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Market Intelligence

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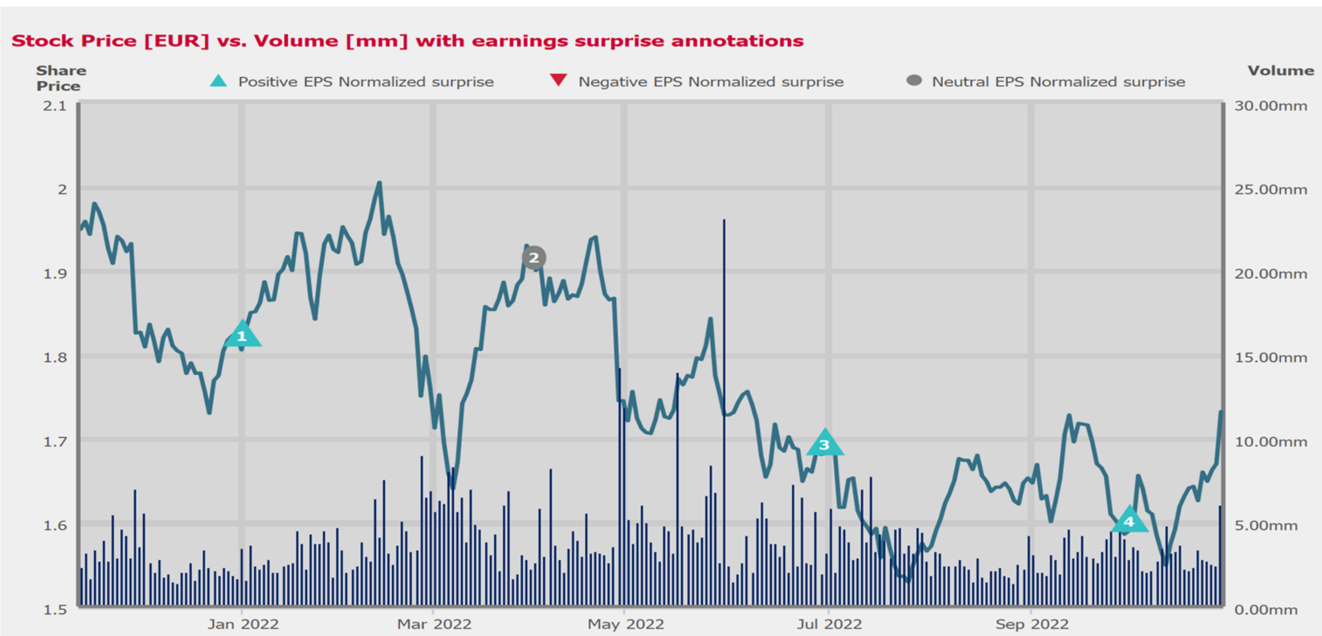
FQ3 2022 Earnings Call Transcripts

Friday, October 28, 2022 9:30 AM GMT

S&P Global Market Intelligence Estimates

	-FQ3 2022-			-FQ4 2022-	-FY 2022-	-FY 2023-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS Normalized	0.04	0.05	25.00	0.05	0.21	NA
Revenue (mm)	5706.89	6134.80	7.50	6027.68	23607.00	NA

Currency: EUR
Consensus as of Oct-28-2022 8:44 AM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ4 2021	0.07	0.10	1 42.86 %
FQ1 2022	0.05	0.05	2 0.00 %
FQ2 2022	0.04	0.06	3 50.00 %
FQ3 2022	0.04	0.05	4 25.00 %

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Call Participants

EXECUTIVES

Felipe Navarro López de Chicheri
Head of Capital Markets & Investor Relations and Treasurer

Fernando Mata Verdejo
Group CFO & Director

Presentation

Felipe Navarro López de Chicheri
Head of Capital Markets & Investor Relations and Treasurer

Good morning, everyone, and welcome to MAPFRE's Results Presentation for the Third Quarter of 2022. This is Felipe Navarro, Head of Investor Relations and Capital Markets and Corporate Treasurer. It is a pleasure to have here with us our Group CFO, Fernando Mata. He will walk us through the trends of the quarter and discuss the main P&L drivers on the investment portfolio. And before his closing remarks, I will walk us through the capital and solvency sections.

At the end of the presentation, we will open the Q&A session. [Operator Instructions] We will try to answer all of them as time allows, and the IR team will be available to answer any pending questions after the call. As a reminder, the replay of this webcast will be available shortly after the call.

And now I would like to turn the conference over to Fernando. Fernando?

Fernando Mata Verdejo
Group CFO & Director

Thank you, Felipe. Good morning, everyone. Before going into the details, I would like to start with a few introductory remarks. Despite an extremely challenging market environment, MAPFRE is reporting satisfactory results. We continue to implement our current strategic plan while adapting it to the current context. This is the roadmap the company needs to move forward in terms of growth and profitability.

Regarding financial targets, both the aspirational targets and the reference framework, are still valid. There is currently no evidence indicating that they cannot be met. As the combined ratios, we already said in previous presentation, is challenging in the current context, it could be subject to revision at the end of the year. We're confident that there are some tailwinds to help the ROE target, such as a very strong premium growth, improving financial results, and positive currency trends.

