

## **Conference Transcription Questions & Answers**

### **VIENNA INSURANCE GROUP (VIG) Results for the first half 2014 Conference Call**

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| <b>Conference Date:</b>     | <b>August, 26th 2014</b>  |
| <b>Conference Time:</b>     | <b>15:00 Central European Time</b>                              |
| <b>Conference Duration:</b> | <b>Approximately 55 minutes</b>                                 |
| <b>Speakers:</b>            | <b>Martin Simhandl, CFO<br/>Peter Höfinger<br/>Roland Gröll</b> |
| <b>Chairperson:</b>         | <b>Nina Higatzberger</b>  |

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Operator: Ladies and gentlemen. At this time we will begin the question and answer session. Anyone who wishes to ask a question may press star followed by one on their touchtone telephone. If you wish to remove yourself from the question queue you may press star followed by two. If you are using speaker equipment today, please lift the handset before making your selections. Anyone who has a question may press star followed by one at this time. Our first question today comes from the line of Michael Huttner of JP Morgan. Please go ahead.

Michael Huttner: Just to say quickly, two questions. The first one is, you have excellent results coming from the Czech Republic in non-life with 88 percent combined ratio and I just wondered how sustainable that is. I do not know about the market dynamics but maybe you can give a quick feel for that. And then the second, Austria for me because I was a bit optimistic. I was hoping that Italy would turn around already, but for me Austria which includes the Italian branch was a bit disappointing and I just wondered if you can give a feel for the underlying trend in Austria or how quickly Italy will turn around and what the number then could go to in terms of non-life combined ratio. Even a general discussion would be very helpful.

Martin Simhandl: Well the first question concerning Czech Republic will be answered by Peter Höfingler and the second about Austria meaning the Italian branch of Donau then I would answer.

Peter Höfinger: Maybe coming to Czech Republic. If you also look in our history in Czech Republic, we always had an excellent combined ratio there over the last years. We have achieved size and a cost discipline where it is combined with very well diversified portfolio with a quite dominant market position which allows us to achieve this excellent combined ratios. Nevertheless, one has to say this first half-year, as also mentioned in the presentation, was also supported by less natural catastrophe damages/claims. Therefore we are on this excellent combined ratio as we always are; at this time, even a bit better.

Michael Huttner: And how much would you expect the kind of floods or NatCats to cost on average?

Peter Höfinger: Well, if you look on the exposures which we see there in the Czech Republic, we are sometimes in the last year hit not only by floods, it was more also hails which this time we had less. So, I would guess normally you could see 1 to 2 percentage points more in the claims ratio due to NatCats.

Michael Huttner: Brilliant. Thank you very much.

Martin Simhandl: Concerning the Italian business, if I understood you clearly. What you said that you would have expected the turnaround already.

Michael Huttner: (Yes, please).

Martin Simhandl: What I can say here, and this is something that is not new, we have changed our reserving levels significantly in the mid of last year and we are on-going reserving on that level. That means each and every premium coming in is

reserved on that levels. We are building up reserves on the IBNR's side on the level that automatically leads to a negative result. This is the one thing that we have to take into account when we are talking about Italy. The second is, that we have significantly brought down the volume of the business. But we have to take into account that when you are bringing down the volume of the business the written premium is going down faster than the earned premium and this, again, we have to take into account.

Michael Huttner:

And when will the building up of the IBNR end or slow?

Martin Simhandl:

Well, there could be two reasons for changing that. The one is if you have new inflow of business, that is the one. The second is when in the end of the day it works out and this is a period in MTPL which is always some years and it is better to hold the reserves and to have them and to be able to release them then than to have the necessity somewhere in the future to build them up.

Michael Huttner:

I understand. So, I'm sorry I do not want to take too much time, but just as a – I know you do not provide guidance – but if I were to think the Austria combine ratio in the second half. A similar number may be a little bit better but would probably be a reasonable assumption given that Italy is in there.

Martin Simhandl:

Well, if we are talking about combined ratio in Austria we have to take into account that the Austrian business of Wiener Städtische for the time being is delivering a very nice combined ratio which, to a certain extent, always could be also fluctuating. In general, of course, out of

Donau it should be estimated that the combined ratio comes down.

Michael Huttner: Combined ratio of Donau comes down. Brilliant. Excellent. Okay, thank you very much.

Operator: And our next question comes from the line of Vinit Malhotra of Goldman Sachs. Please go ahead.

