FINAL

Bloomberg Transcript

Investor Briefing

Company Participants

- Colin Fagen, Chief Executive Officer, Australian & NZ Operations
- John Neal, Group Chief Executive Officer
- Neil Drabsch, Group Chief Financial Officer

Other Participants

- Brett Le Mesurier, Analyst
- Daniel Toohey, Analyst
- James Coghill, Analyst
- Kieren Chidgey, Analyst
- Nigel Pittaway, Analyst
- Ross Curran, Analyst
- Siddarth Parameswaran, Analyst
- Toby Langley, Analyst

Presentation

John Neal {BIO 15681439 <GO>}

Okay. Let's start. Good morning everyone and thanks for attending our update on our operational transformation program. If I'm a little bit confused this morning is because I've just got off the plane from London, and Colin Fagen is whispering go to Wallabies in my ear, which really isn't helping me as I stand up to kick off.

There shouldn't be any speculation around the date. We said I think with our full year results that we'll provide an update halfway through the year on the operational transformation program, and this is it. It's very early for us to be commenting on the half-year results. We'll give you some steer, but obviously we're just into the process of consolidating the half year at the moment.

So really there is two priorities today. Firstly is to give you a more detailed insight into the progress and the absolute reality of the operational transformation program for QBE. And then secondly, to give you a sense of the actions that we've already taken in the first half of 2013 to improve and strengthen QBE's capital position and our balance sheet.

So in that respect, I've got Neil Drabsch, Group CFO with me today specifically to talk about financial strength and flexibility and Colin Fagen, our CEO for Australian and New Zealand operations who will talk through a case study of Australia and the operational transformation program and how it's working for us here.

Okay, straight into an overview of vision and our value creation model which really sets the scene as to why we pursued operational excellence as one of our key strategic priorities. In February this year, we did rollout our refreshed vision and the vision is up there on the slide, it's a fairly lofty ambition. But it's critically important for QBE that we do play to our global strength as both an insurer and a reinsurer. And in that respect, there are four important stakeholders that we must satisfy beyond our customers, our people, our shareholders and the community.

And for the first time in our annual report this year, we rolled out our -- a value creation model that's shown on the slide there. Very importantly at the center of that value creation model is our statement that we will consistently achieve business plans and targets and I can say today that we remain confident in our immediate, which is our 2013 business plans and our ability to deliver on the calls and the margin calls we put in the marketplace.

In addition, we've worked very hard through the first half of this year in particular to define what is core and non-core for us to ensure that we deploy our capital to best effect. In terms of operational excellence, global reach and scale, we have a number of global initiatives in play with the full year results updated to you on our reinsurance placement for 2013, where we believe we've timed up the reinsurance placement and indeed improved it. And I can tell you as of today, we are well-advanced in structuring our reinsurance programs for 2014 and beyond.

Secondly, we did consolidate our thinking around distribution. But one of the very few insurers in the world that has a true global reach and therefore we think that a critical advantage, that we can access our global trading partners from multi-geographies and we believe we're doing that far more effectively than we've done before. And obviously then we have our operational transformation program that will go into in a lot more detail in a few moments.

In terms of financial strength and flexibility, Neil Drabsch will take us through the capital and balance sheet positions as we expect them to be for the half year. And in due course, our analysis of the markets globally is telling us that we believe there will be an excellent opportunities for profitable growth in the future, but where for 2013, our focus has been very much on consolidation.

So taking you into operational excellence. I'm sorry, this is a bit of a busy slide, but the real purpose for us around the operational transformation program is dealt with in the heading in the slide and it's predicated around creating global scalability and an engine for growth. That is the overarching ambition of what we're setting out to achieve.

And the first wave of activity is deliberately not IT-driven and that's for two reasons, and enables us to deliver the benefits more quickly than what other buys been the case. And in our experience, IT tends to increase the investment case and can muddy the waters in terms of the benefits coming through.

So if you look at the left-hand side of that slide, we're focused firstly around process and it's very much about simplifying what we do and standardizing the processes and doing so globally and part of the overarching ambition here is to ensure that we constantly set out to improve the processes and the service that we're providing to our customers. Secondly and in the middle of the slide, there we have set up a Global Shared Services Center and we set that up in Manila. I'll talk a little bit about that in a moment.

And that is a Shared Services Center that will work in the first instance for QBE's three largest divisions, being Australia-New Zealand operations, QBE in North America and QBE in Europe. And then thirdly, on the right hand side of the slide, the ambition there is to ensure that we create a market-leading organization around operational excellence.

So that's about having a single operating model that can apply for QBE to about constantly seeking to improve the process that we deploy, it's ensuring that our actions, and the operational space repeatable and predicated around quality delivery and ensuring that the teams or staff we employ are the best quality that we can employ in that space, and that we do become an employer of choice.

So these four key objectives that we set out to deliver against in setting up a Global Shared Services Center and I'll deal with them slightly in a different order to the way they're positioned on the slide and in the order, which it strikes me as being most important. So the first is really around business growth, so is about creating scalability in our model and making it easier for us to grow and ensuring that we reduced the frictional cost and expense as we do grow.

Secondly really is around service quality and it's ensuring that our customers receive a better service, whether that'd be the brokers and the intermediaries, we deal with all their customers. So that's about improving performance management, improving the turnaround time and all other processes and functions that we carry out and then ensuring as I said before, that we look to continuously improve in what we do.

Thirdly is cost effectiveness and that's really around the standardization opportunities. So if we can standardize what we do, then it avoids cost duplication and that in turn drives economies of scale and then fourthly, we believe that the Global Shared Service Center will facilitate growth through acquisition, and that it will be far simpler to integrate businesses in the future and also to drive high cost synergies out of acquisitions that we do make.

So the question really is around why Manila and why captive model. I mean, needless to say we looked at all of the options. We do through our lender placed insurer in North America, QBE FBS already have just over 300 staff working for us in India. So we looked at the opportunities that sat around that model. We also looked at Central and Eastern Europe where we have operations and indeed, we looked at Latin America as options for us.

But set up on Manila for a number of different reasons, some of which is cited on the top left of the slide. The evidence that we looked at suggested that the infrastructure was more robust and more reliable in Manila than it would be for example in India. Clearly there is proven capability in Manila around operational excellence and there is also a cost competitiveness there. So there was quite a detailed review as to what location and why and as I said, some of those reasons are shown on the slide for you.

There are a number of different delivery models that you can deploy and they're on the bottom left hand section of the slide there. We've chosen a captive model because it -- therefore is a dedicated subsidiary of QBE Insurance Group Limited; it's our business, it's our people, it's our assets. So it's fundamentally part of our business. So it's not services being provided by third-parties, they're not non-QBE employees, they're all QBE employees and we felt this suited our requirements far better than the other options that were available to us.

So just looking at the P&L impact on the operational transformation initiatives. I think I've been fairly clear on saying that it's at least $250 million and that is an expense number. There are claims procurement benefits as well, which we'll talk about a bit later on, but our sense is that it's very hard to evidence the claims procurement numbers as they go through the attritional claims ratio line.

So when we present these figures to the market, we tend it to concentrate around the expense number. So it's expenses, it does include procurement, but only non-claims procurement in the numbers that are being shown there. So just to explain the graph in terms of the bar graph, you've got the cost savings, actually earned in year.

