S1 2020 Earnings Call

Company Participants

- Aki Hussain, Chief Financial Officer
- Benjamin A Walter, Chief Executive Officer, Hiscox Global Retail
- Bronek Masojada, Chief Executive Officer
- Joanne Musselle, Chief Underwriting Officer
- Robert Childs, Chairman

Other Participants

- Andreas Van Embden, Analyst
- Andrew Ritchie, Analyst
- Ben Cohen, Analyst
- Jonny Urwin, Analyst
- Kamran Hossain, Analyst

Presentation

Robert Childs {BIO 1776179 <GO>}

Good morning, ladies and gentlemen. I am Robert Childs, the Chairman of Hiscox. It has been a challenging first half, particularly in the second quarter. It's also been a time to concentrate on staff and customers. With over 3,000 people working from home, we are supporting them through the lockdown and beyond. For our customers, we have done much to alleviate their financial burden. In respect of the business interruption issue, we are supportive of the FCA process, but being proud of our excellent claims paying reputation, we have not found this an easy time. We also played our part for society, generating the support for the ABI COVID Fund with significant donations from the Hiscox Foundation.

Now turning to Page 2. Our long-held strategy is working. You could say it was built for times like these. 30 years in the making, our retail business is now over $2 billion in premium. The future is digital and we are there in the present, $0.5 billion and growing our direct-to-consumer and partnership business. We are also well positioned in our Reinsurance and London Market divisions to benefit from the coming hard market. We have the capital, the people and the reputation.

For more financial details, I will now invite Aki Hussain, our CFO, to present.

Aki Hussain {BIO 19739719 <GO>}

Thank you, Rob, and good morning, everyone. I am Aki Hussain, Group CFO. As he [ph] just said, 2020 has been a tough year for our customers, for colleagues, the society in general, and we're playing our part in helping our employees and customers through this period.

Now, turning to Slide 4 and our business performance. In a challenging environment, our business has delivered a resilient performance. Revenues in our Retail and London Market divisions are up. However, overall Group revenues are down 4%, as we maintained a disciplined approach in Reinsurance and ILS.

For the first time in a number of years, we're reporting pricing improvements in each of the three operating divisions. Our first half performance has, of course, been impacted by COVID-19, and we have set aside reserves totaling $232 million, net of reinsurance, mostly in our Retail division. This includes $150 million we disclosed early in the year for claims arising from the event cancellation, travel and entertainment. The additional $82 million is for estimated losses, mostly IDR [ph] for London Market, UK, Europe property, UK, Europe travel bonds and

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Thank you, Rob and good morning everyone. I'm Aki Hussain, CFO. As you see first 2020 has been a tough year for our customers for colleagues this specifically in general and -- (inaudible) and customers through this period.

