INSURANCE AUSTRALIA GROUP LIMITED
HALF YEAR REPORT FOR THE PERIOD ENDED 31 DECEMBER 2019

APPENDIX 4D (ASX Listing Rule 4.2A)

RESULTS FOR ANNOUNCEMENT TO THE MARKET

	UP / DOWN	% CHANGE	31 December 2019 $m	31 December 2018 $m
Revenue from ordinary activities	Up	5.0 %	**9,012**	8,581
Net profit after tax from ordinary activities attributable to shareholders of the Parent from continuing operations	Down	2.0 %	**287**	293
Net (loss)/profit after tax from ordinary activities attributable to shareholders of the Parent from discontinued operations	Down	101.9 %	**(4)**	207
Net profit attributable to shareholders of the Parent	Down	43.4 %	**283**	500

DIVIDENDS – ORDINARY SHARES	AMOUNT PER SECURITY	FRANKED AMOUNT PER SECURITY
Interim dividend	10.0 cents	7.0 cents

INTERIM DIVIDEND DATE	
Record date	19 February 2020
Payment date	25 March 2020

The Company's Dividend Reinvestment Plan (DRP) will operate likely by acquiring shares on-market with no discount applied. The last date for the receipt of an election notice for participation in the Company's DRP is 20 February 2020. The DRP Issue Price will be based on a volume-weighted average price for a 10-day trading window from 24 February 2020 to 6 March 2020 inclusive.

Eligible shareholders may now lodge their DRP elections electronically by logging on to IAG's share registry, Computershare, on their website at www.computershare.com.au.

Additional Appendix 4D disclosure requirements can be found in the half year financial report of Insurance Australia Group Limited for the period ended 31 December 2019 (Attachment A). This report is also to be read in conjunction with the Annual Report of Insurance Australia Group Limited for the year ended 30 June 2019 and any public announcements made by Insurance Australia Group Limited during the reporting period in accordance with the continuous disclosure requirements of the *Corporations Act 2001* and the ASX Listing Rules.

This report is based on the consolidated half year financial statements which have been reviewed by KPMG.

ATTACHMENT A

INSURANCE AUSTRALIA GROUP LIMITED AND SUBSIDIARIES

HALF YEAR REPORT FOR THE PERIOD ENDED 31 DECEMBER 2019

INSURANCE AUSTRALIA GROUP LIMITED

ABN 60 090 739 923

FINANCIAL REPORT
FOR THE HALF YEAR ENDED 31 DECEMBER 2019

INSURANCE AUSTRALIA GROUP LIMITED
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DIRECTORS' REPORT

The Directors present their report together with the consolidated financial report of Insurance Australia Group Limited and its subsidiaries for the half year ended 31 December 2019 and the Auditor's Report.

The following terminology is used throughout the financial report:

- Company or Parent – Insurance Australia Group Limited; and
- IAG or Group – the consolidated entity consists of Insurance Australia Group Limited and its subsidiaries.

DIRECTORS OF INSURANCE AUSTRALIA GROUP LIMITED

The names and details of the Company's Directors in office at any time during, or since the end of, the half year are as follows. Directors were in office for the entire period unless otherwise stated.

INDEPENDENT NON-EXECUTIVE

Elizabeth B Bryan AM (Chairman)
Simon Allen – Appointed 12 November 2019
Duncan M Boyle
Sheila C McGregor
Jonathan (Jon) B Nicholson
Helen M Nugent AO
Thomas (Tom) W Pockett
George Savvides AM
Michelle K Tredenick
Hugh A Fletcher – Ceased 25 October 2019

EXECUTIVE

Peter G Harmer (Managing Director and Chief Executive Officer)

PRINCIPAL ACTIVITY

The principal continuing activity of IAG is the underwriting of general insurance and related corporate services and investing activities. IAG reports its financial information under the following segments:

DIVISION	OVERVIEW	PRODUCTS
Australia 77% of Group gross written premium (GWP)	This segment is a leading provider of general insurance products to both individuals and businesses in Australia. The Australia division benefits from its access to a variety of distribution channels and an array of well-established brands, as has been summarised below. The Australia division provides consumer insurance products through branches, call centres, the internet and representatives, under the following brands: ▪ NRMA Insurance in New South Wales, Australian Capital Territory, Queensland and Tasmania; ▪ SGIO in Western Australia; ▪ SGIC in South Australia; ▪ RACV in Victoria, via a distribution agreement with RACV; ▪ Coles Insurance nationally, via a distribution agreement with Coles; ▪ WFI nationally; and ▪ CGU Insurance through affinity and financial institution partnerships and broker and agent channels. The division also includes travel insurance, life insurance and income protection products which are underwritten by third parties. Business insurance products are sold through a network of around 2,000 intermediaries, such as brokers, agents and financial institutions and directly through call centre and online channels, under the following brands: ▪ CGU Insurance; ▪ WFI; ▪ NRMA Insurance; ▪ RACV; ▪ SGIO; and ▪ SGIC.	Short-tail insurance ▪ Motor vehicle ▪ Home and contents ▪ Lifestyle and leisure, such as boat, veteran and classic car and caravan ▪ Business packages ▪ Farm and crop ▪ Commercial property ▪ Construction and engineering ▪ Commercial motor and fleet motor Long-tail insurance ▪ Compulsory Third Party (motor injury liability) ▪ Workers' compensation ▪ Professional indemnity ▪ Directors' and officers' ▪ Public and products liability

DIVISION	OVERVIEW	PRODUCTS
New Zealand 23% of Group GWP	The New Zealand business is the leading general insurance provider in the country in both the direct and broker/agent channels. Insurance products are provided directly to customers, primarily under the State and AMI brands, and indirectly through insurance brokers and agents, under the NZI and Lumley Insurance brands. General insurance products are also distributed through agents and under third party brands by corporate partners, which include large financial institutions.	Short-tail insurance ■ Motor vehicle ■ Home and contents ■ Commercial property, motor and fleet motor ■ Construction and engineering ■ Niche insurance, such as pleasure craft, boat and caravan ■ Rural ■ Marine Long-tail insurance ■ Personal liability ■ Commercial liability
Corporate and other	Corporate and other comprises other activities, including corporate services, capital management activity, shareholders' funds investment activities, inward reinsurance from associates, and investment in associates in Malaysia and India.	

RECONCILIATION BETWEEN THE STATUTORY RESULTS (IFRS) AND THE MANAGEMENT REPORTED (NON-IFRS) RESULTS

The discussion of operating performance in the operating and financial review section of this report is presented on a management reported basis unless otherwise stated. Management reported results are non-IFRS financial information and are not directly comparable to the statutory results presented in other parts of this financial report. A reconciliation between the two is provided in this section and the guidance provided in Australian Securities and Investments Commission Regulatory Guide 230 'Disclosing non-IFRS financial information' ('RG 230') has been followed when presenting the management reported results. Non-IFRS financial information has not been reviewed by the external auditor, but has been sourced from the financial reports. IAG's statutory and management reported profit before income tax from continuing operations are the same.

On 24 January 2020 IAG advised that its current half year results would contain a provision for customer refunds. The provision relates to a specific multi-year pricing issue identified by IAG where discounts were not always applied in full to premiums for all customers who may have been eligible. This is not expected to be a feature of the Group's future sustainable earnings profile. As a result, and to ensure consistency of the reporting of key insurance measures and metrics, this item has been shown in the 'Net corporate expense' line in the management reported view of the current period's results. This view is consistent with the approach adopted in IAG's Investor Report.

Reconciliation between the statutory results (IFRS) and the management reported (non-IFRS) results is presented below:

CONSOLIDATED	STATUTORY RESULTS (IFRS)	CUSTOMER REFUND PROVISION	MANAGEMENT RESULTS (NON-IFRS PER INVESTOR REPORT)
	$m	$m	$m
Gross written premium	5,861	101	5,962
Movement in unearned premium liability	143	-	143
Gross earned premium	6,004	101	6,105
Outwards reinsurance premium expense	(2,377)	(19)	(2,396)
Net earned premium	3,627	82	3,709
Net claims expense	(2,433)	-	(2,433)
Commission expense	(506)	-	(506)
Underwriting expense	(1,009)	79	(930)
Reinsurance commission revenue	591	(11)	580
Net underwriting expense	(924)	68	(856)
Underwriting profit	270	150	420
Net investment income on assets backing insurance liabilities	81	-	81
Insurance profit	351	150	501
Net corporate expense	(2)	(150)	(152)
Net other operating income/(expenses)	8	-	8
Profit before income tax from continuing operations	357	-	357

The adjustments summarised above reflect the current half year pre-tax earnings impact of the inclusion of the provision for customer refunds. The gross provision for customer refunds, interest attributable to those refunds and the cost of administering the associated remediation program is $180 million (refer to Note 2.5) and after recognition of a $30 million recovery from our whole-of-account quota share arrangements, the half year net pre-tax earnings impact is $150 million. After tax and outside equity interests, the net cost of this provision to IAG is $82 million. This has been excluded from cash earnings for dividend calculation purposes.

OPERATING AND FINANCIAL REVIEW

OPERATING RESULT FOR THE HALF YEAR

IAG's reported insurance margin of 13.5%, was lower than the prior corresponding half year (31 December 2018: 13.7%), primarily reflecting a repeat of the heavy peril activity which impacted the prior corresponding half year and a lower than anticipated prior period reserve release contribution. The underlying insurance margin in the current half year of 16.9% (31 December 2018: 16.2%), has been broadly in line with expectations and consistent with the second half of the prior year. This reflected further realisation of optimisation program benefits with some offset from increased regulatory and compliance costs and a drag from lower interest rate effects on investment income.

Overall GWP growth of 1.4% was in line with expectations and consistent with the guidance for the 2020 financial year of low single digit growth. This comprised a flat GWP of $4,608 million in Australia and a growth of 6.3% in New Zealand (to $1,348 million), including a favourable foreign exchange translation effect. On a like-for-like basis GWP growth was approximately 2.5% after allowing for Australian business exits concluded in the prior financial year, lower Compulsory Third Party (CTP) rates stemming from scheme change and foreign exchange translation effects. Personal lines growth was primarily rate-driven, while commercial rate increases were a feature in both Australia and New Zealand. Further volume loss in Australian commercial lines contrasted with volume gain in New Zealand.

In October 2019, IAG announced an agreed sale of its interest in SBI General Insurance Company Limited (SBI General) in India and indicated a profit after tax of over $300 million and a regulatory capital benefit of over $400 million. This transaction will complete, and the effects described above recognised, once associated regulatory processes and approvals are finalised. It is IAG's expectation this will occur during the second half of the current financial year.

Net profit after tax

The Group's profit after tax for the half year was $263 million (31 December 2018: $525 million). After adjusting for non-controlling interests in the Group result, net profit attributable to the shareholders of the Company was $283 million (31 December 2018: $500 million) and was 43% lower than the prior corresponding half year. This outcome included the net effect of:

- a relatively flat pre-tax insurance profit of $501 million, as improved underlying profitability was negated by a significant drop in contribution from prior period reserve releases;
- a positive turnaround in contribution from investment income on shareholders' funds, on stronger Australian and offshore equity markets;
- a substantial reduction in input from discontinued operations, owing to the absence of the profit of $208 million on the sale of the Thailand operations which was recognised in the first half of the prior year; and
- inclusion of the aforementioned post-tax provision of $82 million for customer refunds.

