

SPEAKING NOTES FOR SAM MOSTYN

‘Futurism and Business’ – A leadership perspective

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Introduction

- Along with many other Australian public companies, IAG has recently published its 2003 Annual Report. In the lead-up up to producing these reports there is always a great deal of discussion around choosing an appropriate theme. This year we decided to tackle the seemingly simple question, ‘What does IAG stand for?’
- At one level, IAG stands for Insurance Australia Group. We’re Australasia’s leading general insurance group and we trade under a range of well-respected brand names, some of which you’ll recognise – NRMA Insurance, SGIO, SGIC, CGU, Swann Insurance and ClearView in Australia and State and NZI in New Zealand.
- But I say it’s a “**seemly** simple question” for good reason. Answering that question, ‘What does IAG stand for?’ has been a preoccupation of ours for sometime now. So it was particularly fitting that it should be the theme of our 2003 Annual Report.
- Today, I want to talk to you about Insurance Australia Group’s purpose, about how it informs the sort of company we are: what do, how we engage our stakeholders and, most importantly, how it provides the foundation for building a business that is sustainable in the long-term. A business that is primed to meet the challenges of the 21st century.
- We believe that building a successful and **sustainable** business depends on us conducting our business in a way that creates value for society on numerous fronts, across social, environmental and economic dimensions. Our purpose brings together both social and financial goals which, I believe, holds the key to our future prosperity.
- In our experience, this purpose-driven approach to building a sustainable business has many benefits. We earn a mandate to operate from our stakeholders who see us taking our responsibility as Australia’s largest general insurer seriously. We engage our staff around a purpose that is bigger and more meaningful to them than making another dollar for the shareholders. Our company is more attractive to investors who are increasingly focused on corporate social responsibility and corporate governance, rather than just the bottom line. And, finally, we guarantee the long-term sustainability and profitability of our business by positively influencing our competitive environment.

Defining our purpose

- The more I’ve come to understand how insurance works, the more I realise how strong a fit sustainability is for our business – intellectually, conceptually, AND it makes perfect business sense – for our shareholders, customers, our people and the community.

- To appreciate why, it's important to think about what insurance is and what that means for our purpose as an insurance company.
- At the core, insurance is a very simple thing – the community pools money so that, if an individual in the community suffers a hardship, he or she is protected. People hope they won't have to make a claim, but they can live their lives knowing their home, car or business is protected in case they do. Our job, as an insurer, is to pay that money when it's needed. So one way to look at our purpose is to say we pay claims.
- To pay claims, we need to be able to do two things well. First, we need to price risk fairly and appropriately. If we under-price risk, the available funds won't match claims and we go out of business (which isn't good for anyone as the HIH experience brought home). If we over-price risk, people will take their business elsewhere – or they'll choose not to insure at all, which puts them at risk.
- The other thing we need to do well is keep our operating costs down. The price of premiums includes not only the measure of risk, but also the costs that go into providing the policy in the first place. Keeping our overhead and infrastructure costs down ensures we can offer affordable insurance.
- Pricing risk fairly and controlling costs means we can deliver on our purpose of paying claims and providing affordable insurance.
- I think that makes insurance the ultimate community product. Paying claims is not only a business imperative, it's also our social responsibility.
- Now, we could simply operate our business on the basis that all we do is appropriately assess the risk and price the premiums accordingly, and keep our own costs low.
- We have almost 100 years of data about what's been happening in our community, and we can use that information and expertise to help predict what's going to happen in the future. We could operate our business on that basis, as insurance companies have always done, and use this information to simply assess risk and price premiums accordingly.
- However, it's in our business interest to go beyond that simple equation and use this information to *reduce* the risk of an event occurring in the first place. Reducing the risk reduces the cost of claims – which we'd like to think can, over time, be handed back to the community through lower premiums. And satisfied customers (through reduced risk, more affordable premiums) give us the license to grow our business further.
- So our purpose as an insurance company is both about paying claims and using our understanding of risk and claims to advise the community on how to minimise risk. And it's far more important for us to understand the role we play in helping to minimise risk and how that supports our key business of paying claims.

Testing our thinking

- To ensure we weren't kidding ourselves about this purpose, we conducted some research on the community's expectation of our company, and of the insurance and financial services sector more broadly.
- The most interesting finding was the relative weighting people gave to what they believed is our prime responsibility. Not surprisingly almost 90% of people polled told us that we

are totally responsible for ensuring that our people act ethically and honestly in selling insurance.