I'm turning to slides 4 and our business performance. In assumption (inaudible) Revenues in our retail among the market visions are up. However, overall group revenues are down $0.04, as we maintained a disciplined approach in reinsurance and ILS. So the first I mean a number of years, we're reporting pricing improvements in each of the three operating divisions. Our first half performance has of course been impacted by COVID-19 and we have set reserves totaling $232 million net of reinsurance, mostly in our retail division. This includes $150 million, we disclosed earlier in the year for claims arising from the event cancellation travel and entertainment. The additional $82 million for -- mostly -- so market UK your property you can get third-party liability claims in our US allied healthcare business. So the Group reported a loss -- a bottom line loss of $139 million, after Group combined ratio of 114.6%. Ex COVID, the Group generated a profit of $93 million at a combined ratio of 96.5%. Our business remains strongly capitalized and we have materially increased our reserve for this. And in line with our announcement in April, we are not proposing an interim dividend. We recognize the importance of the dividend to our shareholders, and we'll be revisiting the matter early in 2021. Now, turning to Slide 5. As usual, I'll take you through our divisional performance in a little more detail, beginning with Retail. The Retail business grew by 4% with four out of our five business units reporting growth in the first half, with only the UK reporting a small decline of 2%. This is in part driven by the mix of business written in the UK, such as event cancellation cover, which has been particularly hard hit by government measures to slow the spread of COVID-19. We have, as you might expect, experienced a slowdown in GWP in the second quarter as the lockdowns took effect, with April and May reporting the most acute impact. And we are happy, because we see a recovery coming into July. As you've heard me say many times before, our Retail business has over time benefited from secular trends in society with the growth of the gig economy and a growing customer preference to transact directly online. So, looking at the Retail performance through a distribution lens, I'm pleased to report our digital, direct and partnership channel continued to report strong growth with revenues up 14% in the first half, despite the lockdowns. At the half year point, our direct and partnership business revenues now account for 24% of total Retail revenues, and by the end of this year, I expect this to rise to over 25%, and you'll hear more in this from Ben in a few minutes. Retail has been heavily impacted by COVID-19 and we have set aside reserves totaling $175 million in the Retail division. Excluding the effect of COIVD-19, the underlying business franchise remains robust, generating a profit in excess of $100 million at a combined ratio of 95.4%. The combined ratio is benefiting from temporary cost reductions, worth about 1.5 to 2 points. So, on a normalized basis, our estimate for combined ratio is between 97% to 97.5% and remains on track to be within the 90% to 95% zone by 2022. Looking forward, in the second half of the year, we expect to see a $10 million to $15 million negative impact on Retail top line as a result of moratoriums and premium holidays offered to customers. And, I guess, as I said earlier, we are seeing the tailwind of positive rate momentum across the Retail division. Turning to Slide 5 -- sorry, Slide 6. In our London Market division, we are seeing strong growth momentum with a portfolio average increase of 13%. And we're reporting a GWP growth of 5% in constant currency. Rates are now increasing in 15 of the 16 lines we are writing, and we are seeing robust GWP growth where we believe rates are rather [ph] good. There have been a couple of areas in the property division where further rate improvement is required, and underwriting action has been taken to right size the underlying exposures. In the first half of the year, we have experienced above-average large losses, which are contributing around 7 points to the combined ratio. And excluding COVID, the London Market combined ratio stands at around -- at 104%. Turning to Slide 7 and our Reinsurance and ILS division. Here we're reporting a 21% reduction in GWP. This is a result of a number of factors. Firstly, in the early part of the year, pricing was less attractive and we remained disciplined in preserving our capital. We've also seen a reduction in the availability of third-party capital. You'll recall after we reported our full year results, we have received a notice of redemption from one of our ILS investors. You'll also recall from our fourth quarter, we mentioned we exited the casualty reinsurance book. And finally, we are also continuing with underwriting actions on our risk book, which is largely retained book of business and has been a source of above-expected losses in recent years. Now the outlook for our Reinsurance division has become much more optimistic as the year has progressed, as we've seen increasing evidence for material rate improvements at each (inaudible) renewal period. At the half-year stage, we are now reporting an average portfolio rate increase of 11% and expect the positive momentum to continue into next year. We expect this will lead to an increase in our net revenues in 2021. The bottom line results have been impacted by estimated COVID-19 losses. Excluding this, we are reporting a combined ratio of 87.5%. We closed the half year with $1.5 billion of assets under management in the ILS Fund, although the deployable capital is around $1 billion, with the balance either being in run-off or on redemption notice or held as reserves against prior year losses. Moving on to slide 8 and our investment performance. We are reporting a first half investment return of $85 million, a significant improvement from the first quarter deficient, as financial markets recovered. We were cautiously positioned having -- coming into 2020, and this has served us well and enabled to take advantage of market uncertainty by topping [ph] of our allocation to risk assets through March and April. However, as yields continues to decline and spreads narrow, the yield to maturity on our fixed-income portfolio is now at its lowest point ever, at around 0.7%, which of course is not great for bond returned over the next couple of years. You also, no doubt, have noted our allocation to cash at 26% is high at the half-year point. This is the equity proceeds which was held as cash in money market funds, and it's a cautionary drawdown on our financial lines. I expect to repay the financial lines in the third quarter and return the cash allocation to between 10% and 15% by the year end. Turning to slide 9 and our reserves. We are reporting an aggregate favorable reserve development of $63 million. Our 2019 cat reserves are running well and are a key driver for the increase in positive development. In contrast, we are continuing to see adverse development on exited lines, in particular, on healthcare and political risk, totaling around $15 million results. We remain very strongly reserved with a margin above the actuarial estimate of $350 million. This has grown from just under $300 million at the end of 2019. And I now regard the reserve buffer to be at the upper end of my expectations. Our US casualty claims continue to progress in line with expectations and increased with the changes and improvements we've made in our US claims function. I expect a positive effect of operational changes in US claims, combined with underwriting actions and pricing improvements in our US Retail business to effect the bottom line -- that's come through into the bottom line over the next 12 to 18 months. Moving onto slide 10, this is a chart that you are all, I'm sure, very familiar with and it demonstrates or reflects our capital position, which as you can see remains very strong, and has been further bolstered by the equity we raised in May. As you can see, we remain well capitalized in both a ratings and a regulatory basis and we're reporting an estimated regulatory solvency ratio at the end of June of 230%, which equates to a capital surplus of $1.7 billion. I will just remind you that the BSCR continues to be strengthened according to the BMA timetable and we expect a 10 to 15 point reduction by the end of this year, and then into 2021, as (inaudible) 10:54 is adopted. Moving on to slide 11. This next exhibit demonstrates very clearly the capital strength and resilience of the Group and its ability to withstand a combination of severe scenarios. Taking the chart from left to right. In the second quarter, our capital position has improved from a strong starting point with a solvency ratio of 202%, increasing up to 230%. And this is the result of a strong organic capital generation in the quarter, the equity we raised in May, and both partly being offset by additional COVID-19 losses. Moving along, we can see that the balance sheet is then able to withstand -- is able to absorb a North American one in 250-year hurricane, costing up to $200 million net of reinsurance, in addition to the top end of our published UK BI risk scenario. After both of these hypothetical events, we would expect to have a regulatory capital coverage ratio at 179%, which leaves us with ample regulatory capital and it's consistent with an S&P rating. And finally, turning to slide 12 and expenses. As part of the equity raise, we had committed to an expense savings versus our 2020 business plan of between $60 million and $90 million. At the halfway point, we are on track with savings of $38 million achieved. These savings are largely tactical in nature and should mostly be regarded as a one-off, as we have benefited from savings on travel, marketing and recruitment during the lockdown period. Overall, our ambition for the Retail segment expense ratio remains to be in the low-40s and we are targeting a reduction of 1 point per annum for the next few years from 2021 from an normalized Retail expense ratio of around 49% to 50%. The efficiencies will come from realizing the benefits from the investment in technology that we've undertaken the last few years and the growing scale of the Retail businesses. Once again, you'll hear more from Ben on this industry norms [ph]. And now, I like to hand over to our Chief Underwriting Officer, Joanne Musselle to tell you more about what we're doing from an underwriting perspective.

Joanne Musselle {BIO 19106109 <GO>}

Thank you Aki, and good morning all. So I took up the role of Group CUO in January, and was definitely hoping for a less eventful start. A lot has happened since, so I thought we could revisit a slide that we presented at the full year, which set out our expectations for 2020 and provide an update, and this can be seen on slide 14.

So (inaudible) actually our expectation for Re and ILS was to reduce our gross bet in response to what we viewed as inadequate pricing, alongside less deployable third-party capital at 1/1 [ph]. And we have delivered on that expectation with gross written premium reducing by 21%, as we did substantially re-underwrite our non-cat portfolio, including exiting casualty reinsurance and we exercised discipline at the January renewals.

As the second quarter progressed and with the onset of COVID, conditions in reinsurance began to improve and we have achieved strong rate increases at the major renewals, with Japanese wind up 38%, or (inaudible) 20%, and recent Florida renewals up 29%. With the impact of these price increases, our reinsurance gross written premium is now down just 10% year-to-date. Momentum is expected to continue and we are ready to increase our net bet in January with material capital available to deploy on our own balance sheet.