Gross written premium

Total GWP of $5,962 million (31 December 2018: $5,881 million) represented a 1.4% increase compared to the prior corresponding half year. This increase primarily encompassed:

- flat GWP of $4,608 million in Australia; and
- growth of 6.3% in New Zealand (to $1,348 million), including a favourable foreign exchange translation effect.

Insurance margin

IAG's current half year reported insurance profit of $501 million (31 December 2018: $496 million) was 1% higher than the prior corresponding half year. The resultant reported insurance margin of 13.5% (31 December 2018: 13.7%) was slightly lower than the prior corresponding half year. Contributing to this outcome were:

- a significantly lower net prior period reserve release contribution, owing to stronger development and large loss experience in Australian long-tail classes than anticipated; and
- a similar-sized net natural perils claim cost overrun against allowance, in a period of high perils activity centred on a sequence of bushfire events in Australia; offset partially by
- a favourable movement in credit spread impact; and
- an improvement in the underlying margin as summarised below.

Underlying margin

IAG's underlying insurance margin increased to 16.9% (31 December 2018: 16.2%). The improvement reflected rate-driven growth in net earned premium (NEP) and further net benefits from the Group-wide optimisation program, partially offset by higher regulatory and compliance costs and lower interest rates impacting investment income. Short-tail personal lines' underlying profitability remained strong, as earned rate increases broadly matched average claim cost rises and further expense reduction benefits were realised. Long-tail CTP underlying profitability was similar to the prior corresponding half year, with both periods reflecting the capped profitability of the new scheme in NSW. Commercial lines' underlying profitability continued to improve, reflecting further benefits from rate and remediation activity, as well as cost-out effects, while absorbing pressure in Australian agricultural portfolios.

IAG defines its underlying margin as the reported insurance margin adjusted for:

- net natural peril claim costs less the related allowance for the period;
- reserve releases in excess of, or below, 1% of NEP; and
- credit spread movements.

INSURANCE MARGIN	**31 December 2019** $m	**31 December 2019** %	31 December 2018 $m	31 December 2018 %
Management reported insurance margin*	**501**	**13.5**	496	13.7
Net natural peril claim costs in excess of allowance	**99**	**2.7**	110	3.1
Reserve releases below/(in excess of) 1% of NEP	**32**	**0.9**	(47)	(1.3)
Credit spread movements	**(7)**	**(0.2)**	24	0.7
Underlying insurance margin	**625**	**16.9**	583	16.2

* Management reported insurance margin is the insurance profit as a percentage of NEP as disclosed in the Investor Report. Based on the statutory results, the equivalent statutory insurance margin for the current year is 9.7%.

Tax expense

IAG reported a tax expense of $90 million in the current half year compared to $123 million in the prior corresponding half year, representing an effective tax rate of 25.2% (31 December 2018: 27.9%).

Contributory elements reconciling the current half year's effective tax rate to the Australian corporate rate of 30% are:

- differences in tax rates applicable to IAG's foreign operations, principally in New Zealand, Singapore and Malaysia; and
- franking credits generated from IAG's investment portfolio.

Investment income on shareholders' funds

Net investment income on shareholders' funds was a profit of $50 million, compared to a loss of $7 million in the prior corresponding half year. This result included:

- relative strength in equity markets, both domestic and offshore;
- a positive return from alternative investments; partially offset by
- an $8 million adverse fair value adjustment of IAG's 16.9% interest in Bohai Property Insurance Company Ltd in China (current carrying value of $36 million).

In the current half year, the broader Australian index (S&P ASX200 Accumulation Index) delivered a positive return of 3.1% (31 December 2018: -6.8%) and the MSCI World Total Return Index (AUD Hedged) produced a positive return of 8.9% (31 December 2018: -8.7%).

At 31 December 2019, the weighting to defensive assets (fixed interest and cash) within shareholders' funds was 51%, compared to 58% at the end of the prior financial year. To a large extent the lower weighting reflects the source of funds used to redeem the $550 million Reset Exchangeable Securities (RES) in December 2019.

DIVISIONAL HIGHLIGHTS

A. AUSTRALIA

Australia accounted for 77% of Group GWP. This segment delivered a higher reported insurance margin of 12.1% (31 December 2018: 10.7%) despite there being a substantial adverse movement in the prior period reserving effect. Australia's underlying performance remained solid, with an underlying insurance margin of 16.1% (31 December 2018: 14.8%).

I. Premiums

Australia reported GWP of $4,608 million (31 December 2018: $4,606 million) in the current half year which was flat compared to the prior corresponding half year. The overall Australian GWP outcome includes:

- largely rate-driven growth of over 3% in short-tail motor, broadly in line with claims inflation;
- home GWP growth of over 4%, primarily rate-derived with minor offset from volume slippage; offset by
- approximately 9% contraction in long-tail CTP, from a mixture of scheme change driven rate reductions and some modest volume loss; and
- a modest contraction in like-for-like GWP in commercial lines, with mid-single digit average rate increases countered by lower volumes.

II. Insurance profit

Australia reported an insurance profit of $349 million, compared to $304 million in the prior corresponding half year. This equates to a higher reported insurance margin of 12.1%, compared to the 10.7% attained in the prior corresponding half year. This outcome includes the net effect of:

- a significant adverse movement in prior period reserving effects, from 2.9% of NEP in the prior corresponding half year to a small net strengthening in the current half year;
- a $47 million reduction in net natural peril claim costs, but still well above allowance;
- a favourable movement in credit spread impacts of over $30 million; and
- a solid improvement in the underlying insurance margin as detailed below.

III. Underlying margin

Australia's underlying performance remained sound, with an underlying insurance margin of 16.1% (31 December 2018: 14.8%). Contributory factors to the overall improvement were:

- further benefits from the optimisation program, partially offset by increased regulatory and compliance costs;
- further flow-through of average rate increases across commercial portfolios, particularly within packaged products;
- lower interest rates driving reduced investment income and not fully compensated for in pricing actions;
- lower large losses within commercial lines; and
- increased average claim costs in home.

IV. Fee-based business

The principal source of fee income is IAG's role as agent under the Victorian workers' compensation scheme, which is underwritten by the state government.

Total net income from fee-based operations in the current half year was a profit of $6 million, compared to $9 million in the prior corresponding half year. This outcome includes the net effect of:

- an overall contribution of $8 million (31 December 2018: $12 million) from the Victorian workers' compensation business. A similar underlying performance was achieved after allowance for $5 million of prior period fee income (31 December 2018: $10 million), which is typically reported in the opening half of the financial year. The decrease in prior period income was as expected as IAG moves further into its five-year contract and opportunities to generate returns from tail incentive fees and scheme actuarial releases diminish; and
- costs associated with mobility initiatives, including those arising from the trials of the Safer Journeys crash detection and response service.

B. NEW ZEALAND

New Zealand accounted for 23% of Group GWP and produced a lower reported insurance margin of 18.9% (31 December 2018: 24.9%) following a large hailstorm event in November 2019. New Zealand's underlying performance remained strong with an underlying insurance margin 18.9% (31 December 2018: 20.0%). The lower underlying insurance margin largely reflected higher working and large claim experience and was consistent with the performance in the second half of the prior year.

I. Premiums

New Zealand's reported current half year GWP rose by 6.3% to $1,348 million, compared to the prior corresponding half year GWP of $1,268 million. This increase includes a favourable foreign exchange translation effect, with local currency GWP increasing by 4.2% in the current half year, to NZ$1,428 million (31 December 2018: NZ$1,371 million). This result encompassed:

- strong GWP growth from Business, driven by increased rates across main commercial lines combined with volume growth in commercial motor; and
- sound GWP growth in Consumer, led by private motor through a combination of increased rates and volume growth.

II. Insurance profit

The New Zealand business produced a lower insurance profit of $156 million in the current half year, compared to $193 million in the prior corresponding half year. This equates to a reported insurance margin of 18.9% (31 December 2018: 24.9%) with the reduction reflecting a combination of:

- significantly higher net natural peril claim costs, centred on the Canterbury hailstorm;
- a slight moderation in the underlying insurance margin driven by a normalisation of large and working claims experience following the very benign environment experienced during the prior comparable period; partially offset by
- higher prior period reserve releases.

Prior period reserve releases of $14 million were recognised in the current half year, compared to a negligible level in the prior corresponding half year. The current half year's net reserve releases were predominantly sourced from professional indemnity exposures to residual post-Canterbury earthquake risks.

III. Earthquake settlements

Sound progress continues to be made with the settlement of claims associated with the financial year 2011 Canterbury earthquake events. At 31 December 2019 over NZ$6.9 billion of claim settlements had been completed, with 925 claims remaining open out of more than 90,000 received.

During the current half year there was no change to IAG's gross reserved position on the three major earthquakes, with considerable legacy reinsurance protection available for the September 2010 and June 2011 events, and approximately NZ$540 million of adverse development cover available for the February 2011 event.

Outstanding claims include those subject to dispute and litigation or involving high customer utilisation of independent expert advice, as well as recently-received over-cap claims from the Earthquake Commission (EQC). It remains IAG's expectation that finalisation of all residual claims will take several years given associated complexity.

C. CORPORATE AND OTHER

A pre-tax loss of $4 million was reported, which compares to a loss of $66 million in the prior corresponding half year. The movement primarily reflects the increase in net investment income on shareholders' funds of $57 million coupled with an improvement in the Group's share of net profit/(loss) from associates. Further details on the operating segments are set out in Note 1.3 within the financial statements.

I. Share of net profit/(loss) of associates

The Group's share of net profit of associates was a profit of $27 million (31 December 2018: $18 million), including allocated regional costs and amortisation. This result is largely derived from IAG's interests in AmGeneral Holdings Berhad (AmGeneral) in Malaysia and SBI General in India. On 17 October 2019 IAG announced the agreed sale of its entire 26% interest in SBI General via two transactions. These are expected to conclude in the second half of the current year, once associated regulatory processes and approvals are complete.

IAG's share of AmGeneral's profit for the current half year increased to $20 million (31 December 2018: $17 million). The positive outcome comprised the net effect of:

- higher net earned premium driven by sound growth in a subdued market;
- higher investment returns due to mark-to-market gains on investments;
- lower bodily injury-related prior period releases; and
- pricing competition in the partly liberalised market in both motor and fire classes.

IAG's share of SBI General's profit for the current half year increased to $16 million (31 December 2018: $13 million). This improved outcome comprised the combined effect of:

- strong net earned premium growth, reflecting top line momentum;
- higher investment income; and
- lower reinsurance exchange commission.

REVIEW OF FINANCIAL CONDITION

A. FINANCIAL POSITION

The total assets of the Group as at 31 December 2019 were $29,053 million compared to $29,286 million as at 30 June 2019. Movements within the overall net decrease in assets of $233 million include:

- a decrease in investments of $737 million associated with funds outflow for the payment of the 2019 final dividend of $462 million and redemption of all outstanding RES in December 2019 at their face value of $550 million, partially offset by the operating earnings for the half year;
- a decrease of $182 million in investment in joint venture and associates primarily due to the reclassification of the investment in SBI General as held for sale; offset by
- a $518 million increase in right-of-use assets primarily due to the initial application of the new lease accounting standard (*AASB 16 Leases*); and
- a $155 million increase in assets held for sale largely from the reclassification of the investment in SBI General, partially offset by a decrease in assets held for sale following the disposal of the Indonesian subsidiary.

