"ICICI Lombard Limited Q1 FY19 Earnings Conference Call"

July 17, 2018

MANAGEMENT: MR. BHARGAV DASGUPTA – MANAGING DIRECTOR
AND
MR. GOPAL BALACHANDRAN – CHIEF FINANCIAL OFFICER

Moderator: Good evening, Ladies and Gentlemen. A very warm welcome to the ICICI Lombard General Insurance Limited's Q1 FY19 Earnings Conference Call. From the management we have with us today Mr. Bhargav Dasgupta – MD and CEO and Mr. Gopal Balachandran – CFO.

As a reminder, all participant lines will be in the listen-only mode. There will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during this conference call, please signal an operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded. I am now glad to hand the conference over to Mr. Bhargav Dasgupta. Thank you and over to you, sir.

Bhargav Dasgupta: Good evening everybody. We also have with us Mr. Alok Kumar Agarwal (Executive Director – Wholesale) & Mr. Sanjeev Mantri (Executive Director – Retail). I welcome you to the earnings conference call of ICICI Lombard General Insurance Company Ltd. for Q1 FY019. Before we get into the financial results of the Company, I would like to give you a brief overview of the recently ended quarter, post which our CFO, Gopal Balachandran will share the performance numbers.

The General Insurance Industry registered a growth of 12.2% in Q1 FY2019 over Q1 FY2018 with the industry GDPI moving up to ₹373.52 billion for Q1 FY2019 from ₹332.85 billion for Q1 FY2018.

As an Industry, we witnessed increased focus on underwriting discipline as is evident from the improved combined ratio for FY2018. What is encouraging is that this prudent behavior comes at the back of continuing growth momentum. The combined ratio at an Industry level improved significantly to 108.5% for FY2018 from 120.2% for FY2017 based on available information.

At ICICI Lombard, we continued to register an across the board increase in market share in most corporate lines such as Fire, Engineering and Marine Cargo. At the same time we continue to remain cautious when it comes to the Government business segment.

On the Retail side of business, we believe that segments such as SME and Retail health indemnity offer profitable growth opportunity and these remain our areas of focus. In order to harness the potential of these segments, we have been investing towards developing the agency and virtual offices network so as to increase penetration in tier 3 and tier 4 cities. We are encouraged with the outcome as these segments have registered robust growth during the quarter.

Our overall GDPI growth for Q1 FY2019 was slightly higher than the market. Consequently, our market share has increased to 10.1% for Q1 FY2019 from 10.0% for Q1 FY2018.

On an overall level, given the investments we are making in distribution, we expect to continue growing at 15% to 20% levels on a medium to long term basis.

Our underwriting performance measured in terms of combined ratio continue to be robust for Q1 FY2019.

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

Gopal Balachandran: I am happy to take you through the highlights of ICICI Lombard General Insurance Company Ltd. for the quarter ended June 30, 2018. We have put up the results presentation on our website. You can access it as we walk you through the performance numbers.

In terms of our financial performance, the Gross Direct Premium (GDPI) of our Company increased to ₹37.74 billion in Q1 FY2019

compared to ₹33.21 billion in Q1 FY2018, registering a growth of 13.7% as against industry growth rate of 12.2%. Excluding crop insurance segment, our growth for Q1 FY2019 was 14.1%.

We continued to maintain a diversified portfolio in Q1 FY2019 across Motor insurance, Health and Personal Accident insurance, Crop insurance and Property insurance.

Within the Health & Personal Accident segment retail, corporate and mass contributed 35.1%, 62.9% & 2.0% respectively for Q1 FY2019 and 42.6%, 53.8% & 3.6% respectively for Q1 FY2018.

On the profitability front, we registered an improvement in Combined Ratio to 98.8% for Q1 FY2019 from 102.4% for Q1 FY2018. Our loss ratio improved to 76.9% for Q1 FY2019 from 78.1% for Q1 FY2018.