Moving onto London Market. We noted at the year-end, the rating position was improving and this was expected to continue. However, we also noted that not all lines were rate adequate and we still had part of the portfolio to course-correct. And we have done just that. The headline growth figure for the London Market segment of 5% does mask some strong underlying growth in our investment lines as we continue to exit the underperforming premium during 2020 in our binder portfolio. It has, however, been an active half for large claims with above-average large losses and some deterioration coming from exited lines, such as political risk and healthcare. Large losses do not come uniformly through the year and the year-end position will give a better view if this is just timing. More pleasing is the continuing rate momentum, up 13% across the portfolio, driven by contraction of risk appetite and we expect this to continue for the balance of 2020 and into 2021. And for Retail, our expectation was a COR of 96% to 98% with growth in the middle of our usual 5% to 15% target range. Clearly COVID has had a significant impact on our Retail portfolio in the first half, both in terms of claims and growth, but excluding COVID the underlying Retail COR is 95.4% with claims experienced in the UK, US and Europe in line or better than expectation, which is pleasing. So overall, the benefits of the significant portfolio action we have taken and the rate improvement is beginning to become evident, but this will take time to fully earn through the P&L. Moving on to slide 15 and COVID. So the impact of COVID-19 is unprecedented with many in the industry predicting that this will be the biggest insured loss in history. And whilst the range of industry loss estimates is wide and still speculative at this stage, it is clear that it's touched many parts of our portfolio. We previously disclosed $150 million net loss estimates for claim relating to events cancellation, media, entertainment and other segments, including travel on the basis of six months restrictions. And we are actively working with our insurers and brokers to manage these claims and settlements are in line or actually just below our expectation. We have booked an additional $82 million net at the half year to cover claims from London Market, European and UK property, UK and European travel bonds, and we've made a provision for third-party claims from our US allied healthcare portfolio. It's too early to fully estimate the impact (inaudible), although we are materially underweight in our European exposure and we have a modest net retention. Recent business interruption has been a source of much media attention, particularly in the UK, where (inaudible) others in the industry, our standard BI policies do not respond to the general measures taken to stop the spread of COVID-19. This is being challenged and we welcome the FCA test case to bring clarity. Notwithstanding this is not a covered loss, we previously disclosed a risk scenario based on a broad set of assumptions, which result in a modeled range of losses between GBP10 million and GBP250 million net of reinsurance. Whilst noting that a different set of assumptions could give way to a different outcome, we remain confident in this range, even after taking into account the impact of different closure periods for affected businesses. And then moving onto the balance of the portfolio. As we move beyond COVID, there is clearly an increased probability of risk from third-party liability and recessionary impact. We are actively managing this increased risk through portfolio rate and underwriting changes. Excluding COVID, our frequency of claim notifications is materially down year-on-year. We've seen a 10% reduction in big ticket and a 15% reduction in retail. Now some of this will be timing, but some of this will translate to lower claims if people have just done less [ph]. At this stage, it's too early to tell what this noise will [ph] signal and we have yet to take credit for this reducing trends. Slide 16 should be familiar, it shows our portfolio through the different segments. Small commercial, which you can see on the far left, is our largest segment and this has doubled since 2015 and have continued to grow despite the significant economic disruption in our key retail markets. London Market property has slightly contracted, as we complete the portfolio action necessary in the household and commercial binders, which have contributed to higher attrition than we would have liked. But despite exiting 110 [ph] through the full year, the good rate increase we have achieved on the remainder of the portfolio has resulted in a modest reduction to the top line. Our largest growth area can be seen on the far right, and is the London Market casualty. However, its 21% growth is nearly entirely fueled by rate increase with exposure decreasing or remaining flat in our general liability and our public D&O. Another familiar slide is our rating chart on slide 17. So, as a reminder, this chart shows our rates indexed back to 2012 and on a rolling 12 month basis. The rolling calculation does have the impact of delay in some of the positive rate momentum. However, the picture is clearly a positive one. Whilst amounts may be uncertain in some areas, I'm pleased to say that rates are improving in every segment. Particularly in the London Market where rate is up another 13% overall and this is in addition to the 12%, 11% and 7%, we have seen over the proceedings three years. And as you can see, rates have reached a point they have not been for many years. Re, which is the red line, had a slower start to price correction, but rates are up 11%, but the trajectory of that line has an upward and increasingly steep rate, we are confident about the prospects for growth heading into next year. Retail, the green line, which is inherently less cyclical in nature and the flat to downward trend is more a feature of change in business mix than rate, but the trajectory is only up and we are seeing rate above plan in all areas of our retail book. US retail is leading the way at 5% in aggregate and 9% for the excess and surplus lines business. So if we move on to slide 18 and look at the big ticket rates in more detail. So in 2020 -- in London Market, 2020 is the fourth consecutive year of rate rises, where rates are up 45% on a compound basis, since the low [ph] of 2016. So this is being driven by withdrawal of capacity as risk appetites contract globally and a continued benefit from the Lloyd's Decile 10 initiative, which continued to encourage the much-needed discipline in the market. This discipline doesn't just extend to pricing, we're also successfully tightened terms and conditions, as well as reducing commissions. Overall, we are seeing rate improvement in 15 of the 16 lines, including in US public company D&O where rate is up a further 80% and we see an attractive opportunity for growth. Looking at the London portfolio -- London Market portfolio in its entirety, I feel positive about the outlook for the remainder of 2020 and into 2021 with the majority of our portfolio now priced to generate good returns. In Reinsurance, which you can see on the blue chart, we were largely underwhelmed with pricing at the beginning of the year with overcapacity still a feature. And our expectation was to remain disciplined. However, as 2020 has progressed and the uncertainty caused by COVID, we have seen strong rate acceleration through the midyear renewals and I'm confident about the prospects for growth next year. Overall, my focus heading into the second half can be seen on slide 19. It is proactively managing our losses and exposure while capturing the opportunity presented. So just to pull out a few areas, we continue to manage our future exposure and have updated the Hiscox view of risk; the cyber, Japan and Florida. We have clarified our communicable disease exposure and opportunistically purchased increased reinsurance protection ahead of the wind season. Our underwriting has been flexible, providing extensions, suspensions of early renewals to assist our customers, as well as supporting those that have pivoted their business, like the insured who have pivoted his British [ph] business to supply alcohol for (inaudible). We've also updated some of our terms and conditions to reflect the current challenges. Overall, as we head into the second half, I look at our diverse portfolio and I see opportunities everywhere. I will now hand over to Ben Walter, who will talk more about our Retail business.

