ICICI Lombard General Insurance Limited

Q1 FY2020 Earnings Conference Call

July 19, 2019

Management: MR. BHARGAV DASGUPTA – MANAGING DIRECTOR & CEO

MR. GOPAL BALACHANDRAN – CHIEF FINANCIAL OFFICER

Moderator: Good evening, ladies and gentlemen. A very warm welcome to the ICICI Lombard General Insurance Company Limited's Q1 FY2020 earnings conference call.

From the management, we have with us today Mr. Bhargav Dasgupta – MD & CEO of the company and Mr. Gopal Balachandran – CFO.

As a reminder, all participant lines will be in listen-only mode. And there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal the operator by pressing * then 0 on your touchtone phone.

I would now like to hand the conference over to Mr. Bhargav Dasgupta – MD & CEO, ICICI Lombard General Insurance Limited. Thank you and over to you, sir.

Bhargav Dasgupta: Thank you and good evening, everybody. I welcome you to the earnings conference call of ICICI Lombard General Insurance Company Limited for Q1 FY2020. I would like to give you a brief overview of the recently ended quarter, post which are our CFO, Mr. Gopal Balachandran will share the financial performance of the Company.

The General Insurance Industry registered a growth of 9.9% in Q1 FY2020 over Q1 FY2019 with the industry GDPI moving up to ₹ 410.64 billion in Q1 FY2020 from ₹ 373.60 billion in Q1 FY2019, as per IRDAI monthly report. Excluding the crop segment, the General Insurance industry grew at 13.6% to ₹ 391.08 million in Q1 FY2020 as compared to ₹ 344.33 billion in Q1 FY2019 as per GI Council. The combined ratio of the industry was 117.2% in FY2019 as compared 109.9 in FY2018, based on available information. Further, the overall combined ratio of the private multi-line general insurance was 103.6% in FY2019, as compared 101.9% in FY2018 as per GI Council and public disclosures.

Some of the key developments of the GI industry during the recently concluded quarter include:

The Authority had issued a circular on March 28, 2019, notifying the insurance companies to continue to charge the prevailing rates of motor third party liability insurance cover until further order is issued. The Authority has now issued a circular to notify the revised premium rates applicable for FY2019-2020 which is effective from June 16, 2019. Consequently, this has had an impact on our profitability in the current quarter.

The Authority issued a circular wherein the insurers shall make available standalone annual own damage covers effective September 1, 2019. This circular is applicable for both old and new cars and two-wheelers, provided the motor third party cover is already in existence or taken simultaneously. From the standpoint of policyholders, it is a positive development since it gives options, liberty and convenience to buy standalone own damage cover from its own choice of insurers. From our perspective, we see this development as a potential opportunity to gain customers, given our reputation in terms of claims settlement and large network of cashless garages.

Speaking about the company's performance, the GDPI of the company for Q1 FY2020 de-grew by 7.6%. Excluding crop segment the GDPI growth rate was 17.7%, which was higher than the industry growth rate of 13.6%, excluding the crop for the industry. Our GDPI growth was primarily driven by our focus on preferred segments such as fire, marine, motor, liability and health. Consequent to the increase in minimum prescribed rates for certain occupancies under fire segments, this segment registered a robust GDPI growth of 67.3% in Q1 FY2020, thereby aiding the GDPI growth of property & casualty segment. As indicated in our results presentation, the overall property and casualty segment grew by 28.0% in Q1 FY2020 over Q1 FY2019.

On the Retail side of business, SME & Agency channel and Health indemnity continued to grow faster and remain our areas of focus. To harness the potential of these segments, we have been expanding our distribution network so as to increase penetration in tier 3 and tier 4 cities. Our individual agents (including POS) were 38,581 as on June 30, 2019 as against 25,646 as against June 30, 2018.

In conclusion, we continue to aim on growing our business by creating long-term value for all the stakeholders through focus on sustained profitability and prudent risk selection. As we look ahead, we remain excited about the growth potential of the industry as well as our business prospects.

I will now request Gopal to take you through the financial numbers for the recently concluded quarter.

Gopal Balachandran: Thanks Bhargav. And Good evening, everybody. I will now give you a brief overview on the financial performance of the company for the quarter ended June 30, 2019. We have put up the results presentation on our website, you can access it as we walk you through the performance numbers.

The Gross Direct Premium Income (GDPI) of the Company stood at ₹ 34.87 billion in Q1 FY2020 as compared to ₹ 37.74 billion in Q1 FY2019, a de-growth of 7.6%. However, excluding the crop segment, our GDPI increased to ₹ 34.88 billion in Q1 FY2020 as compared to ₹ 29.64 billion in Q1 FY2019, registering a growth of 17.7%. This was higher than the industry growth of 13.6%.

On the profitability front, our combined ratio stood at 100.4% in Q1 FY2020 as compared to 98.8% in Q1 FY2019, primarily on account of long term motor policies and losses from cyclone Fani. Combined ratio was 99.7% in Q1 FY2020, excluding the impact of cyclone Fani, which is estimated at ₹ 0.16 billion.

Our investment assets rose to ₹ 237.11 billion at June 30, 2019 as compared to ₹ 222.31 billion at March 31, 2019. Or investment leverage (net of borrowings) was 4.27x at June 30, 2019 post dividend payment and 4.12x before the dividend payment as compared to 4.09x at March 31, 2019. Investment income increased to ₹ 5.27 billion in Q1 FY2020 compared to ₹ 5.07 billion in Q1 FY2019. Our capital gains was lower by 29.6% at ₹ 1.38 billion in Q1 FY2020 compared to ₹ 1.96 billion in Q1 FY2019.