The total liabilities of the Group as at 31 December 2019 were $22,678 million compared with $22,576 million as at 30 June 2019. Movements within the overall net increase in liabilities of $102 million include:

- a $626 million increase in lease liabilities primarily due to the initial application of the new lease accounting standard; offset by
- a $548 million decrease in interest-bearing liabilities largely owing to the RES redemption.

IAG shareholders' equity (excluding non-controlling interests) decreased from $6,404 million as at 30 June 2019 to $6,177 million as at 31 December 2019, reflecting the combined effect of:

- current half year net profit attributable to shareholders of $283 million;
- payment of the final dividend of $462 million declared in respect of the 2019 financial year; and
- reduction in opening retained earnings of $33 million on initial application of *AASB 16 Leases*.

B. CASH FROM OPERATIONS

The net cash inflows from operating activities for the half year ended 31 December 2019 were $183 million compared with $365 million for the prior corresponding half year. The movement is mainly attributable to the net effect of:

- an increase in reinsurance and other recoveries received of $201 million, predominantly relating to higher claims recoveries from the whole of account reinsurance quota share arrangements;
- an increase in claim costs paid of $171 million, predominantly pertaining to higher payments on prior period natural peril events in Australia and the November 2019 NSW bushfires, partially offset by lower payments on the Canterbury and Kaikoura earthquakes; and
- an increase in other operating payments of $210 million, predominantly driven by the timing of the settlement to creditors.

C. INVESTMENTS

The Group's investments totalled $9,947 million as at 31 December 2019, excluding investments held in joint venture and associates, with over 60% represented by the technical reserves portfolio. Total investments at 30 June 2019 were $10,684 million. The decrease in total investments since 30 June 2019 reflects the combined effect of:

- payment of the final dividend of $462 million in September 2019;
- redemption of the $550 million RES issue in December 2019; and
- net earnings during the period.

IAG's overall investment allocation is conservatively positioned, with over 80% of total investments in fixed interest and cash as at 31 December 2019. Technical reserves were 100% invested in fixed interest and cash, while the equivalent figure for shareholders' funds was 51%. IAG's allocation to growth assets was 49% of shareholders' funds at 31 December 2019, compared to 42% at 30 June 2019.

D. INTEREST-BEARING LIABILITIES
IAG's interest-bearing liabilities stood at $1,532 million at 31 December 2019, compared to $2,080 million at 30 June 2019. The net movement in the period largely reflects IAG's redemption of the $550 million RES issue in December 2019.

E. CAPITAL MIX
IAG measures its capital mix on a net tangible equity basis, i.e. after deduction of goodwill and intangibles, giving it strong alignment with regulatory and rating agency models. IAG targets the following ranges:
- ordinary equity (net of goodwill and intangibles) 60-70%; and
- debt and hybrids 30-40%.

At 31 December 2019, debt and hybrids represented 31.9% of total tangible capitalisation, toward the lower end of IAG's targeted range. The decrease since the prior financial year largely reflects the impact of the RES redemption which was completed in December 2019.

Subject to market conditions, IAG may seek to issue a new long-dated Tier 2 subordinated instrument prior to 30 June 2020 to provide additional liquidity.

F. CAPITAL POSITION
IAG remains strongly capitalised under the Australian Prudential Regulatory Authority's (APRA) Prudential Standards, with Common Equity Tier 1 (CET1) capital of $2,714 million (30 June 2019: $3,082 million) and regulatory capital of $4,254 million (30 June 2019: $4,981 million) at 31 December 2019. IAG has set the following related targeted benchmarks:
- a CET1 target range of 0.9 to 1.1 times the Prescribed Capital Amount (PCA), compared to a regulatory requirement of 0.6 times; and
- a total capital position equivalent to 1.6 to 1.8 times the PCA, compared to a regulatory requirement of 1.0 times.

At 31 December 2019, IAG had a CET1 multiple of 1.15 (30 June 2019: 1.31) and a PCA multiple of 1.80 (30 June 2019: 2.12).

IAG has increased its targeted PCA multiple range from 1.4 to 1.6 times to one of 1.6 to 1.8 times. This reflects reduced reliance on inter-company loans from Australian insurance subsidiaries to IAG's non-operating holding company, as required by APRA following the licence consolidation completed in 2017.

STRATEGY AND RISK MANAGEMENT
A. STRATEGY
MAKING CUSTOMERS FEEL SAFER ON THE ROAD, IN THEIR HOMES AND AT WORK
IAG's purpose means that whether you are a customer, partner, employee, shareholder or part of the communities IAG serves, IAG exists to 'make your world a safer place'. IAG believes its purpose will enable it to become a more sustainable business over the long term, and deliver stronger and more consistent returns for its shareholders.

IAG is focused on building a lean, efficient and modular insurance operation, through its simplification priority, while creating a customer-focused organisation with enhanced capabilities in data, digital, analytics and artificial intelligence, brand and innovation, and driving towards the creation of an agile organisation.

With simplification well-progressed, IAG is now increasing its focus on customer engagement and long-term growth. This includes extending its strategic partnerships to offer products and services that are adjacent to its insurance business, enabling IAG to make its customers and the community feel safer on the road, in their homes and at work. IAG is also leveraging its assets – including its data, customer reach and brands – to launch and scale new businesses in markets that complement these adjacent products and services.

The goals of IAG's strategy are centred around building deeper engagement with its customers and growing the number of customers in the IAG network of brands. IAG seeks to create more value for its customers by making their world a safer place and to increase the lifetime value of its customer relationships.

IAG continues with its three key strategic priorities, supported by organisational capabilities, to deliver its strategy:

I. Customer – world-leading customer experiences:
- Create a delivery platform that transforms customer experiences;
- Better connect customers and automate processes, enabling IAG to reach more customers in a timely manner;
- Develop an innovation approach which provides the ability to think differently and deliver quickly;
- Embed cognitive capabilities and artificial intelligence that anticipate customers' needs; and
- Use data to power decision-making, allowing IAG to better understand its customers.

II. Simplification – simplified, modular and lower cost operating model:
- Reduce organisational complexity by consolidating technology platforms, harmonising products, simplifying processes and systems, and executing the technology strategy;
- Leverage operational partners to optimise the operating model and drive scale economies across the value chain; and
- Improve allocation and maximise utilisation of the preferred repairer network to reduce average claim size.

III. Agility – an agile organisation distinguished by innovation, speed and execution skills:

- Create a disciplined approach to IAG's management and leadership, including building stronger role clarity and introducing agile ways of working;
- Build a talent pipeline based on the skills required to deliver IAG's strategy and help IAG people transition to the future of work; and
- Be recognised as a purpose-led organisation that shapes its internal and external environment.

IAG is well-positioned to transition to the next era of its strategy, shifting its focus more towards customer-led growth.

Financial targets

IAG is focused on delivering through-the-cycle financial targets of:

- a cash return on equity (ROE) 1.5 times its weighted average cost of capital (WACC);
- a dividend payout of 60-80% of full year cash earnings; and
- a top quartile total shareholder return (TSR).

These financial targets are complemented by short-term balanced scorecard objectives for the enterprise, including financial performance (including underlying profit, GWP growth, and operating costs), customer advocacy and growth, people engagement and leadership effectiveness, and IAG's risk maturity performance.

B. BUSINESS RISK AND RISK MANAGEMENT

IAG acknowledges that it has to take risk in an informed manner in pursuit of its strategic objectives and to meet customer, stakeholder, industry and regulatory expectations. IAG clearly articulates the levels, boundaries and nature of risk it is willing to accept, actively manage or avoid in pursuit of the Group's strategic objectives.

IAG uses an enterprise-wide approach to risk management and its risk management framework is a core part of the governance structure, which includes internal policies, key management processes and culture. The Group risk management strategy (RMS) details the IAG principles, risk appetite, policies, key controls, monitoring and governance processes for managing material risks. The RMS is reviewed annually, or as required by the Risk Committee, before being recommended for approval by the Board. IAG's Group Risk function provides regular reports to the Risk Committee on the operation of, and any changes to, IAG's risk management framework, the status of material risks, risk and compliance incidents, risk trends and IAG's risk profile. IAG's Internal Audit function provides reports to the Audit Committee on significant audit findings and other audit-related matters.

Roles and responsibilities of the Board and its standing committees, the Audit Committee, the Risk Committee, the People and Remuneration Committee and the Nomination Committee, are set out in the Corporate Governance section of the IAG website.

IAG is exposed to multiple risks relating to its general insurance business. The risks noted below are not meant to represent an exhaustive list, but outline the material risks faced by the Group as identified in the RMS:

- customer risk – the risk of failing to meet customer expectations leading to lower customer satisfaction, retention rates and new business opportunities;
- culture and conduct – the risk that employee behaviours are consistently contrary to our Purpose, Spirit or our stated Code of Ethics and Conduct;
- strategic risk – the risk that internal or external factors compromise our ability to execute our strategic objectives or our strategy;
- insurance risk – the risk of loss as a result of:
  - inadequate or inappropriate underwriting;
  - inadequate or inappropriate product pricing;
  - unforeseen, unknown or unintended liabilities that may eventuate;
  - inadequate or inappropriate claims management including reserving; and
  - insurance concentration risk (i.e. by locality, segment factor, or distribution);
- reinsurance risk – the risk of:
  - lack of capacity in the reinsurance market;
  - insufficient or inappropriate reinsurance coverage;
  - inadequate or inappropriate reinsurance recovery management;
  - reinsurance arrangements not legally binding; and
  - reinsurance concentration;
- capital risk – the risk that capital is insufficient or excessive given the nature, strategies and objectives of the firm; or not of the best form (the mix of debt, equity & reinsurance is inappropriate);
- market risk – the risk of adverse movements in market prices (equities, derivatives, interest rates, foreign exchange, etc) or inappropriate concentration within the investments funds;
- credit risk – the risk arising from a counterparty's failure to meet its obligations in accordance with the agreed terms. These include investment and derivative counterparties, reinsurers and premium debtors;
- liquidity risk – arises where there are inadequate funds to meet liabilities as they fall due. Liquidity risk arises from loss of access to funding and an illiquid asset portfolio including investments, reinsurance and trade assets;
- operational risk – the risk of loss resulting from the actions or behaviours of people, inadequate or failed internal processes or systems or from external events; and
- regulatory risk and compliance – the risk of legal, regulatory or reputational impacts arising from failure to manage compliance obligations, or failure to anticipate and prepare for changes in the regulatory environment.

A disciplined approach to risk management has been adopted and IAG believes this approach provides the greatest long-term likelihood of being able to meet the objectives of all stakeholders.

IAG's purpose is to make your world a safer place and the Group is committed to managing the risks and opportunities resulting from environmental, social and governance issues. IAG's Social and Environmental Policy provides a framework for identifying and managing IAG's direct and indirect social and environmental impacts, outlines IAG's commitments on material issues, and defines its approach to continuous improvement in IAG's social and environmental performance.