So in 2013, there is a net investment in setting up the service center of $131 million and that's why we've talked about an underlying insurance margin for 2013 of 12%, which therefore includes the 1% investment that we're actually making in 2013 to set up the service center and you'll see for the ending year, we're quickly into a benefit of -- benefit over cost of 50 million in 2014 and 226 million in 2015. The red line at the top is actually showing you the run rate savings. So on a run rate basis by the end of 2014, we're pretty close at 225 million to that 250 million. So as I was saying earlier on, the benefits do deliver quickly due to the absence of IT, it is all about people, process, and location here. So quickly the benefits are coming through.

Second thing to say there is that the costs are actually coming down slightly. So costs are down by 20 million than our original estimates, and you'll see some of the reasons on that, when Colin Fagen presents the case study on Australia. But we are heavily expensing the program. So we're carrying a very little expense through the balance sheet, hence the benefits when they come through will be real. And then the second bullet on the right hand side is talking about the claims procurement run rate savings. So we're talking about at least 90 million coming through on the claims line in addition to the 250 million, that's on the slide on claims procurement savings.

So in terms of the way in which the transformation works, what I'd say is the immediate benefits that were referred to on the previous slide, predominantly come through from our Australian business and our North American business. And that's simply because European operations is the third division to come on stream and you'll see in a minute, they're still developing their plans, it could well be that there will be further savings to be realized when they do flesh out the details of their plans.

I'll break the slide down really into three sections. So in terms of finance, HR, claims and operations, these are really the priorities that are being run through the Global Shared Service Center. So for example, in the instance of finance, a significant proportion of the global workload will be carried out through the Global Shared Service Center with a primary objective of delivering faster group financial reporting.

In HR, most administrative processes will be run out to the Global Shared Service Center and in claims it really depends upon the divisional appetite as to whether it's back office claims roles being run out of the service center or whether it's a blend of different arrangements which for example will apply North America between using on shore third-party adjusters and using the Shared Service Center. But in every instant, complex claims are being retained within the divisions.

Operations really is ensuring that we get the distinction between front, middle, and back office absolutely right and use the Shared Service Center to best effect. So as those full functions that really sit within the Global Shared Service Center and then really from an IT perspective, it's ensuring that we leverage our global franchise, not global buying power when we negotiate contracts, particularly, for example, in the area of application development and maintenance.

And then for non-claims procurement, we're again taking a group-wide view of the way in which we procure services or parties or partners in the way in which we do business to ensure that we can be more strategic in our sourcing and procurement plans.

So just to give you an example of procurement, again quite a busy slide, but it's breaking down in between blue and gray, the benefits we can see in claims and non-claims procurement. So the x-axis across the bottom, going from right to left shows you quick wins to harder wins and the y-axis is showing you low-to-high benefits. So we've ranked where we think we can get best effect from procurement savings, and obviously the size of the bubble is giving an indication of the size of the price.

So you can see from the slide, there are significant claims initiatives in play, and we've got a value attached to those of 90 million. As I was saying earlier on, it's not a number we're calling out in the expense because it's a number that will go through the attritional claims line and the balance for these non-claims procurement savings, which really come from two areas predominantly.

The first is major IT contract negotiation and consolidation, so taking a single view of where and how we deal with IT vendors across the globe and secondly is reduced dependency on either temporary labor or third party consultants through the business.

So then really just through the timeline, just looking left to right, in terms of Australian operations, Colin Fagen will give you a detailed update in a moment. So I'll let him pick up on the pieces there. If you look at the bottom of the slide, North America's planning is actually complete. So they are now actually in implementation mode, so the process has begun for North America to come on stream both within the Shared Service Center and as part of the overall program. The confidence we've got now in the operations probably will see us accelerate some of the activities for European operations that were originally slated to commence halfway through next year. So we may see some earlier traction in that respect and some increased benefits.

An important point to me really is in the bottom right hand corner of the slide, in the program that we're putting in front of you runs through to 2015, but we see operational excellence as something that is intrusive [ph] and should fundamentally be part of the way in which we go about our business. So this is very much a start, a first wave if you like and there will be more activity that will follow.

So before Colin Fagen stands up to take you through the Australia-New Zealand case study, we just got a little video to take you through.

(Video Presentation)

Colin Fagen {BIO 17308097 <GO>}

Good morning everybody. As you can see from the presenter and from a few other places in that video, we're not necessarily selected on a good books, might be just the presenter. Our operational transformation is not only a cost effectiveness project, there are numerous other advantages emanating from this initiatives.

Previously where we have organically grown or grown through acquisition, we've not optimized our synergy benefits or maximized the opportunities for economies of scale. With the operational model that we're building, we have now and we'll have and now have significant scalability as we do continue to grow in this market.

We will not only improve benefits from organic growth, but we'll also gain benefits from the ongoing IT strategy and the ongoing investment in our Group Shared Services Center. And there are opportunities improving our service levels through tighter process controls to improve performance management, to reduce linkage. We are building the foundations for continuous improvement in our operations.

Now in our plan, the original plan was to deliver a cost savings of $85 million per annum. At this point in time, we feel extremely confident of going to exceed that expectation. We're primarily exceeding it for two reasons; potential redundancy costs in the Chinese program are significantly less than what we've expected, and we're also seeing the volumes and take-up rates of work in Manila is also more than what we anticipated. Now I'll give some more background information to both those points throughout the presentation.

So at this point in time, we're probably literally in the peak, this quarter is the peak of the Chinese program for Australian business and this slide shows that to some degree, we've made great progress to-date, a transition experience and clearly lessons learned allowing us to continue to refine our execution processes.

At this point in time, our motor claims are fully live in Manila. Our property claims are primarily -- are in transition and this is primarily our household's portfolio. We have commenced work with our workers' compensation business, our travel business and our Elders business. We've expanded our credit control activities into Manila, that finance transformation is underway.

Electronic business referrals are now live in Manila and in July, we will substantially increase the level of processing that we're having in our underwriting activities in Manila. Our IT transformation is also well and truly underway. And looking -- and we've some of [ph] the outsourcing application development to Accenture, which is really combining and getting economies of scale from our model with our European operations business. And this provides us a great opportunity for us to ramp up IT expenditure in the future, the lower cost model where we have opportunities to improve the business going forward.

We've also selected MphasiS as a global supply for testing, so again achieving economies of scale of our business around the group. The HR services solution design is underway and we have selected a payroll external provider, it's now contracted and we are working on its solution design. Our procurement is currently on track to delivering forecasted savings through streamlining processes and ongoing selection of our supply panels. So overall, we are making significant progress in our business.

As John touched on, here's a few busy slides here. This slide illustrates the methodology employed in our various streams, processes that not just lifted and shifted. They are redesigned to maximize the efficiency before we move them and as John touched on, we are minimizing the IT spend, this is social [ph] with these. So in any changes that require in IT spending, a rule of thumbs any more than two days work, we're actually done undertaking at this point in time.

This is a comprehensive process for knowledge transfer, will involve that technical experts in both Australia and Manila. And if there are any issues on transition, there are go or no go decision guides which insure risk to minimize up on transition. We are also comfortable talking a variable volume ramp up in stabilization phase which was gained and shows successful transition of activities.

We've had already over 50 subject matter experts from Australia and Manila, assisting with the change and that's actually expected to peak at 30 individuals in Manila at any one point in time. So with that subject matter experts in Manila that they are there for the knowledge transfer, they are there for training, and they do assist when we go live on transitions and a number staying for extended periods, to train, to mentor, to coach and to supplement a local leadership.

This slide illustrates an example of a process reengineering and here this is our operations area, which is the underwriting processing area. What it does show in the functions that we moved, is that we're moving components of roles, we're not necessarily moving whole positions. So we're going into a lot of data, this slide shows that the higher volume activities of our operations can be delineated between our Manila and Australian business.

