

2006 AGM Presentation

Michael Hawker

[\[Slide 1: Title slide\]](#)

- Good morning Ladies and Gentlemen, and a very warm welcome to you all, to the 7th Annual General Meeting of Insurance Australia Group.

[\[Slide 2: Year in review\]](#)

- 2006 has been an interesting year for the company, with many highlights and some challenges.

Good Progress on Strategy

- We have made good progress on our strategy to grow the company and to build the platform for a sustainable future. This was despite the fact that the domestic markets were significantly more competitive than the previous few years, with, in particular, the “soft cycle” in commercial insurance intensifying.

Smash Repair Dispute

- After an early, and very public dispute with the NSW Motor Traders Association, and the smash repair industry, which affected our NSW motor portfolio, we finished the year with renewed momentum in that business.
- We focussed on our customers, acknowledged our mistakes, changed our management, renewed our marketing, improved our customer service offerings, and our NSW motor insurance renewal rates have reached their highest level in this portfolio since listing the company.
- [\[Slide 3: Momentum in Personal Insurance\]](#). The graph of our NSW motor insurance renewal rates, illustrates this very well. Unfortunately this had a negative impact on our second half profitability, due to the lag effect of changing volumes on profitability, and this lag effect will take another nine months before it is behind us.

Natural Disasters

- [\[Slide 4: Cyclone Larry & NZ snow storm\]](#). As usual, during the year we dealt with a number of natural catastrophes, including Cyclone Larry in North Queensland, and major snowstorms in New Zealand. The losses we sustained from these two events pushed our losses above the average expected losses from our property insurance portfolios.
- Our people did an outstanding job in helping our customers rebuild their properties, with General Peter Cosgrove signalling out your company as among the best in responding to its customers. In fact he labelled us the “front-runner”.
- Our people take immense pride in being able to respond quickly, professionally and empathetically to our customers.

Asian Expansion

- [\[Slide 5: Established a presence in Asia\]](#) After over two years of research, identifying opportunities, and building relationships, we were able to make some investments in Asia. We believe these markets will provide significant and profitable growth opportunities for the company.
- These markets have high economic growth rates, are being opened to foreign investment, and are under-developed in terms of general insurance. Many local general insurance companies are looking for skilled foreign partners, suiting our desire to enter these markets. The domestic insurers provide quality personnel, good distribution, market knowledge, and customer data. We provide high quality underwriting skills, good risk management and governance capabilities, technology, and data management skills – particularly in motor car insurance.
- Since last speaking to you we have acquired interests in Thailand, Malaysia, and Alba, the first Lloyd's of London multi-line syndicate based in Asia, which is located in Singapore. We have also secured an agreement to purchase 24.9% of China's second largest general insurer, CPIC. We are still waiting for final approvals, although progress has been slower than anticipated.

Awards

- [\[Slide 6: Award winning performance\]](#) We were awarded a number of accolades this year including:

General Insurance Company of the Year

Australia and New Zealand Insurance Industry Awards

Triple Bottom Line Award

World Environment Day Awards, United Nations (Australia)

Underwriter of the Year – NZI

Insurance Brokers' Association of New Zealand Awards (New Zealand)

Large Business of the Year

National Sustainable Business Awards (New Zealand)

Inclusion in the FTSE4Good index and the Dow Jones Sustainability Index

Results

- [\[Slide 7: 2006 Results\]](#) As reported at our end of year results announcement we delivered a net profit after tax of \$759 million, with our second highest ROE and insurance margin since listing.

Double Digit Dividend Growth

- This enabled us to pay a dividend of 29.5 cents a share fully franked, an increase from last year of 11.3%. Due to our strong capital position and the buoyant equity markets inflating our expected annual return, we were also able to pay a special dividend of 12.5 cents a share fully franked.

Review of the Past Five Years

- This year is my fifth with Insurance Australia Group, so I thought it might be timely to review our progress against the five year strategy we set from the financial year ending 30 June 2002.