IAG has long recognised that it needs to play a role in adapting to climate change as well as reducing the emissions that are driving it. IAG's three-year Climate Action Plan was launched in July 2018, with six-monthly scorecard updates articulating its progress. IAG has been carbon neutral since 2012 and has set science-based emission targets for scope 1 (predominantly fleet emissions) and scope 2 (electricity usage emissions) consistent with the 2015 Paris Agreement to limit global average temperature rise to well below 2°C above pre-industrial levels.

IAG's expertise in natural peril data and insights, combined with its research, gives the business a unique insight into the impact extreme weather events have on IAG's customers, business and the wider community. IAG's safer communities partnerships and programs and its role on the Australian Business Roundtable for Disaster Resilience and Safer Communities provide examples of IAG's mitigation and adaptation efforts in response to climate risk.

IAG is committed to continuing to enhance its understanding of climate risk and providing disclosures consistent with the Task Force on Climate-related Financial Disclosures (TCFD) recommendations, an update can be found in IAG's current half year Investor Report. More information can be found in IAG's expanded 2019 climate-related disclosure both within the 30 June 2019 Annual Report and the Safer Communities section of www.iag.com.au.

Detail of IAG's overall risk management framework, which is outlined in the RMS, is set out in Note 3.1 within the 30 June 2019 Annual Report and in the Corporate Governance Statement, which is available at www.iag.com.au/about-us/corporate-governance. Effective from 1 July 2019, the IAG Board approved a revised Risk Management Strategy, increasing the number of risk classes from six to eleven, as defined above. Financial risk was separated into market risk, credit risk, liquidity risk and capital risk and two new risk classes were included, being customer risk and culture and conduct risk.

OUTLOOK

Since the start of the 2020 financial year, IAG has seen multiple extreme weather events which have impacted its customers and their communities. Responding to the needs of customers is particularly critical during such natural disasters and IAG has increased the resource in its call centres and claim and repair management teams to help its customers lodge claims and get back on their feet as quickly as possible.

These catastrophic weather events have also impacted IAG's financial performance, contributing to a lowering of its 2020 financial year reported insurance margin guidance range by 350bps, to 12.5-14.5%.

This has occurred in two steps since 31 December 2019:

- a 150bps reduction, as advised on 24 January 2020, to reflect:
  - an increase in the net natural peril claim cost assumption to $715 million (from $641 million), allowing for high year-to-date peril incidence, including the major hailstorm event in January 2020; and
  - a lowering of full year prior period reserve release expectations, from 1.0% of NEP to 0.5%, following lower than anticipated releases in the first half; and
- a 200bps reduction notified on 12 February 2020, derived from a further increase in the net natural peril claim cost assumption to $850 million (from $715 million) to include the heavy rain event affecting south-eastern Australia in early February 2020. This event is expected to result in a net claim cost of $135 million, in line with the second event maximum event retention (MER).

The revised 2020 financial year perils assumption allows for:

- net natural peril claims of approximately $645 million up until the end of January 2020;
- a net claim cost of $135 million applicable to the February 2020 heavy rain event in Australia;
- an estimate for the five months to 30 June 2020 (excluding the heavy rain event), based on average sub-$100 million (pre-quota share) event experience over the past five years, amounting to just over $170 million;
- the 2020 financial year stop-loss catastrophe reinsurance cover which provides $101 million of protection above $675 million, post-quota share; and
- no further major peril events ($100 million or greater in size, pre-quota share) before 30 June 2020.

As at 12 February 2020, IAG's MER had reduced to approximately $50 million following erosion of the deductible on the calendar 2020 aggregate catastrophe reinsurance cover.

All other 2020 financial year reported insurance margin-related assumptions are unchanged, and comprise:

- incremental improvement from optimisation program initiatives (of ~$160 million pre-tax vs. 2019 financial year), cumulatively approximating the $250 million pre-tax target originally set;
- an offset from higher regulatory and compliance costs, which are expected to increase by up to a further $50 million (vs. 2019 financial year), including increased investment in risk-related resources;
- ongoing drag from a lower investment running yield; and
- no material movement in foreign exchange rates or investment markets in the second half of the current financial year.

2020 financial year GWP growth guidance of 'low single digit' has been maintained. GWP growth in the second half of the current year is expected to be of a similar pace to that recorded in the first half of the year, with contributory factors being:

- anticipated rate increases across short-tail personal lines;
- modest volume growth in short-tail personal lines;
- further CTP premium reduction from cumulative price effects in response to scheme changes;
- further average rate increases in commercial classes; and
- lower commercial volumes in Australia, including business exit effects.

As originally indicated in August 2019, IAG is accelerating its spend on investments in the areas of data, artificial intelligence and innovation, and the associated businesses it is developing. It remains IAG's expectation that the amount by which expenditure exceeds revenue will expand in the 2020 financial year and contribute to an increased pre-tax loss in the fee income line, of up to $50 million.

DIVIDENDS

Details of dividends paid or determined to be paid by the Company and the dividend policy employed by the Group are set out in Note 3.4 within the financial statements.

Cash earnings are used for the purposes of targeted ROE and dividend payout policy and are defined as:

- net profit after tax attributable to shareholders of the Parent;
- plus amortisation and impairment of acquired identifiable intangibles; and
- excluding any unusual items (non-recurring in nature).

CASH EARNINGS	**31 December 2019 $m**	31 December 2018 $m
Net profit after tax	**283**	500
Acquired intangible amortisation and impairment	**15**	29
	298	529
Non-recurring items:		
Corporate expenses(1)	**152**	(5)
Tax effect on corporate expenses	**(47)**	(1)
Gain on sale of Thailand	**-**	(208)
Loss of diversification benefit on sale of Thailand	**-**	4
Non-controlling interest in corporate expenses	**(23)**	-
Cash earnings(2)	**380**	319
Interim dividend	**231**	277
Cash payout ratio(2)	**60.8%**	86.8%

(1) Corporate expenses in the current half year includes a $150 million pre-tax net impact of the customer refund provision. Refer to the 'Reconciliation between the statutory results (IFRS) and the management reported (non-IFRS) results' section on page 2 for further details.

(2) Cash earnings and cash payout ratio represent non-IFRS financial information.

IAG's full year dividend payout policy is to pay dividends equivalent to approximately 60-80% of reported full year cash earnings in respect of any given financial year.

The Board has determined to pay an interim dividend of 10.0 cents per ordinary share (cps), franked to 70% (31 December 2018: 12.0 cps, fully franked). The interim dividend is payable on 25 March 2020 to shareholders registered as at 5pm Australian Eastern Daylight Time (AEDT) on 19 February 2020.

The dividend reinvestment plan (DRP) will operate for the interim dividend for shareholders registered for the DRP as at 5pm AEDT on 20 February 2020. The issue price per share will be the Average Market Price as defined in the DRP terms with no discount for participants. Shares allocated under the DRP are likely to be purchased on-market. Information about IAG's DRP is available at http://www.iag.com.au/shareholder-centre/dividends/reinvestment.

SIGNIFICANT CHANGES IN STATE OF AFFAIRS

During the half year, the following changes became effective:

- On 17 October 2019, IAG agreed to sell the whole of its 26% interest in its joint venture with the State Bank of India, SBI General Insurance Company Limited, via two transactions. Agreements have been reached with Napean Opportunities LLP (part of Premji Invest) to acquire a 16.01% interest and an affiliate of Warburg Pincus LLC to acquire a 9.99% interest. The transactions are expected to complete during the financial year ending 30 June 2020, subject to regulatory processes and approvals.
- On 16 December 2019, IAG Finance (New Zealand) Limited, a wholly-owned subsidiary of the Company redeemed all outstanding reset exchangeable securities at their face value of $550 million.

EVENTS SUBSEQUENT TO REPORTING DATE

Detail of matters subsequent to the end of the half year are set out below and in Note 3.8 within the financial statements. These include:

- IAG's reported profitability in the second half of the current financial year will include net natural peril claim costs from the major hailstorm event which impacted parts of Melbourne, Canberra and Sydney in mid-January 2020, as well as the heavy rain event in early February 2020. The net pre-tax costs of these events are expected to be capped at $169 million and $135 million respectively, in line with IAG's first and second event MERs under its calendar 2020 catastrophe reinsurance protection.
- The Board determined to pay an interim dividend of 10.0 cents per share, 70% franked. The dividend will be paid on 25 March 2020. The dividend reinvestment plan will operate likely by acquiring shares on-market for participants with no discount applied.

LEAD AUDITOR'S INDEPENDENCE DECLARATION UNDER SECTION 307C OF THE CORPORATIONS ACT 2001

The lead auditor's independence declaration is set out on page 12 and forms part of the Directors' Report for the half year ended 31 December 2019.

ROUNDING OF AMOUNTS

Unless otherwise stated, amounts in the financial report and Directors' Report have been rounded to the nearest million dollars. The Company is of a kind referred to in the ASIC Corporations Instrument 2016/191 dated 24 March 2016 issued by the Australian Securities and Investments Commission. All rounding has been conducted in accordance with that instrument.

Signed at Sydney this 12th day of February 2020 in accordance with a resolution of the Directors.

Peter Harmer
Director

LEAD AUDITOR'S INDEPENDENCE DECLARATION

UNDER SECTION 307C OF THE CORPORATIONS ACT 2001

TO THE DIRECTORS OF INSURANCE AUSTRALIA GROUP LIMITED

I declare that, to the best of my knowledge and belief, in relation to the review of Insurance Australia Group Limited for the half year ended 31 December 2019 there have been:

- no contraventions of the auditor independence requirements as set out in the *Corporations Act 2001* in relation to the review; and
- no contraventions of any applicable code of professional conduct in relation to the review.