The triage methodology ensures activities are required in-depth underwriting expertise are performed in Australia by the appropriate staff and the processing and administrative components we're undertaking in Manila. A significant proportion of a more experienced and senior underwriters time has historically been used in basically processing activities. And this change enables more of their valuable time to be more appropriately used in core processing, in core underwriting activities. And this same principle applies for our client's areas, our credit control areas, our general finance areas.

A significant amount of effort has been put into building an employment brand and culture in the GSSC. This is a differentiation factor in our recruitment activities in Manila and all suggest to you that our stronger recruitment protocols around the world are in Manila.

Part from the comprehensive testing we undertake, we'll also have interviews conducted face to face to our panel, which in every instance is included seniors Australian managers. And this has now assisted in selecting high quality recruits, it's also assisted in increasing acceptance rights, where we have offered roles. This is an issue for a lot of organizations building up in Manila.

There's a help build the ownership in a relationship models between our two locations and this is establishing very strong foundations for both our Australian and Manila business with respect the relationships within the business.

Induction is over a week, and this also ensures that our teams in Manila align to the QBE culture. And there are two major advantages in our recruitment which John touched on and that is having a captive organization. Recruits want to work, that have loyalty to organization that want to work for captive organizations. The other advantage that we've experienced is also working on Australian time zones.

So people for some of them, reason preferred of working (inaudible) when compared to some U.S. organizations, so what we're also finding is maintaining the top quality people looking to move to Australian organizations. So overall, this is building an extremely strong depth of talent in our Manila business.

Now designing these projects and the process as we are looking to move, we worked on the assumption that the equivalent of one role in Australia, one FTA role would be equal to one FTA role in Manila. What we are already finding is that, that is being outstripped in productivity, in virtually every area, that is happening very quickly. And some more steps we have up here show that, so we're seeing improvements in various serious like formalization rates in our client areas, we're seeing improvements in various processing functions.

And part of that is not necessarily a criticism of our Australian staff, as in redesigning the models to ensure that is actually very specialized and built for high volume. So in that delineation between the more qualitative aspects of their roles and the more high volume aspects of the roles is actually creating that opportunity for getting that sort of volume increase and it is also an area where we're already outstripping the expectations of this project.

And you might see -- in seeing that statistics up there, this is before actually looking at ongoing business process for engineering within Manila and within the retained organization, within Australia and aligning our future IT investment. So we're seeing further opportunities for improvement in virtually all of that qualitative metrics. Now across a $5 billion business, which is roughly what we have in Australia and on top of that $5 billion, we have $1.35 billion managed fund business. We see opportunities to increase these and some of those small numbers actually have reasonable compound value in our business. And equally when you roll it up to $18 billion to $19 billion business around the globe, these statistics have a real value.

So showing this graph -- we're showing that in the change program, there is hiccups from time-to-time, and that's the reality of our change program of this level of magnitude in our business, which is being driven through the business in a very tight timeframe. So this graph outlines the volume of work in progress in a clients department, which basically covers personal loans and motor and claim portfolios. And it shows the outstanding work on a weekly basis and if you see that line across the number 3,000 that's really the rule of thumb in our business where we start to actually get complaints with respect to service. And that's where you risk losing clients if anything drops stays above that number for any extended length of time.

And if you go back a year or two in significant catastrophe activity, that's when we would have seen that sort of outcome. Now in like February, we spoke to a client staff about the change and the reality of when bringing in this changes, that productivity slightly dropped as a first change, that the first mention of these sort of level of change. On top of that, we had a Tropical cyclone Oswald which happened exactly at the same time frame.

So we had about $73 million in claims of that catastrophe. So these two aspects were combining into our business very quickly. We had already started ramping up our Manila business. What this graph shows in very short time frame, we're actually able to turn around the business and again get the improvement and the expectations in the market.

It's the only exchange program, that reality of these we've got hiccups from time-to-time, but we're very confident that we can improve the underlying business, with the combination of our Manila and Australian operations have it back on track very quickly. So what we're able do is basically in both claims in underwriting areas before that more consistent, more timely and more predictable service over time and this isn't something that we would necessarily had all the time in the past.

It was mentioned in the video that some of the customer feedbacks have been very positive that's been emanating very quickly. We've received a significant amount of positive feedback. So right from the start, we had a strong customer service ethic that's been installed in our Manila operations.

You would have seen in some of John's slides that Manila workforce tertiary qualified, average age of about 34. So a very much of scalable educated talent pool in our business and we expect this to continue as we grow through 2013 and beyond. We expect to have access to an even larger educated talent pool particularly with a level of both private and government investment in this industry in the Philippines, this has seen as a major growth industry for that whole economy.

We've also undertaken a significant amount of communication with activity with our broker network. In the inter-motor [ph] markets, a large number of the international brokers were actually bringing through this style of projects, so they actually do have an intimate understanding of what is involved.

The feedback is pretty simple that we judged on our execution for this change and had time table. So that is why we're working very hard to have the vast bulk of this project finished in this calendar year. And everything is on time table is at this point in time, in fact was slightly ahead of time table.

There's been a lot of speculation, lot of misinformation around retrenchment activity in our business. And this slide outlines the acquisition as at the middle of June. And we've always had the objective of redeploying as many people as possible in our business, and allowing natural turnover to release the Australian roles over time. So as of mid-June, I think we've been extremely successful in our redeployment activities and we've actually only made 39 people redundant in our business. We've also used this to obviously decrease the level of contract -- contractors in our workforce, as we bring down the number of people in Australia overtime.

And in planning this project, in some of the cost numbers you would have seen in the Australian numbers, we were actually built in an assumption of 75% retrenchment numbers. So this is one other reasons why we were significantly below the cost expectations in the business. And in our Australian business, the rule of thumb for probably this next 12 months to two years is an expected turnover of around 16%. So we're very comfortable that natural attrition will actually help us to achieve our objectives and we're comfortable staffing up early and quickly in our Manila business to ensure that the services and workloads are actually kept very flat.

So overall, we provided an excellent balance in both exceeding our financial expectations while minimizing redundancies in our business and allowing natural turn over to continue to take its course.

So overall, we've actually done a lot of the heavy lifting and this will help set up this program for around the globe. We've now to establish a lot more consistency in our business, but not only in our processes and methods, but also our customer service and quality metrics. We have seen significant improved scalability, which will assist in both organic and acquisition growth in the future. We'll also ensure to be maximize the value of IT strategy and IT spend over time. So within Australia, where there is a strong competition for talent, our teams are focused on the higher value activities, the higher value tasks that require valuable technical and relationship management experience. So we are very comfortable with the formation of GSSC, is setting up QBE for a broad and sustainable future in the next few years will have a material improving effect on both our service levels and our financial returns. Thanks.

Neil Drabsch {BIO 2093435 <GO>}

Thanks Colin. It's part of this program, well, I was just not directly associated with transformation program as John pointed out earlier. The value creation model absolutely relies on us maintaining financial strength and flexibility. We're in the financial sector, which a sector that's been through tremendous change through the Global Financial crisis and particularly the requirements of our key regulators and the rating agencies, I think it's fair to say, each of them have raised the bar and the cost of capital is high and certainly the amount of capital that companies in the financial sector, it was obviously pointed directly at the banks, but we -- as the insurers had to follow a suite and it's been part of disruptive period during this process.

A lot of questions probably not unreasonably so about the quality and the quantity of that capital and hence that we've been extremely active over the last two years in making sure that we are in the right position to go forward, particularly as we go through the cycle of change.