- About 60% believe we are totally responsible for managing our business well to help build a secure economy - and by implication, remain profitable so that we can always pay claims.
- Lower, but still significant numbers of people expect us to undertake activities more closely associated with sustainability and corporate social responsibility.
- The point is simple, but critical: consumers don't want environmental and social attributes in lieu of quality, price and excellent service – they want them as well.

Areas of focus

- When we considered our commitment to helping reduce risk, we realised there were two main areas where we should concentrate – two areas that aligned shareholder and societal value: the environment and safety.
- 'Why environment?'
- As I mentioned earlier, IAG has a wonderful resource of historical data – including information about the frequency and severity of weather-related events across Australia and New Zealand.
- 19 out of the 20 major insurance catastrophes in Australia have been weather-related. And global warming only increases the risk of weather-related catastrophes.
- As global water temperatures rise, it has a dramatic effect on climatic events such as wind, drought, cyclones, hail. And it doesn't take much of a change in these weather events for them to have a significant impact on the community. For instance, doubling wind speed creates a four-fold increase in damages. The reason is that most of the Building Code is set to historical wind speeds. When you go above that historical average, the damage is exponential because buildings just aren't made to withstand it.
- Similarly with bushfires. A 1% increase in average summer temperature leads to a 17-28% increase in wildfires.
- Or an increase in rainfall of 25% in a 30-minute period means that a one in a hundred year flood can become a one in 17 year flood.
- As the frequency and ferocity of weather events increases, so will the damages bill and cost of insurance claims.
- So weather and the environment is a pretty big issue for us.
- The other area of focus I mentioned is safety.
- We are Australia's leading provider of workers' compensation insurance and a leading adviser on occupational health and safety issues. So we care about safety in the workplace.
- We also provide a lot of CTP (compulsory third party) car insurance – so we care about safety on the road.

- And we provide home building and contents insurance – so we care about safety in the home.
- By using our information and expertise about risk and investing in initiatives to improve safety and reduce injuries, we can help the community avoid the cost of injuries – the emotional and social costs, as well as the financial ones. We also contribute to a reduction in the frequency and cost of insurance claims – a benefit to our company.
- One initiative we've recently undertaken on the safety front is a partnership with St John Ambulance. St John is Australia's leading provider of first aid training and services, and shares our commitment to safety. We'll be working with St John to help our people and the community improve their safety and reduce injuries.
- So you can see that our approach to risk reduction, particularly in the areas of the environment, global warming and safety, as I've just outlined contributes to the long-term sustainability of our business. It's not just about direct positive impacts on the bottom line. We also ensure the future of our business by engaging our staff around a purpose that is meaningful, by earning a mandate to operate from the broader community who see us behaving responsibly, and we attract increasing selective investors.

Cleaning house

- It's well and good for us to say that we know lots about the environment and safety – but to have a real impact on these areas we really had to start at home. So our first step has been to get our own house in order and start to walk the talk.
- It's an issue of integrity as well as cost benefits.
- On the environmental front, we have set policies around reducing our environmental footprint. Our biggest environmental impact is our greenhouse emissions generated through our high level of paper usage, travel and energy consumption. These greenhouse gases are a driver of global warming, so we are working to reduce our emissions and recently signed the UN Environment Program Financial Initiative.
- Other short-term environmental targets include:
 - reducing our paper consumption by 15%
 - reducing energy consumption by 15%
 - reducing air travel and fuel usage by 5%
- In addition to the environmental benefits, reductions in these areas will also have an immediate impact on IAG's direct operating costs.
- On the safety front our own record was far from good. We found we were actually hurting our people at a rate five times higher than the average for our industry. Our target for this financial year is to reduce that amount by 25%.
- The benefits for IAG and our people are obvious – reduced sick leave, better morale and productivity and reduced workers' compensation claims.
- While it's helpful to have these short term goals, we are clear that there are no "quick fixes" and the work required, both internally and externally, will be over the long term.
- Our aim has been to improve our internal performance and move towards our products and services to integrate socially responsible thinking into all parts of our business.

