



VIENNA INSURANCE GROUP (VIG)

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Conference Call Q&A-Session

Transcription

Speakers:

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Martin Simhandl, CFO
Peter Höfinger
Roland Gröll
Judith Havasi**

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Elisabeth Stadler With this, I would like to conclude the presentation and we are ready to take your questions.

Operator Anyone who has a question may press star followed by one at this time. One moment for the first question, please. The first question comes from the line of Youdish Chicooree of Autonomous Research. Please go ahead.

Youdish Chicooree Good afternoon, everyone. I've got three questions please. Firstly, it's really just to clarify your earnings guidance. I mean, you have increased your pre-tax profit guidance it seems, thanks to a change in the accounting treatment of Austrian housing societies. I mean, I'm wondering just for the fact that more than 95% of the income from these societies is reversed out of minority interest, your tax ratio of 22 and hybrid interest I get to a net earnings for investors in the region of 270 million, which is basically flat on the 2016 level. Could you just clarify whether my thinking is right on this?

And then, secondly, could you update us on your Solvency II position at the end of 2016 and, if possible, an update as of now for example?

And then, finally, could you tell us a bit more about the motivations of expanding in reinsurance given the pricing outlook and the fact that profits are high because of the lack of NatCat activity at the moment. Thank you.

Martin Simhandl To your first question concerning the impact of the housing societies, you should estimate that the impact of the housing societies over that time in comparison to last year is a bit more than doubled. This does not lead, as you think, to a negative or flat development, it leads to a slightly increasing development of the net earnings over the next years and I think the main thing that we want to give to you is that this is the case although we see further decreases on the investment income over the coming years. That means we want to overcompensate these decreases on the technical side.

Youdish Chicooree Sorry, just to clarify on that point, I mean if I annualise what you recognise in 2016, I get just under 19 million in terms of income from housing societies. So, roughly how much of that do you actually retain at a net earnings level?

Martin Simhandl This would be the case if you would do it on a proportional basis but the housing societies over the year are not always, so to say, in line. The last four quarters are not the same like the second and the

first... sorry, not quarters, months of the year. So, overall, you should expect the housing societies have an impact overall somewhere between 60 and 70 million totally instead of roughly 30 million as it was last year.

Youdish Chicooree

Sorry. That's at a pre-tax level, right?

Martin Simhandl

The housing societies do not pay any tax. There is no tax effect on the one side and on the other side. This is what the effect on the earnings before taxes is. What you want to hear surely, a part from that is what the effect on the side of the earnings is. This is roughly €2 million per year.

Youdish Chicooree

Okay, fine. Thank you.

Elisabeth Stadler

Concerning Solvency II, we have not finalised the calculations yet. I hand over to Judith who is responsible for this topic in our Board.

Judith Havasi

Regarding Solvency II figures, we are still in the auditing process, but we don't expect big changes in comparison to the day one figures on the VIG Group level and on the level of the Holding VIG.

Elisabeth Stadler

And reinsurance, Peter?

Peter Hofinger

We have established a VIG reinsurance company 2008 in Prague. We have now a very functioning platform there. We currently have around €360 million on premium and it makes sense to cautiously expand our geographical area, not just in Central and Eastern Europe but also in certain markets in Western Europe, with the clear focus on local primary insurance companies, original primary insurance companies, where we believe that we can offer in certain niches profitable business for us. We are also running quite a cost advantage in our reinsurance company, being based on Prague, so therefore expanding it is just using a platform which is well established here and looking for opportunities.

Operator

The next question comes from the line of Michael Huttner of JP Morgan. Please go ahead.

Michael Huttner

Fantastic. Thank you. I suppose I'm asking part of the questions that my colleague so ably asked. So, on the profit you've reported today, the 405 million, I just wondered if you can say what the underlying figure is. There's a lot of noise in the figures. You know, there's the penalty or the agreement you paid in Poland, there's some start up or write offs in the Baltic area. I just wondered if we could have a clean starting figure to

compare... to judge better the progress to your target in 2019?