So in looking at our value creation model, it's very important that we do understand the importance just of maintaining the financial strength for the immediate purposes, but also for the future growth and the transformation program is just part of that valuation, but at the same time, this company is poised to take advantage of this next cycle growth.

You do have to balance the needs of all of your stakeholders, we have many. We operate in 48 countries, 48 regulators, rating agencies and regulators. I'm sure many of you will understand that, but in doing so and putting the company in a position where it can able to go forward and balance those needs of their stakeholders but at the same time, put ourselves in the decision where we can grow the company and achieve the ambition of getting the right return for our shareholders, to put value into shares is a critical approach and one of the focus for us.

For the last 18 months, so we've been very active, we've had a share placement, we've issued subordinated securities, clearly that's been in line with as the Regulator Australia has come into play with LAGIC. The Board have also taken the view in terms of lower dividend payout and that's not easy for shareholders. But it's the right decision in a company that's going through a transition at the moment in this current environment and that you will see I think the company's balance sheet in normal profit positions now strengthened quite quickly to put it into a strong position for future growth.

We have also recently had the tender for our senior convertible securities. I'll talk about that in a moment, but each of these items have added significantly to the strength of the capital. We have I think responded to the LAGIC requirements and I think generally in the industry, the uncertainty around the APRA LAGIC framework has been resolved.

Described capital amounts will be within our target range, these will vary, particularly for QBE because of our multiple currency operations, but we're quite comfortable within that range and APRA is at the moment heavily focused on conglomerates standards that's not expected to have any major impact to QBE, that we won't be considered a level three group. And I think we will be classified as a GCP [ph] and using the bank criteria, but we will be known as I think an international active insurance group, which is consistent with our size and have global footprint.

Standard & Poor's, a major rating agency also at the end of May, reaffirmed our ratings and in fact took our outlook revised to stable from -- originally from negative. I think this is a very positive move we do a lot of work with the agencies and they take the prospective view of where we are and our plans for the future. I wish your credit rating as expected and consistent with the market trend was taken down to A- consistent whether we see U.S., and other operators in this particular market. Whilst we have taken basic capital additions, which you can see through some of the share issues and strengthening of the subordinated debt, in addition, where another initiatives include a clear plan to reduce borrowings, it should be the correct approach where we are at the moment as profits start to strengthen and also in a marketplace, we have a little bit more stability, our borrowings will start to reduce. We're going to take advantage and we have taken advantage of the low interest rates for borrowing, which clearly going to be here with us for a while, but we are seeing signs of this may improve.

Particularly in relation to our liability management, yesterday, we settled a subordinated debt repay, that was 220 million U.S., prior to that in April, again taking advantage of the lower interest rates, we secured a 600 million short-term fund, which was primarily used to help pay some of that convertible securities. And in relation to those SCS or convertible securities, which did result in the issue of around $300 million of QBE stock, which went out on 27th of June, whilst these securities are complex, they're very flexible for us. We did receive options, we did repay 234 million, we repurchased 317 through the tender.

And some of the investors decided to hold them considering the underlying yield of 2.5% was attractive, 223 and we're still holding our balance sheet around 170 million which they consolidate. So at the end of June, you'll see that we have a still outstanding debt of around 223 million, but understanding internally we are holding still 170 as well, which will the result as we go through the next put period which is on the 15th of May 2015.

And we are on target to debt equity of around below 40% by the year end. We'll see when the half-year results come out, foreign exchange does have an impact on the structure of the balance sheet. So it's not as simple as say in a dollar balance sheet, we're reducing debt with a lot of moving parts. We'll get a bit more color on that when we see the half-year, but the target of getting less than 40% by 31 December is certainly achievable.

There are a number of other initiatives that are underway. John has mentioned before talking about core and non-core, there've been a number of non-core asset sales that we have negotiated. Those will be mainly finalized in the second half. I think that's in Australian noting the potential IPO of Steadfast indicated that Australian broker, the NCIB which is the trade credit broker has proposed to be solid at Steadfast. However that is subject to successful IPO. There is a small broker in Australia Invivo and some of our Central Eastern Europe businesses, again more detail on this as we progress into the second half, but at the moment we're considering that as that pricing should be around in total about 80 million.

There are other initiatives in play, and further non-core assets, nothing particularly material. But these are smaller assets that -- are that don't be that strategic objectives and/or value creation model. And you'll get more detail of that as we go through the period. There are a number of our clients' portfolios that are in runoff. And all we're talking with the some of the businesses we're writing [ph] which were rather to commute those arrangements to fix the liabilities or ultimately perhaps to sell those portfolios. I think the gain that will be seen as a positive, it will help the run-off those businesses do have run off portfolios. Again we'll give a bit more detail on that as we go into the second half.

Also additional reinsurance will be used as required from time-to-time, particularly if profits are in the bank, we can use reinsurance to help us there. So there are a number of initiatives that are underway. So this is been a -- prices has been quite active over the last 18 months. I think we'll see the advantage of that as we go forward. I'm happy to take some questions a bit later on, but in relation to the half year of course, we can't say too much at the moment, because the half-year results are still moving at this point.

So I'll pass over to John and to give you a summary and update of where we think we are in the first half.

John Neal {BIO 15681439 <GO>}

Thanks, Neil. Just recapping on some of those we covered off today. What as Neil said is very early for the half year, we're still confident on our ability to deliver on our full year 2013 forecast. I think through various programs, notably the operational transformation program, I think we're demonstrating our ability to leverage our global reach and scale. I think as Neil just ran you through, we're working very hard on the balance sheet. And in terms of improving our capital position and we'll give you a fuller update on that with the half-year results later on in August. And there are a number of initiatives that are also running through the second half of the year, so that's continuing.

We're very pleased with the strengthening we've done with our executive leadership team and those CEOs settling in well. I've just spent time both in the UK with Richard Pryce succeeding Steven Burns and then also with David Duclos in North America. So that's going well for us and we've also set up a Leadership Academy this year for the first time. So we're also looking at building our leadership team going out into the future.

Trading conditions, I think I described as sort of okay in inverted commas, it fluctuates depending on what market you're in, still very positive, I think here in Australia and actually in North America still seeing good rate increases there. It's still pretty tough in Europe at the moment, with rates so broadly flat but at least, we're seeing good macro tailwinds sort of on our backs rather than in our faces now, so that's good news particularly from the balance sheet perspective.

So just a few quick comments really through the half. So rates are up 5% overall and that's really driven as I was saying just a moment ago by Australia and the U.S. I think that probably up slightly above expectations of the half year, but our assumption is that rates will fall off slightly through the second half particularly in Australia and perhaps also in the U.S. So, rates in the U.S. are particularly strong through the first half.

So it's still very, very early days for the half year, but we're quite relaxed then where we see ourselves at the half year, always accepting and stating the obvious, that we are only halfway through the year. So our annualized first half investment yield is in line with the full year '13 guidance, which is for a return 2.25%. So naturally overall, the weakening of the Australian dollar is good news for us, but it does bring some complications particularly with the currency mix of the U.S. dollar. So it just takes a little bit of unraveling and that's why Neil was saying, he'll take you through that with the half year results in more detail.

And from a set of catastrophe loss experience, it's been fairly quiet through the half, then when you -- really been three notable catastrophe losses, Cyclone Oswald here, but Colin Fagen was referring to climate tornadoes that you will obviously be familiar with in the U.S. and then obviously most recently the European floods, which I think is more severe than most people realize, certainly worst than the floods of 2002, for those of you that remember those floods. So, three notable catastrophe losses, they probably add up, I would have thought something like $15 billion or $16 billion globally, so still a quiet first half.