KPMG

KPMG

Andrew Yates
Partner

Sydney
12 February 2020

CONSOLIDATED FINANCIAL STATEMENTS

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

FOR THE HALF YEAR ENDED 31 DECEMBER 2019

	NOTE	**31 December 2019 $m**	31 December 2018 $m
Gross earned premium		**6,004**	5,984
Outwards reinsurance premium expense		**(2,377)**	(2,373)
Net earned premium (i)		**3,627**	3,611
Claims expense		**(4,617)**	(4,183)
Reinsurance and other recoveries revenue		**2,184**	1,825
Net claims expense (ii)		**(2,433)**	(2,358)
Commission expense		**(506)**	(487)
Underwriting expense		**(1,009)**	(945)
Reinsurance commission revenue		**591**	573
Net underwriting expense (iii)		**(924)**	(859)
Underwriting profit (i) + (ii) + (iii)		**270**	394
Investment income on assets backing insurance liabilities		**89**	111
Investment expenses on assets backing insurance liabilities		**(8)**	(9)
Insurance profit		**351**	496
Investment income on shareholders' funds		**58**	3
Fee and other income		**59**	67
Share of net profit of associates		**27**	18
Finance costs		**(54)**	(48)
Fee-based, corporate and other expenses		**(82)**	(92)
Net loss attributable to non-controlling interests in unitholders' funds		**(2)**	(3)
Profit before income tax from continuing operations		**357**	441
Income tax expense		**(90)**	(123)
Profit after income tax from continuing operations		**267**	318
(Loss)/profit after income tax from discontinued operations	2.2	**(4)**	207
Profit for the period		**263**	525
OTHER COMPREHENSIVE INCOME/(EXPENSE)			
Items that may be reclassified subsequently to profit or loss:			
Net movement in foreign currency translation reserve, net of tax		**3**	36
Items that will not be reclassified to profit or loss:			
Remeasurements of defined benefit plans, net of tax		**(1)**	(7)
Other comprehensive income from continuing operations, net of tax		**2**	29
Other comprehensive income from discontinued operations, net of tax	2.2	**2**	20
Total comprehensive income for the period, net of tax		**267**	574
PROFIT/(LOSS) FOR THE PERIOD ATTRIBUTABLE TO			
Shareholders of the Parent - continuing operations		**287**	293
Shareholders of the Parent - discontinued operations	2.2	**(4)**	207
Non-controlling interests - continuing operations		**(20)**	25
Profit for the period		**263**	525
TOTAL COMPREHENSIVE INCOME/(LOSS) FOR THE PERIOD ATTRIBUTABLE TO			
Shareholders of the Parent - continuing operations		**289**	322
Shareholders of the Parent - discontinued operations	2.2	**(2)**	227
Non-controlling interests - continuing operations		**(20)**	25
Total comprehensive income for the period, net of tax		**267**	574

STATEMENT OF COMPREHENSIVE INCOME (CONTINUED)

	NOTE	**31 December 2019 cents**	31 December 2018 cents
EARNINGS PER SHARE – CONTINUING AND DISCONTINUED OPERATIONS			
Basic earnings per ordinary share	3.3	**12.28**	21.31
Diluted earnings per ordinary share	3.3	**12.16**	20.48
EARNINGS PER SHARE – CONTINUING OPERATIONS			
Basic earnings per ordinary share	3.3	**12.45**	12.49
Diluted earnings per ordinary share	3.3	**12.32**	12.39

The above consolidated statement of comprehensive income should be read in conjunction with the notes to the financial statements.

CONSOLIDATED BALANCE SHEET

AS AT 31 DECEMBER 2019

	NOTE	**31 December 2019 $m**	30 June 2019 $m
ASSETS			
Cash held for operational purposes		**324**	538
Investments	3.1	**9,947**	10,684
Trade and other receivables		**4,029**	4,170
Current tax assets		**100**	107
Assets held for sale	2.3	**216**	61
Reinsurance and other recoveries on outstanding claims		**6,014**	5,779
Deferred insurance expenses		**3,542**	3,451
Deferred levies and charges		**114**	105
Deferred tax assets		**514**	453
Right-of-use assets	1.2	**518**	-
Property and equipment		**139**	181
Other assets		**124**	115
Investment in joint venture and associates	3.6	**362**	544
Goodwill and intangible assets		**3,110**	3,098
Total assets		**29,053**	29,286
LIABILITIES			
Trade and other payables		**2,610**	2,680
Current tax liabilities		**5**	29
Liabilities held for sale	2.3	**17**	27
Unearned premium liability		**6,195**	6,334
Outstanding claims liability		**10,476**	10,296
Lease liabilities	1.2	**626**	-
Non-controlling interests in unitholders' funds		**230**	245
Provisions	2.5	**518**	389
Other liabilities		**469**	496
Interest-bearing liabilities	2.4	**1,532**	2,080
Total liabilities		**22,678**	22,576
Net assets		**6,375**	6,710
EQUITY			
Share capital	3.2	**6,617**	6,617
Treasury shares held in trust		**(50)**	(48)
Reserves		**42**	46
Retained earnings		**(432)**	(211)
Parent interest		**6,177**	6,404
Non-controlling interests		**198**	306
Total equity		**6,375**	6,710

The above consolidated balance sheet should be read in conjunction with the notes to the financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

FOR THE HALF YEAR ENDED 31 DECEMBER 2019

	SHARE CAPITAL $m	TREASURY SHARES HELD IN TRUST $m	FOREIGN CURRENCY TRANSLATION RESERVE $m	SHARE-BASED REMUN-ERATION RESERVE $m	RETAINED EARNINGS $m	NON-CONTROLLING INTERESTS $m	TOTAL EQUITY $m
31 December 2019							
Balance at the beginning of the financial period	**6,617**	**(48)**	**20**	**26**	**(211)**	**306**	**6,710**
Adjustment on initial application of AASB 16, net of tax (see Note 1.2)	**-**	**-**	**-**	**-**	**(33)**	**-**	**(33)**
Restated balance at the beginning of the financial period	**6,617**	**(48)**	**20**	**26**	**(244)**	**306**	**6,677**
Profit for the period	**-**	**-**	**-**	**-**	**283**	**(20)**	**263**
Other comprehensive income/(expense)	**-**	**-**	**5**	**-**	**(1)**	**-**	**4**
Total comprehensive income for the period	**-**	**-**	**5**	**-**	**282**	**(20)**	**267**
Transactions with owners in their capacity as owners							
Share-based remuneration	**-**	**(2)**	**-**	**(9)**	**(8)**	**-**	**(19)**
Dividends determined and paid	**-**	**-**	**-**	**-**	**(462)**	**(87)**	**(549)**
Disposal of subsidiaries	**-**	**-**	**-**	**-**	**-**	**(1)**	**(1)**
Balance at the end of the financial period	**6,617**	**(50)**	**25**	**17**	**(432)**	**198**	**6,375**
31 December 2018							
Balance at the beginning of the financial period	7,082	(27)	(33)	29	(382)	272	6,941
Profit for the period	-	-	-	-	500	25	525
Other comprehensive income/(expense)	-	-	56	-	(7)	-	49
Total comprehensive income for the period	-	-	56	-	493	25	574
Transactions with owners in their capacity as owners							
Capital return, including transaction costs	(465)	-	-	-	-	-	(465)
Share-based remuneration	-	(22)	-	(13)	(5)	-	(40)
Dividends determined and paid	-	-	-	-	(603)	(66)	(669)
Additional investment in subsidiaries	-	-	-	-	-	2	2
Disposal of subsidiaries	-	-	-	-	-	(2)	(2)
Balance at the end of the financial period	6,617	(49)	23	16	(497)	231	6,341

The above consolidated statement of changes in equity should be read in conjunction with the notes to the financial statements.

CONSOLIDATED CASH FLOW STATEMENT

FOR THE HALF YEAR ENDED 31 DECEMBER 2019

	31 December 2019 $m	31 December 2018 $m
CASH FLOWS FROM OPERATING ACTIVITIES		
Premium received	**6,172**	6,020
Reinsurance and other recoveries received	**1,931**	1,730
Claim costs paid	**(4,444)**	(4,273)
Outwards reinsurance premium expense paid	**(2,410)**	(2,317)
Dividends, interest and trust distributions received	**214**	299
Finance costs paid	**(54)**	(45)
Income taxes paid	**(145)**	(243)
Other operating receipts	**935**	1,000
Other operating payments	**(2,016)**	(1,806)
Net cash flows from operating activities	**183**	365
CASH FLOWS FROM INVESTING ACTIVITIES		
Net cash flows on disposal/(acquisition) of subsidiaries and associates	**13**	370
Net cash flows from sale/(purchase) of investments and plant and equipment	**249**	211
Net cash flows from investing activities	**262**	581
CASH FLOWS FROM FINANCING ACTIVITIES		
Outlays for capital return, including transaction costs	**-**	(465)
Repayment of borrowings	**(551)**	-
Principal element of lease payments	**(32)**	-
Net cash flow from issue and redemption of trust units	**(17)**	(30)
Dividends paid to shareholders of the Parent	**(462)**	(603)
Dividends paid to non-controlling interests	**(87)**	(66)
Net cash flows from financing activities	**(1,149)**	(1,164)
Net movement in cash held	**(704)**	(218)
Effects of exchange rate changes on balances of cash held in foreign currencies	**-**	8
Cash and cash equivalents at the beginning of the financial period	**1,698**	1,345
Cash and cash equivalents at the end of the financial period*	**994**	1,135

* Includes $324 million of cash held for operational purposes, $645 million of cash and short-term money held for investments and $25 million of cash and cash equivalents in discontinued operations (31 December 2018: $431 million of cash held for operational purposes, $661 million of cash and short-term money held for investments and $43 million of cash and cash equivalents in discontinued operations).

The above consolidated cash flow statement should be read in conjunction with the notes to the financial statements.

NOTES TO THE FINANCIAL STATEMENTS

1. OVERVIEW

NOTE 1.1 INTRODUCTION

The financial report is structured to provide prominence to the disclosures that are considered most relevant to the users' understanding of the operations, results and financial position of IAG.

The financial report has been organised into the following sections:

1. Overview – contains information that impacts the financial report as a whole, as well as segment reporting disclosures.
2. Significant events and transactions – disclosure of significant changes in the Group's financial position and performance.
3. Interim disclosures – disclosures required to comply with Australian Accounting Standard *AASB 134 Interim Financial Reporting*.

NOTE 1.2 ABOUT THIS REPORT

A. CORPORATE INFORMATION

Insurance Australia Group Limited (Company or Parent), the ultimate parent entity in the Group, is a for-profit company incorporated and domiciled in Australia and limited by shares publicly traded on the Australian Securities Exchange (ASX). Its registered office and principal place of business is Level 13, Tower Two, Darling Park, 201 Sussex Street, Sydney, NSW 2000, Australia. This financial report covers the consolidated financial statements for the Company and its subsidiaries (IAG or Group) for the half year ended 31 December 2019.

This report is also to be read in conjunction with the Annual Report for the year ended 30 June 2019 and any public announcements made by Insurance Australia Group Limited during the reporting period in accordance with the continuous disclosure requirements of the *Corporations Act 2001* and the ASX Listing Rules.

A description of the nature of IAG's operations and its principal activities is included in the Directors' Report.

B. STATEMENT OF COMPLIANCE

This general purpose half year financial report was authorised by the Board of Directors for issue on 12 February 2020 and complies with Australian Accounting Standard *AASB 134 Interim Financial Reporting* and the recognition and measurement requirements of other applicable Australian Accounting Standards adopted by the Australian Accounting Standards Board (AASB), the *Corporations Act 2001* and the ASX Listing Rules.

The current IFRS for insurance contracts does not include a comprehensive set of recognition and measurement criteria. The International Accounting Standards Board (IASB) has issued a new standard (*IFRS 17 Insurance Contracts* – adopted as *AASB 17 Insurance Contracts* in an Australian context) that does include such criteria, with the current effective date of 1 January 2021. However since issuing the standard, the IASB has agreed to propose a one year delay to the effective date to 1 January 2022. This proposed amendment, along with a number of others, have been included in an exposure draft that was issued on 26 June 2019. This exposure draft was subject to a 90-day comment period, which closed on 25 September 2019. Until this standard takes effect, the financial reports of insurers in different countries that comply with IFRS may not be comparable in terms of the recognition and measurement of insurance contracts.

C. BASIS OF PREPARATION

The financial statements have been prepared on the basis of historical cost principles, as modified by certain exceptions, with the principal exceptions being the measurement of all investments and derivatives at fair value and the measurement of the outstanding claims liability and related reinsurance and other recoveries at present value. All values are rounded to the nearest million dollars, unless otherwise stated, in accordance with *ASIC Corporations Instrument 2016/191*.

The balance sheet is prepared with the assets and liabilities presented broadly in order of liquidity.