Growth on a like-for-like basis has been resilient in the insurance business in Spain with strong performance across Latin America, especially Brazil. We've seen high double-digit growth in the Reinsurance unit on the back of a supportive pricing environment. Currency movements have also boosted these figures.

Diversification is key to our resilience. While we continue with a disciplined approach and growing in profitable lines, such as General P&C and Life Protection. We focused on organic growth and our M&A strategy, as always, is extremely prudent. We are not willing to grow organically at any price.

The market environment isn't easy with the geopolitical tensions, persistent inflation, sharp increase in interest rates and a risk of recession in key markets. Nevertheless, profitability has been robust, reaching a net result of over EUR 488 million with an ROE of over 9%, despite the impact from hyperinflationary economies this quarter.

Profit contribution was strong from core operations and better technical results in General P&C and Life Protection, and mitigating ongoing pressure in Motor, with a solid contribution from financial income in many markets. Furthermore, after the sale of nonstrategic assistance operations and insurance subsidiaries in Indonesia and the Philippines, this last transaction has been completed this morning, we have reached our main restructuring targets. After this multiyear process, our footprint has been streamlined, and we have a leaner organization, better positioned to leverage future growth opportunities and allocating capital to the most attractive businesses.

I would like to comment on the Motor business. This segment remains under pressure with high claims inflation, changes in driving patterns and higher mobility, with frequency converging to pre-COVID levels. We are executing profitability initiatives across all regions, focusing on the 3 main drivers: first, tariff increases, both on new business and renewals; second, cost contention, we are actively managing spare parts, logistics, and minimizing repair times, thanks to our preferred garage network and tow trucks, as well as strictly monitoring and structural expenses; and third, even stricter underwriting measures were put in place, canceling business and limiting covers in specific portfolio segments. These measures, especially pricing, take time to [affect] the bottom line, and it could take some quarters to convert to a sustainable Motor combined ratio. However, we are already seeing green shoots in Brazil where portfolio repricing was very quick.

Spain, the technical measure implemented to catch up with current inflation are taking time to feed through P&L. And in the U.S., it could take some more time due to the complex regulatory environment as we will explain later. Finally, MAPFRE continues to have a very strong solvency position and high level of financial flexibility. Dividend upstreaming continues to be strong at subsidiaries. Yesterday the Board approved a EUR 0.06 interim dividend to be paid on November 30, reaffirming the group's commitment to maintaining a stable dividend policy.

The Solvency II ratio, as you know, was 220% as of June 2022, significantly boosted by the Tier 3 bond that we issued in April, mitigating the fall in shareholders' equity. Our net equity has proven resilient, falling less than other European insurers in a highly volatile market, thanks to diversification, high levels of liquidity, and a prudent investment approach.

I will comment on some of the key figures. Premiums are up 12% in euros. If we eliminate, look at on the right box, the impact from currency movements, which added over 5 points to growth, a large multiyear policy issued in Mexico last year, which took away 3 points from growth, and finally, the exit of BANKIA which took away a little under 1 point, premiums would have been up 10.6% with very strong trends in both Non-Life and life.

Regarding the positive currency trends, the most relevant were the U.S. dollar, up around [15%] and the Brazilian real up over 18%. There were also double-digit appreciation in many other Latin American currencies. The combined ratio was 98.4%, with a loss ratio up over 3 points, mainly driven by the pressure in Motor as well as higher frequency of nat cat events. The 27% expense ratio is noteworthy and it's down 1.4 points, supported by very strict cost control in all areas.

The pressure on combined ratio was partially mitigated by the improvements in financial income, despite lower realized gains. So the Non-Life financial result was up around EUR 20 million and over EUR 100 million when adjusting for realized gains. The attributable results reached EUR 488 million with an ROE of around 9%, 8.3% excluding the impact of BANKIA and other extraordinary charges booked at the end of 2021. Finally, shareholders' equity is down around 10%, and only slightly down in the quarter at around EUR 7.6 billion and is mainly due to the reduction of unrealized capital gains from rising interest rates, which was partially offset by the already mentioned currency movements.

As usual, on this slide, we explain the main extraordinary items. First of all, we would like to comment on the impact from hyperinflationary economies. We have restated the financial statements of our subsidiary in Turkey for 2022, applying the international standard for hyperinflationary economies, which had an impact of around EUR 17 million. As other hyperinflation impacts were also significant, mainly in Argentina, which also include the full impact for both entities and both periods in this line. The other nonoperating impacts include the net gains related to the sales of restructuring of the assistance operations and also the insurance subsidiary in Indonesia.

Regarding operating impacts, during the quarter, we had set aside a provision at the Puerto Rican unit for Hurricane Fiona with a EUR 22 million net impact. No relevant claims relevant have been reported so far, but this is our current estimate for this event with a negligible impact at MAPFRE RE. There was also a small negative runoff from the Parana river drought claim, reaching EUR 105 million net loss for the group, of which EUR 59 million is at the reinsurance unit, EUR 46 million is at insurance units, and by country, EUR 37 million corresponds to Brazil and the remaining EUR 9 million to Paraguay.

