted Equator Re's results with the division recording a combined operating ratio of 141%. Excluding this impact, the combined operating ratio would have been 89%.

Now in Europe, despite challenging market conditions for the last five years or so in the region, coupled with the catastrophe activity and a reduced level of prior year development, EO delivered a strong result for 2017, recording a combined operating ratio of 95%. It's important to highlight that we do have North American property cat exposure through both the direct insurance business in Europe, within the international property segment as well as through our reinsurance business.

EO's prior accident year claims development was favorable by $141 million, which benefited the combined operating ratio by around 4%, although this was a lower level than in 2016. The division remains focused on strict pricing disciplines and improving our claims management activities through enhanced data and analytics practices.

Australia and New Zealand continued to show solid progress in 2017, delivering a combined operating ratio of 92%. Our pricing initiatives have delivered average premium rate increases of 6%, excluding CTP, and coupled with enhanced underwriting discipline, tightened terms and conditions and claims management practices have improved

ANZO's attritional ratio, excluding LMI, by around 3% when compared with the prior year. This is, of course, on top of the improvement in the second half of 2016 which means that ANZO attritional has improved by 5% since the first half of 2016.

We've been pleased to see improvement across New South Wales CTP, trade credit, personal motor, commercial motor, and in most of our short-tail personal and commercial lines. We continue to be well reserved in ANZO and our FY 2017 reserve release of 4.5% of NEP were broadly in line with what we achieved in 2016.

We believe we've got further room for improvement in 2018 in ANZO. And we remain well reserved in ANZO and our FY 2017 reserve release of 4.5% of NEP were broadly in line with what we achieved in 2016. We believe we've got further room for improvement in 2018 in ANZO. And we remain very focused on further targeted improvement in our loss ratios across the division, as market pricing remains generally supportive.

Now turning now to investment performance, and our investment portfolio delivered a net return of 3.2% for the year with both our fixed income book and growth assets delivering strong gains and exceeding our expectations and target range of 2.5% to 3%. Throughout the year, mark-to-market capital gains from tightening of credit spreads enhanced our fixed income returns and coupled with proactive management of duration resulted in a 2.1% return from fixed income.

Our fixed income portfolio duration of 1.6 years is broadly in line with the prior year, and we anticipate bond yields to rise in 2018. And therefore, we will most likely manage duration of our fixed income portfolio between 1.5 and 2 years throughout the year.

Our returns have been boosted not just by solid underlying asset class returns, but also by tactical positioning in growth assets, duration and spread duration, which has seen us more meaningfully exposed ahead of periods of outperformance.

Turning to our growth assets, exposure peaked at 13.2% of total investment assets in April, however, after an especially strong performance, has been reduced to end the year at around 10.2%. And pleasingly, we achieved a return of 13.3% in the growth asset portfolio for 2017.

Moving on to financial strength and capital management, and the group's capital position remained strong when measured against both regulatory and rating agency capital requirements despite the severe catastrophe claims activity experienced throughout the year. The catastrophes, dividends paid and the share buyback activity in the second half of the year has resulted in our APRA PCA multiple falling slightly to 1.6 times at year-end and that's down from 1.69 times at 30 June, 2017.

Following our 23rd of January market release, S&P revised the group's outlook from positive to stable, although pleasingly, our S&P capital remains very close to the double AA level, as indicated in the speedometer graph on this chart. We've already commenced work to strengthen the group's PCA multiple closer to the middle of our benchmark PCA range of 1.6 to 1.8 times and return our gearing closer to our benchmark debt to equity range of 25% to 35%, and that will be via a combination of earnings growth and other capital management initiatives, and indeed, the sale of our Latin American operations is part of this. We started the year with a very strong balance sheet, and despite the after tax net cash loss, we're pleased to have finished the year with a balance sheet that remains strong.