The other is on the societies. I didn't quite understand... I think I understood that it's stable but I don't know what the starting figures are. I'm really sorry. On the housing associations, I also understood that the net profit figure retained from them is 2 million out of the 29 odd million, which is a pre-tax.

And then if I look at your comment, or your target to offset the fall of investment income with better technical. So, I have to make some assumptions about what the underlying starting point is. It seems like the investment income you're kind of thinking that might drop 100 million, so from roughly a billion now, to 900 million offset by better technical, that's 100 million, then the other moving parts are pretty much the non-repeat. I'm assuming on the one offs which are in, in today's figures, but that's kind of my assumption but any help on all this would be great. And, yes, a great dividend. Thank you.

Martin Simhandl

I try to explain it in a way that it's better understandable. We have seen positive and negative extraordinary impacts in 2016. The positive were on the HETA. As you know, we have written down these papers, I think in 2014, and we have written down the senior bonds to 50% and the subordinated bonds to zero. Out of that the investment income positively was impacted by 40 million.

On the other hand, we have the negative impact on that agreements we had in Poland of 25 million and of course, you can count some 5 million or even a bit more in the start-up costs in the Baltics. You have to be aware that they will not fully disappear immediately, they will decline over the next years but they will not automatically fully disappear already in the next year.

So, what you see is... and that's what I normally have said, somehow the positive and the negative effects of the last year have equalised themselves as a starting point.

On the other hand, when it comes to the housing societies, to make it very clear, we have shown it I think very detailed. We have some 2 million net effect out of the housing societies in last year. This is the same what we expect also for the next and the coming years. We have seen some 29 million minority effects that will increase, as I said, to a volume of we estimate between 60 and 70 million, and if you count that together, then you see clear the starting point.

When it comes to the investment and you're saying over this period a decrease of 100 million, this is something what I would subscribe it could be even a bit more.

Michael Huttner

Brilliant. Also very helpful. Thank you.

Operator

The next question comes from the line of Michele Ballatore of KBW. Please go ahead.

Michele Ballatore

Good afternoon. I have four questions. So, the first... there are actually two regarding the combined ratios: So, the combined ratio in 4Q was very good. I mean, it was around 95.5% and I think on expense ratio we're okay, but on the loss ratio there was a strong improvement, and I want to know what drove this improvement in terms of lower large claims, lower Nat Cats or reserve release.

And also related to that, the future combined ratio, so your target in the region of 95% up to 2019, what will drive these. I mean, will it be lower expenses or a better loss ratio you're expecting in Austria or in CEE so what are the dynamics here? So, this is the first.

So, the second question regards the premiums growth. I would like to know more the dynamics behind this increase in volume. I mean, we are not talking about a large number, we're talking about 450 million if I'm correct compared to 2016. So, in terms of this split between life, P&C and health. What do you expect in the three segments? How will they evolve in the next three years? So, this is the second question.

The third question is about the dividend. So, you increased the dividend by 20 cents. Your target is at least 30%, but my question is why do you have such a, let's say, conservative and prudent target? Do you expect the growth in CEE or in other regions to require lots of capital? So, why is this distribution policy so conservative compared also to your peers? So, this is the third question.

And the fourth questions regards if you are planning to do an investor day to show the business plan in 2017? It would be very helpful or we are happy with four slides in your presentation, and that's it. So, these are all my questions. Thank you.

Elisabeth Stadler

Okay, so we will start with point four, the investor day. We will pick up your idea and think about this, yes? We will give you information at the right time.

Michele Ballatore

Yes.