But in addition there had been a few risk losses, I think most people have seen rails losses in Utah over the landslip which was pretty big, by any standards and then similarly, there was a fairly notable loss in the U.K. around the rail infrastructure, the significant collapse of a railway line. So there are some risk losses around, but again nothing that would suggest to us that we should be outside of the allowances that we've set aside and nothing as I've said before, we set aside those allowances for the full year. So we'll run those through on the assumption that they will be needed at the half year. But again we'll explain that as we go through the half-year results.

Weighted average discount rates moved in our favor since 31st, December. Obviously, we'll see how that plays out in some detail, but clearly that's going to have a positive impact on the claim central estimates as we run through the half year. And I think as you've just seen through Neil's update, that there are significant number of initiatives that will have been completed by the half year and will continue through the second half to improve our capital position and improve the balance sheet.

So all in all, a lot of work still to be done to complete the half year, but feeling quite comfortable as we stand here today. So without further ado, I was then just going to hand over to questions and answers. Thank you.

Questions And Answers

Q - James Coghill {BIO 14006200 <GO>}

Hi, John, James Coghill from UBS.

A - John Neal {BIO 15681439 <GO>}

Hi, James.

Q - James Coghill {BIO 14006200 <GO>}

It's quite a refreshing change, seeing all these initiatives, especially compared to years gone by. I guess that the challenge from the outside looking in is trying to gauge how much of this is catch-up and addressing past years in under investment and how much is actually propelling you ahead of competitors. I was hoping if you could you just provide us some insight into whether you modeling this transformation on certain insurers that have developed global based practice or whether you think you are lead -- probably ahead of the competition?

A - John Neal {BIO 15681439 <GO>}

Thanks, James. I guess I'd break the priorities for us down in to three constituents. So first and foremost is performance, whatever way you look at it, we are totally focused on delivering against the margin calls that we've put in the marketplace for 2013.

The second, really in the operational transformation program is around the change and I think that's just accepting the reality that globally insurance is getting more competitive year-on-year. And we've got to create a competitive advantage in our acquisition costs. So to try and sort of save nearly 2% of the combined operating ratio is a start for us and that's what, so we got to keep working at it.

I think it's an early start, as Colin Fagen was saying it's running both ahead of expectations in terms of benefit and that less from a cost point of view, so encouraged by what we're doing. I think if we get it right, then it will give us a competitive advantage, because I think insurers excel in a number of areas, but few excel in operational excellence. So I think if we can achieve that, it will really set us aside globally.

And then the third really is ensuring that we build the right leadership teams for feature of the organization and hence the investment we're putting in that aspect to our business. So I think for the time being it's in terms of the pure cost initiatives, it's one recognizing that we've got to be more competitive in an increasingly global world and two, you're absolutely right, it is to put us of ahead of the curve.

Q - James Coghill {BIO 14006200 <GO>}

More specifically, are there insurance models up there, that are (inaudible) maybe both as QBEs and that have outsourced claims on the scale into an offshore platform. And that have had success, I guess that's what I would see as the key risk here and you do flag that you will retain complex clients management on the ground, and it's only the mostly generic and easy to resolve claims that get outsourced, but all the other insurers that have outsourced using an intermediate model with success?

A - John Neal {BIO 15681439 <GO>}

There are. So I think in terms of the complex claims, we define a complex claim is being a claim that has a value of $100,000 or more. So any claim at that level, we would retain as a matter of course, but then we'll lose segment claims and define what aspects of claims you might want to retain elsewhere. I mean if you look at the big U.S. insurers, it's pretty common practice for them to use third-party adjusters and/or offshoring as a mechanism to support their claims initiatives.

So it's a pretty well driven part for the ACE Travelers and then in the European trade for the Zurichs and (inaudible) So it's been done before. So I don't think we're ahead of the curve in setting out to what we're doing. I think we feel that we can learn the lessons for them. What they've done well and perhaps what they've not done quite so well and perhaps improve on that. But we're setting all the first in for this type of program.

Q - Siddarth Parameswaran

Hi, John, can you hear me? John, it's Siddarth Parameswaran from JPMorgan. A couple of question if I can, just the first one, just on the -- what are some of the risks that you see in introducing such a large transformational change all in one go? And in particular, if you could just comment on whether you're taking to cap it, you may be losing some skills as well in and you -- or you may not be developing some skills domestically to deal with some more complex clients particularly if you're losing 15%, 16% of staff every year. Whether there is some risk that you won't actually have in the development of complicated skills going forward?

A - John Neal {BIO 15681439 <GO>}

Yeah, they are good questions. I think on the risks perhaps one think we've not explained careful enough was that we ran a pilot through 2012 in any event to ensure that we ran onshore and offshore functions whether it's claims or other functions in parallel just to sort of test out efficiency and effectiveness measures. That's one part of it. Second part is that we're being quite careful as we hand over processes. So you know we are doubling up on shore and offshore just to make sure that the processes are absolutely in place and meeting our expectations before we switch offshore to onshore. So I think in terms of risks we're being more cautious than perhaps you would normally expect, but I think that's the right way to go.

And in terms of skills, I mean, almost 10 of the other way around, I mean, that's one of the reasons why we set up a captive in Manila and that we would consider the global shared service center if you like to be sub-division of QBE and we don't see why we can't rotate staff through the Global Shared Service Center into other divisions.

So as Colin Fagen said, we've had up to 50 of our Australian staff actually operating in the Global Shared Service Center, I mean success for me will be looking at the people we employed in Manila and having those individuals work for us elsewhere in the organization. And I think ironically, one of the big challenges of the insurance industry has always been knowledge transfer in any event as you've got that generation of 50-somethings into the 60s actually retiring.

So, I think it's teaching us very well-disciplined practices around knowledge transfer to ensure that we can actually through different functions educate our existing workforce, so if anything it's home to our [ph] thought around process.

Q - Siddarth Parameswaran

If I could just ask one more question, just on the rates environment. If you could just break down, just the rate increases between the U.S. and Australia and just if they are real, once again?

A - John Neal {BIO 15681439 <GO>}

So the rates in U.S. through the first half probably slightly ahead of expectations for us. So if you look at the property and casualty classes, so on the program business, rates are up by about 9% and on the property and casualty classes rates are up by about 6%. I think as you know on the lender placed insurance we went through processed last year that agreeing and filing rates across the States which you'll actually see those rates down by 8% this year, 9% next year. So that's exactly as forecast. Australia I might ask Colin to comment.

A - Colin Fagen {BIO 17308097 <GO>}

So going through the year, up until the end of May, average rate increase across the entire portfolios is about 7.3% in total. June, we probably saw -- the rates not hold up to that level but I can't give you a real hard number at this point in time.

Q - Ross Curran {BIO 15090587 <GO>}

Hi gents, it's Ross Curran from CBA. Just wanted to talk through slide 12 where you've got the pictures of the potential savings and particularly the claim savings. Can you just give us a bit more of a feel for the panel optimization on legal business and the loss adjustment optimization, just have that plays through and what we can expect in that?

A - Neil Drabsch {BIO 2093435 <GO>}

So, but basically we're looking at processes where we're tightening up the panels and giving more work to forming individual relationships to actually get more consistency in the service, more consistency in the output, mostly that flowing through virtually all aspects of our client service. I think there's also in some of the parts of that business in the multi-country accounts, we actually have the opportunity of actually explaining that across for a global reach as well. So basically just looking at -- previously we probably haven't had our panels as tight as we would like and so, we see opportunities in both cost and service delivery from those panel providers.