Our other key metric here is our free cash flow or dividend remittances from the businesses to the group. This, obviously, provides cash cover for our external dividend. In 2017, cash remittances remained strong and were only slightly down from the prior period. As I said earlier, the board has declared a final dividend of AUD 0.04 per share, 30% percent franked and the lower dividend payout reflects the impact of the catastrophe claims in the second half of 2017.

Following the introduction of our three-year share buyback facility announced last August, we were active in the market in the second half of the year purchasing a total of AUD 139 million in shares and resulting in the cancellation of 12.9 million shares. We remain committed to our three-year buyback program and intend to take a considered approach in executing the buyback during this year.

I'm excited to be part of QBE. We have some very clear operational and financial objectives to deliver over the coming months to align with the group's focus, a stronger and simpler QBE, as Pat outlined earlier. I look forward to meeting with many of you in the upcoming weeks.

And I'll now hand back to Pat for his closing comments.

Patrick Charles Regan {BIO 15131018 <GO>}

Thanks, Michael. Look, as I hope you can tell, the program of work we've put together doesn't rely on the external environment for help. But it is positive to note for the first time in a long while, we are seeing a more positive rate environment across our major markets. In the fourth quarter of last year, rate increases averaged 3% to 4% across the group and we've seen the continuation and, in fact, slight improvement of that trend in the first quarter, and actually, ANZO, excluding the impact of CTP reforms, running at about 6% albeit across the group there are great variations between markets, product lines, and loss affected areas as you'd expect.

Against this, we probably need to be slightly cautious, at least the possibility of higher level of inflation going forward. It's also worth noting that post the U.S. tax changes, the group will have a lower effective tax rate going forward. In the medium term, that's probably closer to 20% and probably slightly lower than that in 2018.

The announcement of the sale of LatAm is a good step in our program of simplifying the group and also add some capital. We've come through 2017 with a strong capital position that allows the board to reaffirm our dividend payout policy of up to 65% and leaves us well positioned to continue our share buyback program.

Our results do show in 2017 that we have a lot of work to do. That said, we've mobilized a program of work aimed at simplifying the group and driving real performance improvements in 2018 and beyond. My team and I are very confident this is the right program of work for QBE and are very energized about delivering it. And we look forward to updating you all on progress as we go forward.

With that, we will hand it over to Q&A.

Q&A

Q - Andrew Buncombe {BIO 19921333 <GO>}

Thank you. Good morning, guys. Andrew Buncombe, Macquarie Securities. Two quick questions if I can.

A - Patrick Charles Regan {BIO 15131018 <GO>}

Sure.

Q - Andrew Buncombe {BIO 19921333 <GO>}

The first one really for me the obvious one in terms of the gearing, 40.9% to start with. Take off the LatAm sale gets you about to 39% even, still way above your target range of 25% to 35%. It implies about another 850-odd million dollars of sales or material organic growth. I appreciate the comment that there would be organic growth and further capital management but how should we be thinking about this? How quickly should we be thinking about you moving back inside the range?

A - Patrick Charles Regan {BIO 15131018 <GO>}

Look, we've got plans that allow us to move back to our range, obviously as you remember, of 25% to 35% relatively quickly. Even before the LatAm sale of $400 million, we've got $1 billion of cash at the center. So that gives us quite a bit of financial flexibility obviously together with earnings.

Q - Andrew Buncombe {BIO 19921333 <GO>}

Excellent. And second question is on the Australian LMI business, the regulator, it seems like they're being more favorable in the outlook growing that market. Your biggest competitor in the market is positioning themselves for growth. Over the last couple of years, you've been happy to track the revenue sideways. How should we be thinking about that division given it's so capital intensive?

A - Patrick Charles Regan {BIO 15131018 <GO>}

Look, it's an interesting development, wasn't it? I think at the very least, there've been the question in everybody's mind about what the future of the LMI sector looked like longer term. Would the banks continue to use it? It certainly could have more compelling. Now there looks like there's going to be capital credit going forward.