The financial report is presented in Australian dollars, which is the functional currency of the Company.

D. SIGNIFICANT ACCOUNTING POLICIES ADOPTED

The accounting policies adopted in the preparation of this financial report have been applied consistently by all entities in IAG and are the same as those applied for the previous reporting year, unless otherwise stated. The financial statements of entities operating outside Australia that maintain accounting records in accordance with overseas accounting principles are adjusted where necessary to comply with the significant accounting policies of IAG. The significant accounting policies adopted in the preparation of this financial report are set out within the relevant note in the Annual Report for the year ended 30 June 2019.

I. Changes in accounting policies

The following new Australian Accounting Standards and Interpretations are applicable for the current reporting period.

TITLE	DESCRIPTION
AASB 16	Leases
AASB 2017-6	Amendments to Australian Accounting Standards – Prepayment Features with Negative Compensation
AASB 2017-7	Amendments to Australian Accounting Standards – Long-term Interests in Associates and Joint Ventures
AASB 2018-1	Amendments to Australian Accounting Standards – Annual Improvements 2015–2017 Cycle
AASB 2018-2	Amendments to Australian Accounting Standards – Plan Amendment, Curtailment or Settlement
AASB Interpretation 23	Uncertainty over Income Tax Treatments, and relevant amending standards

Adoption of the new and amended accounting standards had no material financial impact on the Group. Information on the impact of *AASB 16* is provided below for clarity.

AASB 16 Leases

AASB 16, which was issued in 2016, sets out the principles for the recognition, measurement, presentation and disclosure of leases. It replaced the previous accounting requirements for leases, under *AASB 117*, effective from 1 July 2019 for IAG.

AASB 16 requires lessees to recognise most leases on the balance sheet in the form of a right-of-use asset (ROUA) and a corresponding lease liability. The standard allows exemptions for short-term leases (less than 12 months) and for leases on low value assets. For IAG, the main impact of the new standard was on leases which were previously classified as operating leases, being predominantly property and motor vehicle related leases.

As a result of the adoption of *AASB 16*, IAG has recognised depreciation expense on ROUAs, on a straight-line basis over the lease term, and interest expense on lease liabilities.

IAG has adopted *AASB 16* using the modified retrospective approach with the date of initial application being 1 July 2019. Under this approach, the cumulative effect of adoption is recognised as an adjustment to opening retained earnings as at 1 July 2019, with no restatement of comparative information.

The modified retrospective approach allows entities to use a number of practical expedients on adoption of the new standard, of which IAG elected to use the following:

- the use of a single discount rate applied to a portfolio of leases with similar characteristics;
- relied on previous assessments of whether a lease was onerous immediately before the date of initial application;
- for some leases which meet the definition of a short-term lease, have not applied *AASB 16*; and
- used hindsight in determining the lease term where the contract contains options to extend or terminate a lease.

The effect of adoption of *AASB 16* as at 1 July 2019 is as follows:

	Increase/(decrease) $m
Assets	
Right-of-use assets	553
Trade and other receivables	35
Property and equipment	(35)
Deferred tax assets	14
Other assets	(6)
Total assets	561
Liabilities	
Lease liabilities	655
Trade and other payables	(29)
Other liabilities	(32)
Total liabilities	594
Equity	
Retained earnings	(33)

On transition to *AASB 16*, the modified retrospective approach provides two options for measurement of the ROUA. The first option is to measure the ROUA as an amount equal to the lease liability adjusted for any prepaid or accrued lease payments. The second option is to measure the ROUA as if *AASB 16* had always been applied from the initial recognition of the lease. These measurement options have been applied on a lease-by-lease basis.

The following is a reconciliation of total operating lease commitments as at 30 June 2019 to the lease liabilities recognised as at 1 July 2019:

	$m
Operating lease commitments disclosed as at 30 June 2019	792
Discounted using IAG's incremental borrowing rate at the date of initial application	(98)
Add: finance lease liabilities recognised as at 30 June 2019	33
Less: contracts reassessed as service agreements	(72)
Lease liability recognised as at 1 July 2019	655

When measuring lease liabilities for leases that were classified as operating leases, IAG discounted lease payments using its incremental borrowing rate at 1 July 2019. The weighted-average rate applied is 2.7%.

II. Critical accounting estimates and judgements

In the process of applying the significant accounting policies, certain critical accounting estimates and assumptions are applied and judgements are made by management, the results of which affect the amounts recognised in the financial statements. The estimates and related assumptions are based on experience and other factors that are considered to be reasonable, and are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which they are revised, and future periods if relevant. The areas where material estimates and judgements are applied are set out below, with further details provided within the relevant note in the Annual Report for the year ended 30 June 2019.

AREAS OF CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS
Claims and reinsurance and other recoveries on outstanding claims
Liability adequacy test
Intangible assets and goodwill impairment testing, initial measurement and useful life
Income tax and related assets and liabilities
Investment in joint venture and associates impairment testing

NOTE 1.3 SEGMENT REPORTING

IAG has identified its operating segments based on the internal reports that are reviewed and used by the Group Chief Executive Officer (being the chief operating decision maker) in assessing performance and in determining the allocation of resources.

A. REPORTABLE SEGMENTS

IAG has general insurance operations in Australia and New Zealand, with reportable segments for the period ended 31 December 2019 comprising the following business divisions:

I. Australia

This segment provides general insurance products to individuals, families and businesses throughout Australia, primarily through NRMA Insurance, SGIO, SGIC and CGU brands, the RACV brand in Victoria (via a distribution and underwriting relationship with RACV), the Coles Insurance brand (via a distribution agreement with Coles) and the WFI brand through intermediaries including brokers, authorised representatives and distribution partners.

II. New Zealand

This segment provides general insurance products underwritten in New Zealand. Insurance products are sold directly to customers predominantly under the State and AMI brands, and through intermediaries (insurance brokers and authorised representatives) primarily using the NZI and Lumley Insurance brands. General insurance products are also distributed by corporate partners, such as large financial institutions, using third party brands.

III. Corporate and other

This segment comprises other activities, including corporate services, capital management activity, shareholders' funds investment activities, inward reinsurance from associates, and investment in associates in Malaysia and India. IAG's captive reinsurance operation (captive) is a corporate function that acts as the interface between the external providers of reinsurance capital and the operating business divisions. IAG does not manage, or view, the captive as a separate business. Consequently, the operating results of the captive are systematically allocated to the operating business segments.

B. FINANCIAL INFORMATION

	AUSTRALIA	NEW ZEALAND	CORPORATE AND OTHER	TOTAL
	$m	$m	$m	$m
31 December 2019				
I. Financial performance				
Total external revenue[1]	**7,135**	**1,771**	**106**	**9,012**
Underwriting profit/(loss)	**125**	**150**	**(5)**	**270**
Net investment income on assets backing insurance liabilities	**74**	**6**	**1**	**81**
Insurance profit/(loss)	**199**	**156**	**(4)**	**351**
Net investment income on shareholders' funds	**-**	**-**	**50**	**50**
Share of net profit of associates	**-**	**-**	**27**	**27**
Finance costs	**-**	**-**	**(54)**	**(54)**
Other net operating result	**6**	**-**	**(23)**	**(17)**
Total segment result from continuing operations	**205**	**156**	**(4)**	**357**
Income tax expense				**(90)**
Profit for the period from continuing operations				**267**
II. Other segment information				
Capital expenditure[2]	**-**	**-**	**50**	**50**
Depreciation and amortisation expense	**67**	**19**	**1**	**87**
31 December 2018				
I. Financial performance				
Total external revenue[1]	6,889	1,651	41	8,581
Underwriting profit/(loss)	215	184	(5)	394
Net investment income on assets backing insurance liabilities	89	9	4	102
Insurance profit/(loss)	304	193	(1)	496
Net investment loss on shareholders' funds	-	-	(7)	(7)
Share of net profit of associates	1	-	17	18
Finance costs	-	-	(48)	(48)
Other net operating result	9	-	(27)	(18)
Total segment result from continuing operations	314	193	(66)	441
Income tax expense				(123)
Profit for the period from continuing operations				318
II. Other segment information				
Capital expenditure[2]	-	-	71	71
Depreciation and amortisation expense	54	26	-	80

(1) Total external revenue comprises premium revenue, reinsurance and other recoveries, reinsurance commission revenue, investment income on assets backing insurance liabilities, investment income on shareholders' funds, fee and other income and share of net profit/(loss) of associates.

(2) Capital expenditure includes acquisitions of property and equipment, intangibles and other non-current segment assets.

2. SIGNIFICANT EVENTS AND TRANSACTIONS

SECTION INTRODUCTION
This section comprises disclosures on the events and transactions that are significant to an understanding of the changes in the Group's financial position and performance since the end of the last annual reporting period. Information disclosed in relation to those events and transactions provides an update on the relevant information presented in the most recent annual financial report.

NOTE 2.1 DISPOSAL OF BUSINESSES

On 30 September 2019, IAG completed the sale of its Indonesian subsidiary, PT Asuransi Parolamas, for a net consideration of $14 million.

NOTE 2.2 DISCONTINUED OPERATIONS

On 19 June 2018, IAG announced it had entered into a sale agreement with Tokio Marine & Nichido Fire Insurance Co., Ltd. (Tokio Marine) for IAG's operations in Thailand and Indonesia. Separate to the transactions with Tokio Marine, IAG agreed the sale of its interest in AAA Assurance Corporation, based in Vietnam. These consolidated Asian businesses have been identified as discontinued operations. The sale of IAG's operations in Thailand and Indonesia were completed on 31 August 2018 and 30 September 2019, respectively, with the performance of these operations being included up to their respective completion dates.

The counterparty to the agreed sale of AAA Corporation has failed to receive the necessary regulatory approvals and will not be proceeding. IAG is assessing alternative exit options for its Vietnam business but still expect to dispose of its economic interest over the coming twelve months.

	31 December 2019 $m	31 December 2018 $m
A. RESULTS OF DISCONTINUED OPERATIONS		
Revenue	**13**	109
Expenses	**(15)**	(109)
Loss before income tax	**(2)**	-
Income tax expense	**-**	(1)
Loss after income tax of discontinued operations	**(2)**	(1)
(Loss)/gain on sale of subsidiaries after income tax	**(2)**	208
(Loss)/profit from discontinued operations	**(4)**	207
Other comprehensive income, net of tax	**2**	20
Total comprehensive (loss)/income from discontinued operations	**(2)**	227
(Loss)/profit for the year attributable to shareholders of the Parent	**(4)**	207
(Loss)/profit for the year from discontinued operations	**(4)**	207
Total comprehensive (loss)/income for the year attributable shareholders of the Parent	**(2)**	227
Total comprehensive (loss)/income from discontinued operations	**(2)**	227
B. EARNINGS PER SHARE FROM DISCONTINUED OPERATIONS		
Basic earnings per share, from discontinued operations – cents per share	**(0.17)**	8.82
Diluted earnings per share, from discontinued operations – cents per share	**(0.16)**	8.09
C. CASH FLOW FROM DISCONTINUED OPERATIONS		
Net cash flows from operating activities	**(4)**	(17)
Net cash flows from investing activities*	**3**	383
Net cash flows from financing activities	**-**	22
Net cash flows for the period from discontinued operations	**(1)**	388

* The net cash flows from investing activities for the half year ended 31 December 2019 includes a net inflow of $5 million from the sale of IAG's Indonesian operations, which is comprised of the net cash consideration received of $14 million and the cash and cash equivalents disposed which totalled $9 million (31 December 2018: a net inflow of $383 million from the sale of IAG's Thailand operations, which is comprised of the net cash consideration received of $506 million and the cash and cash equivalents disposed of totalling $123 million).