Our profit before tax (PBT) grew by 7.2% to ₹ 4.75 billion in Q1 FY2020, compared to ₹ 4.43 billion in Q1 FY2019 on account of lower capital gains.

Consequently, profit after tax (PAT) grew by 7.1% to ₹ 3.10 billion in Q1 FY2020 compared to ₹ 2.89 billion in Q1 FY2019.

Return on Average Equity (RoAE) was 23.0% in Q1FY2020 as compared to 24.7% in Q1 FY2019.

Solvency ratio was 2.20x at June 30, 2019 as against 2.24x at March 31, 2019, continued to be higher than the minimum regulatory requirement of 1.50x.

As we conclude our address, I would like to summarize that we ended Q1 FY2020 with a diversified product portfolio and healthy financials. The company continues to focus on prudent underwriting while improving its competitive position. We continue to build our distribution with our focus on sustainable growth.

I would like to thank you for attending this conference call and we would be happy to take any questions that you may have.

Moderator: Thank you very much. Ladies and gentlemen, we will now begin the question and answer session. The first question is from the line of Hitesh Gulati from Haitong Securities. Please go ahead.

Hitesh Gulati: Sir, I have a couple of questions. Firstly, what is the advance premium amount, which is coming from long-term motor policies on the balance-sheet? And second, just wanted to understand that given that Opex ratio has increased, is this also because of the fact that acquisition costs are getting built in because growth in motor segments are sort of higher than what it was previously? Just wanted some color on that.

Bhargav Dasgupta: As regards your first question, the amount of advance premium on account of long-term motor policies is ₹ 18.65 billion. To answer your second question relating to the expense ratio, there are a few components which need to be noted. Firstly, consequent to de-focus from the crop segment, the overhead allocation has changed as compared to the previous years. Typically, the fixed costs which gets allocated across business lines based on premium, has now got allocated to other lines. Hence, there is a denominator effect. In addition, the sourcing cost of retail business is much more than crop business. So to that extent the expense ratio for retail business is higher. In addition to the business as usual, we also had a brand campaign in this quarter which forms a part of the expenses this quarter.

Moderator: Thank you. The next question is from the line of Deepika Mundra from J.P. Morgan. Please go ahead.

Deepika Mundra: Sir, firstly on the health segment, we are seeing that the mix is becoming more favourable with the retail portion growing faster. Could you just comment a little bit on the pricing side in terms of both retail and group health? How do you see that trending this year?

Bhargav Dasgupta: Let me start with the group health. We saw a pretty decent price increase last year vis-à-vis the previous year of last year. And that's when we entered the group health segment last year, re-entered and refocused on the group health segment. In the current year, relative to last year we are not seeing considerable price increase, because to some extent it happened last year. So in group health, we are not seeing any further improvement. Having said that, we are not seeing any deterioration either. Accordingly, we are being a bit selective. We are reducing exposure for the accounts in which we not getting substantial price increase and the loss ratio is also high. Similar to last year, we continue to focus on small ticket granular group health business, however the growth number is much lower than what we had last year on that segment.

On the retail side, there are two issues to note. Firstly, there has been a reclassification based on the directions received from the Authority.

So this group retail, which is basically the segment that we sell to individual retail customers, but usually through a partner which could be a bancassurance partner or an NBFC partner. This reflects in the aggregate group numbers. We have given the break up in the presentation that we have put up on our website. And there on the retail health side we have not seen price increase. In fact, on the retail indemnity portfolio, we have not increased prices for about six to seven years now. And we believe it is time for us to increase the pricing, which we haven't done yet. On the retail side there is another segment which is otherwise a very attractive segment. It is with the NBFCs and that segment has continued to underperform in this quarter as well. This is one of the negative impact on the overall health portfolio and has been going on for the last two to three quarters now. We were hopeful that the NBFC business would pick up in Q1 FY2020 but it didn’t. We don't see that happening in the next couple of months at least. On the flip side, the bank performance has now really come back very strongly compared to Q1 FY2019. And that has been doing really well for us. So on balance it's not really a pricing improvement in the retail side, it is more growth in policy volumes that we are seeing.

Deepika Mundra: Understood. And sir, just one more question on the motor OD regulation change, which is going to be effective later in the year. Do you think the unbundling will bring in further impact on pricing to what we have seen already?

Bhargav Dasgupta: It would be difficult to predict. At the moment, we are looking at it as an opportunity. For us, there are certain segments of business i.e. segments based on geographies, usages etc. where we did not like the Motor third party loss ratios. Now, we would have an opportunity of focusing on the own damage segment for such businesses. There are many such markets that we are aware of where the OD loss ratio is very healthy while the TP loss ratio is very adverse. So that is an opportunity that we are looking at.

At the same time, I understand the point that you are making wherein someone who may not have the scale on TP is getting very aggressive or may get very aggressive on the OD side. Having said that, the only caveat or comfort that we have is if we see the own damage loss ratios for the industry at this point, I don't know how much leeway companies have on cutting prices any further. So given our distribution, given our service infrastructure and our brand, we at this point see this as an opportunity. The risk that you are articulating remains, and we will have to see what happens from September onwards.

Moderator: Thank you. The next question is from the line of Shantanu Chakraborty from Edelweiss. Please go ahead.

Shantanu Chakraborty: Thank you for giving out the agent numbers, looks like out of all the non-POS agents that you have at the moment, almost a third have come on board in the last 12 months. So just would like some granular colour on when do you think this investment might start to pay off in terms of revenue acceleration? And what are the segments which could get impacted? I'm guessing medical and some part of SME fire. And what is that average activation time, some color on that?