Five year growth rates on track

- [Slide 8: GWP: Four year growth 15.5% p.a.] Our growth rate in Gross Written premiums for the first 4 years has been 15.5%. This growth rate is on track to meet our stretch goal of doubling our Gross Written Premium over five years. Also our business is far more diversified than it was before.
- [Slide 9: Profit: four year normalised growth 15.3% p.a.] For the same period our actual profit growth has grown at an annual compound growth rate of 39.6%. (This percentage growth rate was calculated over the past five years – not the last four, as the company had a loss in 2002, which would have made this percentage growth rate in profit unrealistically high.)
- However, this has been boosted by very buoyant equity markets, and the more realistic way to look at the profit growth is on a normalised basis (ie use the long term expected return on our investment portfolios). On this basis our profit growth has been almost identical to the top line growth rate at 15.3%.
- [Slide 10: ROE four year average 15.7%] Our returns on equity have been improving and have averaged 15.7% over the past four years, which is above our target of 1.5 times our weighted average cost of capital (WACC).
- We have maintained our capital strength with a Standard & Poor's financial strength rating of AA (for our key wholly owned insurance operating entities).
- [Slide 11: Dividends four year growth 29.5% p.a.] Due to the financial performance and the capital strength of our company we have been able to increase the dividends of the company by an annual compound growth rate of 29.5% over the past four years.
- This year we were also able to return \$200 million of excess capital to shareholders with a special dividend of 12.5 cents per share. All these dividends have been fully franked.

Economics of General Insurance

- These financial outcomes have been achieved by remaining extremely focussed on what drives the economics of our business – the general insurance business.

- In the general insurance business, to remain profitable and successful over a long period of time, you must have: a consistently competitive customer proposition; outstanding personnel; a high performance and community-aware company culture; market leading risk management and pricing skills; and be generating annually compounding double digit growth rates in both Premium Income and Profit.

Insurance Cycles

- Annualised double digit GWP growth rates require growth coming from both organic means and through acquisition. Up until this year our growth rate has been generated by an approximate 5.5% organic growth rate and an approximate 17.5 % acquisitive growth rate. This year, due to the combination of the smash repairer dispute, falling premiums in the liability classes due to reducing claims costs following Tort Law reform, premiums falling in many commercial classes due to competitive pressures, and premiums falling in some classes to unprofitable levels, our organic growth rate actually reduced.
- [\[Slide 12: Australian general insurance cycles\]](#) You can see from the slide shown that the Australian general insurance market is in a period of declining profitability.

Acquisitions

- As general insurance markets tend to have cyclical profit patterns, having the ability to acquire businesses in markets that are improving in profitability and also provide diversification, both in terms of earnings and capital, is critical to our company's success.
- Over the past four years the company has successfully acquired 10 businesses, disposed of two, and been under-bidders on many more. These acquisitions have all been earnings accretive within 18 months, and have substantially broadened the capacity and expertise of the company.
- [\[Slide 13: Our operations today\]](#). The offshore acquisitions have also provided the company with many more profitable growth options, as can be seen from the slide. Our five year strategy objective of building an Asian foothold has been achieved.
- More recently we have also had the opportunity to build a foothold in the UK market, with the purchase in September of the Hastings and Advantage insurance companies. In addition to the business fundamentals being attractive, the economics of this transaction are enhanced by the diversification of capital between the motor liability markets in the UK and Australia.
- We have built a very capable acquisition team, which has executed the last four acquisitions, using largely internal resources.

Improving Company Competitive Capabilities

- Of course building sustainable companies requires building strong internal capabilities. Put simply, this requires having well trained people who are

strongly committed to the company, driving systematic improvements in your customer proposition, managing resources efficiently, maintaining strong risk management and governance standards, and having an understanding of your impact on the community.

Customer Measures Strong and Improving

- [\[Slide 14: Customer measures strong\]](#). As you can see from the slide, the brand health of our retail brands is improving, with NRMA still the premier insurance brand in Australia.
- Our customer retention and renewal rates are high and improving, we have improving claims satisfaction in Australia, improving customer satisfaction in New Zealand, and our complaints continue to fall.