COVID losses are decreasing in 2022, reaching just under EUR 30 million till September, EUR 37 million less than 2021. Financial gains and losses are down by EUR 42 million. We were able to partially compensate the falling financial investments with higher gains from real estate transactions. Finally, the other line -- the line, sorry, Other for 2022 includes the tax impacts in Spain and Peru already commented in previous presentations. Full disclosure, as always, of the different components of these items is included in the annex at the end of this presentation.

Premiums -- yes, during 2022, insurance operations contributed over EUR 15.6 billion in premiums and over EUR 481 million in results. Iberia's performance continued to be extremely resilient. Premiums are up 1%, and excluding BANKIA, they would have been up over 3%. Non-Life premiums increased 3.5% with a strong performance in General P&C and Health. The combined ratio is up 1 point to 97% due to the pressure in Motor, where the ratio continues to be slightly over 100%.

Positive trends in other Non-Life segments are mitigating this impact with the ratio in General P&C under 96%, are held now under 97%. Portugal has an excellent combined ratio and remarkable growth figures. Iberia continues to be the main contributor to profitability with an almost EUR 300 million net results. And just as a reminder, last year's BANKIA profit contribution accounted for around EUR 30 million, which is basically the difference between the 2 [subsidiaries].

In Brazil, premiums were significantly up with healthy growth trends in Agro, Motor, and Life Protection. Brazil was the second largest contributor to profit with a net result reaching EUR 93 million, up over EUR 43 million. Strong improvements in Life Protection and high financial income have mitigated pressure in Motor and the impact from the drought. The overall combined ratio was excellent under 90% with very strong trends in General P&C, including the Agro segment. There was a strong turnaround in the Motor combined ratio, which was 110% in the standalone third quarter, down 10 points compared to the previous quarters. Currency appreciation has also been a positive driver. All in all, the outlook for Brazil is much more positive with a EUR 50 million profit contribution in this quarter.

Let's [go on] LATAM. Premiums in LATAM North were up around 30% when adjusting for the multiyear policy and LATAM South grew 29% in euros. Local currency growth was solid in most segments, and it's worth mentioning Mexico up 17% on a like-for-like basis, Peru up over 23%, Dominican Republic up 15%, and Chile up 31%. Overall, in both regions, the strong recovery in Life Protection and profitability, together with improved financial income and currencies, offset the pressure in Motor. The net result was up in both regions.

Premiums in North America are up nearly 29%, supported by dollar appreciation. On a like-for-like basis and also stripping out the impact of the Century business was transferred from ASISTENCIA and currency movements, premiums were relatively flat. Performance continues to be affected by rigid tariff regulation, growing mobility trends, and increased severity. There was also a EUR 22 million net loss during the quarter in Puerto Rico, as I already mentioned, due to the provision set aside for Hurricane Fiona.

In Eurasia, premiums are flat due to the impact of the hyperinflation in Turkey, where premiums are now growing 16%. The net loss is mainly due to the loss in Turkey, which amounted to EUR 23 million as a result of the inflation. Italy, Germany, and Malta are showing trends in line with previous quarters. At MAPFRE RE, premium growth is supported by positive pricing trends and U.S. dollar appreciation. The combined ratio is 97.5%, with a net result of over EUR 93 million, which was pretty strong considering the impact from the Parana drought as well as higher frequency of nat cat claims, such as Hurricane Ian or various weather events in Europe.

The result is down in the year, mainly due to a lower level of realized gains in the investment in the financial investment portfolio. In Assistance, streamlining effort is evident with volumes down almost 60%. We come to the end of our restructuring process with further businesses sold during the quarter, with a net impact of EUR 8 million on the result. Excluding this, the unit will have been a breakeven.

I would like to spend some time commenting on the Motor business. First of all, most insurers are experiencing business deterioration even with big [losses] in this segment in many markets. It's not exclusively a MAPFRE problem. This segment is currently experiencing several headwinds and it is extremely exposed to inflation and higher mobility. There are also other trends that are putting pressure on the loss ratio: changes in driving patterns; supply chain disruption, which are affecting spare parts logistics; and leading to longer repair times.

And finally, regulatory intervention, it's not only a matter of frequency, as I mentioned. This is more caused by insufficient premiums to cover the current level of costs. We have quickly defined and executed profitability initiatives across all regions. These measures will take time to [affect] the bottom line, especially in the case of tariff increases, and it could take some quarters to converge to a sustainable combined ratio.

At MAPFRE, there is pressure in Motor across all countries, with some exceptions, with Peru and Puerto Rico standing out with combined ratios below 95%. As you can see on the slide, the fleet is falling down by almost 200,000 vehicles year-to-date. And our future growth appetite will depend on the profitability outlook for this segment as we do not want to grow at any price.

In Iberia, rate increases for new business were implemented in the fourth quarter of 2021, while increases on renewals are being gradually implemented through the year to converge with current inflation. We have recently accelerated, obviously, these measures. Average premium are now relatively stable during 2022 after several years of declines. We are still seeing a reduction in coverage and other underwriting measures are implemented to maintain the churn ratio stable. On the spend side, we continue with a very strict cost contention, both for internal and external claims costs, including spare parts, logistics, and provider network agreements. We are increasing the number of preferred garages and pre-directing clients to our network. As you can see on the graph, the combined ratio could be reaching its peak. However, the tariff increases will still need some time to feed through the P&L.