Bhargav Dasgupta: So, Shantanu, if you heard the calls in the last three or four quarters, we have been saying that this is an investment that we are making for the long-term. We started making the investment in the last quarter of the previous year and we are continuing to make it in terms of our distribution largely in tier 3 and tier 4 cities and also some of the satellite towns of big cities.

We call this as a Virtual Office initiative in the tier 3 and tier 4 towns. We have seen the pickup in growth of business from those towns has been quite significant already. The benefit is beginning to play out. We started seeing the benefit play out from the last quarter of the previous year. And this quarter we have continued to see that benefit. To give you some numbers, our agency channel has grown about 24.7% in this quarter. Considering the muted environment that the industry is in, this is a pretty healthy number. We see this trend continuing, because we think that whatever we have invested and we are continuing to invest will start becoming productive in six to nine months from then. Hence, we believe that this whole year we will see the benefit. And rest of it will depend on how much investment that we continue to make in terms of adding distribution channels.

Moderator: Thank you. The next question is from the line of Ajox Henry from B&K Securities. Please go ahead.

Ajox Henry: Sir, my question is with respect to the distribution. On the virtual offices, what is the current status now? Because last call we said we had almost 900 offices, so how have we expanded on that front? Number one. Number two, SME growth, your presentation noted that there is a 29.5% growth in Q1 FY2020. How far do we see that traction continuing? And third is with respect to the motor-dealer touch points, so we were kind of behind on that and we wanted to expand on that. So this quarter how did we grow in that as well? So that were my questions.

Bhargav Dasgupta: On the VO count, the number is scaling up every quarter. This quarter the total VO premium was ₹ 143 crores. This number for Q1 FY2019 was negligible at about ₹ 60 crores.

To answer your second question on SME, that's grown at about 29.5% this quarter. If you see our SME business over the last four years, we have consistently been growing at the rate of 25% to 30%. And this is on account of our investment in distribution and products. We have done a lot of work in terms of bundling different covers into very simple convenient combined offering, investing in technology for policy issuance using BOTs, reviews, RPA (Robotics Process Automation) solutions, etc. to help design digital platforms for our agents to sell SME policies. We believe that on the SME side there is still a very large opportunity. The current VO premium has been largely on account of motor insurance. However, we believe gradually we will be able to add the health and SME in some of these remote markets.

As regards the third question, I was not clear since on the dealership touch point we are by far the biggest player. We have 60% penetration in terms of the dealer points. We don't have 60% market share, but we are present in at least 60% of the dealer points in this country. This has clearly been our strength.

Moderator: Thank you. The next question is from the line of Avinash Singh from SBI Capital. Please go ahead.

Avinash Singh: Sir. I just had one question on investments. So any color on that exposure from the housing finance companies and some other stressed groups. And the question on that would be that today you may not have that exposure but did you sort of had exposure earlier and you booked certain losses on that? So any color on this exposure around that stressed housing finance or other financial services companies?

Bhargav Dasgupta: So the answer is, no. We do not have any exposure in IL&FS, it's not as if we sold at a discount and shown zero exposure. We did not have any exposure to DHFL either. So we didn't have to book any losses for these exposures.

Moderator: Thank you. The next question is from the line of Nidhesh Jain from Investec. Please go ahead

Nidhesh Jain: Thanks for the opportunity. First, any color on motor OD, the loss ratios are almost seven, eight quarters high. Do you think the competition is incrementally giving any further stress to the loss ratio? If you could give any color on the competition in motor OD and its impact on our loss ratio?

Bhargav Dasgupta: So, Nidhesh, there are two factors driving this. One is the long term policy. By design and by simple arithmetic, the loss ratios will creep up because you are sitting on the money upfront. ROE maybe fine, but the loss ratio will creep up, particularly for TP. Even for OD, the loss ratio will go up because wherever you are selling a three year policy or a five year policy, you are passing on the benefit of renewal cost and also distribution cost being much lower to the customer. Hence, effectively in OD, the loss ratio will keep on increasing while the expense will come down. However, in TP the loss ratio will increase while the investment increase. So that is because of the change in dynamics of the fact that long-term policies have come in place.

The second factor is overall competitive intensity that has increased, as discussed previously. Again, driven by the fact that long-term policies have come in, insurance companies are seeing it as an attractive opportunity. So they are willing to discount the own damage a bit more than what they were doing in the past. We believe that industry loss ratios would be much worse on the own damage. Our OD loss ratio is about 68%. The industry loss ratio is roughly in the mid-70% for OD. Accordingly, there is not much margin for insurance companies to cut prices further. If you look at the distribution cost for OD, being a retail policy, there are expense viz. policy servicing expenses etc. At that level of loss ratio it is very difficult to make it viable.

Nidhesh Jain: Sir secondly, if I look at Q3 and Q4 performance, your combined ratio was pretty strong, but underwriting value was not being delivered because you were highlighting that it will get deferred. So in this quarter we are seeing the opposite phenomena where combined ratio is close 100%, but we are seeing some underwriting value emerging probably due to the last two, three quarters. Is this correct understanding?

Bhargav Dasgupta: Your understanding is correct. The growth numbers have been a bit muted. And if you see the combined ratio, there is expense allocation since the crop segment is going out of the book. But overall the actual underwriting number has improved because the loss ratio has improved from 76.9% in Q1 FY2019 to 75.5% in Q1 FY2020. Gopal, you want to add anything?