Benjamin A Walter {BIO 18021194 <GO>}

Thanks, Jo. Good morning, everyone from a very early New York. I'm Ben Walter, CEO of our Retail division. Clearly, as Aki described, it's been a tough six months for Retail as we have borne much of the impact of COVID from a loss perspective. But I'm pleased with the resilience of the top line of the underlying performance, and as importantly, the resilience of our teams. So we have kept our operations running smoothly throughout the lockdown period. I'm pleased to say that our key operational metrics have stayed within their target service levels from day one, which is a testament to the robustness of our systems and the commitment of our people. Years of investment in both have paid off handsomely this half. And as you can see on slide 21, even as the business grapples with so much disruption, our Retail businesses have continued to deliver on their long-term objectives. We grew 4% in the first half and as Aki said, we are reaffirming our commitment to returning to the 90% to 95% combined ratio range in 2022. Key to that commitment is underwriting discipline. As we said before, we have cut back materially in unprofitable and marginal areas. Two examples you will be familiar with are US Private market D&O and media and between those two lines alone, we have now cut $80 million of premium. It's worth noting, the private company D&O is very different than the public company business we write in London, and due to slower price rises and increasing employment liability exposure, we still do not see rates adequate to grow here. In the UK, we have discussed before that the private client growth had shrunk modestly as we needed to seek rate to fund increasing escape of water claims. While those increases have cycled through, further discipline has been warranted as commission levels have reached to what we deem to be unsustainable levels. We've seen a number of broker panels tender with commissions as high as 32.5% and we think these levels -- these are levels that do not represent good value for the customer. So we have declined to participate at the expense of the top line. Fortunately, we have more than made up for those reductions with growth in our core small commercial business even in the face of the COVID-induced economic slowdown. The smallest risks where we have a unique right to win and an increasingly efficient operational platform, continue to grow as a share of the book. On a global basis, we only saw these books shrink slightly in April and May with a return to growth in June. Our direct and partnerships business, in particular, continues to be a growth engine and we are on a run rate for over $500 million in 2020, which will be a full quarter of the Retail business. I'll give some more detail on this in just a moment. Finally, we made good progress on both our large system replacements and our nearer-term digital initiatives. Again, I will share some detail on this shortly. On page 22, you can see the 10-year trajectory of our direct and partnerships business, which has delivered a 19% CAGR over that time and still delivered 14% growth in H1, despite being much larger in scale and of course, despite the pandemic. We started that business in the UK, which has slowed in growth in the past couple of years, but that masks the aforementioned underlying dynamic, which sees a modestly shrinking personal lines book more than offset by a fast growing commercial book. In the US, we have seen tremendous growth to over $300 million, but in our view, this business is still in its early stages as the entire market is experiencing a shift to digital distribution and we are ideally positioned to capitalize. Despite the macro environment and the launch of the first phase of its new IT platform in May, June was the best month yet for US direct and partnerships. Europe is a bit more nascent, but growth has picked up in the past couple of years and in time, we expect the Continent to follow the same global trends we have seen in the UK and the US. And finally, our motor business in Asia has hit its stride this year and is now growing nicely towards scale. As you can see, digital insurance is fast becoming the cornerstone of retail across the world and we will continue to invest behind that opportunity. Slide 23 gives you a sense of what that investment looks like and how we are starting to reap the benefits. In addition to our core system replacements in all of our key geographies, we are also finding ample opportunities to digitize both the front and back end of the insurance value chain. With $1.3 million retail customers and growing, we expect to eclipse 3 million transactions this year, and this shows no signs of slowing down. We have already automated more than a third of them, but we are targeting much more. Given our scale, the potential improvements to both cost-efficiency and customer experience is significant. Our efforts to date have focused on four key technologies, and I'd like to share a couple of examples. First, APIs, or application program interfaces, are the future of digital insurance trading. They allow us to seamlessly integrate our partner systems with ours using both proprietary and industry standard protocols, depending on the market. In the US alone we have nearly 40 partners trading with us in this way, meaning their employees can place business with Hiscox without ever leaving their native internal platform. Second, machine learning has finally come of age for insurance applications with off-the-shelf solutions now available to integrate directly into our own systems. In the UK, we are using a solution to read plain language emails in our broker channel and automatically route them to the right place for one-touch resolution. We are already seeing accuracy rates well into the 90s and the software automatically learns from its own errors to improve. Machine learning becomes even more powerful when it is paired with robotics, which can automate repetitive tasks of ever-increasing complexity. For example, we were planning to migrate our UK policies from the old system to the new with a large team of people. Instead, we now have a robot doing it automatically with a smaller team just to oversee the process and (inaudible). Europe in particular has seen strong success with robotics and is now processing hundreds of thousands of routine transactions. And finally, self-service, which is certainly a cost saver as it takes the work out of our hands, but increasingly is a customer demand. Our customers want control for most basic routine activities. They still want to talk to someone about sophisticated insurance issues, but the days of calling someone to update your credit card are unsurprisingly long gone. We have made a lot of progress, but as you can see on slide 24, there is much more we can do even with the technology we already have in-house. Natural language processing has countless more applications in our markets. And as I said, our customers are always demanding more self-service options. We also see significant opportunity in our claims experience, where digital submissions and payments are faster, more accurate and often more secure. But we are also constantly evaluating new technologies as they mature. COVID has certainly taught society that we can do much more than we ever thought with video chat and the same is true of text and other forms of communication. Customers want to choose the way we service them and we will accommodate that. And there are developments on the internal side as well. For example, we're now looking at software that can diagram and mine our operational processes and model improvements before any changes are made, lowering transition risk and speeding up, both the pace of change and the elimination of waste. Taken together, on slide 25, I hope these things give you a sense of why we remain so optimistic about the long-term prospects for Retail. The shift to digital is inexorable and it has only been hastened by COVID. We have been investing in these capabilities for years and that head-start, particularly in small commercial, puts us in a strong competitive position to capitalize on the trend. We know that the coming months will be challenging until life can return fully to normal. Our customers are having a tough time out there right now, but we know from experience that when economic recovery comes, SMEs are some of the first to benefit as they can form and respond nimbly. Our market shares remain low and when firm formation is high, we tend to do disproportionately well. And finally, much like the diverse choices afforded by our strategy of blending big ticket with retail, we are fortunate to enjoy a global footprint in the SME space. Some countries will recover faster than others and we can flex our investments accordingly. Thank you very much. Now, I'll hand over to Bronek for business performance and outlook.