In Brazil, there have been multiple tariff increases, more may be needed to keep up with growing inflation, but we are already seeing green shoots with a combined ratio falling to 116% at September. On the right-hand side, we have canceled nonperforming brokers focused on higher risk portfolios, such as commercial trucks and buses, with vehicles insured in this segment down year-on-year.

In the U.S., we were very quick to increase tariffs ahead of most of our competitors in Massachusetts, and have already put through 2%, 3% increases during 2022, with an additional rate hike requested in the second half of the year that should be expected to be implemented for 2023. We are also implementing measures on the cost side, such as increasing adjusters on payroll, redirecting more clients to our preferred repair shops, et cetera. We are planning a stricter underwriting policy and further aligning commissions to portfolio performance.

Nevertheless, in the U.S., the combination of inflation, frequency pickup, and regulators [stalling] on rates, has driven the whole market to be underpriced and reflecting the combined ratio that deteriorated 4 points in the fourth quarter at standalone. This measure will help bring the Motor combined ratio down to sustainability levels, although it will still take some time while maintaining the fleet stable and best-in-class service levels for our clients.

Please turn to the next page. Thank you, Felipe. On this slide, I would like to comment on the Life business and insurance units. In Iberia, premiums were down 6%. This reflects the exit from BANKIA last year. And excluding this impact, the premiums would have been up 3%. In Brazil, the Life Protection business, which is currently strong contributor to the results, is showing healthy growth, up 28%, boosted by the significant real appreciation.

The Life result has significantly improved, more than doubling due to the lower COVID impact in LATAM as well as general improving trends in the region. On the right side, you can see that the total COVID impact in LATAM in the quarter was just EUR 6 million, in line with last quarter's figures and more normalized clients experience.

The uncertain geopolitical and macroeconomic context has negatively affected assets. There was a fall in the value of our investment portfolio as well as pension and mutual funds, bringing assets under management down by over 9% overall. Rate increases have been significant across regions with Spanish govies up 207 basis points during the year, while Italian bonds are up over 330 basis points and the U.S. Treasuries are also up 230 basis points. Spanish sovereign debt continues to be the largest exposure in our portfolio with over EUR 9 billion followed by Italian debt with EUR 2.5 billion. A large share of these positions are, as you know, allocated to immunized portfolios, reducing our exposure to future higher rates.

Now I would like to go over the breakdown of our EUR 28 billion fixed income portfolio. On the top are the details of our euro area actively managed fixed income portfolios, which have a market value of around EUR 11 billion. On the bottom are the details of fixed income portfolios in our main markets with a total value of nearly EUR 5.5 billion. The remaining EUR 11.5 billion are mainly Life portfolios in Spain with some type of ALM matching or duration immunizations, which are more neutral to changes in interest rates.

The largest move in our portfolios this year was the strong reduction in duration across portfolios as well as the investment of around EUR 370 million in inflation-linked bonds in Iberia and MAPFRE RE. As a consequence, we observed a reduction in the accounting yield due to the features of those investments. And for this reason, we present figures carving out this part of the portfolio you got on the right side of the slide. These positions have outperformed plain vanilla bonds during the period. As you can see, excluding these bonds, the accounting yield is significantly up in MAPFRE RE, up over 45 basis points, pretty significant, and up 10 basis points in the Iberian Non-Life portfolio.

As a reminder, the loan duration in Iberia Non-Life is due to the burial portfolio. And excluding this, the duration will be around 3.48 years. The portfolio in LATAM also includes approximately EUR 1.9 billion of fixed income securities linked to inflation or floaters linked to central bank rates, which represent around half of fixed income portfolios in the region. On the bottom, you can see the details of the fixed income portfolios in other markets with duration significantly down and portfolio deals up in all markets and regions.

The increases have been noteworthy in Brazil with an increase of nearly 250 basis points and over 150 basis points increases in LATAM North and South. This trend should continue in coming quarters as long as central banks put more emphasis in taming inflation threats. And as we mentioned before, we have already seen an over EUR 100 million increase in underlying Non-Life financial income year-on-year.

Now I will hand over the call to Felipe.

Felipe Navarro López de Chicheri
Head of Capital Markets & Investor Relations and Treasurer

Thank you very much, Fernando. Shareholders' equity stood at EUR 7.6 billion, which represents a 10% decrease during the period. Net unrealized gains on the available-for-sale portfolio were down EUR 1.8 billion, mainly due to the increase in interest rates. The largest impact was in Iberia, down nearly EUR 970 million, followed by North America and MAPFRE RE with around EUR 300 million for each.

Currency conversion differences are up over EUR 700 million on the back of a notable appreciation of the U.S. dollar as well as the Brazilian real and other Latin American currencies. Just to note, the EUR 35 positive evolution in Turkey during the year includes an

EUR 11 million of negative currency differences and a positive EUR 47 million impact from the hyperinflation adjustment. On the right, you have the usual breakdown of currency conversion differences, annual movements, and sensitivity analysis.

In this slide, on the chart on the left, you can see the breakdown of capital structure, which is slightly down, amounting to EUR 11.4 billion, which is mainly equity. Leverage is at 23.6% with a total debt down around EUR 400 million, reaching EUR 2.7 billion. We have reduced the balance of the syndicated credit facility to 0. On the right, you can see a Solvency II ratio of nearly 220% as of June, 210% excluding transitionals. This is up over 14% compared to March, largely due to the Tier 3 debt issuance as well as market movements and organical capital generation.