Elisabeth Stadler

Concerning combined ratio and especially future combined ratio, you know we have this target of 95% already in the last year. We set up some measures, some activities. Our plan is to have both, on the one side, lower expenses and on the other side, of course, better loss ratios. So, we have set up a lot of measures like anti-fraud, closed file review, we talked about this a lot and on the other side we have some effects looking deeper into the costs, having some common back office, trying to find some synergies. We even mentioned if its cost efficient, we even would like to do some mergers. We have acquired some smaller companies where we are thinking how to include them, how to save costs, how to reach effects of scale.

Then the premium growth dynamics, we can't split it at the moment between life, property and casualty and health. Of course, we have behind the planning in all our countries together with all our companies to have the different health plans. We have five countries where we want to expand in health insurance. We have told you that we want to expand the reinsurance business, although this leads to an increase in premium and, of course, we have some other activities. We want to increase the bank assurance activities. We see a lot of potential there. Maybe you know most of existing insurance contracts being sold through the bank counters or through the banks selling channel are at the moment life and accident insurance. We would like to expand this, especially to non-life products and health insurance, and we have the bank cooperation with Erste Bank in ten countries, so there is a lot of potential not only in Austria but also in a lot of the CEE countries.

Concerning combined ratio...

Peter Hofinger

Maybe to the question to the fourth quarter, more or less you have also the answer in your question. We had a bit... this year a different distribution of our claims, of our middle to large claims. We had a higher frequency of mid and large claims in the first half and we had a significant lower in the fourth quarter. Also, there was a total absence of Nat Cat losses in the fourth quarter which we had in the fourth quarter 2015. These are the main effects.

Michele Ballatore

Thank you.

Elisabeth Stadler

Yes, and the dividend policy, Martin will try to explain it.

Martin Simhandl

First, as you know, our dividend policy is a long term unchanged policy and what is the idea behind? I think what I tried already to elaborate when I did the presentation of the quarterlies it seems that our premium volume is flat. In fact, if you look behind it and

you exclude the single premium business, we have in comparison to other groups I would say a quite dynamic premium development. This is the one thing.

The second thing is, and this is also from a solvency perspective, of course to be estimated is that our life portfolios in the CEE region, our traditional life portfolios are rather young ones and that means that the asset portfolios automatically are growing over time. This, of course, needs also additional equity and, last but not least, apart from the organic growth, and we see the organic growth, we see it rather again not so much in the single premium business which may be at minimum for this year and further go down. Apart from that, we see also some possible acquisitions. As you know, we have mid-term targets in some of the countries and that could raise some opportunities if we think, for example, in Poland.

What I also want to stress, and I didn't point it out in the presentation, when you look at organic growth in Croatia, for example, and Hungary where we have closed the gap to the 10% market share, in the same time we have improved the combined ratio. I think that's exactly the way we want to go.

Michele Ballatore

Thank you.

Operator

The next question comes from the line of Daniel Bischof of Baader Helvea. Please go ahead.

Daniel Bischof

Yes, thank you. Good afternoon. Two questions remaining from my side. The first one on the Austrian non-life business, I understand that there is still a drag from the Italian business, both on the cost and loss ratio side in 2016. What sort of impact will you expect for this year here?

And then, secondly, could you clarify the situation in Romania? So, on the slide it says that the maximum tariffs are now below your average premium. I mean, how do you react to this and how would you expect that this issue will be resolved in six months' time?

Elisabeth Stadler

Thank you. Concerning Austria, the non-life business and the question looking how deep Italy is involved in the figures on the cost ratio and loss ratio, of course this is still the case. Our business is really very minimised there at the moment. We run a business there with a premium of 15 million of euros and I would say the loss ratio is for the existing business very okay but we still have some old claims. As you know, in Italy it takes three to five years until you will have handled all the old

claims. There are a lot of court cases and therefore the cost ratio in Italy is still affecting the Austrian cost ratio.

Concerning Romania, we had a lot of discussions with the Romanian authorities and Roland will give you the deeper insight.