Bronek Masojada {BIO 1776109 <GO>}

Thank you, Ben. Turn to Slide 26. You've had a good overview of the business thus far, but one of the themes, which goes through us is clearly the impact of UK business interruption. As both Rob and Jo said, we welcome the FCA initiative to have a test case to try and clarify the impact of wordings. We always felt that this process would have ramifications for the industry as a whole, and that was really confirmed when two weeks ago at the beginning of the trial, the FCA said that in their view, the decisions by the judges would impact 60 insurance companies and almost 400,000 policyholders, of whom Hiscox have only a small proportion.

Turning to slide 27. As you all know, the hearing concluded last Thursday and at the final stages the judges said they would be giving a judgment in mid-September. I think that's clarity less than six months after the lockdown began is of value both to customers who need certainty and also to ourselves. Clearly there is the opportunity for both either the FCA or the insurers to appeal and if that was to happen, there is an expectation that the appeal would be heard during calendar 2020 with a judgment either before the end of the year or early in 2021. Clearly Hiscox's expectation is that we -- our interpretation will prevail, but we will have the claims capability to handle claims if that is not the case.

Turning to page 28, I think it's worth taking a step back and reminding ourselves of the guiding principles of the Hiscox business strategy. We continue to believe in the retail opportunity. You've seen in the first half that Retail has grown by 4% and over time, we remain committed to that 5% to 15% range, recognizing though it will get more difficult as we get bigger.

To build on what Ben said in terms of the digital response, if you think about what we've gone through in the first six months, in January in both our US and our UK commercial business, the direct and partnerships division, we saw more business than the prior period a year ago. In April, it was 60% and it's fair to say we were all worried about the longer-term impact, but in June and July it's bounced back to very similar to January and in some cases above January, and that shows the underlying strength of that business. For the bigger ticket business, clearly we are now -- it says we shrink and expand according to the pricing environment and given the pricing environment at London Market and Re and IL are enjoying, we are firmly in the expand mode and we feel that, as Aki set out, we have the capital to do that. So finally on slide 29, we look forward. The company has clearly been incredibly resilient in a very challenging six months. Our staff have been amazing, working from home, providing service to brokers and to customers, as well as dealing with the challenges of COVID-19. The Retail performance was -- ex COVID-19 was a combined ratio of just over 95%, driving $100 million worth of profit, and has Ben has outlined, the investment in digital technology has paid off. As we look forward, we see growth opportunities and profit opportunities across the business. The rates, there is momentum, clearly the most momentum is in the London Market business, but Reinsurance is catching up and we are already seeing upticks as Jo highlighted in the Retail businesses around the world. We have the capital, but more importantly, the risk appetite to go in the big ticket lines, and as we look into 2021 and beyond, we believe that the long-term growth story for Retail is undiminished and that we are well placed to take advantage of that. So with this, we bring our presentation to the end and we will open up for questions.

Questions And Answers

Operator

Ladies and gentlemen, we have now come to the question-answer session. (Operator Instructions).

A - Bronek Masojada {BIO 1776109 <GO>}

Thank you Johan [ph]. So I will compere in terms of the questions. So I know many of you want to ask more than one question at a time, and we will then decide who of the management team will be the right people to answer.

Operator

All right. Thank you. We have first question from Kamran Hossain. Hi, Kamran, your line is open now. Please go ahead with your question.

Q - Kamran Hossain {BIO 17666412 <GO>}

Hi, morning, everybody -- morning everyone. So I've got three questions. The first one is obviously the data on I guess submissions is really encouraging as far as Retail. Could you maybe talk about any internal net promoter scores that you have, or you've indicated that you might have to hand about whether there's been any impact on the business -- on the Retail business generally and more particularly kind of on the US, whether there has been any read across at all [ph].

The second question is, I think it's really positive that you've got lower claims frequency elsewhere, but you're not going to begin to recognize it. When will we begin to recognize this? One year, two years, is this an early 2000 scenario again? And the third question is, if there is a second wave of lockdowns, kind less local more national, any thoughts about how we should think about that going forward? Thank you.

A - Bronek Masojada {BIO 1776109 <GO>}

Thank you. Kamran. I think Ben can answer the question around the Retail impact and how we are measuring our market position. Aki can handle the claims frequency, when we will recognize that, and maybe Jo can talk about the second wave.

A - Benjamin A Walter {BIO 18021194 <GO>}

Sure, thanks, Bronek. Hi, Kamran. In terms of NPS scores and impact on the brand, we have done a couple of dips across the world. Those are light touch surveys where we take the pulse on where we are and so far we have seen our NPS scores hold up at the levels that they were before COVID happened. Clearly that's a concern and something we're watching very closely. But we haven't seen a significant impact to date and the growth in the business relative to the economic environment would bear that out.

What we are seeing more broadly, and we've done this -- I happen to be on the Board of the Trade Association in the States, and what we have seen is a dip in confidence in the sector overall, I expect that on both sides of the Atlantic, as a lot of these issues have played out very publicly in light of the pandemic, but that seems to have been broad based across the industry, and thus far we have not seen a material impact to our NPS scores or our brand tracking survey.

A - Bronek Masojada {BIO 1776109 <GO>}

Thanks Ben. Aki?