Vinit Malhotra: Yes, good afternoon. Hi, Vinit from Goldmans. Just two points please. One is on the weather losses. If I just look at the second quarter, the 50-odd million that I can calculate, if you could just provide a bit more guidance because the combined ratio for the second quarter standalone from 98 point does feels a bit too low if you had such a large 5 odd points of weather impact in the discreet second quarter. Are there any reserving moments? I just want some more clarity because I know from speaking to IR that 20 million was a big flooding loss in May, but you still have 30 million more to go. If you could comment on this. The second thing is just on your decision on taking the charge for Hypo. I understand this is mostly in the life unit so today you have taken the charge gross. So is it a fair assumption that once you have more clarity you would then allocate between shareholder and policyholder and so I just wanted to understand that. Thank you.

Martin Simhandl: Maybe I start with the second question to answer and the first question then will be answered by Peter Höfinger. Concerning Hypo it is true that the bigger part of the Hypo bonds is in life. When it comes to the question: What part of that goes to the shareholder and what part to the

policyholder? We have to be aware of the fact that in Austria the fixing of the profit participation is done after the end of the year. That means that when you are preparing your financial statements, some when in January/February then you are deciding the level of profit participation of the last year. Insofar, the question: How much goes to the shareholder and how much to the policyholder? At the end of the day, there you only can give a clear answer maybe in March.

Vinit Malhotra: Sure, but just to be clear, just to understand, is there any special characteristics about this loss which we should know in context of the allocation rules?

Martin Simhandl: No.

Vinit Malhotra: ... there is nothing special yet.

Martin Simhandl: There is nothing special. The only special effect of that is that out of our view this is a legal regulation that most probably is not in line with Austrian Constitution.

Peter Höfinger: Maybe the other question, to weather related claims. I think the main difference between this year and last year is that last year we had one big event and therefore the NatCat covered the re-insurance. NatCat cover was much more supporting us in covering these losses. This year we had a higher frequency on smaller events, so therefore even though the gross impact is significantly lower, we have a quite similar net impact in the second quarter. Nevertheless, if you also look on our development of the claims ratios of the bigger countries, you know the floods were mainly in Serbia, Bosnia Herzegovina and then just

smaller events in the bigger countries. Therefore, the claims ratios in the bigger countries have improved also in the second quarter which was supporting the overall claims ratios.

Vinit Malhotra: So there is no reserve movement of any note in the quarter?

Peter Höfinger: There is no specific reserve movement. No.

Vinit Malhotra: Okay, alright. Thank you.

Operator: And our next question comes from the line of Maciej Wasilewicz. Please go ahead.

Maciej Wasilewicz: I think a couple of my questions were already asked but I have got two left. The first one is just, could you just help me normalise the growth in the topline because there are two impacts that I noticed as you are presenting. Maybe there is more. There is the FX, which you have already said 3.6 percent is underlying ex that. But there is also the STEP product in Poland. What is the underlying growth excluding both of these? Is it about 2.5 percent or is there anything else that would make it any different? The second question, which is already touched on by Michael and I am sorry to return to it, but is there any way I can get a rough idea of what the Italian impact was on that combined ratio in Austria? You said that the Italian combined ratio is above a 100. Can you give us any rough idea of how much premium came from Italy for example or something like that? I am not sure whether or not you can. Thank you.

Martin Simhandl: First, the premium development. We are saying that on a like-for-like basis it is a plus of 3.6 percent and this is including FX; Polish Short-Term Endowment Product and Italian branch business. If we only would take into account the FX it would be roughly 1 percent.

Maciej Wasilewicz: Thank you.

Martin Simhandl: The second question was concerning the Italian branch business?

Maciej Wasilewicz: Yes, I just wanted to understand...

Martin Simhandl: The effect on the combined ratio?

Maciej Wasilewicz: Yes.

Martin Simhandl: Again here, and this we said also the last time and the time before the last time, you always have that problem if you have a situation where you have a branch. Then the question of a proper combined ratio for the branch itself is not easy to be answered because you have cost allocations and things like that and that is the reason we have not calculated that simply.

Maciej Wasilewicz: Okay, well since both my question was very quick, maybe I can ask a third and that is just on capital. You made a very big point in the presentation around S&P giving you an excellent capital rating. I am just wondering if there is any change in message here at all or are we still waiting for the Solvency II to resolve this year before we know whether or not you can do something about capital such as, perhaps, returning a bit of the very large excess that you have seemed to have developed over time?