Engaging with stakeholders

- Our actions around risk reduction in the areas of environment and safety, both internally and externally with the community are about creating a long-term, sustainable and profitable future for our business.
- Earning the mandate to stay in business, grow our business, and improve our profitability is critical. By defining a purpose that brings our economic and social goal into alignment I believe we bring about better outcomes for our company and the community. We're very focused on 'win-win' initiatives – such as recycling plastic bumper bars which reduces landfill and reduces claims costs.
- Our investment in socially responsible activities is not at the expense of our economic responsibility. We seek to actively engage with our stakeholders to raise awareness about our purpose and the rationale behind it. We want to establish on-going dialogue with our stakeholders and the community on the issues that are at the heart of how we at IAG want to run our insurance business.
- I'll now talk about how our purpose-driven approach to sustainability impacts on some of our major stakeholders groups.

Customers

- In line with our purpose of paying claims and advising the community on how to minimise risk, we strive to be aggressively pro-active in making sure customers know exactly what the risks are in their areas, and whether or not they are covered.
- This begins with our products and our business processes, is supported with research and further business and product innovation, and extends to our public advocacy and education programs.
- For example, when seasonal risks like winter fires in the home or storms threaten, we can do a lot to help people be prepared through widespread media awareness raising campaigns. In early winter this year IAG worked with the NSW Fire Brigade to alert the community to the risks of fires in homes by revealing the Top 10 causes of fires during winter such as candles and incense, overloading powerpoints and kitchen fires.
- This campaign was based on figures from our claims analysis and assessors' work on the ground with customers directly affected by winter fires.
- We also work with our customers and the broader community so that we learn from disasters and are better prepared for the future. Following the havoc wrought by the Canberra "fire storms" we not only helped our customers get their lives back to normal as soon as possible by paying claims and providing alternative accommodation, we've also focused on helping with the rebuilding task. IAG organised a Help Expo, a weekend long event where people could get access to expert advice and support on the rebuilding in a safe and environmentally sustainable way.
- Another example of using our claims experience and risk expertise to help customers and the community better manage their risk is an on-line tool we've recently launched which brings together the considerable amount of environmental and safety information held by the NRMA Insurance's Technical Research Centre. People can use the tool to compare up to 200 new cars on criteria like greenhouse gas emissions, crash safety, rear visibility, and repair costs. The tool is available via the NRMA Insurance website.

- Our approach to corporate philanthropy also reflects our purpose and is driven by both social and economic goals. Specific programs include St John Ambulance, KidSafe, State Emergency Services, and a Community Help program to encourage volunteer work among our employees – all aimed at actively reducing risk in the community.

Investment community

- As we know, social and environmental performance is also becoming increasingly important to investors, particularly superannuation funds. The Commonwealth Public Service Superannuation Fund and WorkCover SA are two funds that are asking companies to demonstrate their social and environmental performance. Major investors can't be kept at bay with glib and glossy spin.
- We are seeking to take a leadership role in this area by demonstrating to investors that we are managing environmental and social risk and responding to their requirements. We are also seeking to drive what analysts expect from companies in their reporting by encouraging new ratings to measure companies on environmental and social sustainability issues.
- For example, when IAG held its annual market update briefing earlier this year, to update analysts and investors on how we were performing against our strategy, we briefed the audience on climate change, the potential impacts for our business, and what we were doing to manage that risk.
- We need to move away from relying on the simple tool of short-term focused reputation indexes as a means of measuring corporate social responsibility. Reputation indexes fail to capture cultural change, which is only evident externally in the long-term.
- As a public company in the insurance sector, it's fair to say we're heavily regulated. But to communicate our purpose to the market, we don't just comply with these regulations, we set our own benchmarks.
- So when we develop our Annual Report, we are thinking about how we can articulate the role of insurance and how to reduce risk in the community AS WELL AS how the business is performing financially.
- We are looking at developing an investment strategy that will include socially responsible investment criteria in our stock selection processes, and we will use our voting power and engagement of companies we invest in to promote positive social and environmental outcomes.
- In late 2004 we are looking to publish a social accountability report. By going above and beyond standard regulatory reporting requirements to update the market on our environmental, safety and economic performance, we want to demonstrate our commitment to transparency and disclosure.