Roland Gröll

If you look at the situation in Romania first of all I think we are quite happy that it was possible despite not the easiest environment to show a profit of about €10 million once again. Nevertheless, at the end of this year we were affected by these capped tariffs. As you've mentioned, it's planned that it will last till the end of May, after the six-month period. Nobody can say that seriously... because it's a political decision, if the situation will be prolonged or not. There are signs in the one, but also in the other direction, so it's simply speculation if I will tell you yes or no.

We are prepared and we did a lot of preparation work not to be hit too strong by these capped tariffs. Generally spoken, I think if it will end in May this year, results in Romania should not be affected tremendously. If the situation will be prolonged, we'll have to reconsider our MTPL strategy in Romania. But it's simply too early to give a concrete answer.

Daniel Bischof

But maybe a general question that... I mean, whenever it seems that there is a silver line, the next issue arises in Romania, and I think economically you have been loss making for the last six years in a row now, and I don't know how you think about this business there and, I mean, whether it makes sense to be in such a difficult market?

Roland Gröll

I think it's never one of our positive stories if we discuss Romania, but we did also in 2015 and 2014 profits there, not high ones but profits. And if you look at the development in 2016 the 11 million are by far not satisfying but it's also kind of a starting point for us.

And, of course, it depends how the market behave and how the legal environment will develop. But nevertheless, if you look at the insurance penetration in Romania, we have €100 per capita. If you do not want to compare with the European Union 15 or Austria, but even if you compare with the Czech Republic, for example, there is 5x difference, so a huge potential there.

And the MTPL is important but it's not the only business line in Romania. We're also very strong in motor hull/casco insurance, also in non-motor. We see high potential in health and also a further improvement with

our partner, Erste Bank in Romania, BCR Bank, so there are also huge potentials not only negative impacts. MTPL is the bad story but there are also a lot of good stories available in Romania.

Daniel Bischof

Okay. Thank you very much.

Operator

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

Sami Taipalus

Good afternoon, everyone. Just a couple of questions from my side. So, the first one is on your guidance... sorry, not your guidance, your targets I suppose. I was just wondering what the assumptions are underlying the plan? Do you assume any M&A in these targets and what sort of reinvestment rates do you actually have in the targets?

The second question is about distribution and you're talking quite a lot about digitisation and similar things. I'm wondering if you're anticipating any changes to your distribution structure, I guess particularly in Austria? And then just a couple of number things, I wanted to check: the first one is are you anticipating any investment costs in relation to this agenda 2020, and also could you just give us what the net catastrophe losses were in 2016? Thank you.

Elisabeth Stadler

Let me start with the question concerning the distribution structure in Austria. I think it's quite clear that Austria is not so well developed in digitisation and direct sales as some of the CEE countries and countries in Western Europe. There is still only a really very, very small portion of new contracts being brought through the direct sales channel. But, nevertheless, we are working on this idea. We are working on this idea together with our bank partner. You may have heard that we work together with Erste Bank and that we have installed a project of finding new ideas, finding better cooperation and, of course, which should lead to more business and more profit for both sides. And as our bank partner, Erste Bank is doing a lot of direct activities with their clients, we try to involve us or the Austrian companies and to try to sell the insurance contracts maybe in some cases direct too.

On the other hand, you know that we have very wide distribution channel in Austria. We have a lot of tied agents in our companies. This is the model which still works in Austria very, very well. I would say that the majority of our clients like to inform themselves via internet or via some prospects or electronically but many of them like to conclude their contracts face to face with their insurance agents.

Then we are quite a strong broker market in Austria. Brokers are combining themselves to bigger broker networks, so I think we will still have these channels in Austria in a quite big amount too. And, which is very important, is the banking channel in Austria. Already more than 50% of life insurance contracts are brought through this channel and all the banks and the insurance partners try to extend these channels also to other products especially non-life products.

So, I think we will see a slight change in the Austrian distribution situation but we mainly will see the tied agents, the independent agents, the brokers, the banks, and in a small part the direct sales channel, which is going to increase but I would say quite slowly.