Our Investment assets rose to ₹198.73 billion at June 30, 2018 as compared to ₹161.46 billion at June 30, 2017. Our Investment leverage (net of borrowings) was 4.01x at June 30, 2018 as compared to 3.90x at March 31, 2018. Investment income for Q1 FY2019 increased to ₹5.07 billion from ₹4.55 billion for Q1 FY2018. Capital Gains in Q1 FY2019 was at ₹1.96 billion compared to ₹2.15 billion for Q1 FY2018.

Our Profit before tax (PBT) increased by 47.5% to ₹4.43 billion in Q1 FY2019 compared to ₹3.00 billion in Q1 FY2018. Our Profit after tax (PAT) for Q1 FY2019 was ₹2.89 billion compared to ₹2.14 billion for Q1 FY2018, registering a growth of 35.1%.

Return on Average Equity i.e. ROE, was 24.7% for Q1 FY2019 compared to 22.4% for Q1 FY2018.

Solvency ratio was 2.04x at June 30, 2018 as against 2.13x at June 30, 2017 and higher than the minimum regulatory requirement of 1.50x.

As we conclude our address, I would like to summarize that we ended Q1 FY2019 with a strong balance sheet supported by robust reserving and risk management. We continue to build our distribution with our focus on profitable growth.

I would like to thank you all for attending this conference call pertaining to our earnings for Q1 FY2019. We would now be happy to take any specific questions that you may have.

Moderator: We will now begin the question and answer session. We have the first question from Ashish Sharma from Enam Asset Management.

Ashish Sharma: I have one question on the strategy of the company. We have seen a strong growth in Q1FY19, but what we have seen is that the underwriting profit is not there. I think there is a trade-off between growth and underwriting profit. So will we be focusing more on the growth or we will solely focus on the underwriting profits?

Bhargav Dasgupta: Let me first explain the way the numbers are calculated in India and then I will respond to your specific question. So, if you look at the way combined ratio is calculated in India it has two components, one is the claims ratio which is net incurred claims divided by net earned premium, so it is on the basis of the earning of the premium. On the expense ratio side, however, it is the total expenses divided by the net written premium.

The reason why it happens is that in India we do not have DAC, i.e. deferred acquisition cost. Globally, most markets would have DAC. When you write the business in the immediate point of time, you take the acquisition cost as P&L hit immediately. So, to address that aspect, as an industry, the combined ratio we calculate is based on

the formula that I laid out. What this means is that the moment the combined ratio is less than 100% we are creating underwriting value, as in we have created underwriting profits.

But we may not be able to account for it in that quarter because we have taken the full hit of the acquisition cost. When you look at our combined of let's say less than100% at this point, effectively it means that if we stop the company immediately as of 30th June and don't do anything going ahead, the earnings of the business that we have written and the claims that we will pay will leave us with a surplus at the end, assuming we have no expenses. So we have created underwriting value.

In terms of our approach, I think we have always been stating, and I will repeat, our focus always has been on profitable growth. It is obviously idealistic to assume that both will happen, growth and profit always, but on balance if you have to compromise one, we will compromise growth. In our history, there have been years where the market has been very underpriced or aggressively pricing.

We have actually let go of the business and we have de-grown even in certain years. But the focus has been on profitability. I will give you another data point, as a company if you look at our 10 year CAGR, from 2008 to 2018 our GWP CAGR has been 13.9%, while your profit after tax CAGR of 23.7%. As a company we have grown profits at a rate of compounded annual growth rate of 23.7% while the top-line has grown at a lower rate.

So that has always been our approach to business over the time. Ideally, obviously we want to do both, we want to grow, and there are opportunities like what we are seeing right now with the market becoming more sensible in terms of pricing, we are seeing an opportunity to grow as well as benefit in terms of bottom-line.

Ashish Sharma: As the sector matures and as the underwriting profits improve will we be more focusing on profitable growth rather than just the growth? Too much of profits also sort of brings extra regulatory restrictions. Does that mean the participants need to always do a tradeoff between growth and profitability?