Q - Ross Curran {BIO 15090587 <GO>}

So this is a benefit of sort of probably integrating, this is that perhaps having been done in the past, is that?

A - Neil Drabsch {BIO 2093435 <GO>}

No, it's a component of that, but also to bounce back to Sid's question before and probably a little bit of James' question, also looking specifically the Australian business. We probably are focused on making sure that our loss ratio is in line, first a couple years ago, and so, we really focus on getting our loss ratio down to around 16 points and compared to most of the market, mostly our direct competitors, also just that was probably the best in the market in the calendar year last year.

So then coming into managing the expense components into that and the interactions to our client's loss ratios as this is the next stage of our change program. So we believe that we can get further improvements in the underlying claims ratio, but we think we're already starting from a very strong position in the claims ratio and that willing to twine with our expenses as well.

With respect to risk in such a large change program, I think it's more of a risk doing nothing, nothing is more of a risk actually extending the change program have a too prolonged period, it does unsettle the business for a short time, so ensuring that we actually move through this change in a relatively speedy process and delivering that change with the pretty a well-known in date transparently whether that change is actually more important.

Q - Ross Curran {BIO 15090587 <GO>}

Sort of specifically on the loss adjuster optimization, can you just explain?

A - Neil Drabsch {BIO 2093435 <GO>}

So looking at Hayward, where we're into 20 assistants, so that we have more active, he's undertaken by the loss adjuster's at earlier stages or by individual client staff, looking at how we actually have more transparent information shared between our claims teams, both offshore and within Australia. We can go -- get you with more details afterwards if you like.

Q - Toby Langley {BIO 15924432 <GO>}

Good morning, guys. It's Toby Langley from Nomura. Neil's comments about selecting core versus non-core business, I wonder if you could give us some sense as to the metrics by which you're evaluating businesses and how you're making a decision there. Is it you need to make sure a transaction is accretive or is it better just to have the cash and give your sales a flexibility?

And then maybe, if you could give us some further metrics if possible beyond the 80 million of cash proceeds, what kind of premiums, capital or earning that you're kind of sacrificing here in order to do this?

A - Neil Drabsch {BIO 2093435 <GO>}

Well, I'll start it off. When over time, we find that there are businesses that either been acquired or part of our existing business that not deemed to be part of what we would call core. I mean, clearly we've been looking carefully strategically at our businesses and those that will create a value in time ahead.

For example in Australia, the two that we nominated in the slide and in fact to insurance brokers, a broker primarily acts for the insured, not the insurers, there's a natural differentiation there in terms of the client. And therefore, we feel that the brokers in the situation, which sit better perhaps in this case particularly, say with Steadfast who is a specialist broker structure, we're quite will and that also meet our objective, the business whilst it's profitable.

Objectively it actually get still out true value creation as we're insurer and we can do that we believe our relationship with a broader provider such as a Steadfast or as we do with those brokers, would create value for both sides of the equation. At the end of the day, you're looking to try and provide the policyholder with the best form of service as well. So they're two very simple examples where we identifying a broker rather than say an underwriting agent, is better to be owned by some of the other entity.

Throughout time we do acquire -- we have acquired businesses that haven't performed because of conditions that perhaps has not been greater for example in Macedonian operation, economic conditions in that country, it really been quite poor, relative to our sector. And therefore let's deem not to ultimately do add value and therefore, as well a small business. It's one that we feel could be, we would be that'd best to retire from that and leave it and put our energy elsewhere.

At the end of the day, what we're trying to do is to turn where is the best place for our capital to be placed. That's not only in terms of risk, but also in those assets that can produce profits, nothing particularly is targeted, but everything is under the microscope in terms of whether a business can produce the right return, and more importantly with a strategically major ultimate objectives.

A - John Neal {BIO 15681439 <GO>}

I'd just add, it's not necessarily negative comments. So there are instances where we think we've got market-leading skills and when we've done an analysis of the market opportunity we think we could be larger. So it's really driven off sustainable performance and profitable growth.

So there are some areas of our business where given the right market conditions, we believe the business that we operate in could be substantially larger. So I mean, a simple example of that is that last year we went through a process from management point of view, consolidating our reinsurance businesses under one leadership team and at the right point in the market cycle, we do believe that, that business could be larger. You might remember from previous discussions, our reinsurance business has outperformed our insurance business by seven points over time on the combined operating ratio.

So again that's an area where we think we could grow. So core is about maximizing opportunity and use of our capital as much as a negative comment about businesses that we think we shouldn't be in.

Q - Toby Langley {BIO 15924432 <GO>}

Can you give us any flavor of the kind of slide rule that you apply with regard to return and growth being the kind of front-end center around retaining or not retaining business?

A - John Neal {BIO 15681439 <GO>}

Yeah, so I think if I give you two sets of opposite examples, if you look to say Neil's reference to Macedonian business in Central and Eastern Europe, a profitable business for us, but not one in which we could easily see any growth coming for us. So we would deem not to be called. And therefore, we thought it's appropriate to sell that business. There are one or two others in that category, and you'll see us talk more about those as and when we're in a position enabled to do so. In other areas again, similarly in small business, but in the Pacific Islands that business grows about 10% per annum for us and the results are absolutely excellent. So we consider that to be our core business, which is highly profitable and can grow. So these are certainly not defined by size, but as Neil said, we have absolutely analyzed and looked at every business in every region we operate in and define what categories they fall into.

But it is actually ultimately about leveraging those areas where we can grow the business.

Q - Toby Langley {BIO 15924432 <GO>}

Okay, and if I can ask the second question for Colin around the productivity improvements on this on the slide I think it was page 21, you called out some specific examples. But can you give us a sense for the kind of aggregates wins in terms of delivered productivity versus your initial expectation, so we get a flavor for how the overall benefit is coming through from the Manila business?

A - Colin Fagen {BIO 17308097 <GO>}

It's hard to measure exactly at this point in time because we have some of the moving parts at once. But as I said the half year, we'd be able to weigh -- the cost of this project within the overall cost structure that we had last year. So that gives you a feel for how that's flowing through our business. So we've been able to basically buildup the Manila business, bring through the productivity improvements and where the same cost structure that we have in our core business at the same point last year.

Q - Toby Langley {BIO 15924432 <GO>}

Thanks.

Q - Kieren Chidgey {BIO 7268946 <GO>}

Kieren Chidgey, Deutsche Bank. Couple of questions if I could, I'll start on the cost program. The 250 million target, in fact a third of that roughly coming from Australia and New Zealand, how can you guess that the U.S. that of the remaining benefits? Can you give us split for the U.S. and Europe?

A - John Neal {BIO 15681439 <GO>}

Yeah, the remaining, if you look at the -- it's easier to say, Europe at the movement is really only about 15% of the total. I'll let you back so the U.S. from that. Certainly my expectation is the European number will grow because Europe is such a consolidated business substantially operating in around the London and UK, we'll definitely will leave that till last. So the biggest prize if you like in terms of cost efficiency, but also I think creating scalability around the business has always been in North America. I think Colin volunteered to lead the way has put the hard yards in setting up the Global Shared Service Center, but the biggest prices is North America for sure.

Q - Kieren Chidgey {BIO 7268946 <GO>}

Thanks and just to follow up on the productivity, obviously it's early days, you put staffing you've got additional support in terms of these 50 experts over there at the movement, but the one risk with these offshore top operations is high levels of staff turn out now so you know is there a reason that productivity diminishes through time and sort of the knowledge decreases, as we start to say that turn over pick-up?