The fully-loaded ratio was also strong at 210%, proof of our low dependence of the use of transitional measures. During the first 9 months, the different group holding companies have received around EUR 650 million worth of dividends from its subsidiaries. The considerations received from the sale of our Indonesian and Philippine subsidiaries will contribute as well to the dividend payment. The company enjoys at present an excellent liquidity position, consequence of ordinary cash generations together with the amounts received from different disposals, namely BANKIA, CCM, Indonesia, Philippines, and different ASISTENCIA subsidiaries.

This position has been increased by the Tier 3 issue. This is an excess of operating cash balances, particularly in the Life subsidiary in Spain. As a consequence, MAPFRE at the end of September is not using the EUR 1 billion syndicated facility at all, reducing the leverage to 23.6%. The excess that has not been upstreamed yet will be deployed into our profitable growing subsidiaries to finance organic growth.

I will now hand the floor back over to Fernando.

Fernando Mata Verdejo
Group CFO & Director

Thank you, Felipe. Let's go with the closing remarks. All in all, MAPFRE's geographical and business diversification continue to be key for MAPFRE, allowing us to offset headwinds from the Motor line. And although the market context continues to be challenging, our growth is robust, and profitability has been resilient.

MAPFRE RE has strongly contributed to results despite the nat cat activity during the quarter and should continue to benefit from a supportive pricing environment. LATAM premium volumes and profit contribution are worth mentioning, growing in local currency. Profitability is boosted by lower COVID losses and higher interest rates.

In Motor, we are actively taking measures to restore profitability across all geographies and results are starting to be seen in some regions. We remain committed to our strategic plan, closely monitoring the current geopolitical situation and how it might affect growth and profitability. So far, the general framework is still valid. The combined ratio of 94% to 95% will be challenging in the current context and could be subject to a revision at the end of the year.

On the other hand, there are several other tailwinds that will help meet the 9% to 10% ROE target, such as a very strong premium growth and improving financial results, and finally, the positive currency impact. Also, our transformation and ESG targets remain fully valid. And with the appointments announced today, now over 42% of the Board of Directors is comprised of women.

Our excellent solvency and capital base, together with a strong cash generation, are supporting the payment of a EUR 0.06 interim dividend in November, in line with our commitment to a sustainable dividend path. Regarding the arbitration related to the BANKIA exit, we expect the resolution to be delivered early 2023, next year. We have finalized the restructuring processes in place and move forward with our transformation to better adapt to current market needs. Finally, I would like to mention that this morning, we have completed the closing of small operations in the Philippines.
Thank you very much for your attention, and I will now hand the floor over to Felipe to begin the Q&A session.

Question and Answer

Felipe Navarro López de Chicheri
Head of Capital Markets & Investor Relations and Treasurer

I'm sure that you have already -- you are already familiar with the Q&A session process. Just let me very quickly remind you that you can use the Q&A tool on the bottom of your screen to send your questions, and we will try to clarify all your doubts as time allows. And now let's start with the first question that comes from Michele Ballatore from KBW. He wants to know if there is anything to highlight in terms of major nat cat effects in MAPFRE RE.

Fernando Mata Verdejo
Group CFO & Director

I've got some notes over here. Let me get them. We explained some of the cat effect on the -- during the presentation. I'm going to just focus on the main ones. First, Hurricane Fiona; as we mentioned in the past, we expected that most of the flooding should be covered by the National Flood Program -- National Insurance Flood Program. We got a small portfolio, so we get some flood claims in Puerto Rico.

Anyway, no relevant claims, relevant means significant, have been reported so far. They're currently about some 5,000. I will say, that there are attritional claims and a significant percentage of which will not exceed deductible. So in the end, we will close those claims without any payment. Regarding relevant accounts, I mean municipalities, they have not yet reported anything. So we have to wait. This is -- we are at a very early stage. But so far, it's good. Provisions out there, well, we booked -- we don't have final claims, are based on our experience and estimates and also exposures on the main areas affected by the hurricane. I didn't mention, but MAPFRE RE has booked a negligible pretax from MAPFRE Dominicana, it's not important. And on MAPFRE RE side, we shouldn't expect any relevant impact from third-party business.

The second is Hurricane Ian, the one that impacted Florida, particularly Fort Myers area. It's a low exposure area for MAPFRE, very limited impact in Florida in direct insurance. There is a bunch of claims in the automobile. As you remember, in this state, the portfolio is in a runoff position. MAPFRE RE, which is a good thing, has not had any specific coverage in this state for years and could only possibly have limited exposure from insurance programs from a nation-wide direct insurance companies.

So at the close of September, MAPFRE RE booked a EUR 20 million pretax reserve. It's based on a top-down analysis. It's a rough estimation based on model information and early conversations with some cedant entities. Despite being a very complex claim that will take a lot of time to be adjusted, MAPFRE RE's limited exposure leads us to believe that it will not surpass a midsized event in any case. Midsize means EUR 40 million, EUR 50 million.