D. RECOGNITION AND MEASUREMENT
A discontinued operation is a component of the entity that has been disposed of or is classified as held for sale and that represents a separate major line of business or geographical area of operations, is part of a single co-ordinated plan to dispose of such a line of business or area of operations, or is a subsidiary acquired exclusively with a view to resale. The results of discontinued operations are presented separately in the statement of profit or loss. When an operation is classified as a discontinued operation, the comparative statement of profit or loss and other comprehensive income is re-presented as if the operation had been discontinued from the start of the comparative period.

NOTE 2.3 ASSETS AND LIABILITIES HELD FOR SALE

On 17 October 2019, IAG agreed to sell the whole of its 26% interest in its joint venture with the State Bank of India, SBI General Insurance Company Limited (SBI General), via two transactions. Agreements have been reached with Napean Opportunities LLP (part of Premji Invest) to acquire a 16.01% interest and an affiliate of Warburg Pincus LLC to acquire a 9.99% interest. The transactions are expected to complete during the financial year ending 30 June 2020, subject to regulatory processes and approvals. As a result of the sale agreements, IAG's investment in SBI General has been reclassified as being held for sale in the current financial period. The assets and liabilities that were classified as held for sale as at 30 June 2019 related to IAG's consolidated businesses in Vietnam and Indonesia. The sale of IAG's operations in Indonesia was completed during the current financial period.

	31 December 2019	30 June 2019
	$m	$m
Cash held for operational purposes	**1**	10
Investments	**23**	33
Trade and other receivables	**1**	3
Reinsurance and other recoveries on outstanding claims	**1**	3
Deferred insurance expenses	**2**	3
Other assets	**7**	8
Goodwill and intangible assets	**-**	1
Investment in associate	**181**	-
Total assets held for sale	**216**	61
Trade and other payables	**5**	7
Outstanding claims liability	**5**	9
Unearned premium liability	**7**	10
Other liabilities	**-**	1
Total liabilities held for sale	**17**	27

RECOGNITION AND MEASUREMENT

Non-current assets (or disposal groups) are classified as held for sale if their carrying amount will be recovered principally through a sale transaction rather than through continuing use and a sale is considered highly probable. They are measured at the lower of their carrying amount and fair value less costs to sell, except for assets such as deferred tax assets, assets arising from employee benefits, financial assets and contractual rights under insurance contracts, which are specifically exempt from this requirement. Assets and liabilities classified as held for sale are presented separately in the balance sheet.

An impairment loss is recognised for any initial or subsequent write-down of the asset (or disposal group) to fair value less costs to sell. A gain is recognised for any subsequent increases in fair value less costs to sell of an asset (or disposal group), but not in excess of any cumulative impairment loss previously recognised. A gain or loss not previously recognised by the date of the sale of the non-current asset (or disposal group) is recognised at the date of derecognition.

Non-current assets (including those that are part of a disposal group) are not depreciated or amortised while they are classified as held for sale. Interest and other expenses attributable to the liabilities of a disposal group classified as held for sale continue to be recognised.

NOTE 2.4 INTEREST-BEARING LIABILITIES

Final Maturity Date	Principal Amount	31 December 2019 Carrying Value $m	31 December 2019 Fair Value $m	30 June 2019 Carrying Value $m	30 June 2019 Fair Value $m
A. COMPOSITION					
I. Capital nature					
a. ADDITIONAL TIER 1 REGULATORY CAPITAL[1]					
Reset exchangeable securities					
No fixed date	$550 million	-	-	550	558
Capital notes					
No fixed date	$404 million	**404**	**434**	404	432
b. TIER 2 REGULATORY CAPITAL					
AUD subordinated convertible term notes					
15 June 2044	$350 million	**350**	**356**	350	352
15 June 2045	$450 million	**450**	**462**	450	457
		800		800	
NZD subordinated convertible term notes[2],[3]					
15 June 2043	NZ$350 million	**336**	**355**	335	355
II. Operational nature					
Other interest-bearing liabilities		**2**	**2**	3	3
Less: capitalised transaction costs		**(10)**		(12)	
		1,532		2,080	

(1) Instruments issued prior to 1 January 2013 are eligible for inclusion in the relevant category of regulatory capital up to limits prescribed by APRA under transitional arrangements. Any capital that is ineligible to be included in Additional Tier 1 Capital as a consequence may be included in Tier 2 capital to the extent there is residual capacity within Tier 2 transitional limits.

(2) At the reporting date, the Company recognised accrued interest of $1 million (30 June 2019: $1 million) which is presented within trade and other payables.

(3) IAG is a "dual listed issuer" that is listed on both the ASX and the NZX Debt Market. As such, IAG is subject to some, but not all of the NZX Main Board/Debt Market Listing Rules ("NZX Listing Rules"). In particular, the rules set out in Appendix 17 to the NZX Listing Rules do not apply to IAG.

B. SIGNIFICANT MOVEMENTS DURING THE PERIOD

On 16 December 2019, IAG Finance (New Zealand) Limited, a wholly-owned subsidiary of the Company redeemed all outstanding reset exchangeable securities at their face value of $550 million.

C. RECOGNITION AND MEASUREMENT

The interest-bearing liabilities are initially measured at fair value (net of transaction costs) and subsequently measured at amortised cost. Based on market conditions at any point in time, the carrying value of the liabilities may not be representative of the fair value of the liabilities.

The fair value for all interest-bearing liabilities is calculated using their quoted market price in active markets (fair value hierarchy level 1), except for the AUD subordinated convertible notes where their fair value is calculated using their quoted market price in a market that is considered to be lacking sufficient depth to be considered active (fair value hierarchy level 2).

NOTE 2.5 PROVISIONS

	31 December 2019 $m	30 June 2019 $m
A. PROVISIONS		
Employee benefits	**309**	349
Restructuring provision	**29**	40
Customer refund provision	**180**	-
	518	389

B. SIGNIFICANT MOVEMENTS DURING THE PERIOD

During the current half year IAG recognised a gross provision of $180 million for customer refunds, interest attributable to those refunds and the cost of administering the associated remediation program. This relates to a specific multi-year pricing issue identified by IAG where discounts were not always applied in full to premiums for all customers who may have been eligible. In establishing this provision, assumptions have been made around the quantum of the premium impact for affected customers, the compound interest attributable to the base premium amount and the costs associated with operating the associated remediation program. A related recovery of $30 million has been recognised from IAG's whole-of-account quota share arrangements. This recovery has been offset within the reinsurance premium payable balance. The appropriateness of all underlying assumptions will be reviewed as the remediation program progresses and adjustments will be made to the provision where required.

C. RECOGNITION AND MEASUREMENT
The Group recognises provisions when there is a present obligation arising from a past event, an outflow of economic resources is probable, and the amount of the provision can be measured reliably. The amount recognised is the best estimate of the consideration required to settle the present obligation at the reporting date, taking into account the risks and uncertainties surrounding the timing and amount of the obligation.

3. INTERIM DISCLOSURES

SECTION INTRODUCTION
This section includes information that is required to be disclosed in accordance with the interim reporting Accounting Standard (*AASB 134*), Corporations Act and ASX Listing Rules, and which are relevant to understanding the changes in IAG's financial position and performance since the end of the last annual reporting period.

NOTE 3.1 INVESTMENTS

All investments are designated at fair value through profit or loss. Investments are recorded and subsequently remeasured to fair value at each reporting date. Changes in the fair value are recognised as realised or unrealised investment gains or losses in profit or loss. IAG recognises transfers into and transfers out of fair value hierarchy levels (described below) as at the end of the reporting period. Purchases and sales of investments are recognised on a trade date basis, being the date on which a commitment is made to purchase or sell the asset. Transaction costs for purchases of investments are expensed as incurred. Investments are derecognised when the rights to receive future cash flows from the assets have expired, or have been transferred, and substantially all the risks and rewards of ownership have transferred.

The inputs used to determine the fair value for securities recognised under each level of the fair value hierarchy are set out below.

I. Level 1 quoted prices
The fair value is determined by reference to quoted prices (mid-market) in active markets for identical assets and liabilities. For IAG, this category includes government securities and listed equities.

II. Level 2 other observable inputs
The fair value is determined by reference to quoted prices in active markets for similar assets or liabilities or by reference to other significant inputs that are not quoted prices but are based on observable market data, for example interest rate yield curves observable at commonly quoted intervals. For IAG, this category primarily includes corporate and other fixed interest securities where the market is considered to be lacking sufficient depth to be considered active. There have been no significant transfers between Level 1 and Level 2 during the current and prior financial periods.

III. Level 3 unobservable inputs
The fair value is determined using valuation techniques in which a number of the significant inputs are not based on observable market data. Level 3 investments are primarily invested in interest-bearing instruments and unlisted equity held via unlisted trusts. The fair value of these unlisted trusts is based on the net asset value as advised by the external investment manager of these funds who has responsibility for the valuation of the underlying securities. The investment manager may use various valuation techniques in the determination of fair value based on a range of internal, external and third party inputs where available. This category also includes IAG's unlisted equity interest in Bohai Property Insurance Company Limited (Bohai). The fair value of Bohai is supported by comparable industry transaction multiples observed in the local market. During the current financial period, in addition to changes in fair value, movements in level 3 investments included:

- purchases of $94 million (31 December 2018: $253 million) and sales of $8 million (31 December 2018: $133 million) in interest-bearing instruments;
- purchases of $34 million (31 December 2018: $40 million) in unlisted equity with no sales in the current financial period (31 December 2018: nil); and
- there have been no significant transfers between Level 2 and Level 3 during the current and prior financial periods.

The table below separates the total investment balance by hierarchy category:

	LEVEL 1	LEVEL 2	LEVEL 3	TOTAL
	$m	$m	$m	$m
31 December 2019				
Interest-bearing investments	**1,488**	**6,151**	**375**	**8,014**
Equity investments	**950**	**266**	**427**	**1,643**
Other investments	**-**	**290**	**-**	**290**
	2,438	**6,707**	**802**	**9,947**
30 June 2019				
Interest-bearing investments	2,256	6,169	279	8,704
Equity investments	1,051	315	414	1,780
Other investments	-	200	-	200
	3,307	6,684	693	10,684

NOTE 3.2 EQUITY

	31 December 2019 Number of shares in millions	30 June 2019 Number of shares in millions	31 December 2019 $m	30 June 2019 $m
SHARE CAPITAL				
Ordinary shares				
Balance at the beginning of the financial period	**2,311**	2,367	**6,617**	7,082
Capital return and share consolidation, including transaction costs	**-**	(56)	**-**	(465)
Balance at the end of the financial period	**2,311**	2,311	**6,617**	6,617

All ordinary shares on issue are fully paid and have no par value. Ordinary shares entitle the holder to a vote at the general meeting of the Company and to participate in the dividends and the proceeds on winding up of the Company in proportion to the number of, and amounts paid on, the shares held. Dividends, if declared, are subject to there being distributable profits available and not breaching APRA capital adequacy requirements.