We actually – our top line in LMI for the first time in a while was up very slightly in 2017 versus 2016. I don't think we're looking for big growth in LMI going forward. To your point, returns have normalized somewhat. You may have seen; you may not had had the chance to see yet. Our combined ratio is 50% for LMI in 2017. There was a couple of factors in there. We had a more normal commission ratio. We also tucked a bit of risk margin away in LMI, but I think that sort of the overall level of volume that we've got now is comfortable and I think the developments that we all read about in terms of capital are probably supportive of that.

Q - Andrew Buncombe {BIO 19921333 <GO>}

Excellent. Thanks.

Q - Daniel P. Toohey {BIO 16751863 <GO>}

Yeah. Thanks. Daniel Toohey from Morgan Stanley. Firstly, just touching on the higher retention on cats and maybe you can confirm whether that was part of your original guidance. So the retention that has gone from $1.15 billion to $1.2 billion.

A - Patrick Charles Regan {BIO 15131018 <GO>}

Yes. So the guidance we put in place, yes, does include the $1.2 billion attachment point for the GLRC.

Q - Daniel P. Toohey {BIO 16751863 <GO>}

Okay. And then just maybe stating the obvious, but the LatAm sale obviously excluded from guidance (33:03)?

A - Patrick Charles Regan {BIO 15131018 <GO>}

Yeah. It may be stating the obvious, but it's a good question to ask. So as you can tell by the fact that we announced the LatAm sale this morning, that has been finalized over the weekend. We put our target ranges, obviously, for the first time about a month ago, so they did not contemplate at the time the sale of Latin America. And as I say, that kind of went through and we signed that over the weekend. I think in terms of our combined ratio, it doesn't make a huge difference. We'll end up owning LatAm for most of this year as it goes through to completion. But yes, formerly the targets envisaged us owning LatAm.

Q - Daniel P. Toohey {BIO 16751863 <GO>}

Okay. Just moving to Europe, I noted you changed the Ogden rate from minus 0.75% to 0.25% positive.

A - Patrick Charles Regan {BIO 15131018 <GO>}

0.25%.

Q - Daniel P. Toohey {BIO 16751863 <GO>}

Can you just in – I mean if you back out the reserve releases, current accident year profitability, the combined's running close to 100%. Is there any concern there with continuing reserve strengthening? You talked about financial lines deterioration.

A - Patrick Charles Regan {BIO 15131018 <GO>}

Yeah.

Q - Daniel P. Toohey {BIO 16751863 <GO>}

The one-off – maybe quantifying perhaps the one-off U.S. long-tail liability strengthening within that as well.

A - Patrick Charles Regan {BIO 15131018 <GO>}

Look, I think it's a fair question. I think that if you've seen, and I'm sure you've all followed some of the trends in the London market more broadly and that that market has seen a number of years of price declines and that's kind of slowly eaten kind of current accident year margins. And I think our business has done well probably by comparison to a few others so we have lots of companies in that market posting results well north of 100%. So our combined was 95%. I think Michael mentioned we had about 4 points of prior year. So, yes, you're right.

I think a couple of things I'd say. One is, you're right, we did have some financial lines impact. I won't quantify that more than we talked about today. I think that the other thing I'd point to as well is our ongoing underwriting discipline there. For the first time in a long while, we are seeing a more positive pricing environment – the absence of a headwind. It's not a storming hard market but we are seeing the modest single-digit price increases there, which is helpful.

Q - Daniel P. Toohey {BIO 16751863 <GO>}

Okay. And just finally, there's no top line targets consistent with your view previously...

A - Patrick Charles Regan {BIO 15131018 <GO>}

No.

Q - Daniel P. Toohey {BIO 16751863 <GO>}

...but under the Brilliant Basics model, can you give us some idea of what ROE your target in your cells and where you want to get the ROE to?

