CFO's review

We are pursuing disciplined management and allocation of capital where we see opportunities to support our operations and deliver on our core business objectives to make you safer on the road, in your home and at work.

Nick Hawkins
Chief Financial Officer

During the year, we continued to invest in simplifying the business, and we made some modest capital allocations into adjacencies – ventures and businesses related to our general insurance business.

In June 2019, we bought a 51% stake in Carbar, a digital car trading platform that caters to the growing appetite for alternative forms of vehicle ownership and gives us an opportunity to design complementary forms of insurance.

We also made a small investment in a joint venture with the RACV. We are enhancing our motor repair model to improve customer convenience, and to get cars back on the road quickly, with high quality repairs. Our joint venture also involves two repair partners and initially covers six sites in metropolitan centres.

Migrating capital

Within our core general insurance businesses, we are migrating capital back from Asia and returning it to our shareholders.

This year's results include a gain of over $200 million on the sale of our Thailand operations, which was completed at the end of August 2018. We now expect the agreed sales of the Indonesia and Vietnam operations will complete early in the 2020 financial year, and we are exploring a potential sale of all or part of our 26% interest in SBI General in India. We are in advanced discussions with a number of bidders, which may result in one or more transactions being completed.

Quota shares

Over the last few years we have made quota share arrangements a key plank of our capital approach. Quota shares are basically a more efficient use of reinsurance capital. We now have 32.5% of our consolidated business subject to quota share on a whole-of-account basis, comprising:

- the 10-year, 20% arrangement with Berkshire Hathaway commencing 1 July 2015, for losses occurring after that date; and
- three agreements for a combined 12.5% from 1 January 2018, with Munich Re, Swiss Re and Hannover Re. The average initial term of these agreements is in excess of five years.

The respective quota share arrangements deliver similar benefits and financial effects, including:

- reduced earnings volatility, as insurance risk is effectively exchanged for a more stable fee income stream;
- a lower requirement for catastrophe reinsurance and reduced exposure to volatility in associated premium rates; and
- a reduction in IAG's regulatory capital needs.

This financial year, the combined quota share arrangements released around a further $100 million in regulatory capital.

We completed the capital management initiative we announced last year

In August 2018 we announced a $592 million capital management initiative of 25 cents per ordinary share. The initiative acknowledged the fact that our capital position was surplus to our own targeted benchmarks, reflecting cumulative quota share effects, as well as the absence of significant operational demands on our capital and the impact of the sale of the Thailand business.

We completed this initiative on 26 November 2018 after receiving shareholder approval at last year's annual general meeting. Shareholders received a capital return of 19.5 cents per share and a fully franked special dividend of 5.5 cents per share.

At the same time, we completed a share consolidation, equal and proportionate to the capital return, which reduced the number of IAG ordinary shares on issue by approximately 2.4%, while preserving each shareholder's proportional ownership of the company.

Debt restructure

We have continued to restructure our debt arrangements to make them more efficient and effective:

- on 19 March 2019, we redeemed $350 million of subordinated notes on their first issuer call date; and
- on 28 March 2019 we issued $450 million of Tier 2 subordinated debt.

Our $550 million Reset Exchangeable Securities issue has a reset date in December 2019, after which it ceases to be eligible for regulatory capital purposes. Our present intention is to redeem the Reset Exchangeable Securities at the reset date, using the funds from the $450 million subordinated debt issue in March 2019.

Our capital position remains strong

We continue to be strongly capitalised, with regulatory capital of approximately $5 billion at 30 June 2019. At that date, our Common Equity Tier 1 ratio was 1.31, and 1.12 after allowance for payment of the final dividend, against a target benchmark of 0.9-1.1. Our debt to total tangible capitalisation ratio at 30 June 2019 was 36.5%, which was within our targeted 30-40% range.

Our core operating insurance subsidiaries continue to hold 'very strong' 'AA-' ratings from Standard & Poor's. IAG is rated 'A' as a non-operating holding company.