Gopal Balachandran: As mentioned in the opening remarks, the combined ratio has gone up on account of the long-term motor policy. However, this has been offset, to some extent, by the gains that we realized on the investment book. In addition, this will be the first year where we will witness the full impact of the long term motor policy regulation. The regulation came into effect around September 1 of 2018. Hence, FY2019 only saw some element of impact. Whereas FY2020 will be the full year where we will witness the full impact of the new regulation. As far as the combined ratio is concerned, you will potentially get to see it operating around 100%

level. However, you will get to see the investment income contribution to be relatively higher.

Bhargav Dasgupta: To add, our investment leverage has gone up to 4.27x which is exactly the point that the Gopal is making.

Nidhesh Jain: And sir lastly on the crop insurance, you said you are still holding the IBNR despite you have not written any crop insurance I think for last two quarters. So is it on a conservative basis or do you think that loss will come in future?

Bhargav Dasgupta: No, this is because we wrote Rabi. If you recollect our Q4 FY2019 earnings call, we mentioned that the Kharif season looked to be much better. However, at that time, we didn’t have complete data for Rabi, In fact we still don't have the complete data for Rabi. The complete picture will come by the end of Q2 FY2020. Hence, we are holding reserve on the Rabi crop. Our sense is that the Rabi performance has not been very good. We are not sure if we will get any major relief in the second quarter based on the early estimates that we are getting on the Rabi side. So it's not as if we are being conservative, I think we are being realistic on that.

Moderator: Thank you. The next question is from the line of Harshit Toshniwal from Jefferies. Please go ahead.

Harshit Toshniwal: Two questions, one on motor third-party premium. Just want to understand that since H2 of last year we saw a large amount of growth in the motor TP business in the Q3 and Q4 quarters. But when I would be looking at FY20 H2, then is it that because of loss of renewal for some of the businesses that my growth numbers for TP of FY20 is going to look a bit lower than the run rate which we are doing in H1?

Bhargav Dasgupta: In Q3, Q4, on a base effect it could be, but it's not because of any lack of renewals. If you see Q1 FY2020, we didn't have any price increase. So that has had an impact in terms of numbers as well for TP. And last year as we scaled up our agency which resulted in picking up our commercial vehicle and private car businesses. However, in the current year, given that the price increase on TP for commercial vehicle has not been in line with our estimations, we are getting a bit more cautious on the commercial vehicle book. So we are moderating growth for commercial vehicle business. Having said that, we are glad that the overall renewal performance is actually better in preferred target segments. So it's not because of renewal, it could be because of base effect of H2 FY2019, that the growth may look slightly slower. In addition, moderation in commercial vehicle business for the current year, lack of third party price increase in Q1 FY2020 will also contribute to slower growth.

Harshit Toshniwal: Okay. But the reason I was asking is that because the long-term policies in two-wheeler and cars which we have sold in the H2 FY2019, specifically the third-party premium, those particular set of customers won't be there for next two or three years.

Bhargav Dasgupta: Let’s say if you had written a one year two-wheeler policy in September 2018, the renewal rate one year later was around 28%-29% for us. Now 100% of that TP will come to us, we will book it out of the cash that is sitting on our books that we talked about in the beginning of the call. Around ₹ 1,865 crores is the amount not booked as premium income but is sitting as cash as advance premium. So 100% of this policy we will book.

Harshit Toshniwal: Okay. And one more thing, on the fire insurance can you throw some light on what exactly are we… so the increase which we have seen, what are the segments and how much are we re-insuring back with reinsurers on this portfolio? More about the profitability of that part, if it has changed drastically in the first half.

Bhargav Dasgupta: So, the fire dynamics have again changed largely driven by the reinsurers' action. In March 2019, GIC, who dominates the reinsurance market in this segment, had prescribed minimum rates for eight occupancy i.e. large industry segments like power, steel, rubber, pharma, textile, etc. These segments historically had high loss ratio and insurance and re-insurance industry has settled huge losses. This means that all general insurance companies have to charge rates as prescribed by IIB. IIB looks at the industry burn costs, which is the average loss for a particular occupancy and prescribes a minimum viable rate. This has increased price in these segments manifold.

Now, given the fact that in almost all treaties there is a GIC participation or GIC leadership, effectively, the market price for these eight occupancies have gone up. The industry growth for fire segment has been about 48% in this quarter and our growth has been around 67%. We have done better than the market because of our robust SME business, corporate business, distribution network etc. Also, we are witnessing some market share shift from older companies to us, that has benefited us incrementally. This is the reason why our growth in the fire segment has been high.

To answer your second question of reinsurance, we traditionally take a proportional reinsurance where we cede the policy premium and also the claim in the same proportion to the reinsurers. In addition, we also buy an equivalent of a stop loss, which we call “excess of loss covers” for the book that we retain. Now, given what we saw fire policy rates going up for the industry, we have taken the decision to retain a bit more than what we used to do in the past. If you are doing a proportional reinsurance of x percentage, we have now done it at x minus 10%, you have written 10% more on our books, because we like fire portfolio now at these prices. If you look at the net-written premium or net earned-premium, you will see the mix of fire in our portfolio is increasing. The earned premium mix of fire segment was 1.5% in Q1 FY2019 as compared to 2.1% in Q1 FY2020. In conclusion, this increase was driven by two things – firstly the high GDPI growth number and secondly, the high retention ratio.

Harshit Toshniwal: And one more last question, if that's possible. So when I look at the reinsurance rates kind of back calculating it for segment, then for health it comes to be as high as 70%-80%. Rather 50% of our reinsurance fees comes from health business primarily. So, what is it that makes us allow such high reinsurance rates, somewhere around 80%-85%?