A - Patrick Charles Regan {BIO 15131018 <GO>}

Yes. Great question. So we haven't today, as we've talked before, given top line targets. I don't think that's probably in our interests, although when we went through this similar program in ANZO, we haven't really ended up reducing top line kind of at all albeit we've been helped by obviously kind of what has ended up as a good pricing environment there. I think as we've done that with – there's a couple of things we've targeted in the cell review process. This might sound a bit obvious and it is a bit obvious – making sure every single cell can deliver a performance of a combined ratio less than 100%, and it's amazing what you can achieve just by getting them all to do that.

In terms of ROEs, I think we haven't given medium-term targets on ROEs today. I think as we do look to the medium term, it is a realistic target for us to try and achieve a double-digit ROE. That's what we should do across the group and, obviously, that's an aim within our cell review process as well.

Q - Nigel Pittaway {BIO 3406058 <GO>}

Hi, it's Nigel Pittaway here from Citi. You mentioned the Australian business and you haven't really surrendered much business, but I think GWP did go backwards for the period, certainly in local currency. I mean have you finished your rationalization of that business, do you think...

A - Patrick Charles Regan {BIO 15131018 <GO>}

Just a very tiny amount, Nigel.

Q - Nigel Pittaway {BIO 3406058 <GO>}

It was very slight, but nonetheless, it was...

A - Patrick Charles Regan {BIO 15131018 <GO>}

Very slight. So slight I'm surprised you could even see it.

Q - Nigel Pittaway {BIO 3406058 <GO>}

Pretty strong against pretty strong rate rises.

A - Patrick Charles Regan {BIO 15131018 <GO>}

I think what we saw in the ANZO results was retention was very good. So the focus for the team has been really - so retention was kind of at around 82%. So keeping hold of the high-quality business we've got - and that is a business that's got lots of high-quality business - so first and foremost, we were more selective on new business. So if you do the maths of an average 6% ex CTP rate increase, if there was a reduction, it was in the amount of new business we're writing, which is what we intended to do.

Q - Nigel Pittaway {BIO 3406058 <GO>}

Right. Okay. But are you through that, do you think?

A - Patrick Charles Regan {BIO 15131018 <GO>}

You should ask Vivek this. Is every portfolio exactly as he wants it? No. I would have said that the same. Are we through the major, heavy duty lifting of that? Yes.

Q - Nigel Pittaway {BIO 3406058 <GO>}

Okay. Then turning to North America, I mean presumably these first two things you've got on slide 7, you've already done, right. So the commercial auto's exited. Have you narrowed the program focus as much as you intend or is there more of that to go? And then the personal lines is still to do, is that right?

A - Patrick Charles Regan {BIO 15131018 <GO>}

Mostly yes. So commercial auto is done. There's a little bit more to go on programs, although the big dollars of that have been done, and personal lines, we will need to do a little bit more of focusing. The biggest bulk of premium within the personal lines numbers comes through the Westwood Agency business, we may have talked to you about before. That's very good, got a nice distribution model there that gives us some competitive advantage. The business we write through the independent agents, which is a bit smaller, less clear that we've got competitive advantages.

Q - Nigel Pittaway {BIO 3406058 <GO>}

And then the sort of industry focus that you're sort of saying, the industry verticals and refining your underwriting appetite in middle market. I mean how different is that to what you're currently doing?

A - Patrick Charles Regan {BIO 15131018 <GO>}

It's not meant to sound completely different. What it's really signaling, I think, is as we grow that business out, we've got to be smart at how we do it. We can't compete broadly across all industries and all geographies in the U.S. against the mid-market competition. That wouldn't be smart. So we've got to pick our spots for how we do that. We've done that successfully in Specialty. We'll look to do that - if you like, replicate that model across the commercial business as well. So it'll be picking both certain geographies to do that and certain industries to do that in as well. It's not completely different to what we've done, but it's just saying we need to be smart as we kind of very selectively grow going forward.

Q - Nigel Pittaway {BIO 3406058 <GO>}

Okay. Thank you.

