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## IAG FORMS STRATEGIC RELATIONSHIP WITH BERKSHIRE HATHAWAY

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- Strategic partnership<sup>1</sup> strengthens existing relationship and harnesses complementary capabilities of both companies
- An initial 10-year 20% quota share agreement across IAG's consolidated insurance business; reduces IAG's earnings volatility and capital requirements
- Berkshire Hathaway takes approximately 3.7% stake in IAG via \$500 million placement
- Enhanced strategic and financial flexibility provides IAG with scope to pursue growth opportunities and consider capital management

Insurance Australia Group Limited (IAG) has entered a strategic relationship agreement to establish a long-term partnership with Berkshire Hathaway Inc, one of the world's largest and most successful companies. The agreement enables both parties to draw on each other's strengths to better meet customer needs and deliver superior business outcomes.

The strategic partnership is underpinned by a 10-year 20% quota share arrangement across IAG's consolidated insurance business and an approximately 3.7% investment in IAG by Berkshire Hathaway via a share placement.

IAG Chairman Mr Brian Schwartz said: "The Board is delighted to welcome Berkshire Hathaway as a strategic partner and shareholder. We believe the partnership is an endorsement of our strategy, the strong franchises we have created in the Asia Pacific region, and an acknowledgement of the complementary capabilities we can bring for our customers. We look forward to a long and mutually beneficial relationship."

IAG Managing Director and CEO Mr Mike Wilkins said IAG and its shareholders would see long-term value from the partnership which is expected to deliver significant benefits to both companies.

"Our relationship with Berkshire Hathaway will provide IAG with significant capital flexibility while enhancing our ability to deliver improved consistency of earnings. It also further enhances IAG's personal and SME insurance proposition and, importantly, it provides a springboard for future business innovation and development for both companies.

"We look forward to the benefits that will flow from the combination of IAG's underwriting skills, supply chain management expertise and deep customer knowledge, coupled with Berkshire Hathaway's specialty insurance expertise," Mr Wilkins said.

IAG and Berkshire Hathaway have had a successful reinsurance relationship since 2000. Under the expanded relationship, the two companies will work together exclusively to enhance their customer offerings.

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<sup>1</sup> The partnership is in the nature of a long-term strategic relationship - comprised of the agreements referred to in this media release. It is not a legal-form partnership under the Partnership Act or equivalent laws.

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Under the terms of the partnership, IAG will acquire Berkshire Hathaway's local personal and SME business lines. In return, Berkshire Hathaway will acquire the renewal rights to IAG's large-corporate property and liability insurance business in Australia. The rights to be transferred by IAG represent less than 1% of its annual Gross Written Premium (GWP).

In relation to the strategic partnership's impact on IAG's return profile, it is expected to enhance the Group's ability to deliver a through-the-cycle 15% return on equity.

Warren E Buffett, Chairman and CEO of Berkshire Hathaway, said the quality and strength of the IAG business were pivotal to his company's decision to enter the relationship.

"We have worked with IAG for more than 15 years and over that time we've developed a good understanding and respect for their people, what they offer and the way they do business. For us, they are a natural partner with a strong management team and brand presence.

"Our strategic partnership with IAG will help fast-track our entry into this region, and provides us with opportunities to leverage IAG's extensive capabilities while also making our expertise available to IAG," Mr Buffett said.

Berkshire Hathaway has investments across a wide range of industries including general insurance and reinsurance. It is one of the top 10 publicly-listed companies globally, with a market capitalisation of around US\$350 billion. It launched its specialty insurance business in Australia earlier this year.

#### **QUOTA SHARE ARRANGEMENT**

IAG and Berkshire Hathaway have entered into a 10-year whole of account quota share arrangement effective 1 July 2015. Berkshire Hathaway will receive 20% of IAG's consolidated GWP and pay 20% of claims.

Berkshire Hathaway will also reimburse IAG for its share of operating costs and pay a percentage-based fee which recognises the value of accessing IAG's strong core franchise.

The arrangement will enable IAG to further diversify its capital funding mix while also delivering a more stable income stream.

IAG is one of the world's largest purchasers of catastrophe reinsurance cover. The quota share arrangement will reduce IAG's exposure to the geographic concentration of insurance risk in Australia and New Zealand, lowering IAG's future catastrophe reinsurance needs and its exposure to potential volatility in reinsurance rates.

IAG expects the quota share arrangement will result in a reduced capital requirement of approximately \$700 million over the next five years, with around \$400 million of that benefit expected to be realised in FY16.