Employee Engagement is Improving

- [\[Slide15: Employee engagement\]](#). To measure the level to which our people are committed to our company, we use an internationally recognised measure developed by Hewitts. Using this measure over the past four years we have systematically improved the “engagement” of our people.
- We are an accredited training organisation, and this year we have developed, and launched an Insurance Academy for our commercial classes of business, both in New Zealand and Australia.

Managing Resources Efficiently

- [\[Slide16: IT costs down, effectiveness up\]](#). Over the past four years we have implemented a number of efficiency initiatives. These have enabled the company to keep its operational costs flat within existing businesses over the past three years.
- One area in which we have had considerable success is with our information and technology. We have reduced IT costs for the company by 3.9% p.a. over the past four years, when at the same time improved the reliability by over 40% p.a., and increased dramatically the functionality.
- With respect to costs, it should also be noted that we are carrying the cost of our Asian Regional Management infrastructure, which we introduced to effectively manage the growth of our Asian businesses. This regional structure can be significantly leveraged, as our growth aspirations within Asia can be locally managed, without adding further regional management infrastructure.

Our Impact on the Community

- [\[Slide 17: Our Sustainability Report\]](#). For the past three years we have published our Sustainability Report. Today I am releasing our third Sustainability report which is titled “A single person can make a world of difference”.
- This report illustrates that we have made substantial progress on a broad set of community measures. It can be found on our website www.iag.com.au.

Carbon Neutrality by 2012

- As an insurance company we have been very concerned about the risks and impact of climate change on our community for a number of years.
- We have been working, on ways to reduce our own CO₂ emission footprint, alerting the community about the risks of climate change, and researching opportunities for our customers to benefit from CO₂ reducing activities.
- These activities have been beneficial to our business, through reducing cost, attracting employees, and enhancing our customer proposition.
- Today I would like to further our efforts, by announcing our intention to be carbon neutral within the next five years.

Outlook

- [\[Slide 18: Outlook slide\]](#) I mentioned earlier that we have renewed momentum in our NSW personal lines business. I indicated the improvement in our renewal rates, but we have also had improvements in our sales conversion levels. [\[Slide 19: Sale conversions trending up\]](#).
- This has been driven by a combination of three factors: - Implementation of our new technology giving us a single customer profile, competitive pricing and a revitalised marketing campaign.
- [\[Slide 20: First three months of this financial year\]](#). In the commercial lines of our business the “soft cycle” continues. Despite this, we have performed in line with the same period last year both in terms of Gross Written Premium, and Insurance Margin. We will continue our disciplined underwriting approach that is focussed on maintaining insurance margins and strong customer relationships, rather than chasing unprofitable business.
- Our New Zealand business continues to perform solidly, however the AUD:NZD exchange rate has been unfavourable over the past few months.

Full Year Guidance

- [\[Slide 21: Outlook: year ending 30 June 2007\]](#). Having purchased the businesses in the UK recently, we have firmed our full year guidance.
- At the time of our results we expected our GWP to grow by 5-10%. With this UK purchase we expect the GWP growth rate to be at the higher end of the range, between 8-10%.
- There is also some possibility that it could go above the range as we have more potential acquisitions in the pipeline.
- We also still expect the normalised ROE to be in excess of 15% for the year.

- For the first six months we expect GWP to grow by 3-5% over the same corresponding period last year.

Summary

- [\[Slide 22: Strategy remains on track\]](#). In summary our strategy remains solidly on track. We are building platforms for long-term growth and profitability, both organically and through acquisition.
- The businesses have momentum, in a highly competitive market environment.
- We are improving the inherent capability of our business, and we are strongly capitalised.
- [\[Slide 23: IAG share performance\]](#). We remain focussed and committed to our strategy that has delivered solid returns for our shareholders over the past four years, and I am confident that it will deliver ongoing value in the coming years.

Thank you for your support.

[\[Slide 24: AGM Slide\]](#)