
IAG delivers sound results for FY17

Key financial indicators:

- Insurance profit \$1.3 billion (FY16: \$1.2 billion)
- Reported insurance margin 14.9% (FY16: 14.3%)
- Underlying insurance margin¹ 11.9% (FY16: 14.0%)
- GWP \$11.8 billion (FY16: \$11.4 billion)
- Net profit after tax \$929 million (FY16: \$625 million)
- Cash return on equity (ROE) 15.2% (FY16: 13.0%)
- Full year fully franked dividend 33 cents per share (cps)

IAG today announced an FY17 insurance profit of \$1.3 billion and a reported insurance margin of 14.9%, a 6.8% and 60 basis points (bps) respective increase on FY16.

This improvement was driven by higher than expected prior period reserve releases, partially offset by a natural peril claim cost increase which resulted in an allowance overrun of over \$140 million.

Gross written premium (GWP) grew by 3.9% to \$11.8 billion, with like-for-like growth in excess of 4%. This was driven mainly by higher rates on short tail motor in response to claims inflation as well as continued momentum in IAG's Australian commercial rates.

IAG's underlying insurance margin, its preferred business performance measure, fell 2.1 percentage points to 11.9%, which included the adverse impact of higher claim costs in its short tail motor businesses in Australia and New Zealand, and elevated large losses in its commercial classes. An additional factor was the increase in IAG's natural peril allowance in FY17, which accounted for a third of the underlying margin decrease.

Net profit after tax increased 48.6% to \$929 million and included a significantly higher contribution from investment income on shareholders' funds which reflects stronger equity markets.

IAG Managing Director and Chief Executive Officer Peter Harmer said the company was on track in its work to strengthen the overall performance of its businesses.

¹ IAG defines its underlying insurance margin as the reported insurance margin adjusted for:
– Net natural peril claim costs less related allowance for the period;
– Reserve releases in excess of 1% of NEP; and
– Credit spread movements.

“Today we delivered a sound result, bolstered by improved investment markets and higher than originally expected reserve releases from our long tail business.

“Overall GWP growth reflects positive momentum in our commercial business and rate responses to claims inflation, particularly in our short tail motor insurance businesses in Australia and New Zealand.”

Mr Harmer added that the company was well-advanced with its plans to address the rising cost of claims.

“We have a number of initiatives underway that look at how we can reduce the cost of managing claims in a way that creates affordable insurance options for customers both now and into the future. We expect these initiatives, which are being created in consultation with our customers, to be finalised in the first half of the 2018 financial year.”

IAG’s reported insurance margin of 14.9% included:

- Significantly higher than expected prior period reserve releases of \$457 million, equivalent to 5.4% of net earned premium (NEP)
- Net natural peril claim costs of \$822 million which exceeded allowance by over \$140 million and included three significant events: the Kaikoura earthquake in New Zealand, the Northern Sydney hailstorm and Tropical Cyclone Debbie
- A favourable credit spread impact of \$20 million, compared to an adverse effect of \$37 million in FY16.

IAG’s effective tax rate was 23.6% over the year, slightly higher than the previous year (22.3%). Both years included favourable tax effects on FY11-related earthquake reinsurance recoveries. The effective tax rate was 28.8% in 2H17 and is expected to remain at a similar level in future periods.

STRATEGY UPDATE

Mr Harmer said the company was focused on its three strategic priorities – customers, business simplification, and people and business agility – which are being brought to life through its leading and fuelling themes.

“Leading has our customers at the core and aims to make the experience they have with us world class, through technology, smart ideas and the way they interact with us.

“Over the year we’ve refined how we work with customers on product and experience design; empowered our frontline people to solve customer needs in real time; and provided excellent experiences around claims and repair. These have all contributed to a steady increase in our net promoter scores across our brands.

“We’ve developed a leading customer model to better understand our customers and their needs, hopes and life stages, so we can provide the products and services our customers want, when they want them and in the way they want them delivered.

“We recently opened our new Sydney-based innovation incubator, Firemark Labs, following the successful launch of our insurtech hub in the emerging global technology hotspot of Singapore.

“Both Labs are supported through our \$75 million new ventures fund, Firemark Ventures, and combined they create a powerful products and services innovation pipeline, and the opportunity to leverage the insights and experience of our external partners to design new customer experiences.