Martin Simhandl:

When it comes to our capital position, we had done an improvement on our capital structure last year concerning the hybrid. If we do not do anything then the second part of the hybrid will be callable in 2018. So insofar, you can see that there are possibilities when market environment is fitting, that is the one thing. The second thing when it comes to Solvency II. I think we have a rough feeling and the feeling is not bad. What we still have to wait is what kind of figures on what basis different groups will publish. This is still now not extremely foreseeable because the so-called economic capital what some of the groups are calculating and publishing. None of the groups still now has an approval for internal models and some of those economic capital levels are even differing from their Solvency II internal models, but overall my feeling is not bad.

Maciej Wasilewicz:

Thank you.

Operator:

And our next question comes from the line of Sami Taipalus of Berenberg. Please go ahead.

Sami Taipalus:

Yes, hi thank you for taking my question. Two brief questions please. First of all on Poland: a couple of your peers have made some slightly more positive noises about pricing in Poland and non-life pricing in Poland suggesting that there might be some improvement in the second half in 2014. Is that something you would kind of agree with and also on Poland? Some of the peers have also mentioned that there is a rising trend of bodily injury claims or should we say lawyers making use of bodily injury claims in Poland. Is that something you are seeing

as well? Then the second area I wanted to ask about was, you mentioned the strong development you have had in administrative costs which have been impressive. But if I look at your expense ratio in the non-life business, it is roughly unchanged since 2008. So I am wondering what are the moving parts that are offsetting the improvement in admin costs and how should we expect those to develop going forward? Thank you.

Martin Simhandl:

Maybe I start with the second question and Peter is answering the first two sub-questions. Concerning the overall expense ratio in comparison to the admin cost, it is very simple. We are an insurance group that is mainly concentrated on CEE region and in the CEE region the less developed the insurance markets are, the more they are motor markets and it is completely clear that the sales costs in motor, especially in motor MTPL normally are significantly below other business lines. So, in changing the structure of our portfolio and this is something what we are doing since years that we are increasing the non-motor part in our portfolio. We see out of that always quite a substantial increase on the sales costs especially on the commissions. We have to take into account that this normally is a quite solid and profit offering business in non-motor and insofar we think this is the right way.

Peter Höfinger:

We come to Poland, if you look on our figures. We have decided that we will be very disciplined in the motor business. So therefore, we are not following sometimes certain market developments specifically in fleet business. We have reduced premiums in the last months/quarters. Therefore we are also losing a bit of our motor portfolio.

We are compensating it mainly with property business and here in the SME segment where we feel that the price sensitivity is not as high as it is in motor. Most probably maybe other market participants, which had not been so disciplined over the last quarters, will need to return back to hardening their premiums. You see also in our claims ratio in Poland we had an improvement in our claims ratio. This is due to this decision to stay disciplined in the area of the motor business.

Sami Taipalus: And any comment on the bodily injury claims side of things?

Peter Höfing: We see this topic of bodily injuries in Poland, but we also saw it in the past that there can be claims and claims where there is a higher, I will say claims inflation on bodily injuries. But also here, we do believe that we have a quite strict claims management that we are able to cope with this topic.

Sami Taipalus: Okay, thank you.

Operator: And our next question comes from the line of Thomas Neuhold of Kepler Cheuvreux. Please go ahead.

Thomas Neuhold: Yes, good afternoon two questions from my side. Firstly on your re-investment policy. We have seen another decline bond yields in Central Europe. I was wondering if the low interest rate environment assists in the future, how this might impact your re-investment policy. And secondly I was wondering if you can give us an update on your acquisition pipeline. Thank you.

Martin Simhandl:

Okay, maybe I try to answer both. First, re-investment policy, in principle our investment policy is unchanged, yes. This means we want to be invested in good qualities, as you see we have over the years increased the ratio of governments. We have slightly increased the other corporates. We have decreased the financial in the corporate sector. To give you a flavour in Austria, which is Euro and Euro has the lower interest rate, the re-investment yield in the first half-year was roughly 3 percent. Of course, if interests are staying down and spreads are staying down that means in the end of the day that the re-investment rates are going down. Important, and that is the second thing, in such a situation is that you have quite a solid view on asset liability matching. It is completely clear on the one hand that you cannot completely match, especially in life insurance because it is simply a product having also options for the customer to finish the contract. But, on the other hand, you should not be too far away. Last, but not least, in that respect there are some kinds of investments that could support you, on the long end of the duration and this is especially real estate and here especially housing side with quite stable cash flows based on an evaluation out of the consumer price development.