A - Aki Hussain {BIO 19739719 <GO>}

Hi, Kamran. I guess regarding the frequency, as you heard from Jo, the frequency has dropped quite significantly in our Retail business, but it's difficult to tell right now to what extent that -- differences between noise and signal. So we are reserving works (inaudible), and in terms of the duration of these policies, they tend to be pretty short duration. So by this time next year, we will pretty much know whether it is real, and by then, I expect in the second half of next year to be recognizing that favorable experience.

Q - Kamran Hossain {BIO 17666412 <GO>}

Thanks Aki.

A - Joanne Musselle {BIO 19106109 <GO>}

Hi, Kamran. Just picking up on the question on the second wave. So for events and contingency, the impact is significantly reduced as exposure just runs out. We previously disclosed if the restrictions continued for further three months to the end of the year, then there is a potential $25 million. And once we do have some exposure in 2021, it is more limited, because events, which have not been scheduled, and we're obviously not reloading our aggregate yet, the business interruption, we remain of the view that the intense, and the words into our policies in the UK are clear, but given this has been disputed, we felt it sensible to provide some clarity to avoid any future disputes. And in line with others in the market, we're making some changes for new and existing customers in relation to the communicable disease. So our portfolio is steadily migrating into the clarified world then [ph]. So in our disclosed risk scenario, we did adopt different assumptions and we did include some headroom in those assumptions, given the uncertainty, but ultimately would depend on when the second lockdown occurs, the length, severity, to be really confident of the ultimate impact.

Q - Kamran Hossain {BIO 17666412 <GO>}

Thank you, Jo.

A - Bronek Masojada {BIO 1776109 <GO>}

Great, thank you. Can we take (inaudible) the next question?

Operator

We have next question from Jonny Urwin from UBS. Hi, Jonny, please go ahead with your question.

Q - Jonny Urwin {BIO 17445508 <GO>}

Hi guys. Good morning. Just two if I may please. So firstly, I guess on the additional $82 million of COVID losses, I mean there was obviously a lot of focus on that this morning in the investment community, given I think people just expect the $150 million to be reiterated for now pending the FCA outcomes. I mean, can you guys give us a bit more detail on that, how capital investors get comfort that this number doesn't keep rising, ex the FCA outcome, maybe what's the total IBNR on the (inaudible) that might help.

And then secondly, the reserve, thus, has increased over a stronger best estimate, you're now saying it's at the top end of the range, the very top end of the range. When we think about the Retail combined ratio guidance, some of last year's deterioration was driven by claims experience and some was driven by a deliberate slowdown in the release patterns. The question is, does this stronger buffer mean that the release profile can perhaps normalize a bit sooner than we're expecting? Thank you.

A - Bronek Masojada {BIO 1776109 <GO>}

Great, thank you, Jonny. I think both of those, around the context of $82 million and then the reserve buffer are for Aki.

A - Aki Hussain {BIO 19739719 <GO>}

Thank you, Bronek. In terms of the additional $82 million, Jonny, I think, the last one of your question was (inaudible) we don't tend to disclose the details of that, but what I can say is that the vast majority of the additional $82 million is IBNR and currently our (inaudible) is consistent with our reserving style and these are precautionary reserves that we are setting aside, and they are not reflective of the credit that we've currently received. And, frankly, as far as we are concerned, any point in time with all this reserve (inaudible) be sort of expected loss from a basis and that's exactly what we've done with the additional $82 million.

In terms of the reserves, you're right, we are now at the top end of my expectations at $347-odd-million [ph] and also then present above the actuarial estimates. The relative sort of increase in the reserve buffer has been driven by 2019 cats running very well, and I expect that to continue into the second half of the year and we will take a view at the end of this year as to what happens there.

With respect to Retail, I think the guidance that we provided last year that we would expect the Retail business to get back to 90% to 95% zone by 2022 still remains our position. The business is progressing well, you can see that reflected in the underlying (inaudible) for the first half of 2020, where part of the reason that we've got to a 95% combined of course is the expense reductions we've taken, but also the improved experience we are seeing in the US, but I'd caution against accelerating the expectation to get back into 90%, 95%.

Q - Jonny Urwin {BIO 17445508 <GO>}

Thank you.

A - Bronek Masojada {BIO 1776109 <GO>}

Great. Shall we take the next question please?

Operator

We have next question coming from Andrew Ritchie from Autonomous. Hi, Andrew. Your line is open now.

Q - Andrew Ritchie {BIO 18731996 <GO>}

Hi, there. Thanks. Good morning. First question, I think is for AKI, I want to just explore the capital scenario a bit more, the slide, which ended the 179 [ph]. I guess the two things to think about is that you've actually said that you've assumed the UK BI risk scenario of GBP250 million, but today you've told us that there could be more losses in reinsurance potentially related to the FCA case. So I'm not sure why you wouldn't allow for that in your kind of worst case capital. I guess the other thing in that capital slide is it doesn't reflect the BSCR changes. Do you just assume those are offset by capital generation, which I guess they hopefully should be. What's your thinking around that? Or maybe just tell us what the additional capital tools could be to ensure in those worst cases, plus the reinsurance cost in the UK BI dispute that you could still end up landing around that kind of level? Few other quick ones. I noticed your one in 200-year exposures at the back of the presentation for nat cat have gone down significantly for US, I'm guessing that's the purchase of the additional retro/reinsurance, but you indicated you grew in July. So have those come back up again as a result of July, is that still a good ballpark? And then the only final question, it's really hard to understand what London Market profitability is on the kind of, let's call it the new business, i.e. free of some of those legacy losses, some of those large losses, which appear to be an older business. I mean, it looks like the (inaudible) underlying combined is in the mid-90s. I mean, is that a good guide as to where the kind of new business is being written? Thanks.

A - Bronek Masojada {BIO 1776109 <GO>}

Thanks, Andrew. I'll suggest that Aki you take the capital scenarios on the London Market underlying. And Jo, if you can comment on the -- what's happening to the one in 200 and how you think that will work through. Aki?