Q - James Coghill {BIO 14006200 <GO>}

James Coghill, UBS. Pat, a couple of questions, one on capital and one P&L question. Capital one, just following on from the earlier question, I was just hoping that you could be a little bit more specific about what you're saying there because the text is a constrained (sic) [considered] (40:17) approach to buybacks in first half 2018. Michael seemed to indicate that buybacks were off the cards in 2018.

A - Patrick Charles Regan {BIO 15131018 <GO>}

Yes.

Q - James Coghill {BIO 14006200 <GO>}

And understandably, you haven't crystallized that $1 billion number again anywhere to-date, so perhaps you could just put a better structure around what the real capital return plans are, that these aren't just ongoing hollow promises.

A - Patrick Charles Regan {BIO 15131018 <GO>}

Let me be a bit more specific then, James. So the program was $1 billion over three years. So even I can do the maths, it's 330-ish a year. Our intention is to do that run rate this year. I think we only used the word considered because sometimes if we're not in the market every single day, people are calling us up saying, well, you're not in the market today. So we'll just be considered as and when we do that, but that type of run rate's what we're expecting to do in 2018.

Q - James Coghill {BIO 14006200 <GO>}

Okay. And then the second question was on Asia. So, I mean, it looks like the run rate will reduce further – this is on premium – into financial 2018. So you could be running $300 million of premium there over the course of this year. Could you just give us a little bit more color as to how many of these portfolios contributed towards that combined ratio, the 116% combined?

A - Patrick Charles Regan {BIO 15131018 <GO>}

Yeah.

Q - James Coghill {BIO 14006200 <GO>}

How should we be thinking about that reversing into 2018?

A - Patrick Charles Regan {BIO 15131018 <GO>}

So I certainly don't expect the premium to be anything like what you just said, James. I think should we expect some level of premium reduction in Asia? Yes. I think as we go through, that's inevitable. So the 2018 portfolios all contributed to some degree in the 115%. The biggest, half of the – if you do the maths, we had about a $100 million underwriting loss in Asia. Half of that came from Hong Kong workers' comp.

So our job is to prove that by not writing construction business going forward, dealing with the claims handling better, having booked up the reserving that we're not going to repeat on that going forward. And the other $50 million, which is a higher level of frequency across a number of portfolios – marine, property; by market, you've got a bit of Hong Kong, a bit of Singapore and a bit of Indonesia. They would be the major markets to do. So we just need to get a bit better at all of those really.

Q - James Coghill {BIO 14006200 <GO>}

So just to clarify that, so the Hong Kong, the workers' comp, I mean, I know you're going to say yes to this. But are you pretty confident that you've adequately reserved at the end of 2017? Is there a lot of variability around how that runoff portfolio, for want of a better expression, could perform? Is there a lot of variability or do you think you've got that...

A - Patrick Charles Regan {BIO 15131018 <GO>}

No, we think we've reserved well at the end of 2017.

Q - James Coghill {BIO 14006200 <GO>}

The answer I thought I'd get.

A - Patrick Charles Regan {BIO 15131018 <GO>}

There's been a few moving parts on how we have handled those claims internally to QBE, and there's been a bit in the market as well in the workers' comp market in Hong Kong that have inflated cost, but we think we're on top of all of that.

Q - Ross Curran {BIO 15090587 <GO>}

Hi. It's Ross Curran here from Deutsche Bank. Just a follow-up to James' question on the buyback. When you say the run rate's similar, I thought originally there was a cap in your buyback of 330-odd million dollars. Is that still the cap or are you going to catch up the $200 million that you've - your shortfall? So are we going to buy back $850 million of shares over the next two years or is this...

A - Patrick Charles Regan {BIO 15131018 <GO>}

In terms of - I think I said the $330 million for 2018.

Q - Ross Curran {BIO 15090587 <GO>}

So that's an $800 million-odd effectively buyback in total run. Is that working better (43:57)?