Bhargav Dasgupta: I think it is too early in our cycle to worry about a situation where as an industry we will be making too much of profits which will call for some regulatory actions. If you look at an industry level, the last year's combined ratio for the industry was 108%. So it is not as if we are making a lot of money as an industry. What we want to achieve is an outperformance vis-à-vis industry numbers by a greater focus on risk selection. We do a lot of work on analytics in terms of automation and digitization to keep our costs under control. That is the endeavor that we have had and that is what we will continue to focus on. The other statement that we have always made is that we believe there is a huge growth opportunity in this market at this time and so we are continuing to invest for the future.

If you look at the penetration of insurance, it is still 0.93% according to Swiss Re Sigma report, which is way lower than what similar economies in the world display in terms of penetration numbers. So we have a long runway of growth and it is our belief that at this point in time we should invest in terms of building out distribution for the future. We are at a cusp where market share is shifting to some of the more service oriented and efficient players and we want to invest for that growth. So we do not want to run a book of, for example 92% combined ratio but would rather run a book of high 90s and give a ROE in the ballpark of 20% plus and deliver growth which is higher than the market in the segments that we like.

Moderator: Our next question is from Avinash Singh from SBICAP Securities.

Avinash Singh: If I look at the overall expense ratio, commission plus OPEX, it has improved quite a lot, and that too in the backdrop where your reinsurance commission, and particularly for crop, has gone down. This means overall improvement in OPEX is very strong. What sort of sustainability do you see in improvement in the expense ratio?

On the segmental results, if I look at two lines, first in the group health side, net premium growth is very strong but your underwriting losses have also grown significantly. Now the question is, there was a talk of improvement in pricing on the group health side, but at least the result does not reflect that. Secondly in Crop, the difference between underwriting and operating profit is significant. Are the states and the center making timely payment as the difference between underwriting and operating looks meaningful?

Bhargav Dasgupta: Both the questions are very valid ones. On the first one, in terms of sustainability of the expense ratio, we look at our business more from the angle of combined ratio. There could be times when we may invest and increase the expense ratio for focusing on better quality business from a loss ratio perspective. While we obviously look at our overall expenses and manage the expense actively, the measure that we of look at for ourselves as a company is the combined ratio, because that is really the core objective that an insurance company should have. So, we may see some fluctuation in the expense ratios going back and forth, but I think the objective that we have articulated for ourselves is to keep the combined ratio directionally under 100%.

In terms of the specific question that you had, what I would urge you is to appreciate that the accounting norms create optical volatility in numbers in our business. So just to give you a couple of clarificatory comments on that, the group health business optically shows a very high underwriting loss this quarter, while that is largely because we sourced a lot of the business towards the end of the quarter, and as

I explained we have incurred the full cost upfront, it has not earned full benefit which will get earned in the due course because the sourcing cost is what we have accounted for right up front.

So that is why optically it looks like a very high number. But what we measure for ourselves internally is, are we sourcing the business at a viable loss ratio. At this point in time we are reasonably happy with the group health portfolio that we are getting. We see three segments, one is the SME segment, second is the mid-corporate or mid-sized corporate segment and the third is the large segment, I am talking about pure employer-employee group health segment and am not including mass or retail here.

Now, within these sub-segments the SME is growing really well. SME segment generally has been very profitable from a group health perspective. The mid-sized segment market this year has also been good growth driver for us. However, we are not winning the large ticket sizes in the group health segment. So if you look at the number of wins that we have had, we have completely defocused on ticket sizes of more than Rs. 2 crore of premium on the group health. While there are lot of private companies that we have seen which have picked up ₹ 15 crore, ₹ 20 crore, ₹ 30 crore, ₹ 40 crore premiums, but we have consciously defocused from that segment, even within group health. So, the growth that you are seeing in the group health is actually more granular than lumpy.

Avinash Singh: Since it is more granular, expense could be a bit higher when compared to YoY. Does that mean higher underwriting losses in this quarter?

Bhargav Dasgupta: Absolutely. In terms of Crop, your question, so if you see last year same quarter we had a 140% loss ratio because some of the previous quarter losses still drove into last year first quarter. But what we did, if you remember, the reserving that we did as of 31st March 2018,

we took in our understanding as much as the possible loss because we took whole 110% plus the full reinsurance cost into our P&L last year. So the scope of spilling over to this year is in our minds limited.