Bhargav Dasgupta: So, it is not 80%, 85%, but it is a high rate, because there are certain types of health businesses, basically the benefit constructs where the exposure is very high on account of large claims if an individual suffers from critical illness that is reinsured. And given that the overall portfolio is profitable, you get a pretty high commission on that segment.

Harshit Toshniwal: So the number when I look at, comes at around 75%-80%. So, reinsurance commission which we receive versus the premium which we are ceding, that ratio moves between 75% - 80%, maybe last two, three years in health.

Gopal Balachandran: Yes. So when you look at it from net of reinsurance basis, I think you could effectively see that number operating at those levels of commission. And as Bhargav said, it is all a function of what kind of loss experience that you exhibit. And corresponding to that is reinsurance. That's what they look at not necessarily only in this line of business, but across lines of businesses. They would also look at the portfolio behaviour exhibiting to the reinsurers. And they would give a function of a commission that you would get to see as a minimum level of commission. Corresponding to the portfolio experience, they will also supplement it with for the profit commissions, depending on what the reinsurance terms are.

Moderator: Thank you. The next question is from the line of Preeti RS from UTI Mutual Fund. Please go ahead.

Preeti RS: Sir, just to understand as a thumb rule what would be the broad mix of primary to renewal sales in the motor business?

Bhargav Dasgupta: Sorry, we didn’t get your question, Preeti.

Preeti RS: Broad mix of the primary sales insurance versus the renewal insurance sales.

Bhargav Dasgupta: So basically the mix of new versus renewal?

Preeti RS: Yes.

Bhargav Dasgupta: It is largely 50:50 for the overall motor book for us. Let me give you the latest number for the quarter. Generally, it's generally been about 48:52. For this quarter specifically the number is 44.6% for new, and 55.4% for renewal.

Preeti RS: Sir, if you look at the motor OD trends, we have been outperforming the industry, at least for this particular quarter. So what part of this growth is actually structural, I mean, how do you explain this? What do you attribute this market share gains to?

Bhargav Dasgupta: This is largely the same reason why we have been growing in the last couple of quarters, it's basically the investment that we made in distribution from early last year and we continued in quarter three. So agency channel has really grown for us, almost 25% as we have explained. Secondly, even as new OEMs are coming into the market, for example, the new ones that have just come recently like KIA, MG etc., we are entering even those tie-ups. If any new OEM comes to the market, we have been a preferred partner for most of them and that doesn't change. We have also added a few new OEMs in the last year that has helped us in terms of increasing the OEM numbers. And lastly, the virtual office helped us gain business in tier 4 markets where earlier we did not have a significant presence in the past and so the dealer could have given the business to someone else. As we are going into the hinterland, our share of the dealer business from those local markets is now increasing. These are not new OEMs, existing OEMs, but we are getting into smaller towns where we may not have control over the dealership. So distribution is really what is helping us.

Preeti RS: So does that also explain the mix of CV going to 55% and two-wheeler dropping by similar amount?

Bhargav Dasgupta: Just to clarify, our CV mix is roughly 17.0% whereas the private car mix is 55%. Let me take you through the CV growth factors and will ask Gopal to provide explanation on the change in mix of private car and two wheeler. CV growth was largely driven by agency for us last year, and also because till last year for three years prior to that we had seen pretty good increases in third party price rates by the regulator. And we found certain segments of business which we did not find profitable earlier, we started writing those businesses last year. So CV business for us grew as a category last year. This year we are again calibrating, because as I explained earlier, we have not seen the price increase in CV this year and hence CV is coming down. Let me ask Gopal to continue.

Gopal Balachandran: I would like to add that on the long-term motor policies, as we explained, there has been pass through of cost to the customer. So if you look at it from an average ticket size standpoint, the average ticket size has clearly come down relative to the prior periods. For us, two-wheeler is a very large proportion of the overall motor business. This would also explain the relative proportion of two wheelers coming down in this quarter vis-à-vis in the earlier periods. But that largely gets offset with the higher amount of the advance premium which moved up from roughly ₹ 1,300 crores at the end of FY2019 to about ₹ 1,865 crores at the end Q1 FY2020.

Moderator: Thank you. The next question is from the line of Shreya Shivani from CLSA. Please go ahead

Shreya Shivani: Sir, I just wanted clarity on the financial year of FY2020. If you can give a guidance or some clarity on the GDPI, net premium numbers. Also, combined ratio you mentioned that it should be around 100%. What do you think the loss ratios, what range should we expect that to be in?

Bhargav Dasgupta: We don't give a guidance on the breakup of the loss and expense ratio as a practice. We rather prefer to give a guidance on the combined ratio since our approach to a business segment is driven by combined number. This is because there could be segments where the loss ratio is very low but the expense ratio is very high, and vice-versa. Accordingly, instead of loss ratio, we will focus on combined ratio.

The second metric that we focus on as a company is ROAE. As mentioned earlier, we want to maintain an ROAE above 20%. And if you see the Q1 FY2020 number, we have been able to deliver it as per expectation. The ROAE will also be driven by the investment leverage, given the impact of the long-term policy. So even if let's say combined deteriorates a bit from last year's 98.5% to say, 100%, we believe the investment float will compensate for that.

In terms of GDPI growth, we believe that industry and our Company will continue to grow between 15%-20% in preferred segments on a medium to long term horizon. This year, given that we are dropping the crop segment, we did not win a single tender in Kharif. So assuming that crop segment, that was about 17%-18% of our business mix last year, goes out in the current year, our total top line will be muted. However, our preferred segments, we will endeavour to grow at 15%-20%.