A - Neil Drabsch {BIO 2093435 <GO>}

We do recognize that, that is a risk and some organizations have had issues with that and that's why we've spent so much time on our employee value propositions, very much looking at the work on induction, looking how we bring people in the organization, but don't underestimate that the (inaudible) within the Philippines of working for a captive and working for an Australian company as well. This has seen as a better segment of the workforce to working. So I think at the moment, we've spent a lot of time and a lot of effort on training, having that people comfortable in working in the organization and we think all the signals are that our turnover is significantly less than any of the comparable organizations and that you are able to get that data.

We also vendor in a number of other organizations undertaking similar activities is both the outsourcing and as captives. We feel pretty comfortable, we've learned a lot from the lessons, that they share with us fairly openly.

Q - Kieren Chidgey {BIO 7268946 <GO>}

Just a follow up question on cost. What are your expectations right on wage inflation in that offshore service sort of going forward? Obviously there is a cost improvement initially by going in, but if you say how wage growth on a go forward basis?

A - Neil Drabsch {BIO 2093435 <GO>}

You'd probably anticipate how our wage growth in Australia, but I also think Australia virtually has institutionally -- institutionalized wage inflation as well, starting from much higher base. So mathematically, we don't see that as a particularly large issue. We don't see it as super inflation by any means at this point in time and we've spoken to a number of organizations what the expectations are over the next few years.

The government in the Manila is looking at bringing more graduates out of the universities and looking at supporting specifically these styles of industry. So we're actually seeing the government recognizing that this is a factor that they need to moderate wage inflation at the time, stop it becoming super inflation, so that it doesn't create an issue with respect to global competitiveness for the Philippines. So there's a lot of infrastructure work actually being done in Philippines also, so they don't fall into the trap we may have seen in one or two other countries around the world, like India to make sure this issue.

Q - Kieren Chidgey {BIO 7268946 <GO>}

Thanks and one final question, just for John on the rates outlook. Just following up on Sid's earlier question, but more in regard to the perspective outlook particularly given we're starting to see reinsurance rates softening at recent June renewals in the U.S. and then here again in Australia for one July. Perhaps you could just talk to your thoughts on a go forward basis as we head into second half?

A - John Neal {BIO 15681439 <GO>}

Yeah, that's a good question. I mean, the reinsurance rates in June, I think you're probably referring to in Florida we're off by about 15 points to 20 points. I think international reinsurance rates are probably off by about 10. In terms of our selling reinsurance, we don't sell a lot in fact, Florida books only $10 million. So not a big impact for us, but being honest, it's a little bit disappointing, I mean, I thought that the rates might hold up a little bit better than they did.

So our sense is that direct rates will fall off slightly in the second half of the year. So in Australia, we shouldn't be surprised by that because I think having had three consecutive years of pretty hefty rate increases, I don't think that's sustainable indefinitely. So we forecast rates falling off slightly in the second half.

In the U.S. my sense is that in the P&C classes rates will move along at about 5% to 6%, we might not quite see there sort of up to 9% in the program business. But we will keep an eye on the reinsurance rates. I think as you know, most of the reinsurance pricing is driven by property cap can be very fickle. So I think if you do see an active hurricane season, I mean Q3 in U.S. and those rate changes will quickly reverse.

Q - Kieren Chidgey {BIO 7268946 <GO>}

Thanks.

Q - Daniel Toohey {BIO 16751863 <GO>}

Thanks. Daniel Toohey from Morgan Stanley, hi John. Just a question in terms of the competition for talent in Manila and the capability that exist in Manila. Can you provide any color on other insurers that are using Manila either as an offshore or captive?

A - John Neal {BIO 15681439 <GO>}

Yeah, I think Collin sort of hit the nail on the head in some respects. If you look to the operation that we are running in Manila or it's like any other QBE operation anywhere else in the world. So it looks and feels like any other modern office environment that we would create anywhere, and that's exactly what we are intending to do. So when people are asking questions around turnover, we assume turnover levels that could be up to 17%.

We're running well under half of that at the moment. So we are quite encouraged by those statistics.

And I think that's fueled by the second point is that by having such a significant business in Australia, we can actually run quite friendly working hours and even when we bring the U.S. on stream, it's easier for us to use shift work and shift operations. So if you're working exclusively for one of the other American insurers, that's operating in Manila, then you are working in pretty anti-social hours. I think we've got an advantage in that respect.

So at the moment, we are feeling confident of the model that we've set up, the captive, the way in which it's operating gives benefits for us and that's certainly coming through in terms the ability to recruit and some of the turnover statistics.

Q - Daniel Toohey {BIO 16751863 <GO>}

Okay, just a second question more aligned to the dividend, and how we should think about that with respect to the currency movements from the U.S. EPS and the payout being AU dollars?

A - Neil Drabsch {BIO 2093435 <GO>}

Yeah. Thanks, Daniel. The dividend payout policy is, the Board put forward is 50% of the cash profit. So using that criterion, you will see in the slide, we've indicated you probably see that balanced 40% on an interim and 60% on a final. The Board have yet to finally approve that but I think that's just putting forward, but we -- logically as we see this develop and particularly with a greater part of our earnings in the second half and the first half.

Therefore and in terms of currency, currency it will be reported in U.S. dollars, remember the dividend is paid in AU dollars so there will be a translation, so obviously if the AU dollar keeps weakening, there will be translation and the dividend will be paid in AU dollars since, so I think relatively you can do your own numbers on that budget.

Q - Daniel Toohey {BIO 16751863 <GO>}

Okay. So there is no capital that's kept in AU dollars likely that you said just a straight translation?

A - Neil Drabsch {BIO 2093435 <GO>}

Straight translation.

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

Brett Le Mesurier from BBY. Couple of questions, what proportion of the $250 million savings comes from reductions in salaries? And the second question, you see didn't comment anything, didn't make any comments on reserve strengthening presumably that's of course you're not expecting that there will be any in the first half?

A - John Neal {BIO 15681439 <GO>}

Dealing with the last point first, I think we didn't see an prior year issue, if that's where the question's going in terms of the first half. That's not something that's troubling us and I think it's a hard question to answer absolutely here we're midway through all of the actual reviews sort of taking place. So some portfolios will have prior year movements, some will have prior releases, but in the aggregate, I don't see a particular issue, that's sort to giving me any course of concern.

In terms of the savings, they're coming from three areas really, once a procurement, non-claims procurement number that we called out in the slides. Two is from labor arbitrage, yes it's obviously cheaper to employ people in Manila than is to employ people in Sydney, New York or London, and thirdly is in process efficiencies.

So if you were looking at the splits, it's roughly 20% is non-claims procurement, and then the balance is equally split between labor arbitrage and processing improvement. And the reduction in headcount, that you're expecting from it.

In reduction in headcount, we're not expecting a huge reduction in headcount overall. If you stand back and look at the statistics, we employ 18,000 staff and about 1,300 contractors. So by design we'll have a much, much lower dependency on contractors than we ever had before.

Q - Nigel Pittaway {BIO 3406058 <GO>}

Okay, it's Nigel Pittaway here from Citigroup. First question just in the 9% rate rise you're getting in program business in the U.S., is your sense that, that's ahead of market or is that broadly in line with market?

A - John Neal {BIO 15681439 <GO>}

I think it's broadly in line with market. Our program business is quite property cap exposed, so it's got more of a property bias in the balance on the book. So I think on property cap pricing that's being moving, quite markedly. And it's also partly by design and that we would expect that type of business to run with combined operating ratios in the 80s rather than 90s. We pushed the rating pretty hard.