Second, acquisition pipeline, I am sure that you understand that I am not talking what we are looking at for the time being. You can be sure that we are always looking at, that is the first thing and what I can again repeat is that, of course, we think that countries like the Baltics could be interesting. That Poland could be interesting, that maybe Hungary could be interesting and

even Ukraine could be interesting or one or other countries. You can be aware that we are following each and every situation and the big advantage we have is out of our market position we are able to be opportunistic. Maybe this is the right moment that I tell you that our market share in our core markets, the ten core markets we have defined, has now increased from roughly 19 percent to 20 percent. So in the region where we are present not only we have ended up with the result I could tell you, but we have also further improved our market position, as the market leader.

Thomas Neuhold:

Thank you.

Operator:

And our next question comes from the line of Bernd Maurer of RCB. Please go ahead.

Bernd Maurer:

Good afternoon gentlemen, two questions I have. First on Hypo Alpe Adria, how did it come that you exactly impaired 50 percent Why not more, why not less and should we reckon with any further write downs regarding Hypo Hypo Alpe Adria bonds in the coming quarters; that is point one. Point two refers to Ukraine. I know it is a very small market for Vienna Insurance Group, but I wonder how it is relatively holding up that well, just about 10 percent premium declines and still are a profit before tax of 1/1.5 million. I would be interest how is business going on from your point of view and what are your scenarios for the future for your business?

Martin Simhandl:

First, Hypo Alpe Adria, how did we come to the 50 percent? Well, simply we have to somehow to estimate how we estimate the probability that this law will stay in

force or not. It is completely clear that this law will be challenged before the Constitutional Court of Austria and what experts are telling us that the probably that this law will be abolished by the Constitutional Court is significantly higher than 50 percent. The way how we are approaching it is that we think we should be more cautious than we ended up with the 50 percent.

Bernd Maurer: Okay will....

Martin Simhandl: Of course, if, what we do not think, because Constitutional Court would decide that law would stay in force then we would simply have to write down the other 50 percent.

Bernd Maurer: When do you expect the ruling of the Constitutional Court?

Martin Simhandl: I do not think it will last very long. I am not sure if it is this year, but next year – why not?

Bernd Maurer: Do all Austrian insurers will handle Hypo the same way?

Martin Simhandl: I think you have to ask the others.

Bernd Maurer: Okay, but there is no common sense from the, let us say, from the insurance association or whatever?

Martin Simhandl: I would not estimate that those experts we were asking would tell something significantly different to other companies.

Bernd Maurer: I understand, Mr Simhandl.

Martin Simhandl: You will have to be aware, these are very recognised experts.

Bernd Maurer: Yes.

Martin Simhandl: So, insofar, but simply you have to ask the other companies.

Bernd Maurer: I understand.

Martin Simhandl: Concerning Ukraine, maybe to give you two kind of flavours. The one is that we, the premium is going down by 10 percent. If we are looking at the premium development in local currency it is up by more than 15 percent. That is the one thing, it is not going down it is going up. Second, when we look at the result, what negatively impacts the result is that we have a devaluation in the Hrywnja (UAH) and if you have such an effect then you have a negative impact on the spare parts prices, which influences especially the casco insurance result. Normally this is not a long time effect, so it should come back. That is the one thing, the second thing concerning what is going on in East of Ukraine maybe sometimes it is an advantage which out from the view of three years before maybe was not that advantage for us as we were not that strong in the East of Ukraine.

Bernd Maurer: Okay, thank you.

Operator: And our next question comes from the line of Ralph Hebgen of KBW. Please go ahead.

Ralph Hebgen: Yes, hi Ralph Hebgen from KBW in London. Hi, just a few things more on the Hypo if I may. First, what was the coupon payment attached to the sub-debt issue of Hypo. Second, I understand that your total exposure to debt issuance by Hypo is higher than the EUR50 million. I believe it is about EUR100 million. How much do you think

is the risk that other debt issued by the bank would have to be written down by the bank as well? Then, just a general operational view on rates developments in P&C, if you could just basically outline what you saw as a rate development in your various market in P&C? Thank you very much.

Martin Simhandl:

Concerning Hypo I will try to answer and the second question maybe Peter will try to answer. First, the interest rates of those bonds being affected are between 4 and 5 percent, which in fact at the time when they were issued and that was the time when we were buying that, that was nearly the same as a senior bond. Because, the main reason for the pricing was not the quality of the issuer, but the quality of that it was a guarantee or a warrantee from the Region of Carinthia. It is a very specific situation that the Austrian Parliament at the end of the day has decided to, so to say, to declare those warranties to be null and void. This is something that never has happened before and me, personally, I would estimate that it will not be extended. I think it would not be in the favour of this Republic. And insofar, I do not think that there is a further threat for other papers. The other papers are, some of them being, again, guaranteed by or warrantied by the Region of Carinthia and some of them being guaranteed by the Republic of Austria itself. No papers having simply senior completely unsecured or other completely unsecured. Yes, that is the situation concerning Hypo, but I have to admit that I would not have thought that it could happen what happened. Maybe the second question will be answered by Peter.