A - Patrick Charles Regan {BIO 15131018 <GO>}

No, I think - so the $1 billion still stands and our intention this year will be to do $330 million.

Q - Ross Curran {BIO 15090587 <GO>}

And then pick up the shortfall in FY 2019?

A - Patrick Charles Regan {BIO 15131018 <GO>}

Well, pick up the shortfall in FY 2019 or the early part of FY 2020. I wasn't more specific on that.

Q - Ross Curran {BIO 15090587 <GO>}

Thanks. And then just secondly on Dan's question around the guidance including the LatAm sale, can you talk through - because the LatAm investment assets tend to be high yielding assets as a whole. Can you talk through the impact of the run yield of dropping the LatAm assets out of that portfolio going forward?

A - Patrick Charles Regan {BIO 15131018 <GO>}

Yes. So I think on both the combined ratio – if you excluded LatAm out of the combined ratio and out of the investment yield, it is curiously a similar impact to both which is somewhere in the region of 20 to 25 basis points, so if you deduct both from both.

Q - Ross Curran {BIO 15090587 <GO>}

And then, finally, you've talked a bit in the presentation about investments in market data and analytics. In terms of OpEx into next year, are we talking a step-up in OpEx to catch up on this market data investment? Is that how we should be thinking about it?

A - Patrick Charles Regan {BIO 15131018 <GO>}

Yes. So, no, I mean yes, we are going to – I think there's some areas we need to invest in. I think David and Michael would agree, there's equally some areas we need to save money in as well. So we've talked in the detail of the financials about our expense ratio being somewhat flat in 2018, and I would kind of think about that as us needing to invest in a number of areas, whether it be data analytics and/or some of the Brilliant Basics capabilities as well as saving in a number of areas as well. So expect us to do both.

I think beyond that, I think it is reasonable that we should reduce our expense ratio. I think that is something that Dave has got in his mind and certainly in his mandate, and that should deliver a lower expense ratio as well as a lower of dollars of expenses going forward. As I mentioned super briefly in my speech, we'll talk to you a little bit more specifically about that going forward.

Q - Ross Curran {BIO 15090587 <GO>}

Thank you.

Q - Brett Le Mesurier {BIO 5909278 <GO>}

Brett Le Mesurier from Shaw's. You told us what the risk margin change was in the outstanding claims liabilities, but there's no comment on premium liabilities. Can you comment on what movements have been made in that risk margin?

A - Patrick Charles Regan {BIO 15131018 <GO>}

Yes, it's up slightly, Brett, both in dollars and in percentage terms as well.

Q - Brett Le Mesurier {BIO 5909278 <GO>}

And how does it compare to two years ago the last time the number was given?

A - Patrick Charles Regan {BIO 15131018 <GO>}

I didn't go back to two years ago, but it's up compared to last year.

Q - Kieren Chidgey {BIO 7268946 <GO>}

Hi. I'm Kieren Chidgey, UBS. Just a follow-up question on cost, the LatAm sale. What are the sort of expected separation costs as a result of that? And also, in terms of stranded costs from an ongoing point of view, what should we be thinking about?

A - Michael John Templeton Ford {BIO 17494941 <GO>}

Yeah, look, stranded costs, not a lot. There are some but they're not significant. We've called out a profit on sale in the release, which considers what the costs have been, transaction costs.

Q - Kieren Chidgey {BIO 7268946 <GO>}

So the separation costs are within that profit number?

A - Michael John Templeton Ford {BIO 17494941 <GO>}

That's right.

Q - Kieren Chidgey {BIO 7268946 <GO>}

Just secondly on the group underwriting performance, Pat, the way you broke down the divisions regionally excludes that corporate line which I noticed in stat (47:39) accounts booked a $90 million underwriting loss. So, can you just talk to sort of why that was so elevated this period?