On a market level, Ian has been a catastrophic hurricane, a Category 4, with the impact more than EUR 100 billion in damages, for an insurance claim of EUR 60 billion in insured capital. So it's a big, big hurricane. So let's say that we wrote the right business in Florida. So we won't book a significant impact from Ian.

Another nat cat event in that case in Europe in summer, we had several hailstorms in France, surpassed the EUR 6 billion in impact for the total industry. For MAPFRE RE it will be a midsize event, again. So far and with the information that we had at the end of the third quarter, EUR 20 million pretax had been reserved. But for the future quarters, we could expect a certain deterioration due to the complexity of this type of claim. So perhaps we should expect some negative runoff during the fourth quarter.

That's basically -- in Spain, as usual, September has been a month with a lot of winds and also heavy rains, particularly on the coastal areas, but nothing relevant. This is seasonal. And let's say that those nat cat events, they're already included in the third quarter combined ratio. So that's basically from the nat cat activity, which, by the way, has been pretty active. But so far, let's keep our fingers crossed. October has been pretty quiet. So let's assume that the rest of the hurricane season remain the same.

Felipe Navarro López de Chicheri
Head of Capital Markets & Investor Relations and Treasurer

Yes. Let's hope for this. Thank you very much, Fernando, for your very comprehensive answer, because Andrew Sinclair from Bank of America and Paz Ojeda from Banco de Sabadell were asking about Hurricane Ian and if we were expecting further losses from hurricanes Fiona or Ian development on the fourth quarter.

Fernando Mata Verdejo
Group CFO & Director

Yes. We are still at quite early stage. And let me say from Ian, particularly, we shouldn't expect -- nothing relevant. Fiona is different because that could have some, not relevant, but negative loss development during the quarter. But let's say that we're happy. And regarding this cat exposure and our cat appetite particularly reflects the impact of these losses.

Felipe Navarro López de Chicheri
Head of Capital Markets & Investor Relations and Treasurer

Okay. We are moving now from the reinsurance to other areas. Now Michele Ballatore from KBW wants us to clarify how our restructuring process in Brazil is going and if there's anything to highlight for third quarter 2022.

Fernando Mata Verdejo
Group CFO & Director

Yes. Regarding Auto, as being said, a reduction in portfolio -- loss-making portfolios; significant increases, particularly on a monthly basis, on rates; reduction of our payroll was carried out, the voluntary redundancy scheme as well in Brazil; and basically, reduction in internal costs and also price increases. That's basically the restructuring process in Brazil. We're happy. We saw a significant drop in loss ratio. [10] basis points is extremely -- a sharp drop. We're now going to see a more mature, more stable portfolio, such as -- or larger portfolio such as the U.S. and particularly Iberia, but we're quite happy with the current trend in Brazil.

Felipe Navarro López de Chicheri
Head of Capital Markets & Investor Relations and Treasurer

Okay. Paz Ojeda is insisting on the same subject because of the turnaround in the combined ratio in Brazil in the Motor business. She's asking, could you elaborate the reasons behind this? And is this sustainable in the future?

Fernando Mata Verdejo
Group CFO & Director

When we compare Brazil with other geographies, particularly Europe and particularly Spain or the U.S., I always say that Brazil is extremely dynamic. It's a country which everything is extremely high speed. And so the market is accepting well, very well, increases in tariffs. It's a country that there's no hyperinflation, but they're suffering inflation for many, many decades and going up and down, and this changes in CPIs. So let's say that we should expect further, probably not at that pace, but further decreases in combined ratio in coming quarters. Obviously in the mid run -- in the medium term, the target is to hit 100%. So that's basically the target for MAPFRE.

Felipe Navarro López de Chicheri
Head of Capital Markets & Investor Relations and Treasurer

Okay. Farquhar Murray from Autonomous is asking why the combined ratio in accidental health decreased in Iberia from 103% in June to a little under 97% in September. Was there any reserve release?

Fernando Mata Verdejo
Group CFO & Director

The answer is no. There is a seasonal reason as well. Summer usually is a low-reporting season. And I don't promise. I would like to have it and report it. But usually, wintertime [as well] is a catch-up season. So we are still quite confident that we will hit below 100% for the full year. But so far, it's seasonal, cost control as well, and also the reduction in internal expenses.

Felipe Navarro López de Chicheri
Head of Capital Markets & Investor Relations and Treasurer

Andrew Sinclair from Bank of America would like to update -- an update on the Iberia P&C pricing versus claims inflation trends. I think it's quite a hot topic. And Maks Mishyn from JB Capital is asking for how -- for our outlook on average premium in Motor in Spain for the coming year. Those are quite hot topics and our competitors are showing some figures right now. So your comments.

Fernando Mata Verdejo
Group CFO & Director

I expected both topics. Andrew, a very good question. We discussed previously in the presentation. I'll give you more color, sure. Our churn ratio for General P&C in Iberia is pretty low. So we based our premium growth on renewals rather than new business. On the contrary, there are other peers that are based on new business. So for renewals, there is an yearly update of capitals and values at year-end, so let's say, this increase in values is being automatically transferred to premiums. So basically, the increase in average premium is based on this.