So, this year we have seen loss ratio come down, but again there is some amount of timing gap here because we have provided on the crop at 117%, so what we have done this year is that we said till last year we were providing 100% in aggregate but this year what we said we will provide 100% on the loss ratio plus we will account for what we believe is a reasonable expectation on the reinsurance cost.

When I say reasonable expectation on reinsurance cost is because the reinsurance cost also varies depending on the mix of business that gets finalized at the end of the year, which is why earlier we used to book it at the end of the year but that creates a bit of a shock in the last quarter last year.

So, we said at least on a reasonable basis what we believe the reinsurance cost would be, we have taken the full hit in this quarter. It could move up by 2% - 3% at most really, not much and on the loss ratio we have taken a full 100% hit in this quarter on the loss ratio. So that is why optically you are seeing 117% loss ratio on crop. The reason why the combined ratio, the underwriting number in that sheet looks positive is again because of timing mismatches, while on the group health side the lack of DAC negatively impacted us. Here the reinsurance commission that we book on the gross business that we pass on to the reinsurers is also booked upfront.

Avinash Singh: There is a gap in your underwriting and operating profit which means you are earning investment income. So, what sort of a float incoming is coming in, because what we have heard in the past is that there is very little to no investment income in this business? But here there is a meaningful contribution from investment income in this segment.

Gopal Balachandran: If you look at both the segments, particularly with respect to the group health side, we end up getting premiums on day one and till the time whenever there is an outflow on account of claims is the time when you would see an outflow of money happening. So, obviously there is an element of float that we enjoy in the interim till the time there is an outflow on claims.

On the crop segment in specific, as far as the farmer share is concerned, that portion of the premium is something that we are able to kind of realize at the point of underwriting the risk. It is with respect to the share of the Government is something that we see coming at a lag of on an average of anywhere between 9 to 12 months.

But whenever the premium comes in so far as the Government dues are concerned, we do not end up paying the reinsurance premium to the reinsurance partners immediately and are paid as per defined timelines in accordance with reinsurance contract terms. So we are able to enjoy float in so far as that part of premium is concerned.

Moderator: The next question is from Nidhesh Jain from Investec. Please go ahead.

Nidhesh Jain: How should one look at the investment income, because on a quarter-on-quarter basis there has been a lot of volatility, both on the capital gains and normal investment income. If you look at last quarter the investment income excluding capital gains was around ₹2.8 billion which has grown to ₹3.2 billion this quarter. I can understand there will be volatility in capital gains, but excluding capital gains, why is there so much volatility?

Bhargav Dasgupta: So, one of the things that we have been explaining for some time is that when interest rate goes up, it actually benefits our business because we have roughly 80% of bond portfolio. There is obviously a mark-to-market loss that happens, but as per the accounting

standards our business is HTM business, so we do not account for that mark-to-market losses.

However, the incremental flow that we get, we start earning higher interest because of interest rates going up. So, if you see the quarter on quarter movement on the interest income numbers, last year Q1 we had about ₹ 241 crore, this year we have about ₹ 311 crore, that is a 29% increase. Two main factors, one is the overall quantum of the float that we have obviously has increased and also the interest rate that we are investing in these new floats are coming at a higher number.

Nidhesh Jain: What is the weighted average duration of our investment book?

Gopal Balachandran: About 4.55 years.

Nidhesh Jain: So, almost 20% of your book will reprice in one year at the incremental interest rates?

Gopal Balachandran: Yes.

Nidhesh Jain: On the distribution side, you mentioned that you are focusing on agency and virtual offices. How is the growth trend there and what percentage of our business comes from those channels?

Bhargav Dasgupta: The total number of agents that we had as on 30th June 2017 were 20,775. Compared to this, we have 23,811 agents as on 30th June 2018. We have roughly added about 3,000 agents and these are typically the experienced agents who are migrating to us.

In terms of growth, the SME business which is largely driven by the agency channel, the small brokers and to some extent banca, grew at a robust pace of 40% in the first quarter. It has been a remarkable quarter largely driven by the investment that we made in the agency side. The other segment that the agency drives for us is the retail

indemnity for health. The retail health indemnity portfolio grew at a rate of 31% for this quarter.