A - Patrick Charles Regan {BIO 15131018 <GO>}

Nothing specific I'd talk to in this period. I mean, generally speaking, we've got obviously a few things going on incrementally in Equator this year, particularly because of the cat losses. Going forward, we should be the sum of the divisions plus Equator equals group.

Q - Kieren Chidgey {BIO 7268946 <GO>}

And my question was not around Equator. It was the group excluding Equator. I think you call it corporate and other.

A - Patrick Charles Regan {BIO 15131018 <GO>}

I think that would only be expenses or so in there. So we had one or two one-off expenses in the underwriting line of corporate.

Q - Kieren Chidgey {BIO 7268946 <GO>}

And are they recurring into next year?

A - Patrick Charles Regan {BIO 15131018 <GO>}

No, most of them should not be recurring into 2018.

Q - Toby Langley {BIO 15924432 <GO>}

Hi. It's Toby Langley from Bank of America Merrill Lynch. The conditions that you talked to in the final quarter of last calendar year, and those that you see today, is it the right interpretation to suggest there's upside risk to your guidance, or are you sitting on those conditions when you put those out?

A - Patrick Charles Regan {BIO 15131018 <GO>}

Look, it'd be very silly of me to sit here and say there's upside risk to our guidance at this point in time. I think – and there's a long way to go still in the year. All of us are very curious as to how pricing will evolve in all of the major markets – North America, Europe. It's not been as firm in some areas. The reinsurance rate increases are not as much as people thought. It's a little bit better in some other areas, our international markets business, for example. But it's very early on, very early days for that. It's been kind of okay so far, but it's only – it's not even the first quarter yet.

Q - Toby Langley {BIO 15924432 <GO>}

And then if we can just come back on your point around there's quite a lot of not unconnected targets. You've got your debt/equity ratio. You've got your PCA target. You still want to make your buyback commitment. And this year, we can see some capital coming in the door. But help us be a bit creative here, what else do we need to see for you to tick all of those boxes and be sat here next year having achieved all of those?

A - Patrick Charles Regan {BIO 15131018 <GO>}

Not a lot really. On the PCA, we get a benefit from LatAm. So our 1.64 goes up a bit. That gets us pretty close to the middle of our range without doing anything else. We're already in pretty good shape and then you add a little bit for S&P. So that's sort of good. Cash remittances, as Michael said, are good and that leaves us with a healthy amount of cash at the center. We've obviously added or will add later this year $400 million to that, so that gives us some flexibility on what we do with debt. So they would be the main components.

Q - Toby Langley {BIO 15924432 <GO>}

Thank you.

Q - Ashley Dalziell {BIO 17763474 <GO>}

Hi there. It's Ashley Dalziell from Goldman Sachs. Just a question on investments, you've suggested the asset duration will sort of hover in the 11/2 to 2-year range this year. But beyond that, is there still a aspiration to better match the balance sheet?

A - Michael John Templeton Ford {BIO 17494941 <GO>}

Over time potentially. But in the next 12 months, just between 11/2 and 2 years, we're quite comfortable with given the shape of the current curves.

A - Patrick Charles Regan {BIO 15131018 <GO>}

Yeah. I mean, we've been sitting at QBE for a long while hoping for interest rate rises. So it may be that we're finally on the cusp of that again. Let's see. I mean let's see how that plays out. Ultimately, we'll only match asset and liability duration when we're returning to a more normal interest rate environment, and nothing yet. Anymore?

Q - Mark Hancock {BIO 20707105 <GO>}

Yeah. Mark Hancock from Precept. I don't know if you've talked about reinsurance, but I assume you've been looking at the program since the end of last year and you might have made some changes, and can you just talk to sort of the cost of the program, but also the benefits and the sort of the bad payroll losses we encountered last year, is that likely to be more immunized under what you may have undertaken?