Peter Höfinger:

Maybe, just mentioning some of our main markets. Clearly, if you look Austria, Austria is quite stable what concerns the pricing. If you look to Czech Republic, Czech Republic still what we see is pressure on the motor pricing. Nevertheless, and this is maybe true for older markets where we see pressure on motor pricing. We do not see anymore so much competitors which are willing to price below their technical costs. Even though there is a pricing pressure, I would say that people are willing to spend just for winning market share this tendency we do not see currently so significantly as we maybe saw it sometimes in the past. You also know that in Romania where specifically we had this issue with a local competitor. This local competitor is now under State administration. So also this is supporting that there are more economically decision in the pricing of the competition, which is allowing us to benefit then there from this situation.

Furthermore, what we see that in a situation like this, again, our multi brand strategy which allows us to have a multi-distribution approach is a significant advantage. Because it allows us having very specific pricing for the specific segments within a country and therefore somehow better balanced the price sensitivity in the motor business, than maybe some of our competitors with a single brand and maybe not such a well elaborated multi-brand approach. Mentioned was already Poland where we see still the pricing pressure in motor, specifically fleet business where we have decided to keep our discipline and moving and compensating this with other segments

where we are currently quite successful and growing quite attractively.

Also if you look to Slovakia, Slovakia there is still price pressure on motor, but it is not further going down. What we are also able throughout the region is to win corporate business. Corporate business locally, where we on the one side we have program policies, organised throughout Vienna and then issuing policies locally. So, there is a certain demand and willingness by clients to, again, have local issued policies, local claims handling, local wordings and then maybe what has been some years ago more in fashion to have freedom of service policies in these various countries. Where maybe some of the people have realised that service which they get; tax issues related to it; administration issues between head office of these people with the local companies is not worthwhile to get a capacity from somewhere outside the region. So maybe this is a short overview how we see pricing.

Ralph Hebgen: Thank you very much, can I just have one follow-up which is, again, on the Hypo bonds. Just to confirm I understand or I believe the coupon payment is now no longer continuing.

Martin Simhandl: This is true.

Ralph Hebgen: Okay, thank you very much.

Operator: Ladies and gentlemen, as a reminder if you would like to ask a question, please press the star followed by one on your touchtone telephone and our next question is a

follow-up question from the line of Michael Huttner of JP Morgan. Please go head.

Michael Huttner: Thank you so much. I am sure the question asked in a better way just, I probably missed the answer, but given what is a strong recovery of profits and you cite the strong capital and shareholders' equity is up. I mean all the indicators are positive. Can we expect a nice rise in the dividend as well or is it too early to talk about that?

Martin Simhandl: Dividends we are always talking about when we have a result of the year.

Michael Huttner: Okay, that is fair enough. Thank you.

Operator: And our next question is also a follow-up question from the line of Bernd Maurer of RCB. Please go ahead.

Bernd Maurer: Thanks for taking me again. I want to come back on Romania please. Mr Höfinger I think you mentioned before that the competitive environment is now improving with your main trouble-maker under State control and you stated some increasing competitive or let us say economic rational. However, in first half the combined ratio is still significantly above 100, you are around the breakeven level. How long do you think it takes that you earn money from the insurance business? That Romania is not only stabilising at the low level but that we all can see some improvements? That you return to profitability? Some nice profits there in the combined ratio of visibly below 100?

Martin Simhandl: I understand your question. I will answer it in the following way. What we see for the time being, on the one hand, is some improvement on the market conditions. On the other

hand, as you know, we have elaborated a lot on the structure of our business et cetera. We have to see on the other hand by accepting that our premium volume has shrunk significantly although we did a lot of cost measures we had to accept also an increasing cost ratio. It makes it not that easy to bring a very short-term down the combined ratio in the way we all would like. So it I think it depends from different developments. The one is; how is the market itself going on? Is the market more and more becoming, so to say, rational. There are some signs, but I'm very cautious when it comes to Romania when I look back what I would have said three years ago and insofar I am cautious.

The second question is, under what conditions and when again, we come in a situation that we have not further decreased our business and then in comparison and in combination with that what can we do again to improve our cost ratio. These three items together will be very important when it comes to further positive developments of combined ratio.

Bernd Maurer:

Alright, thanks a lot.