“Fuelling means making changes to the way we operate by simplifying our processes and systems and optimising our resources to be more efficient. The savings we achieve will enable investment in our leading themes, while contributing significantly to our operating cost reduction targets.

“We’re on track in partnering with global experts to simplify processes and reduce complexity, and advanced on our work to reduce our 32 policy and claim systems to two. We have started work on rationalising our product range from 1,500 to just over 400; and on 1 August 2017, following court approval, consolidated our Australian insurance licences from nine to two.

“We took a significant step in July to simplify our business when we created one Australian business, headed by Mark Milliner as CEO Australia. The Australia Division brings together the Consumer, Business, Satellite and Operations divisions with responsibility for customer, product, distribution and operations functions.

“All these actions are core to us achieving the commitment we made in December 2016 to reduce our gross operating costs by an annual run rate of at least 10%, or \$250 million pre-tax, by the end of FY19; and we are on track to achieve this,” Mr Harmer said.

DIVIDEND AND CAPITAL POSITION

The final fully franked dividend of 20 cps, to be paid in early October 2017, brings the full year dividend to 33 cps. This equates to a cash payout ratio of 79%, at the upper end of IAG’s policy to distribute 60-80% of cash earnings in any financial year.

IAG’s capital position as at 30 June 2017 was strong, with its Common Equity Tier 1 (CET1) ratio 1.09 against a target benchmark of 0.9-1.1. The Prescribed Capital Amount (PCA) multiple was 1.70, compared to a target range of 1.4-1.6.

After allowing for the final dividend, the adjusted CET1 ratio would be at the lower end of IAG’s benchmark range, while the PCA multiple would be slightly above the mid-point of the equivalent target range.

As part of its broader capital management program, IAG is exploring additional reinsurance quota share opportunities with its counterparties which have the potential to further strengthen IAG’s regulatory capital position.

DIVISIONAL RESULTS

Australia reported GWP growth of 3.4%, a lower underlying margin of 11.5% and an increased reported margin of 17.5%. Within this:

- Consumer produced a strong 13.9% underlying margin. GWP increased by 5.5% to \$6.1 billion (FY16: \$5.8 billion), with growth in both short tail home and motor lines, as well as long tail CTP. Consumer’s reported margin of 21.8% benefited from higher

than expected reserve releases from long tail classes. Long tail CTP profitability improved in 2H17, particularly in NSW, with lower claim frequency as a result of initial reform measures in late calendar 2016.

- Business reported relatively flat GWP of \$3.0 billion (FY16: \$3.0 billion). Factoring in the sale of the Swann Insurance car dealership business, like-for-like GWP was over 4% higher, reflecting positive momentum in commercial rates and maintained retention levels. A lower underlying margin of 6.9% (FY16: 9.7%) included an elevated large loss experience in property classes, particularly in 2H17. A slightly lower reported margin of 9.2% (FY16: 10.0%) included higher reserve releases.

New Zealand's underlying margin of 14.8% was slightly lower than FY16 (16.9%), with increased claim cost pressures notably in motor. GWP growth of 7.2% included a favourable foreign exchange effect. Local currency GWP growth of 4.3% included rate-driven increases and volume growth in personal lines and a recovery in commercial lines pricing in the second half. A lower reported margin of 7.6% reflected a sequence of significant natural peril events, including the Kaikoura earthquake in November 2016.

Asia consolidated GWP declined by 5.2% while its overall earnings fell to \$10 million (FY16: \$26 million), as Thailand and Malaysia incurred the effect of increased competition and, in Thailand, flood-related claim costs. The combined developing markets of India, Vietnam and Indonesia made a positive contribution, as India moved into profit on improved claim and expense outcomes, supplemented by higher investment income.

OUTLOOK

IAG expects to report an improved underlying operating performance in FY18. Low single digit GWP growth is anticipated in FY18 reflecting:

- Ongoing rate initiatives to help address short tail claim pressures, notably in motor
- Further positive rate momentum in commercial classes, both in Australia and New Zealand
- Modest underlying volume growth, close to system
- Lower NSW CTP pricing, in recognition of the greater certainty attached to claim outcomes as a result of scheme reform
- An up to \$60 million reduction in GWP with the exit of Swann Insurance from the motorcycle dealer channel and the residual effect of the divestment of the Swann Insurance car dealership business in early FY17.