Claims, fortunately, they're pretty low considering the current context. There is a pickup in September, but it was based on the same that we mentioned. It was a seasonal reason is the rain and winds that they when transferred to the consortium and they were retaining MAPFRE. But basically, we're pretty happy with the P&C trend, and our expectation is that we will keep the same level for coming quarters.

Regarding average premiums in Motor Spain is very complex. Let me elaborate a little bit longer. First, the reason is the aging of the Spanish fleet is 13 years old. And as long we've not seen a significant increase in the new cars sold, the average premium will be -- or the trend will be lower year-by-year. And this is basically because it is a transfer from full covers to TPL and also the value of the scrap -- the scrap value of the cars as well are going down. So this is the main reason because we've not seen yet a significant increase, and you compare with the last 10 years, we're not seeing as significant increase in the average automobile premium.

It doesn't mean that we're not increasing for new business and renewals the average premium. The thing is being offset by what we mentioned, lower coverage and also lower value of the cars. On a monthly basis, as we mentioned, there's a slight increase on renewals in order to keep the portfolio stable. We published the numbers of units. As you saw, we're not hungry just to increase units. And if we had to cancel nonportfolio accounts, we will do it.

On the new business, even increases in tariffs are higher. But the general answer is CPI is very important in Spain and increases in rates are based on General P&C, but on our internal increase of cost. So we will keep this trend in the coming months in order to achieve a sustainable combined ratio for Automotive in Spain.

Felipe Navarro López de Chicheri
Head of Capital Markets & Investor Relations and Treasurer

There's quite a technical question coming from Paz Ojeda from Banco Sabadell. Could you please confirm if we have increased the unexpired risk reserves to tackle the premium sufficiency? And if yes, the amount booked?

Fernando Mata Verdejo
Group CFO & Director

I don't have the number with me, but I'm sure the only reason behind this could be VERTI, which is running losses. And every 3 years, we update the provision for unexpired risk, and we will get back to you. But my answer is, probably it's VERTI.

Felipe Navarro López de Chicheri
Head of Capital Markets & Investor Relations and Treasurer

Yes. We will get back to you on a written way. Coming from Andrew Sinclair, when do you expect the Iberia Motor combined ratio to peak?

Fernando Mata Verdejo
Group CFO & Director

If you see the trend on a monthly basis, the curve is flattening. There is still a slight increase, particularly in those loss ratio. There is as well decreases in the expense ratio, but we haven't [curved] yet the trend. But we're very close to the turnaround point, and it will come in months. As long as the average -- a higher premium average is feeding into P&L, we will see in the combined ratio for sure very soon.

As well, let me tell you that the number of units that grew during the first and second quarter, in this third quarter, there is a small reduction in order. We do not have appetite, rather than keep the fleet stable. And there is a tradeoff in terms of increase of average premium and also the units. And we've seen that in this third quarter.

Felipe Navarro López de Chicheri
Head of Capital Markets & Investor Relations and Treasurer

I think it's very important, the conservative approach that we are taking.

Fernando Mata Verdejo
Group CFO & Director

Absolutely.

Felipe Navarro López de Chicheri
Head of Capital Markets & Investor Relations and Treasurer

Another question on -- in Spain is related to the Baremo. What do we expect for the 2023 in Spain Motor?

Fernando Mata Verdejo
Group CFO & Director

Quite interesting question. Back to the June presentation, MAPFRE is booking on a quarterly basis the expected increase in the Baremo. As we mentioned, as of June, it was a EUR 10 million increase already booked. We did an update in the third quarter. We're expecting -- today has been published in the -- published government -- the official government public, and has been this morning. We have to analyze, but let me say that according to the general update, the minimum indemnities should be updated on the pension increase, means that 8.5%. It's pretty high. There's other indemnities that they could arrive, but so far we have not analyzed in very detailed the current information.

If there is an 8% to 9% increase in the Baremo, the parallel increase in the combined ratio should be 2 percentage points, more or less, for MAPFRE's portfolio, means that it has to go directly to premium. That's pretty clear. There is no potential internal expense reductions to be applied to this. It's practically in full indemnities, and we had to put in tariff. That's the thing.

Felipe Navarro López de Chicheri
Head of Capital Markets & Investor Relations and Treasurer

We move now to North America. Since we mentioned already that there was some topic on the new tariff increases for the first day of 2023. Paz Ojeda from Banco Sabadell, she's asking if we could update on remaining tariff increases.

Fernando Mata Verdejo
Group CFO & Director

Yes. As we mentioned, we filed with the Commissioner of Massachusetts for a further increase. Originally, the expected was close to 5%. We removed this rate hike, and we updated with the current persistent inflation. And the average -- when we mentioned 3% or 3.2%, [the 2] previous rate hike and the expected increase is a little bit higher than 6 percentage points. We don't have actual an updated information, but we should expect this approval to be in place for January 1. And we -- our expectation is both previous increases, both they were approved. This one also will be approved.

I don't know whether or not it has been published, but in a few days, we will know the final outcome of this. So we're pretty confident. And the good thing is that with the 3 rate increases, we are in a much more positive position almost to offset too much the current inflation CPI in the U.S., particularly in the Massachusetts states for these 2 years in order to hit 100% combined ratio, the sooner the better. It will take some quarters, probably at beginning of 2024, end of 2023. But the outlook is much more positive than the one we had at the second quarter presentation.