A - Patrick Charles Regan {BIO 15131018 <GO>}

Yeah. So the good news was that 50% of our program was pre-placed for 2018 – actually probably more than 50% because the aggregate treaty was already placed. So we've gone through and placed the rest of the program with actually minimal increase in cost, so the team did a nice job of that. The structure of the program is very, very similar from 2018 as it was in 2017. Then we noted there's a slight increase in the attachment point for the aggregate treaty, which we've factored into our guidance. So it's a very similar treaty and, actually, the incremental cost was pretty minimal.

Q - Mark Hancock {BIO 20707105 <GO>}

So would you be on risk for the same payroll losses if they were repeated this year?

A - Patrick Charles Regan {BIO 15131018 <GO>}

I think we've talked about before that on the aggregate treaty we buy, that gives us a lot of protection so that for 19 out of 20 years, you would expect large risk events and cat events to be completely contained in the limits of the treaty. Last year's estimated, I don't know, was a 1 in 50, 1 in 60-year type of event. So, obviously, when you've got that, it goes outside of everybody's reinsurance treaties and is incremental cost for everybody and we were no different to that. The core structure of the program is essentially the same in 2018 as it was in 2017. So if it was another 1 in 50 or 1 in 60 years, then yes, that would have an impact.

Q - Mark Hancock {BIO 20707105 <GO>}

And just question on the tax rate, you said it would be slightly lower. Well, you actually didn't say slightly. You said it would be lower than 20%. Do you mean slightly lower or do you mean there's a significant amount of tax losses arising from 2017, so your tax could be negligible?

A - Patrick Charles Regan {BIO 15131018 <GO>}

Oh no. No, I mean slightly lower.

Q - Mark Hancock {BIO 20707105 <GO>}

Yeah.

A - Patrick Charles Regan {BIO 15131018 <GO>}

Not - I mean slightly lower.

Q - Mark Hancock {BIO 20707105 <GO>}

Okay. Thanks.

A - Patrick Charles Regan {BIO 15131018 <GO>}

I think we have a call on the telephone. David? Question on the telephone.

Operator

David Humphreys, your line is now open. Please go ahead.

Q - David Humphreys {BIO 18797143 <GO>}

Yeah. Two questions if I may. Firstly, on your growth in Specialty in North America, and I've asked in the past about the capabilities you think you have. When you grow into new spaces, you told me that you've got good handle on risk selection and pricing control. What confidence can you give us on growth in E&O and transactional liability?

A - Patrick Charles Regan {BIO 15131018 <GO>}

Yeah. David, it's a good question. I asked for a specific bit of work to look at that over the last couple of months, just to make sure that the new business we're adding was the right quality and our reserves were the right levels as well. So there's nothing to flag that came out of that work. I would say to you that we're going to be growing at a much lower rate on that going forward. Probably the only place in the world where you know in 2018 there's not - rate available is in that kind of professional lines market. So, I think the team had done a decent job building the book of business we've got. But I think the rate of growth going forward will be much more modest.

Q - David Humphreys {BIO 18797143 <GO>}

Okay. Second question. Looking at your underwriting accounts, your unclosed (55:05) business has increased by $130 million to now represent about 8% of GWP. That seems odd in a book that's shrunk more broadly across the board. Can you comment on that?

A - Patrick Charles Regan {BIO 15131018 <GO>}

When you say unplaced business, David, do you mean unearned premium?

Q - David Humphreys {BIO 18797143 <GO>}

No, unclosed (55:24) business, so receivables (55:27).

A - Patrick Charles Regan {BIO 15131018 <GO>}

Receivables within the book. Most of the trends on that were to do with the movements in various kind of cats so, obviously, our reinsurance receivables increased. Our premium receivables, there's no specific trends on that to highlight, I don't think.

Q - David Humphreys {BIO 18797143 <GO>}

Perhaps you can pick it up offline.

A - Patrick Charles Regan {BIO 15131018 <GO>}

Sure. Do we have any more questions on the phone? Anymore in the room?

Very good. Well, thank you for joining us all today, and we look forward to seeing you all soon.