IAG's reported margin guidance range for FY18 is 12.5-14.5% with the following underlying assumptions:

- Net losses from natural perils in line with a flat \$680 million allowance which factors in strong aggregate reinsurance protection for the six months to 31 December 2017, limiting a first event retention to \$20 million
- Prior period reserve releases of at least 2% of NEP (FY17: 5.4%), on the assumption that the current unusually benign inflationary environment continues
- No material movement in foreign exchange rates or investment markets
- A neutral impact from the optimisation program as benefits are matched by related costs.

While prior period reserve releases of at least 2% of NEP are expected in FY18, it remains IAG's belief that long term reserve releases of around 1% of NEP are a recurring feature of its reported operating results in benign inflationary periods.

IAG FY17 FINANCIAL PERFORMANCE

	1H16 A\$m	2H16 A\$m	1H17 A\$m	2H17 A\$m	FY16 A\$m	FY17 A\$m	FY17 vs FY16 Mvt
GROUP RESULTS							
Gross written premium	5,543	5,824	5,802	6,003	11,367	11,805	+3.9%
Gross earned premium	5,734	5,677	5,868	5,824	11,411	11,692	
Reinsurance expense	(1,632)	(1,551)	(1,624)	(1,603)	(3,183)	(3,227)	
Net earned premium	4,102	4,126	4,244	4,221	8,228	8,465	
Net claims expense	(2,589)	(2,808)	(2,625)	(2,638)	(5,397)	(5,263)	
Commission expense	(423)	(386)	(416)	(422)	(809)	(838)	
Underwriting expense	(654)	(653)	(669)	(678)	(1,307)	(1,347)	
Underwriting profit	436	279	534	483	715	1,017	
Investment income on technical reserves	174	289	37	204	463	241	
Insurance profit	610	568	571	687	1,178	1,258	+6.8%
Net corporate expense	(14)	(207)	(4)	(4)	(221)	(8)	
Interest	(51)	(48)	(51)	(42)	(99)	(93)	
Profit/(loss) from fee based business	10	(8)	(1)	(33)	2	(34)	
Share of profit from associates	8	12	9	12	20	21	
Investment income on shareholders' funds	38	59	105	144	97	249	
Profit before income tax and amortisation	601	376	629	764	977	1,393	+42.6%
Income tax expense	(67)	(151)	(109)	(220)	(218)	(329)	
Profit after income tax (before amortisation)	534	225	520	544	759	1,064	
Non-controlling interests	(40)	(37)	(45)	(31)	(77)	(76)	
Profit after income tax and non-controlling interests (before amortisation)	494	188	475	513	682	988	
Amortisation and impairment	(28)	(29)	(29)	(30)	(57)	(59)	
Profit attributable to IAG shareholders	466	159	446	483	625	929	+48.6%
INSURANCE MARGIN							
	FY16		FY17				
	A\$m	%	A\$m	%			
Management reported insurance margin	1,178	14.3	1,258	14.9			
Net natural peril claim costs less allowance	59	0.7	142	1.7			
Reserve releases in excess of 1% of NEP	(125)	(1.5)	(372)	(4.4)			
Credit spread movements	37	0.5	(20)	(0.3)			
Underlying insurance margin	1,149	14.0	1,008	11.9			

About IAG

IAG is the parent company of a general insurance group (the Group) with controlled operations in Australia, New Zealand, Thailand, Vietnam and Indonesia. The Group's businesses underwrite over \$11 billion of premium per annum, selling insurance under many leading brands, including: NRMA Insurance, CGU, SGIO, SGIC, Swann Insurance and WFI (Australia); NZI, State, AMI and Lumley Insurance (New Zealand); Safety and NZI (Thailand); AAA Assurance (Vietnam); and Asuransi Parolamas (Indonesia). IAG also has interests in general insurance joint ventures in Malaysia and India. For further information, please visit www.iag.com.au.

Media

Amanda Wallace
Telephone. +61 (0)2 9292 9441
Mobile. +61 (0)422 379 964
Email. amanda.wallace@iag.com.au

Investor Relations

Simon Phibbs
Telephone. +61 (0)2 9292 8796
Mobile. +61 (0)411 011 899
Email. simon.phibbs@iag.com.au

Insurance Australia Group Limited

ABN 60 090 739 923
388 George Street
Sydney NSW 2000 Australia
Telephone. +61 (0)2 9292 9222
www.iag.com.au