Moderator: Thank you. The next question is from the line of Neeraj Toshniwal from Emkay Global. Please go ahead.

Neeraj Toshniwal: Sir, basically just wanted to know on the long-term motor OD, how we are doing on that, any attachment towards bundled policy?

Bhargav Dasgupta: If you are talking about the renewal rates of the OD for a TP that we have written, we will only be able to tell you from September 2019 onwards. In terms of the long-term two wheeler policies where we are selling a five year TP, the proportion buying OD cover also is now about 20% for two wheelers. What is positive is in this quarter is that Maruti has now started driving the long-term OD as well, and that number for Maruti's business segment has increased close to 40%. So in aggregate, given that Maruti is almost half, that number for private car overall is about 9%. This increase from around 2%-3% that we had in the last quarter is a positive indication.

Neeraj Toshniwal: Right. So that is helping even the higher numbers coming in, so just wanted to get some color on that. So on overall motor scenario, which has been really bad, any comment on that? I think there has been lot of production cut, and the new vehicle sales has been very poor, so how do we see that, I mean, on the insurance per say as well?

Bhargav Dasgupta: For us, it will be driven by four key factors. One is the new vehicle sales, the numbers that SIAM is publishing. I will just add one small caveat to that, SIAM publishes numbers based on what the OEMs push into the dealer network. When the dealer sells a policy to the final customer, we believe that the actual sales number to the end customer is not as bad as what SIAM is talking about. We believe, based on our interactions with the dealerships and our personal experience, we believe that number is a single-digit negative, could be minus 7%- 8% for private cars. It is a similar number for two-wheelers as well. Even though it is a negative number, but not as big a negative as the headlines that you may be seeing.

The second factor is long term policies. As explained, that the long-term policies that we wrote, particular for two-wheelers, 100% of them will renew, at least for the long-term. In comparison to the past this is now a positive scenario. And as more and more three year or five year own damage penetration increases, it will continue to benefit us.

The third factor is market share shift. If you see the growth that we had in motor segment in Q1 FY2020, the overall growth is largely driven by the upscale in our distribution network. Our overall motor growth is 14% in Q1 FY2020, which is much higher than the industry growth numbers. So if you see the industry growth number for overall motor is about 4.3% while our growth number is 14%.

The last factor is Motor TP rate hike. In Q1 FY2020, we did not witness third party price increase. The price increased effective June 16, 2019. To that extent, we can potentially see 4%-5% price increase in our Motor TP book. Having said that, we will have to watch out for further price correction on the OD side. These are the key factors that drive the overall GWP growth numbers for us.

Moderator: Thank you. Next question is from the line of Sanket Godha from Spark Capital. Please go ahead.

Sanket Godha: Just wanted to understand the size of benefit based premium, health benefit based premium in our overall number. That is first question. And second thing was, just wanted to understand how much VO has started contributing to our overall GDPI, and which segment is driving VO growth? And the last question which I have is our concentration with respect to Hero as an OEM?

Bhargav Dasgupta: On the first one, so far as the benefit product is concerned, we had roughly 21% growth. It was about ₹ 2.4 billion in Q1 FY2019 which increased to ₹ 2.90 billion in Q1 FY2020.

To answer your second question on contribution of VO to overall GDPI, the amount for Q1 FY2020 is ₹ 1.4 billion. The comparative number for Q1 FY2019 was ₹ 60 crores or about ₹ 0.60 billion. The investment that we have made has now begun to play out. We will continue to see the impact of it for the rest of the year as well, given the increase in distribution network in the previous year.

Sanket Godha: Yes, but the segments which are driving growth in VO are from motor or health?

Gopal Balachandran: So as explained earlier as well, I think at this point of time the growth on the virtual office is largely contributed by motor segment. When we witness the achievement of a critical number, we will want to use this distribution investment to do cross-sell of other products as well.

Sanket Godha: Okay. And finally on the Hero concentration we have with two-wheelers, Hero OEM concentration?

Bhargav Dasgupta: Concentration in the sense? As mentioned earlier, we have tie-ups with most of the OEMs. We are there with Honda, Hero, TVS, Royal Enfield and even Bajaj now.

Sanket Godha: No, my question is that the 25% of GDPI which we collect in motor business on two-wheeler, out of that how much would be driven by Hero Moto Corp?

Bhargav Dasgupta: Roughly about 30%-35% of the two wheeler business comes from Hero?

Sanket Godha: 35%, right?

Bhargav Dasgupta: Of the two-wheeler business.

Sanket Godha: Yes, I got it. And finally if I can squeeze in one more question, within fire are we focusing on doing home dwelling? Are we significantly present there given we have a decent bancassurance tie-up, the homebuilding fire insurance to be focus area, given it is highly profitable?

Bhargav Dasgupta: Yes, we do, and most of the bancassurance tie-up that I am talking about, we do home insurance as part of that. If you are asking for a comparison with other insurance companies, there is a classification issue - we classify it as part of a miscellaneous line of business whereas some companies classify it as fire line of business.

Sanket Godha: So, can we get the size of that business, if you can quantify and rupees billion?

Gopal Balachandran: We will give it to you separately.

Moderator: Thank you. The next question is from the line of Rishi Jhunjhunwala from IIFL. Please go ahead.

Rishi Jhunjhunwala: Firstly, on fire, so you mentioned about the rates going up substantially, which is reflected in the GDPI growth as well, and that in most of the cases you have proportional treaties. So I am assuming that if loss experience were to remain the same then loss ratio should improve dramatically in the fire segment. Is that a right understanding?