Moderator: The next question is from the line of Nishant from Temasek. Please go ahead.

Nishant: The motor TP loss ratio has improved sharply by about 6%. Given that this is actually on model basis and not on incurred basis, what is the assumption change that has happened for the improvement in profitability?

Bhargav Dasgupta: There is no assumption change. It is just that what we talked about in the last year was that there was some amount of, what you see is a financial loss ratio, so that accounts for any changes in results that we may do for the back book. So, one of the thing that we talked about in the past also was that last year we had strengthened the dismantled pool further, even though we believe we had got one of the best reserving standards on that, we still have strengthened the dismantled pool portfolio last year. This year we are not having to do any more strengthening.

Nishant: So this is more indicative of forward-looking steady state?

Bhargav Dasgupta: Yes, kind of.

Nishant: Referring to slide number #8 of the presentation, what goes under the head of property, is it just fire or is it actually retail residential property protection?

Bhargav Dasgupta: Logically, we should have separated property and casualty. But it has got most of the corporate lines. We put it together because the casualty segment is comparatively small. Going ahead, we should call it property and casualty. Property includes fire, engineering, marine, liability. Everything else apart from health, crop and motor.

Nishant: You mentioned of the DAC hitting your profitability on some business lines and upfronted commission benefitting you on crop. The company registered a ROE of 24.7% in Q1FY19. What would be the ROE trajectory for the full year?

Bhargav Dasgupta: I think we should not look at our business on a quarterly basis and should not extrapolate quarterly numbers for the full year or for the longer term, because our business by definition is volatile and the accounting principles create some amount of arbitrary volatility that we have to live with on the insurance side. Secondly, on the investment side we take capital gains when we believe it is the right time. We also remain reasonably optimistic that we will manage to keep the combined ratio below 100%. On the investment side what you have seen is over the last two years, the investment leverage has kept on going up. The investment leverage was 3.90x for FY18, whereas for Q1FY19, it is about 4.01x. It is reflective of two things, one is the strong reserving that we do and also the improvement in terms of combined ratio both reflecting in this number.

Nishant: If we split up the capital gains, how much of it would be due to redemption or just maturity of instruments and how much of it would be due to trading gains of sorts where you are effectively converting that HTM instrument into a trading instrument and hence monetizing it?

Gopal Balachandran: It is not so much for the bond side. It is largely on the equity side. We took a call that we remain slightly cautious on our outlook on equity side in the medium-term. So we wanted to rebalance the portfolio by moving away from some of the stocks that we felt were fully priced. Therefore, it is not so much of a bond churn, but is more of equity.

Moderator: The next question is from Saurabh Das from Franklin Templeton. Please go ahead.

Saurabh Das: You are very cautious on the Government related businesses, given that we also had some adverse experiences in the past. So there is this universal health scheme which is being expanded to a greater section of the population. Can you share your thoughts on what is the company's stance on that? The second question is on a different product line which is auto third party. What is your take on an out of court settlement process versus the regular court processes? Is there any thought change in the way you run that business given that there is a motor vehicle act pending? Will that have any impact on how you look at the business line?

Bhargav Dasgupta: Answering the first question in terms of how we see the NHP scheme, I think we have been having some discussion on this over the quarters and we felt we needed to look at three major aspects. One is, there was at a point in time a plan to cap the pricing, which was extremely worrisome from insurance industry perspective. Now that has been withdrawn, there is now going to be free pricing based on tender, market discovery of pricing. Second concern that we have had with these schemes is that in the past we have seen huge receivable problem on the health side.

On the crop side the scheme is sensible in a sense that you do not have to pay claims till we get the premium money. But that wasn't the case with the earlier health schemes. So this was one of the issue that as an industry we had raised in the discussion with the Government. The good news on that is they have accepted our point and they have now said that there will be an escrow mechanism where 45% of the money will be given upfront, 45% will be given after six months and balance 10% will be given on the 10th month of the policy period. There was initially a talk of guarantee kind of hold back of 10%, that has also been waived. So these issues were obviously very concerning in the past and we would have not looked at the scheme at all with those clauses. Both of these have been changed, which is a big positive. The third aspect that we have

always raised with the Government is that we are there to pay all genuine claims, but we have issue with paying fraudulent claims.