Concerning guidance...

Martin Simhandl

Well, you asked about M&A and the reinvestment rates, we do not plan M&A's into our planning. We would only give it if it is something that we have already concluded because we don't think it's appropriate to estimate something what you cannot really foresee. Of course, we are always prepared to enter into negotiations and there is always something on the radar, but in the end of the day if you would include it into the planning, you would have a pressure to maybe do some acquisitions that are not worth to be done, and that we do not want to have.

Secondly, when it comes to reinvestment rates, we clearly have to differentiate between the countries. We have, on the one hand, the Euro Zone countries, like Austria, Slovakia. We have Czech which is from an interest rate sometimes even below the Euro Zone and here the reinvestment rate on the fixed income side are somewhere between 1 and 2%. That depends also on life and non-life because non-life has a shorter duration.

When it comes to other countries like Poland or Romania, you should estimate it's near the local government yield that we are planning because this is the biggest part of the capital markets in these countries.

What I also want to stress is the fact that the part of the new investment goes, especially in Austria, into real estate. Real estate, as you know, we account at cost. That means that we have the ordinary depreciation to be included and that means in the starting point of such investments, you have rather low yields. On the other hand, over time this leads to significant hidden reserves and you can see that also and you will see it again in the notes. Already last year you saw 900 million of that

real estate hidden reserves and be sure they have increased.

Sami Taipalus Okay. Can I just follow up on that very briefly? Do you assume that reinvestment rates stay where they are now in your earnings outlook?

Martin Simhandl Yes.

Sami Taipalus Okay. So, you don't presume any pick up or anything like that?

Martin Simhandl In fact, if I would really be able to estimate something for the future, be sure I wouldn't be here. Then I would be a very rich man. I think nobody can really predict where interest rates are going. So, in our view the most appropriate way to approach that is that you think that the current situation more or less stays. Of course, it could change over the next years. There are some indications for that but nobody really knows.

Peter Höfingler And the other question, whether related claims, the total net losses for 2016 is 112 million.

Sami Taipalus And the investment costs, shall we anticipate anything in terms of this programme?

Elisabeth Stadler Of course we will do some investments, maybe buy some tools or maybe have some advisers or something like this, but it's already included in our existing prognosis and we have business plans. We only do investments if we have a business plan and see that they are compensated on the other side by additional earnings out of these projects.

Sami Taipalus Okay, great. Thank you.

Operator The next question comes from the line of Michael Haid of Commerzbank. Please go ahead.

Michael Haid Thank you very much. Good afternoon. I have to come back, first of all, on the implementation costs of the Agenda 2020. Do you think it is sufficient to invest 100 million per annum into IT and only 50 million of that into digitisation? And are all of these investments expensed or do you plan to capitalise some investments?

The second question is on Poland. You highlighted that Poland is a difficult market. Some insurers and competitors of yours indicate that in motor insurance in Poland we see currently significant hardening of rates. I wonder what your view is on that.

And then a third question is on reinsurance. I understand that you plan the expansion into Central

and Eastern Europe, Austria, Germany, other Western European countries now. In reinsurance it is never a good idea to have any volume target, but I wonder what volume do you have in mind when you say expanding in reinsurance? How much capital would you be willing to deploy to reinsurance? And do you plan to show it as a separate segment?

Peter Höfinger

Maybe, I should start with the last two questions. Coming to Poland, right, we see a hardening of the market and we are very happy about it, we are profiting, we are growing in the motor segment out of the increase of the tariffs. Significant hardening is maybe too much but let's see. If our competition is seeing it, maybe then the significance will increase.

Coming to reinsurance I fully agree with what you have said. One should take care to give volume targets. In reinsurance volume can be generated quite quickly. Very clearly there is also much more of a profit target. There are certain scenarios and ideas of what could be appropriate opportunities for generating volumes. For the time being it is not planned to have reinsurance as an own segment. I think there are some years to come when the importance for the Group would become bigger.