Bhargav Dasgupta: If the loss experienced in terms of total loss cost remains the same, loss ratio will improve.

Rishi Jhunjhunwala: So basically you have been doing less than 100% loss ratio in fire for the past two, three years. So assuming the similar kind of loss costs remain, then there should be substantial improvement in the loss ratios?

Bhargav Dasgupta: That is the reason why we have decided to write 10% more of that book this year. That is our expectation as well. It is essential to note that fire segment is a business which is difficult to predict because one large loss happens there can be some implications. But what we have done is, we have also tried to granularize that business through the SME business. And the other thing that you should note is that this price increase that we are talking about has happened for 8 high hazard industries, “occupancy” as we call it. In the past, we were anyway a bit cautious about those segments. So the incremental benefit that we have got has not so much been because of this, we also got benefit because of the overall growth in the other segments as well.

Rishi Jhunjhunwala: Understood. On the motor side, the growth that we have seen on the OD specifically, is much better than the industry on the GDPI side. How much of that would be due to market share gain on the volume side versus a mix change?

Bhargav Dasgupta: If you see own damage component, our market share has grown from 11.4% in Q1 FY2019 to 12.8% in Q1 FY2020. If you look at third-party, the market share again is a bit muted, it has grown from 6.4% in Q1 FY2019 to 7.1% in Q1 FY2020. So it is a bit of mix in the sense that there has been more OD, and that's largely driven by the fact that if you see our private car market share has grown, CV market share has not grown as much, and CV has more third-party and less OD.

Rishi Jhunjhunwala: Okay. No, I was more asking say even within OD, the fact that when we do more passenger or more commercial versus two-wheeler, the premium ticket size goes up. And as a result GDPI will look better, rather than the volume change in terms of number of policies sold.

Bhargav Dasgupta: So, we have not grown in the two-wheeler as much as private car. We have done well and grown more in Private car. But across the board we have seen decent growth. Specifically, one new factor to consider, if you look at the share of the OEMs, that also has grown for us. So that was roughly about 12.5%, that's grown by a couple of percentages more.

Rishi Jhunjhunwala: Understood. And you talked about long -term OD, 20% for two-wheeler and 9% for four wheelers. Just wanted to understand, I mean, how has the pricing been for you and for the industry, when we talk about five year and three-year OD policies? Because say a couple of months ago at least at that time the pricing was largely linear to the number of years when we did some of the checks, but just wanted to understand, is it largely in-line with how TP rates have been for long term or do we really have some bit of better pricing in there?

Bhargav Dasgupta: As in, how do we price our motor OD long-term policy compared to TP policies?

Rishi Jhunjhunwala: Yes. So basically, if you were charging ₹ 15,000 for a four-wheeler for one year would it be ₹ 45,000 for 3 years or slightly less, for example, ₹ 35,000?

Bhargav Dasgupta: You are correct. The long term OD polices will be discounted. For TP, as you know, is a formula that the regulator has given and that's a rate tariff, so it's kind of equally apportioned across a three year or five year, as the case may be. For OD, let's say if it's a three year policy, rather than pricing it at 3 times, we have given some benefit to the customer since we won't have any renewal effort in the one year, we will not send the policy, there is no cost of printing the policy, etc. Equally, the distribution commission for the second year is slightly lower than what we normally pay for renewals. In addition, we have the investment float. So all of that has been factored in. So if you see the price for a private car, rather than 3 times for three year, it is about two to 2x to 2.25x for a three year policy. So, we are giving the discount, which is why as we explained, the loss ratio will gradually creep up for own-damage component also, but the expense ratio will come down because all these expense benefits are being passed on to the customer. And equally, the investment float will play through.

Gopal Balachandran: Even for the industry, you are actually getting to see an increase in the OD loss ratios. If you were to see, for example, a year back loss ratios for the industry as a whole, we would be roughly in the range of 66%-

67%. If you look at the latest numbers that has touched to a level closer in the mid-70%.

Rishi Jhunjhunwala: Right. Because the other thing I wanted to check was basically how does the recognition work? Is it just 1/3 for three years, even for OD?

Bhargav Dasgupta: So there is a recognition based on a certain formula that we were following. In May 2019, the regulator has given a specific number on how you allocate the premium over three years. It is largely linked to the IDV of the vehicle. So you would recognize more in the first year and less thereafter.

Rishi Jhunjhunwala: Fair enough. And one last question on your new business strain, how much that would have impacted this quarter's earnings growth?

Bhargav Dasgupta: Which is what you get to see on the expense ratios, Rishi. You would have definitely seen an increase in the expense ratio numbers. And also if you were to see the growth rates for us, it has been 17.7% (excluding crop) in Q1 FY2020 over Q1 FY2019 on the preferred segment businesses.

Gopal Balachandran: Rishi, one more clarification on the response that I gave in terms of the mix of business. As I said, the two-wheeler business for us has not grown in-line with the private car business. So to that extent it could also be because of the higher ticket of private car numbers. But basically the point that I am making is that it's not because of any vacation of a certain dealership or a certain category of business.

Rishi Jhunjhunwala: No, of course. I just wanted to clarify that. Thank you so much.

Moderator: Thank you. The next question is from the line of Nischint Chawate from Kotak Securities. Please go ahead.

Nischint Chawate: Sir, just a couple of questions. What is the impact of Cyclone Fani? I mean, if you could quantify it.