NOTE 3.3 EARNINGS PER SHARE

	31 December 2019 cents	31 December 2018 cents
A. REPORTING PERIOD VALUES		
Continuing and discontinued operations		
Basic earnings per ordinary share(1)	**12.28**	21.31
Diluted earnings per ordinary share(2)	**12.16**	20.48
Continuing operations		
Basic earnings per ordinary share(1)	**12.45**	12.49
Diluted earnings per ordinary share(2)	**12.32**	12.39

(1) The basic earnings per ordinary share is determined by dividing the profit or loss attributable to shareholders of the Parent by the weighted average number of shares of the Parent on issue during the reporting period. The treasury shares held in trust are deducted, but earnings attributable to those shares are included.

(2) Diluted earnings per share is determined by dividing the profit or loss attributable to shareholders of the Parent, adjusted for the finance costs of dilutive convertible instruments, by the weighted average number of ordinary shares and dilutive potential ordinary shares, primarily as a result of debt instruments that possess a conversion feature.

	31 December 2019 $m	31 December 2018 $m
B. RECONCILIATION OF EARNINGS USED IN CALCULATING EARNINGS PER SHARE		
Profit attributable to shareholders of the Parent which is used in calculating basic and diluted earnings per share	**283**	500
Finance costs of convertible securities, net of tax	**22**	24
Profit attributable to shareholders of the Parent which is used in calculating diluted earnings per share	**305**	524
Profit from continuing operations attributable to shareholders of the Parent	**287**	293
(Loss)/profit from discontinued operations attributable to shareholders of the Parent	**(4)**	207

	31 December 2019 Number of shares in millions	31 December 2018 Number of shares in millions
C. RECONCILIATION OF WEIGHTED AVERAGE NUMBER OF ORDINARY SHARES USED IN CALCULATING EARNINGS PER SHARE		
Weighted average number of ordinary shares on issue (adjusted for treasury shares held in trust) used in the calculation of basic earnings per share	**2,305**	2,346
Weighted average number of dilutive potential ordinary shares relating to:		
Convertible securities	**198**	208
Unvested share-based remuneration rights supported by treasury shares held in trust	**6**	4
	2,509	2,558

NOTE 3.4 DIVIDENDS

	31 December 2019		31 December 2018	
	Cents per share	**$m**	Cents per share	$m
A. ORDINARY SHARES				
Special dividend paid on 26 November 2018 fully franked based on a tax rate of 30%	-	-	5.5	130
2019 final dividend paid on 30 September 2019 70% franked (31 December 2018: 2018 final dividend fully franked) based on a tax rate of 30%	**20.0**	**462**	20.0	473
		462		603
B. DIVIDEND NOT RECOGNISED AT REPORTING DATE				
2020 interim dividend 70% franked (31 December 2018: 2019 interim dividend fully franked) based on a tax rate of 30% to be paid on 25 March 2020	**10.0**	**231**	12.0	277

C. DIVIDEND REINVESTMENT

A Dividend Reinvestment Plan (DRP) operates which allows eligible shareholders with ordinary shares to elect to receive their dividend entitlement in the form of ordinary shares of the Company. The price of DRP shares is the volume-weighted average share price (VWAP), less a discount if determined by the Directors, calculated over the pricing period (which is at least five trading days) as determined by the Directors for each dividend payment date. A copy of the terms and conditions for the DRP is available at www.iag.com.au/shareholder-centre/dividends/reinvestment.

The DRP for the 2019 final dividend paid on 30 September 2019 was settled with the on-market purchase of 10.5 million shares priced at $7.99 per share (based on a daily VWAP for 10 trading days from 23 August 2019 to 5 September 2019 inclusive, with no discount applied).

NOTE 3.5 DERIVATIVES

	31 December 2019			30 June 2019		
	Notional contract amount	**Fair value asset**	**Fair value liability**	Notional contract amount	Fair value asset	Fair value liability
	$m	**$m**	**$m**	$m	$m	$m
A. REPORTING DATE POSITIONS						
I. Net investment hedges (hedge accounting applied)						
Forward foreign exchange contracts	**918**	**17**	**(11)**	788	4	(5)
II. Investment-related derivatives (derivatives without hedge accounting applied)						
Bond futures	**3,181**	**-**	**-**	2,781	-	-
Share price index futures	**(65)**	**-**	**-**	(144)	-	-
Forward foreign exchange contracts	**4,772**	**75**	**-**	3,845	20	(15)
III. Treasury-related derivatives (derivatives without hedge accounting applied)						
Forward foreign exchange contracts	**916**	**3**	**(1)**	1,033	7	(5)
Interest rate swaps	**536**	**10**	**(2)**	535	11	(2)

B. RECOGNITION AND MEASUREMENT

I. Hedge accounting

The foreign currency exposures arising on translation of net investments in foreign operations are hedged (net investment hedge) using forward exchange contracts and the designation of certain foreign currency borrowings as hedging instruments. The fair value is determined using observable inputs (level 2 in the fair value hierarchy).

II. Derivatives without hedge accounting applied

The fair value of the bond futures, share price index futures and options are measured using a quoted price in an active market (level 1 in the fair value hierarchy), whilst the fair value of the interest rate swaps and forward foreign exchange contracts are determined using observable inputs (level 2 in the fair value hierarchy).

NOTE 3.6 INVESTMENT IN JOINT VENTURE AND ASSOCIATES

Summarised information of interests in material joint venture and associates accounted for on an equity basis is as follows:

	COUNTRY OF INCORPORATION/ FORMATION	PRINCIPAL ACTIVITY	CARRYING VALUE		OWNERSHIP INTEREST	
			31 December 2019	30 June 2019	**31 December 2019**	30 June 2019
			$m	$m	**%**	%
AmGeneral Holdings Berhad (AmGeneral)	Malaysia	Insurance underwriting	**348**	356	**49.00**	49.00
SBI General Insurance Company Limited (SBI General)	India	Insurance underwriting	**-**	172	**-**	26.00
Other			**14**	16		
			362	544		

As at 31 December 2019, IAG's 26% interest in SBI General of $181 million has been reclassified as held for sale. Refer to Note 2.3 for further details.

NOTE 3.7 CONTINGENCIES

As at 31 December 2019, the Group had a contingent liability in respect of the matters outlined below:

- As was communicated in an ASX announcement dated 11 April 2019, a representative proceeding has been filed by Johnson Winter & Slattery in the Federal Court of Australia against IAG subsidiaries, Swann Insurance (Aust) Pty Ltd and Insurance Australia Limited, on behalf of Jones Asirifi Otchere. Given that these proceedings remain at a relatively early stage, it is currently not possible to determine the ultimate impact of this claim, if any, upon IAG. IAG is defending this claim.
- As advised on 24 January 2020, a proactive review of IAG's pricing systems and processes is ongoing. The outcome of this review and the scale of any further costs over and above the customer refund provision recognised during the current half year are presently uncertain.

NOTE 3.8 EVENTS SUBSEQUENT TO REPORTING DATE

As the following matters occurred after reporting date and did not relate to conditions existing at reporting date, no account has been taken of them in the financial statements for the current half year ended 31 December 2019. These include:

- IAG's reported profitability in the second half of the current financial year will include net natural peril claim costs from the major hailstorm event which impacted parts of Melbourne, Canberra and Sydney in mid-January 2020, as well as the heavy rain event in early February 2020. The net pre-tax costs of these events are expected to be capped at $169 million and $135 million respectively, in line with IAG's first and second event MERs under its calendar 2020 catastrophe reinsurance protection.
- The Board determined to pay an interim dividend of 10.0 cents per share, 70% franked. The dividend will be paid on 25 March 2020. The dividend reinvestment plan will operate likely by acquiring shares on-market for participants with no discount applied.

NOTE 3.9 NET TANGIBLE ASSETS

	31 December 2019	30 June 2019
	$	$
Net tangible assets per ordinary share	**1.33**	1.43

Net tangible assets per ordinary share have been determined using the net assets on the balance sheet adjusted for non-controlling interests, intangible assets and goodwill.

DIRECTORS' DECLARATION

In the opinion of the Directors of Insurance Australia Group Limited:

- the financial statements and notes 1 to 3.9 are in accordance with the *Corporations Act 2001* including:
  - giving a true and fair view of the financial position of the Group as at 31 December 2019 and of its performance, as represented by the results of its operations and its cash flows, for the half year ended on that date; and
  - complying with Australian Accounting Standard *AASB 134 Interim Financial Reporting* and the *Corporations Regulations 2001*; and
- there are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable.

Signed at Sydney this 12th day of February 2020 in accordance with a resolution of the Directors.

Peter Harmer
Director

INDEPENDENT AUDITOR'S REVIEW REPORT

TO THE SHAREHOLDERS OF INSURANCE AUSTRALIA GROUP LIMITED

Conclusion

We have reviewed the accompanying half year financial report of Insurance Australia Group Limited.

Based on our review, which is not an audit, we have not become aware of any matter that makes us believe that the half year financial report of Insurance Australia Group Limited is not in accordance with the *Corporations Act 2001*, including:

- giving a true and fair view of the Group's financial position as at 31 December 2019 and of its performance for the half year ended on that date; and
- complying with Australian Accounting Standard *AASB 134 Interim Financial Reporting* and the *Corporations Regulations 2001*.

The half year financial report comprises:

- Consolidated balance sheet as at 31 December 2019;
- Consolidated statement of comprehensive income, Consolidated statement of changes in equity, and Consolidated cash flow statement for the half year ended on that date;
- Notes 1 to 3.9 comprising a summary of significant accounting policies and other explanatory information; and
- The Directors' declaration.

The Group comprises Insurance Australia Group Limited (the Company) and the entities it controlled at the half year's end or from time to time during the half year period.

Responsibilities of the Directors for the half year financial report

The Directors of the Company are responsible for:

- the preparation of the half year financial report that gives a true and fair view in accordance with Australian Accounting Standards and the *Corporations Act 2001*; and
- such internal control as the Directors determine is necessary to enable the preparation of the half year financial report that is free from material misstatement, whether due to fraud or error.

Auditor's responsibility for the review of the half year financial report

Our responsibility is to express a conclusion on the half year financial report based on our review. We conducted our review in accordance with Auditing Standard on Review Engagements *ASRE 2410 Review of a Financial Report Performed by the Independent Auditor of the Entity*, in order to state whether, on the basis of the procedures described, we have become aware of any matter that makes us believe that the half year financial report is not in accordance with the *Corporations Act 2001* including: giving a true and fair view of the Group's financial position as at 31 December 2019 and its performance for the half year ended on that date; and complying with Australian Accounting Standard *AASB 134 Interim Financial Reporting* and the *Corporations Regulations 2001*. As auditor of Insurance Australia Group Limited, *ASRE 2410* requires that we comply with the ethical requirements relevant to the audit of the annual financial report.

A review of a half year financial report consists of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with Australian Auditing Standards and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

In conducting our review, we have complied with the independence requirements of the *Corporations Act 2001*.

KPMG

KPMG

Andrew Yates

Partner

Sydney

12 February 2020

Ian Moyser

Partner