A - Aki Hussain {BIO 19739719 <GO>}

So thank you, Bronek. Hi, Andrew. In terms of capital, and the scenario that we set out there, as you can see in the scenario, we started off with a pretty robust capital position with the priority actions we've taken in terms of raising equity and then of course the organic capital generation position is very strong, prior to reflecting those fiscal [ph] downside scenario. Now you could always ask more or take away from the scenarios, but the point here is that those two aggregate scenarios added to around $500 million of net downside and it still raises with the capital position around 180% mark. And do recall from our equity presentation -- strategy presentation (inaudible) equity raise some months ago, that -- note that [ph] capital ratio is around 160, 170 mark, in between that range, that's consistent with an A rating, and still leaves us with ample capital. So even after taking this $0.5 billion or (inaudible) the cash position remains very strong. One specific point regarding Re, I guess we have to think about that is, this is not an isolated situation that affects today's COGS [ph]. Re -- our reinsurance and ILS division has a -- currently and historically has had a pretty small market share within -- I guess the term we use is underweight UK and Europe and that is our historic view on pricing in nat cats [ph]. We also reinsure a significant amount of the business that we write in Re anywhere between -- for our cat business, it can be up to 90% across the portfolio and around 75% in reinsured. So to the extent that losses will come through our Reinsurance and cat, we currently don't expect them to be significant and importantly, relative to the market, it will be a pretty small share. (inaudible) that needs to be factored in this scenario. In terms of the strengthening of the BSCR, actually we expect that the strengthening will take away maybe 10 to 15 points from the solvency ratio that's reflected in our starting point for the first stage of strengthening, we have yet to reflect the full strengthening for 2020, which we will do on our year-end results. I would expect the bulk of that to be offset by the organic capital generation. You saw that -- you can see the capital generation in Q2, which is 9%, that's been partly elevated by the improvement in investment returns. Across the year in a normalized year, so underlying, excluding COVID-19, I would expect the capital generation to be somewhere between 18 and 22 points and that should offset any strengthening required or driven by the BMA. Just moving on to the London Market profitability, I think your assessment of the current year underlying combined ratio is there thereabouts. As I said, we had about a 4 point impact from COVID-19 and a further 7 point impact from above-average large losses. But I guess the important question is what about the business that we're writing now? The business that we are writing now, given the rate increases that are coming through that we've seen this year and also towards the back end of last year, we believe now it is just around 90% or just below in terms of a combined ratio. Ultimately that will start to feed through into the P&L. You know the way how these patterns work here. Given the mix of the business, we have some short tail, some longer tail in terms of the property binders and so on. I expect that a decent profit performance will start to come through into 2021, certainly into the second half of 2021. So we're pretty pleased with the business that we're writing now.

A - Bronek Masojada {BIO 1776109 <GO>}

Thank you, Aki. Jo?

A - Joanne Musselle {BIO 19106109 <GO>}

Thanks, Bronek. Yeah. So you're right. So at the beginning of the year, we felt that reinsurance rates were not sufficiently attractive to grow, and post COVID, in March, we purchased some reinsurance in the form of industry loss warranties at prices that were commercially attractive to both protect our capital (inaudible) the upcoming wind and you will see that on slide 41 where that has reduced the mean modeled loss on the US windstorm to just shy of $200 million and that was -- if you looked at the -- go back to the end of the year that was over $300 million. The vast majority of that has been driven by the additional $100 million of ILWs. You write that with models at the end of April, and we have written in our June and July renewals, so rather we made them [ph] 20%, we're down 10% year to date, including the June and July renewals. So whilst that mean model loss will increase a little bit, the majority of that driver is the purchase of the ILWs.

Q - Andrew Ritchie {BIO 18731996 <GO>}

Okay, thanks.

A - Bronek Masojada {BIO 1776109 <GO>}

Thank you, Andrew. Thank you Jo. We have questions Johan [ph] outstanding from Ben Cohen. (Technical Difficulty) We will take those two questions and then we will draw the Q&A to close. So if you'd like to choose one of them, then we can go ahead.

Operator

All right. Now we have next question coming from Ben Cohen from Investec. Hi, Ben. Your line is open now.

A - Bronek Masojada {BIO 1776109 <GO>}

Hi, Ben.

Q - Ben Cohen {BIO 1541726 <GO>}

Two things I wanted to ask about. Firstly, could you just -- you talked a lot about Retail growth in different context, so just one wondered, we would just tie you down a little bit more about how much you see the Retail division growing this year and also the outlook for next year. Maybe just recap in terms of sensitivity to economic growth.

The second thing I wanted to ask about was really just the uncertainty still around COVID losses from a third-party point of view. You've obviously made some estimates in the first half of the year. I wondered just where you feel you are in terms of getting ahead of loss notification. And I suppose a third related, in terms of the potential impact that that might be to the reinsurance portfolio from the UK BI ruling, I just wondered, is this really just a very, very small loss that we're looking about? Why was this something that you didn't see fit to warn about at the time of the Q1 update with the equity raise? Thank you.

A - Bronek Masojada {BIO 1776109 <GO>}

Okay. I think in terms of regional growth, clearly Ben will be able to comment on that. In terms of the third-party, Jo, and then the final question Aki.

A - Benjamin A Walter {BIO 18021194 <GO>}

Hi, Ben. I'm afraid on Retail growth, I'm not going to give you much more certainty on 2020, we withdrew guidance given the uncertainty in the broader environment. And I'm afraid that uncertainty still remains. So I'm pleased with the growth we had in the first half contextually. And clearly if the economic environment continues to heal, that will be a fair tailwind for us, but we just can't be sure at this point, given the fact that this is still going on, the pandemic is still live, different countries are responding in different ways, we don't know what the next phase looks like and we are loath [ph] to commit to a growth level while we find ourselves in this situation. Clearly once the situation stabilizes and the pandemic starts to either be a normalized way of life or more hopefully starts to be behind us, we will look to return the business to the 5% to 15% target growth range.

A - Bronek Masojada {BIO 1776109 <GO>}

Thank you, Ben. Thank you.