#### **BERKSHIRE HATHAWAY TAKES SHAREHOLDING IN IAG**

In recognition of the strength and depth of the relationship, Berkshire Hathaway will acquire 89,766,607 new fully paid IAG ordinary shares at \$5.57 per share, for a total consideration of \$500 million. The price was set at the IAG closing share price on Monday 15 June 2015.

As part of the strategic agreement, Berkshire Hathaway will at least maintain its initial shareholding for the term of the quota share arrangement.

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IAG has an option to place up to a further 5% of IAG's expanded issued capital to Berkshire Hathaway within 24 months. Under a standstill agreement, Berkshire Hathaway will not increase its shareholding in IAG above 14.9% for the period of the partnership agreement.

## **CAPITAL**

IAG's capital position is significantly strengthened through the \$500 million share placement and the estimated reduction in capital requirement of \$700 million over time from the quota share arrangement.

This enables IAG to continue to pursue growth opportunities, including those in Asia, as well as consider appropriate capital management options.

## **STRATEGY**

IAG's strategic priorities remain unchanged with its strong businesses in Australia and New Zealand, which represent the majority of the Group, continuing to offer growth opportunities.

The company will also continue to pursue appropriate Asian growth opportunities in its six target markets of India, Thailand, Malaysia, China, Vietnam and Indonesia.

In India, IAG is looking to expand its presence by increasing its stake in SBI General, the general insurance joint venture with State Bank of India, from 24% to 49% following recent legislative changes on foreign ownership. The company expects this to be completed before the end of the 2015 calendar year.

IAG also recently acquired an insurance licence in Indonesia, its sixth target market, via the acquisition of PT Asuransi Parolamas, a small general insurance company. IAG is now focused on securing a distribution agreement with a recognised local partner to capitalise on opportunities presented in a market with low insurance penetration and a growing middle-class.

The company will also consider participating in any potential industry consolidation in Thailand, and further opportunities to expand its presence in Malaysia via the highly successful joint venture, AmGeneral Holdings Berhad.

In China, Mr Wilkins said IAG is investigating further opportunities to participate in that insurance market on a national scale.

"China is a source of enormous potential growth for IAG and we are actively working on opportunities to increase our presence in that market.

"Asia continues to represent an important plank of IAG's strategy given the relatively low penetration of insurance in our target markets. This, along with the rising affluence and consumption of the emerging middle-classes, presents an opportunity which we believe all forward-thinking Australian companies should pursue," Mr Wilkins said.

## **FY15 / FY16 GUIDANCE**

IAG's FY15 reported insurance margin guidance range remains unchanged from the 10.5-12.5% position stated on 29 April this year. While subject to the finalisation of year end processes and valuations, the assumptions underlying the reported insurance margin guidance remain:

- Net losses from natural perils of \$1 billion (updated in April);

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- Prior period reserve releases equivalent to around 2% of net earned premium (NEP); and
  - No material movement in foreign exchange rates or investment markets in 2H15.

FY15 GWP growth expectations are also unchanged from the view presented in February with IAG anticipating an outcome at the lower end of the 17-20% guidance range provided at the outset of the financial year.

IAG expects its FY16 reported insurance margin to be in the range of 14-16%. This includes further realisation of benefits from the Wesfarmers integration and the new Australian operating model, as well as the effect of the Berkshire Hathaway quota share arrangement announced today. The latter is expected to enhance the reported insurance margin by approximately 200 basis points. IAG's expectations for FY16 GWP growth are in the range of 0-3%.

Underlying assumptions incorporated in the FY16 reported insurance margin guidance are:

- Net losses from natural perils in line with allowance of \$600 million (after allowance for the quota share effect);
- Prior period reserve releases equivalent to at least 1% of NEP; and
- No material movement in foreign exchange rates or investment markets.

#### **About Insurance Australia Group**

Insurance Australia Group Limited (IAG) is the parent company of a general insurance group with controlled operations in Australia, New Zealand, Thailand and Vietnam, employing more than 15,000 people. Its businesses underwrite over \$11 billion of premium per annum, selling insurance under many leading brands, including: NRMA Insurance, CGU, SGIO, SGIC, Swann, WFI and Lumley Insurance (Australia); NZI, State, AMI and Lumley Insurance (New Zealand); Safety and NZI (Thailand); and AAA Assurance (Vietnam). IAG also has interests in general insurance joint ventures in Malaysia, India and China. For further information please visit [www.iag.com.au](http://www.iag.com.au).

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