We have been suggesting to the Government that there should be some kind of a centralized data driven monitoring for claims rather than leaving it to the local level intervention, because there are challenges when you try to manage it at a local level. That is something that we have not seen any real progress on, but on the other two we have seen progress.

Now coming to where we see this scheme is headed. If you have seen the number of states and they have divided into category A and category B, different states already indicated whether they want to go with a trust model or with the insurance model. If it is a trust model that is anyway out of scope for the industry, so what is left is the states which are going with the insurance model.

Thereafter, we have to see how the industry conducts itself in terms of bidding, because these are all going to be tender driven policies. So I am just giving you the overall lay of the land in the way it has changed over the last three-four months. Where we stand at this point in time is that in the first tender that came out was Nagaland and we did not bid. We thought the pricing was a bit aggressive, though there is a belief that given that it is Nagaland, the general expectation of claims is usually low, so it could still work at that price. But at that price some of the mainline states will not definitely work.

So we will have to watch how the industry conducts itself in terms of bidding war. We are not very excited about writing a lot of this business at this point in time in-spite of these positive changes that we have seen. We will watch it and even if we finally end up quoting for a tender based on a price that we believe is sustainable.

Saurabh Das: Interesting. Is there a reinsurance possibility on this product line?

Bhargav Dasgupta: There is enough reinsurance capacity in this product line. People are willing to back us and that is not a problem.

Saurabh Das: On the auto third-party segment?

Bhargav Dasgupta: The change that is being proposed in the auto third-party segment is prospective, it is not retrospective. So when we look at the settlement strategy we have a very active management process. Apart from the fraud process, when we look at settlement we have a certain logic of what we settle out of court, what we settle fast and what we want to take till the end where we want to fight. So wherever we have enough concrete proof that we believe will stand up in court, we fight those cases till the end. We believe our exoneration rates are one of the highest in the MACT Courts though there are no public data. Where we believe there is genuineness of the claim we try to settle fast because the claims inflation we assume is higher than the return on investment that we get on the float money so it makes sense to settle fast.

Saurabh Das: So, as of now there is very little in terms of actual data to show, or do you have a trend wherein your out of court settlement proportion is changing over the years?

Bhargav Dasgupta: The number of cases that we are settling are more than the number of cases that we are getting every year.

Moderator: The next question is from Neeraj Toshniwal from Emkay Global. Please go ahead.

Neeraj Toshniwal: You said that the major recovery or the improvement that is reflective of strengthening in motor TP have not been taken this time? How do we see the trend going forward?

Bhargav Dasgupta: While the financial number is as per accounting principles, we also look at what we call our sourcing loss cost in the sense that the

business that we are sourcing today, and what we believe will be the ultimate loss ratios going ahead. There has been some underlying changes in the market. Third party price increase hasn't happened but it has happened for certain segments like medium and heavy commercial vehicles, on which in the past we were cautious. But there are some structural changes in terms of growth, in terms of the consistent price increases that we got in that segment. So, we are increasingly finding pockets of commercial vehicle which is now in our opinion viable which may not have been last year or the year before that. So we are increasing bit of exposure there but on balance the way we look at our business the sourcing loss ratio is what we track and at this point in time we are reasonably happy with the sourcing loss ratio that we are getting for the business we are writing.

Neeraj Toshniwal: We do not have much presence in the heavy commercial vehicle segment. How do we see this segment that in terms of claims?

Bhargav Dasgupta: If you go back to our numbers in 2012, we had a very large share of the commercial vehicle market because third-party component was going into the pool. In a pool, all of us had a quota, so whether we wrote it or not it was coming to us. So it made sense to write commercial vehicles those days because the own damage component was profitable.