Roland Gröll

According your question IT investments. Thanks for the question because obviously there is a misunderstanding. We plan to invest next year roughly yearly 100 million volume but out of that not 15 million but roughly 50% of this planned investment goes into digitisation.

Michael Haid

5.0.yes? Do you capitalise some of this investment or is this all expensed?

Roland Gröll

The first its investment and then expences, so we plan to capitalise it with a depreciation period of between five and ten years.

Michael Haid

Okay. Thank you very much.

Roland Gröll

...that what we capitalise is capitalised in our plans. That's in the plan that we have to show immediately as expense is also in our plans included in our expenses. So, out of this plan and this planned investments, no surprises profit wise or expense wise.

Michael Haid

Okay. Thank you very much.

Operator

The next question comes from the line of Frank Kopfinger of Deutsche Bank. Please go ahead.

Frank Kopfinger Yes. Good afternoon, everybody. I have one remaining question and I have to apologise, I would like to come back to your earnings target. The 450 to 470 million, they point to an improvement of 60 million. Then also you suggested that you have to offset the decline in the running yield which could be more than 100 million, so you have to bridge a gap of more than 160 million.

My understanding is that from the housing societies, from the accounting on the fully consolidated basis, you could bridge some 30 to 40 million and the remaining 120 million then accordingly would be then bridged by this growth initiatives or cost measures. Could you shed some more light on these 120 million gap, where it's coming from, is it mainly from growth, profitability or also put some more data to the initiatives that you pointed at, be it the health insurance or the bank insurance part?

Martin Simhandl Well, as you said it, it comes from all of that, yes, and of course we have plans behind but in the end of the day what exactly comes from what part is not so easy to be estimated and on the way, and we are talking here about three years, if the one part does not come, you put more efforts on the other side.

So, it's coming from the claims side, it's coming from where we have some initiatives, it's coming from the underwriting side, it's coming from the cost side, it's coming from profitable new business in life.

Frank Kopfinger Maybe on the other way, could you say how much or how profitable your bank assurance is, as of today?

Roland Gröll To answer this generally is not so easy, but if you look at the big picture our main bank partner, Erste Bank, which we work together in six countries, they bring us a premium volume of €1.3 billion and a profit of roughly €100 million. So, if I compare it with the results of other life insurance competitors, it looks quite profitable for us.

Frank Kopfinger Okay, thanks.

Operator The next question comes from the line of Bernd Maurer of RCB. Please go ahead.

Bernd Maurer Good afternoon. My question first is the Czech Republic. In the third quarter in the conference call following your third quarter results, you stated that competition is worsening in the Czech Republic, the environment is fine, the competition is worsening, and that you rather do not expect that a very good combined ratio in the low 90s could be defended in the coming years. In 4Q we saw still an excellent combined ratio in

the Czech Republic of below 90%. My question is... I ask you to give a bit of an update on the competitive situation in the Czech Republic, as it is your most important CEE market. Did anything change following your comments in November to the positive, to the negative, an update please here?

Elisabeth Stadler

Yes, you are quite right. Competition is worsening in the Czech Republic, that's quite clear. We had I would say some summer storms and some bad weather, claims in the second and in the third quarter, and the fourth quarter was really an excellent one, so they could manage to show again an excellent combined ratio.

We see, or we have a little bit the same fears for the next year and we are quiet exactly observing the situation at the moment.

Bernd Maurer

So, to sum up it should remain quite good but perhaps now that the excellent levels are what we observed in 2016 and in the years before?

Elisabeth Stadler

Absolutely correct. Yes, they had really excellent combined ratios and maybe it could be a little bit worsening but it still will be very, very good.

Bernd Maurer

Thank you very much.

Nina Higatzberger

It seems that there are no further questions and I would like to end today's conference. Thank you for your interest and questions and goodbye.