Bhargav Dasgupta: So the impact of Cyclone Fani on the net, which post the reinsurance some of the amounts will be paid by the reinsurer is ₹ 16 crores in this quarter. The gross loss will be roughly ₹ 35 crores. So, if you look at the combined ratio for us excluding the impact of Fani losses, it would be 99.7%. And if you see our share of total insured loss of the industry as we understand it today, this number is roughly about 1% of the industry losses. So the trend of our share of loss being much lower than our natural market share continues even for this event.

Nischint Chawate: Now, what is the outlook for growth in the fire segment this year? I mean, I guess it's a combination of higher tariffs and volumes. But any sense, I mean, can we expect a 40% plus industry growth for the full year or 60% plus for you, how should we think about it?

Bhargav Dasgupta: At this point, the industry is expected to grow and sustain this level of growth. Because as explained, it’s a structural change because of what GIC has done for those 8 occupancies.

Nischint Chawate: How large are these 8 occupancies and what is the percentage?

Bhargav Dasgupta: These occupancies constitute roughly about 35% percent of the industry. The second thing to keep in mind is that Q1 is a very strong quarter for fire, because most of corporate renewals happened in Q1. So, in terms of volume the number may be a bit muted, but growth numbers should be maintained relative to the other quarters. The last point that I will make is that there is a committee that the regulator has formed to relook at the IIB rates. So this GIC price increase recommendation is largely based on, as I explained, IIB burn cost. There could be two possible outcomes – firstly, it could be that increase in the number of occupancies, we are only talking about eight occupancies, we could see more occupancies being covered by GIC. In that case the premium could rise even for other industry segments. Equally, in any of the burn costs the actual calculation shows that the burn cost should be lower than the current number that IIB has, it could come down a little bit. Our estimate is that it's probably more of the first one, i.e. more sectors may get covered. So we think the fire growth rate in the industry will continue for some time. Even the other rates for natural catastrophe, the price that we charge for earthquake and natural catastrophe perils, what we call as STFI rates, that has also gone up a little bit this year. So all that should sustain.

Nischint Chawate: And on an average how much has been the rise in this 35% of business?

Bhargav Dasgupta: It's not a percentage, it's by a factor. It's increased by 4x to 6x in some segments. The average for all these 8 occupancies, the rate increase is more than 2x.

Nischint Chawate: Okay. Now the health business, I guess you mentioned that group business was kind of more profitable last year and competition seems to be creeping up a little bit. So any guidance on loss ratios on the health side?

Bhargav Dasgupta: Let me clarify. What I had said was that last year vis-à-vis previous year to last year i.e. FY2018, we saw very sharp price increases. So the loss ratio came down significantly compared to the previous year. Now, as prices increase, we also entered with a few new corporate accounts, because it became viable for us to enter with those accounts. This year relative to the previous year, we are not seeing any similar increase in prices. But we are not seeing any major deterioration either. Our sense is that group health prices are largely holding. We don't expect the group health business to grow at the same pace as we had in the last year.

Nischint Chawate: But around 75% loss ratios should possibly be maintained, I think that's what we can assume?

Bhargav Dasgupta: We think it should be maintained. In fact, what we are doing is, accounts that we entered last year, not all of them have performed as well as we would have anticipated. If it does not perform as well then we would want to either increase the prices or reduce exposure. We will continue calibrating. So at least the effort from our side will be to reduce the loss ratio rather than let go off.

Nischint Chawate: And any scope of retail business kind of getting more interested, the individual basis?

Bhargav Dasgupta: That is one of the key thrust area for us as a company. And if you see what the numbers that we have given out in terms of growth across segments, for the retail business we have had a very good quarter, in spite of the fact that very large part of business which comes from NBFCs have not seen high growth. In fact, we have seen a small de-growth for obvious reasons due to slow-down of disbursements happening in some of the NBFCs. The pure retail indemnity business, which is largely driven to agency, the new indemnity business has seen growth by close to 49%. Of course, that doesn't reflect in the overall numbers because the overall number has renewals also, and our renewal book is relatively small for the indemnity piece. But the new business is growing quite well for us, largely again driven by the agency scale up that we have done and that we are continuing to do.

Nischint Chawate: Sure. Finally any guidance on crop business this year?

Bhargav Dasgupta: I think it will remain same. We will continue to be selective. We don't believe that the crop business, given the reinsurance terms, can be viable. At the end of the day it is social insurance. We believe that given the reinsurance interest terms, breakeven rates for crop businesses is now at around 75% to 80%, which is not a number that you can expect to earn from a social insurance scheme for a sustainable period. So we are remaining cautious till the reinsurance market changes. And at this point, we have not won a single new tender for the Kharif season. We will see what happens in Rabi. Our sense is that the same trend will continue in Rabi also. The only other commentary on the crop is the fact that there is still some business of the Rabi book of last year for which we will have actual loss experience in the second quarter account. Now, whether the loss reserves that we are holding is adequate or not, will be determined by the data we receive.

Nischint Chawate: And just one final clarification, you mentioned that in the car segment around 9% of the new business is a comprehensive policy.

Gopal Balachandran: The three year own damage and three year third-party policies constitutes 9% of the overall private car business.

Nischint Chawate: That's right, that's around 9% for you?

Bhargav Dasgupta: Correct. That number in the last quarter was about 3%.

Moderator: Thank you. Ladies and gentlemen, that was the last question. I now hand the conference over to Mr. Bhargav Dasgupta – MD and CEO, for closing comments.

Bhargav Dasgupta: Thank you guys for coming and joining us on this call and we look forward to interacting with you in the days ahead. Thank you.

Moderator: Thank you very much, sir. Ladies and gentlemen, on behalf of ICICI Lombard General Insurance, that concludes this conference. Thank you.