When the pool was dismantled in 2012 the third-party component also started coming to the net and that is when we defocused from that segment. So we actually rapidly reduced our exposure to the large commercial vehicle segment at that point in time. What has changed is, some of these underlying environmental changes that have happened. What we have also seen is the trendline in terms of frequency of the claims. Overall accident frequency is also coming down in this country because of better vehicles being built, better roads etc. Over the years, we have built a data pool in terms of hot

spots, the accident spots, which we are factoring before re-entering some of the segments.

Neeraj Toshniwal: What is your view on the new proposal on the multi-axel segment? How do you see overloading stopping? Do you see pricing change for insurance for these products?

Bhargav Dasgupta: I do not see pricing change for insurance for these products.

Neeraj Toshniwal: Now we are more focused on the commercial lines so, what is the outlook?

Bhargav Dasgupta: We are not more focused in commercial lines. If you see our business mix we were 50% private car, 33% two wheelers, 17% commercial vehicle, while industry would be 40% - 45% for commercial vehicle and private car. So, we are significantly underrepresented in the commercial vehicle segment. What we are seeing is we are now opening up some of cells, certain locations which are beginning to become viable from our predicted ultimate loss ratio perspective. So you may see slight increase in share of commercial vehicle, but it will be nowhere near what the market mix is.

Neeraj Toshniwal: Loss ratio in the fire segment has been on the very higher side. Is it a one off?

Bhargav Dasgupta: This is a one-off event and if you look at it on the quarterly basis it will always be volatile. It is one of claim. The claim is reinsured and the net hit for us is not significant. Net hit is about ₹10 crore to ₹ 12 crore for us.

Moderator: Next next question is from Rishi Jhunjhunwala from IIFL.

Rishi Jhunjhunwala: You have talked about going slow in the crop segment. What we saw last year was almost three-forth of the business was coming from

one state, so clearly there was a high concentration risk. Based on your presentation it looks like we have cut down on the number of states as well as on the districts in this year, which means the concentration would be going even higher. If we want to defocus or derisk this portfolio don't you think we could possibly be looking at diversifying in terms of number of states rather than increasing the concentration? Also with MP being the last year in this year how do we think about next year in terms of protecting your existing book?

Bhargav Dasgupta: On the first question, you are absolutely right. It would be ideal if we could diversify across multiple states. But the other consequence of that is it would inflate the total crop book for us which we did not want. So the way we have looked at it is, we have looked at climatic zones, we have added Maharashtra and we have also focused on other states. Madhya Pradesh was bad last year. But MP in general is a state that behaves well and we do not worry about ground level governance issues and moral hazard risk there. Maharashtra, from a crop perspective has been a sensible state. So, we looked at diversification into certain states that we like in terms of their behavior and within that we have looked at agro-climatic distribution, climatic zones across crops, particular crop in a cluster over the last 10 years, how that crop has behaved and accordingly we have selected zones. So we have done a lot of granular work in terms of selection of the clusters that we have taken. We did not want to build further diversification by adding more states simply because we did not want to increase this book significantly. Regarding second question Yes, MP will get over this year and next year we will have to take a call how we want to run this business that we are discussing and debating and we will firm up our mind during the year.

Rishi Jhunjhunwala: Have you increased your ceding ratio in crop substantially this year?

Bhargav Dasgupta: No, it is similar. 26% is what we retained on net and roughly about 74% is reinsured. Our stop loss ratio also has not changed and is same 110%.

Rishi Jhunjhunwala: We have seen some slowing down of growth on a year on year basis in the motor OD segment. What are the implications of the MISP as it have been around seven-eight months since its implementation. Theoretically it should have resulted in increase in market share for the larger players, including us. So, is our growth rate actually lower than the industry?

Bhargav Dasgupta: MISP has had a tremendous benefit in terms of reduction in the distribution cost. Some of the expense ratio savings that you are seeing this quarter is also driven by the fact that the distribution cost for the industry has come down. One of the things that we have been saying from September, even before the MISP came was that we never believed and we do not believe that 100% of the benefit in terms of distribution cost reduction would get passed on to the insurance companies.

That is not possible and that has not happened. So part of the benefit has flowed to the customer in terms of pricing correction. So, we think July number should be very good as the month of June was very good for the automobile industry. But that apart, we have not seen a similar growth for the own damage component for the industry.