Suppliers

- We're also seeking to use our leverage with suppliers to achieve social, environmental and economically beneficial outcomes.
- As Australasia's largest general insurance group, millions of people in Australia and New Zealand buy our insurance products. We have important supply chain relationships – in

areas like motor vehicle repairs and the building industry – and we're one of Australia's biggest buyers of household white goods and brown goods (eg. TVs, videos, etc)

- We can influence the whole market by expecting standards of our suppliers that are in-line with our own social and environmental standards.
- So for example, we can ask our NRMA Insurance preferred smash repairers to use recycled parts when they are suitable. And we can encourage the transferring of knowledge between repairers, so the use of better and more efficient repair practices becomes more widespread.
- We can also influence our customers to make choices that are better – socially and environmentally. When our customers make a claim for household items such as fridges, washing machines and entertainment systems, we might be able to offer them replacement products that are more energy efficient or 'green'.

The role of employees

- IAG employs some 11,000 people who can each impact on the knowledge and actions of hundreds of stakeholders every day.
- We believe that the engagement of our people is a critical to reaching our goal of becoming a high performing culture, which is critical to the long-term sustainability and profitability of our business. And we believe that a clear and socially responsible purpose is at the centre of fostering that engagement.
- We are working to engage our people around our purpose, in the same way we engage our other stakeholders. We are working on establishing trust and recruiting them as advocates for the business. And it's hard work!
- Doing this well means our employees can answer questions about insurance and the way we do business at IAG, whether the question comes from a customer during a normal workday, or from friends at a backyard BBQ on the weekend.
- It also means our employees understand our business and can feel a sense of ownership of the business, particularly with customers.
- For example, our people's understanding of IAG's help philosophy means that when catastrophes occur they are willing to go above and beyond the call of duty. Take our experience during the Canberra Bushfires. In addition to our catastrophe operational support team reporting to work, we had countless assessors and teleclaims operators voluntarily visiting Canberra to help process claims and get our customers' lives back to normal as soon as possible. In fact, the idea of our Help Expo that I mentioned earlier, came from one of our people on the ground in Canberra who saw an opportunity to go above and beyond in helping the community rebuild. It's astounding to see this is action.
- We measure engagement within IAG on an ongoing basis. And at the moment we have a lot we can improve on. Our initial interrogation of the company revealed engagement around 50%. Within two years we'd like to move that to 65% engagement, in line with other benchmarked high performance organisations. One of the ways we're doing that is through forming a clear vision that aligns the economic and social purpose of our business.
- We expect our investments in employee engagement to have measurable impacts in a number of areas. We expect to see improvements in customer satisfaction and retention,

and employee productivity and retention. By reducing turnover and absenteeism and improving workplace health and safety, we will see reductions in operating costs through lower workers' compensation claims and savings on recruitment costs.

Lessons learnt

- I mentioned earlier in my presentation that IAG's purpose as an insurance company is to pay claims and use our understanding of risk and claims to advise the community on how to minimise risk.
- I believe that in aligning our financial and social goals in this way we build a foundation for our future prosperity.
- This purpose also provides the platform for our engagement with our various stakeholders. It defines how we run our business and how we consider the issue of creating value.
- But before I close on a note of buoyant optimism and high-minded principles, let me share with you some of the lessons we've learnt on our journey so far.
- It takes lots of hard work to embed sustainability through an organisation. You need to have a commitment to the long-term. CEOs only stay for an average of 5 years so it can't be linked to particular people.
- That said, it takes strong leadership to move a company in this direction and bring business and social goals into alignment. Our CEO is also our chief safety officer.
- One area I've found particularly challenging is gaining the support and understanding of some of our management. Not because they don't see the vision, but because we haven't answered their questions about how that vision translates into action. It's a good reminder of how important it is to be clear about what our purpose means for every area of our business. And how it translates into our expectations of managers' obligations.
- Social investment has to be measured against financial, people and stakeholders criteria. Must be linked back to the business to make sense and be sustainable in the long-term. We're working hard on this, but there is still a lot to do around educating the investment community of the importance of these issues.
- Reports on sustainability and social responsibility are good, but the cynicism of the community about the ethics of corporations needs to be addressed through more than this. Real action, real impacts on the community. Not just talk. Provide evidence of transparency.
- By sharing IAG's experience with you today, I hope to prompt some thought and discussion around the power of a purpose that brings together both the economic and social goals of a company and how that purpose can form a platform for a sustainable future. As I've outlined, the benefits of this approach, in our experience, have been many. They include earning a mandate to operate from our external stakeholders, engaging our people, making our business more attractive to investors – all of which contribute to the long-term sustainability and profitability of our business by positively influencing our competitive environment.