Q - Nigel Pittaway {BIO 3406058 <GO>}

Secondly, just on the run-off portfolio as you're hoping to commute. I mean is it right to think of those as mostly being in the U.S. or is that an incorrect assumption?

A - John Neal {BIO 15681439 <GO>}

Yeah, I mean, that's where the focus of our energy is being. I mean I don't think it will be exclusively there. What we've done is we've stood and we stood back and looked at a number of runoff businesses we've got. So we've got some run-off business here in Australia, some in London as I think you know and have had for a long time and obviously in the U.S. as well. And they're pretty capital hungry particularly from a rating agency perspective. So we've been looking at them all, though we have had a particular focus around some of that U.S., program business to see if we can button that up and those conversation is still ongoing.

Q - Nigel Pittaway {BIO 3406058 <GO>}

Is there likely to be any cost with that or is that all covered with the?

A - John Neal {BIO 15681439 <GO>}

I don't know at the moment, to be honest with you and I mean that could be a defining factor on whether we think there's an opportunity there or not.

Q - Nigel Pittaway {BIO 3406058 <GO>}

And thirdly just on the LPI, I think you said obviously there's another significant rate reduction coming through next year at 9% and you said the half year --

A - John Neal {BIO 15681439 <GO>}

There is no actually. It's -- the actual impact of the rate reductions that we're agreed last year is 9% on a full year basis, because of the time it's taken to effect them this year is 8%. So it's one rate reduction.

Q - Nigel Pittaway {BIO 3406058 <GO>}

Okay. I guess that still begs the question of given placement rates is a key driver of that business, you did make a comment at the last results briefings that you felt that 2013 would be the low point both in terms of premium and profitability --

A - John Neal {BIO 15681439 <GO>}

Yeah.

Q - Nigel Pittaway {BIO 3406058 <GO>}

-- for the LPI business. Can you just sort of maybe flesh out why you're saying that given most people expect placement rates to come --

A - John Neal {BIO 15681439 <GO>}

Yeah, it's driven by volume, to be honest with you Nigel. I mean that's I think 2013 was seeing that lender placed business generate about $1.1 billion, $1.2 billion of gross written premium. It's pretty lumpy. If we are successful, which we believe will be through the second half of this year in winning some new clients, then that tends to add pretty substantial volume to the broker business and as you know it's a fairly high cost operating model that services those loans. So really what's driving the increase in combined ratio is not so much the rate reduction, which obviously has an impact, but the cost base is reasonably fixed, so of a lower income in the combined ratio is simply higher. So you know a couple of wins on the new business front, but obviously these gross written premium go up and I think the combined ratio improve.

But we've had a better run on that business and we probably feel we would in for longer. It's still performing well by P&C standards, but just not quite as well as it's done in the recent past.

Q - Nigel Pittaway {BIO 3406058 <GO>}

And then maybe just finally, obviously you've alluded to the fact that the discount rate is going to be favorable for Central estimates, any thoughts about whether or not that will go to P&L or be offset with movements in risk management of this type?

A - Neil Drabsch {BIO 2093435 <GO>}

No.

Q - Nigel Pittaway {BIO 3406058 <GO>}

No, if you can't give us any idea what the attempted one --

A - Colin Fagen {BIO 17308097 <GO>}

No, Nigel, I mean it's a -- there's activity, moving parts at the moment. So until we complete our actuarial work and we'll get to cash flows, what we're doing globally at the moment with all our divisions is that the divisions and now adopting IFRS international accounting standards, which is a fully discounted model. So effectively all discount goes through the P&L and you'll be able to explicitly see where we've reinstated those as risk margins. But it's very, very hard today to give you any guidance.

A - Neil Drabsch {BIO 2093435 <GO>}

We'll certainly show you what we've done when we've done it.

Q - Toby Langley {BIO 15924432 <GO>}

Hi, it's Toby again from Nomura. I want to ask a follow-up question on some of the comments around the rates environment and also reinsurance pricing, because there appears to be some emerging concern, is a bit of an overspill of capital from the reinsurance basis and some of those players may pursue, made attempt to deploy capital into the primary environment particularly in the U.S. and I was just wondering if that's something that you already starting to experience and whether we've got a view on whether it played out further from here?

A - John Neal {BIO 15681439 <GO>}

Yeah, you've probably seen or if you haven't we should circulate it V.J. Dowling's report on where that capital is coming from, say, it's either a lot of money or not a lot of money, depending on how you look at it, you've got $7 trillion tied up in defined benefits pension funds in the U.S. and about 140 billion is falling into the reinsurance market. So it's not really a lot of diversification of that as such investment is taking place.

We've been here, Neil could probably answer the question better than me. We've been here three times before in my time, seeing some divestment into sidecars and reinsurance school of 2001, school of 2005. It tends not to last, it's tends to be at a time when more conventional investment instruments are not producing the right level of return. I think the moment we'll start to see those convention instruments come back, I think you'll see the capital step aside.

So from our perspective might mean that we've got a way to couple of years before we can grow that reinsurance business in a way in which we wanted to, but for us we write roughly $1.4 billion of reinsurance and we spend roughly $2.3 billion in buying reinsurance. So I would say it's sort of a slight net positive for us as we look to restructure our reinsurance programs and leverage some value for 2014. So it's a bit of a win and a loss for us. But I think if you look out beyond the short term or anything the capitals particularly durable, it's all going for property cap, it's not going for the longer term of classes.

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

You don't see any medium, long-term threat to primary lines though from the reinsurance incumbents looking to put food on table are moving into your space?

A - John Neal {BIO 15681439 <GO>}

Not I don't and not from the reinsurance capacity. I think what's more interesting is about a halfway of setting up it's ENS [ph] team by recruiting quite aggressively from AIG, which I think is quite a strong attack potentially on the Lloyds market, for example. But not the reinsurance capital, it's simply not got the distribution leverage which we've gone.

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

Thanks.

Q - Siddarth Parameswaran

Hi gentlemen, it's Siddarth again from JPMorgan. Just a follow up question on just whether there is any scope for actually reducing your distribution cost, so whether the commission rates are lightly to be flat going forward?

A - John Neal {BIO 15681439 <GO>}

Yeah it's a good question, Sid, I mean, it's -- I think you only have to look at the share prices and brokers to really see he's doing well at the moment. I think -- we do think if I'm being honest with you, think commission costs have risen too much. It's a tough sort of let's say educated daily discussion with brokers as to the appropriate remuneration, different parts of the world.

And I think what we need to do, to be honest with you, is between insurers and brokers is just to eliminate the duplication that exist between us. So there is too much of the same tasks being undertaken by the broker and the insurer and that's where ultimately we can be constructive in terms of simplifying process and insuring that both of us don't need to charge for the same task.

I think it's important we do that. So if we look out three, four, five years and you look at pure acquisition costs, the combination of expenses and commissions and we're targeting 2% short-term, it's going to have to come down by more.

A - Colin Fagen {BIO 17308097 <GO>}

John, we don't have any calls from the teleconference, just bearing in mind the time perhaps maybe one more question from the floor, if you'd like.

A - John Neal {BIO 15681439 <GO>}

No, it looks like we don't. Thanks very much. Thank you, everyone. Thanks for coming.

A - Colin Fagen {BIO 17308097 <GO>}

All right. Thank you.

A - John Neal {BIO 15681439 <GO>}

Thank you.