A - Joanne Musselle {BIO 19106109 <GO>}

Yeah. So with regard to third-party losses, in the way that we're thinking about COVID, we have reserved losses, which are more directly impacted by the pandemic. So that's things like events cancellation et cetera. We've now moved into things which are more affected by the economic interruption and the economic shocks, so that's the potential business interruption and travel.

And then you're right, as this pandemic moves then we're looking into this third-party liability. We think about it in a couple of ways. We think about third-party almost direct liability COVID-related, and that would be what we reserved at half year. So that would be the allied healthcare impact where we see a direct COVID-related potential third-party.

I suppose indirect COVID, we have seen some notifications on our portfolio, so I'll give you an example. Accountants [ph] BI in the UK, we've had some claims, which are for filing of furlough -- late filing of furlough, and whilst these are indirectly related to COVID, they are just part of the normal claims frequency that we see within accountants and whilst they're not doing some of the things like filing tax et cetera. So we're dealing with those as part of the loss ratio, and any of those will be taken care of in the Q2 reserve Ben. And then as we move forward and we forecast what is the impact with regard to any increased view of risk, so whether that be through recessionary loss or through are there any third-party litigation as we move into 2020 and 2021, whilst of course it is quite speculative at this stage, it's really important for us to understand, because we've taken all of that into our underwriting and we would look to see if there is an increased view of risk, regardless of where that's coming from and make sure that our underwriting action, whether that be portfolio action or the rates, indeed that we're getting mitigates the impact of any sort of increase that we see with regard to view of risk.

Q - Ben Cohen {BIO 1541726 <GO>}

Right. Thank you.

A - Bronek Masojada {BIO 1776109 <GO>}

Aki?

A - Aki Hussain {BIO 19739719 <GO>}

And then on the final point regarding the reinsurance accounts, I think at the time -- well, I know on the time of the equity raise, we were quite clear in explaining that exposure to losses in the reinsurance account was uncertain, but also to remind you, today [ph], that the Hiscox Re, now that's underweight in Europe and with only modest net premium retentions. So frankly the disclosure that we have today is simply reiterating that and providing a little bit of caution, there could be something. But frankly, I'll focus on the fact that we are underweight in Europe, this is something that's not unique to Hiscox, but we are underweight Europe with modest retentions and if anything (inaudible) expected to be for most [ph].

Q - Ben Cohen {BIO 1541726 <GO>}

Thank you Bronek. Johan, I think there's one more from Mr. Van Embden.

Operator

That's right. We have next question from Andreas Van from Peel Hunt. Hi, Andreas. Your line is open. Please go ahead with your question.

A - Bronek Masojada {BIO 1776109 <GO>}

Good morning, Andreas.

Q - Andreas Van Embden {BIO 1795530 <GO>}

Hi, hello, everyone. Good morning, Bronek. And good morning all. Thank you very much for taking my questions. I just have two focus points. One is on Hiscox Re, and looking forward at the 1/1 renewals, I just wanted to -- in terms of your plans for next year, with the R & ILS [ph] capital retrenching and you're alluding that could retrench even further in second half of the year ahead of the renewals, could you maybe comment on how much net risk you are planning to retain at 1/1, just describe perhaps the move from the gross to net, there is going to be a significant change going into next year and perhaps how much capital that that could potentially consume.

And my second question is around the UK Retail and business interruption exposures. Could you maybe discuss your reinsurance protection program within UK Retail? What assumptions have you made for reinsurance retentions within your stress test of GBP10 million to GBP250 million and perhaps discuss how much room do you have in your UK Retail reinsurance program to absorb for the losses or pass on for the losses to your reinsurers. Thank you.

A - Bronek Masojada {BIO 1776109 <GO>}

Okay. I think in terms of the 1/1 plans for Hiscox Re, Jo, I think that's probably one for you to talk about. And in terms of the reinsurance, Aki, do you want to respond to that?

A - Joanne Musselle {BIO 19106109 <GO>}

Yeah, thanks Bronek. Yeah. So as we look forward to 1/1, I mean, as I said, the rates are accelerating where 11 [ph] inclusions of the mid-year and we do see that accelerating, so we do think it will be an interesting market for us at 1/1. We do have the capital and we are looking to deploy that on our own balance sheet. I mean with regard to what that exactly looks like, we're looking through that at the moment and as we always do with our business planning, we make a judgment about the inflection points around rates and the makeup of our portfolio in terms of gross to net. But with the market we do foresee, we are confident that the rate acceleration that we are seeing, we'll look forward to 1/1, so we are excited.

A - Bronek Masojada {BIO 1776109 <GO>}

I mean I think, if I can expand on Jo's. At the moment, Andreas there is a slightly balancing act that Jo and the team are performing between third-party capital, ILS, and our net retained appetite. Thanks to the capital raise and we clearly have more net appetite to deploy both in London Market and Re and we'll be making the precise decision as the year progresses. I mean on the one hand, it is, as I say, because of the cat cuts on ILS, we may write less gross written premium. But certainly our expectation is that net written premium will grow. And it's a fact, the very existence of that cat capital, which is driving the rating increase across the market as a whole, so it's one of those balancing acts, but very clearly, as Jo says, it's the balancing act, is driving price increases.

So Aki, do you want to just talk briefly about the UK reinsurance program.

A - Aki Hussain {BIO 19739719 <GO>}

Of course. I mean, I guess the answer is pretty short. We don't intend to disclose the details of the reinsurance program. I would reiterate the previous messages that we put out there, we do have a comprehensive reinsurance program, supported by high quality top-tier reinsurance panel and we're pretty confident to recover that we have.

A - Bronek Masojada {BIO 1776109 <GO>}

Okay, alright, thanks, Aki. And with that I believe there are no -- there is no other questions in the queue. So thank you all for your time. Just to reiterate, I mean I think it's clearly been a challenging first half, but the business has been very resilient, both operationally and its ability to respond to customers. And as we look forward, clearly there is a market opportunity, particularly in the big ticket area that has been explained. We're not going to lose sight of the ability to keep on growing Retail and we are positive about the profit and growth opportunities that we see this year and clearly into 2021. Thank you all for your time.