Felipe Navarro López de Chicheri
Head of Capital Markets & Investor Relations and Treasurer

Good. So the message is that it will take time. But now we are -- we look to the North America with a much optimistic -- in a much optimistic way. There is a question coming from Natixis from [Felipe Maria]. Do you intend to be more active on major risk -- I mean Global Risks?

I think that's an unit that's been reconfigured in the last year. So now Global Risks has much less retention and has much lower appetite for retaining some extra risks.

It's providing with a good result and a good result that is steady in time. So we don't expect major changes in the Global Risk and no major surprises on the profit and loss activity either. Global Risks is now embedded into the -- into MAPFRE RE and is benefiting from the present situation in the -- for the group. I don't know, Fernando, if you want to add something.

Fernando Mata Verdejo
Group CFO & Director

No, it was a pretty good answer.

Felipe Navarro López de Chicheri
Head of Capital Markets & Investor Relations and Treasurer

Okay. Paz Ojeda related with Baremo as well. Do you think that it could trigger a hardening market? And if it was the case, it will be as it was enforced in 2016?

Fernando Mata Verdejo
Group CFO & Director

Yes, Paz, I don't blame you. I wasn't aware either in the morning and Ramon Carrasco, our CRO, which is [indiscernible], he told me, and I have not analyzed in detail. But let me say, if the comparable is like when the first increase of Baremo happened like 5 years ago. And at that point, it was really hit for the industry. And over the 2, 3 years in which the average premium grew. And so we should expect the same happen in 2023 and almost 2024.

Finally, the increase -- the average increase for Baremo is above 8%. It will be a significant increase of cost. And as I mentioned, for our portfolio it's like 2 percentage points in the combined ratio -- in the loss ratio. So it's difficult, extremely difficult to assume that we can absorb this cost with efficiencies. Doesn't make sense at all.

Felipe Navarro López de Chicheri
Head of Capital Markets & Investor Relations and Treasurer

Thomas Bateman from Berenberg, he is asking on MAPFRE RE. He says that they are benefiting from better pricing. But on a constant currency basis, he assumes that the premiums are growing only up a little. So could you please give us some color on how MAPFRE RE exposures have changed over the past 12 months?

Fernando Mata Verdejo
Group CFO & Director

Well, let's say, the premiums are not only up a little. We're quite happy with performance and premium growth in MAPFRE RE. There is no new risk and I mentioned that we have 5 operations in Asia. And let's say that the premium growth appetite is pretty clear, more retention for current risk because we know our cedant entities very well, we know the region we are operating. So the only thing is being opportunistic with the current trend that the market is hardening and let's put more capital and more premium growth on these regions and the risk...

Felipe Navarro López de Chicheri
Head of Capital Markets & Investor Relations and Treasurer

I would add that it's not only because of the currency exchanges. There are a hardening in certain markets that we've been experiencing already. We mentioned in the past that we were not happy with the pricing in -- for cat risks in Europe, and now after the events in France and with the hailstorms in Central Europe, we're experiencing some hardening that was already mentioned in the Monte Carlo market.

So what we expect is that those things are improving, and they will be feeding the profit and loss account and the combined ratio in the future months. So it is not only because of the currency expenses, but -- sorry, of the currencies, but because as well of the hardening of the market.

I have another question from Thomas Bateman from Berenberg. He's asking about the expense ratio improvement. How much cost was taken out from the business in the quarter and which regions? And how much was by the improvement just due to the higher premiums?

Fernando Mata Verdejo
Group CFO & Director

I don't know the right answer. [For just to] split into 2, but let me tell you, Thomas, that it's this quarter and previous quarter as well and across all regions. We're applying restructuring and reducing expenses across the board, but let me remind you that last year, we booked like EUR 175 million just in Iberia to implement a further reduction of expenses. Also in Brazil, where there is a significant reduction of the payroll, also in the U.S. as well, and we're reducing our internal expenses. Across all countries and line of business, there is a cut cost and reduction. It's not only this quarter. Obviously, the increase of earned premiums is helping to reduce the loss ratio. But the reduction in amounts in all countries and regions is remarkable for the 3 quarters here.

Felipe Navarro López de Chicheri
Head of Capital Markets & Investor Relations and Treasurer

It seems that there are no more questions. So just in case -- we have received some questions through the platform that we feel that have already been answered through the Q&A. If you need any further clarification, please do not hesitate to contact us later.

And before we go, we remind you that we are holding a virtual group meeting with analysts and investors on Wednesday, November 2, at 4:30 P.M. Central European Time. You should have already received the invitation. If you haven't signed up yet or didn't receive the details, please send an e-mail to the IR team, and we'll get the information to you. Please, don't hesitate.

And additionally, on November 7, we are holding a meeting in MAPFRE's offices in London with sell-side analysts. If you haven't confirmed your attendance yet, please do as soon as possible. And please remember that you can contact the Investor Relations team any time if you have any doubts about the results released today. So thank you very much for your attention.

Fernando Mata Verdejo
Group CFO & Director

Thank you very much for your presence and enjoy the weekend. Bye-bye.

Felipe Navarro López de Chicheri
Head of Capital Markets & Investor Relations and Treasurer
Thank you.