Now, coming to your specific question on market share, the OD growth rate for the industry for the first quarter was 4.7%, whereas we grew at 5.6%. Where we have grew less in the market is the third-party segment where the market has grown at 11.9%, and we have grown at 8.5%, to a large extent driven by the fact that the TP price increase was largely in the CV and large CV segment where we have a very low share.

The two-wheeler, where we have a very large share, did not see much of a TP growth. So that is one of the reasons why our TP growth has been a bit less. Again, one of the concern that we have been voicing is that we were always worried about some market conduct issues in some of the larger dealerships, and that has played out. We are seeing some behavior which we cannot really support or endorse in terms of breaching the limit of distribution commission.

Obviously the regulator is also aware of these developments and they are watching it. I think they have done some round of investigations of a few companies and they will do the rest soon. So, we are hopeful that some of these things are not long term in nature. What we have also done is we have added a huge amount of distribution to the smaller towns and that is giving us a good traction. The reason why our OD number has grown is because of penetration in Tier-III and Tier-IV cities, the virtual offices that we have set up, smaller dealerships that we have gone into which we believe is pretty sustainable in the long term.

Moderator: The next question is from the line of Prakhar Sharma from CLSA.

Prakhar Sharma: The investment book is up almost ₹1,600 crore on a QoQ basis. You reported a profit of less than ₹ 300 crore. So seems like you have borrowed this quarter. Can you explain what is driving this? On a QoQ basis also, the borrowing book is up almost ₹1,100 crores. Basically, I am going by the number that, last March 2018 you have ₹18,200 crore and now you have ₹19,900 crores as your investment book.

Gopal Balachandran: The number that you see in the balance sheet as at the end of March is about ₹18,200 crore and at the end of the June quarter, the number is about ₹19,873 crores. We have witnessed steady flow of premiums from time to time. So that is largely contributing to the increase in

the overall investment book. Also, with respect to the improved performance from the combined ratio standpoint, we have seen a positive improvement in the incremental contribution to the investment book. We were also able to realize certain outstanding receivables in this quarter, particularly with respect to the dues from the Government on the crop insurance side which were remaining outstanding as at the end of 31st March.

So, all of this has contributed to the accretion happening to the overall investment book. So far as borrowings are concerned, it continues to be at ₹4.85 billion.

Prakhar Sharma: Is the current liability increase of ₹1,100 crore, practically the dues for your clients, basically the potential loss value?

Gopal Balachandran: Yes, exactly. One of the things that we have always been talking about is of the total reserves that we create as a company. Almost about 55% to 60% of those reserves continue to remain as outstanding, and largely contributed by the third party segment which has got a long tail in so far as settlement of claims are concerned. And that also kind of adds to the kitty so far as the investment book is concerned. Which is why if you look at the investments to net worth in terms of the increase in float, that has seen an increase from 3.9 to 4.01 times.

Prakhar Sharma: Is it possible to share within your unrealized gain book which was almost like ₹600 crore plus and now is about ₹70-odd crore, what is the split between equity and debt?

Bhargav Dasgupta: Most of the change has been largely because of the bond portfolio. The bond portfolio which was at that point in time largely kind of breakeven has become negative because of the interest rates moving up in this quarter. On the equity side we have taken out some gains. On the equity side, we still have more than ₹500 crore of equity gains.

Prakhar Sharma: So that can still be booked?

Bhargav Dasgupta: Yes, that can be booked.

Prakhar Sharma: You mentioned that the SME business is growing well, at around 42% growth. Can you explain what is this business, because it probably is concoction of a few lines of businesses?

Bhargav Dasgupta: So, it is basically what a typical corporate would buy covers. This would be fire, engineering, marine, this would be small ticket over the counter goods and products. But these are smaller corporate, SMEs. So the distribution model for large corporate is a direct sales model. Here we work with small brokers and agents and these are the guys who go out and source this business. The business is very granular and our experience over the years is that, this has been a very profitable portfolio for a couple of reasons. One, the agents have very strong relationships with these corporate and they are able to get reasonably sustainable prices. Secondly, there is obviously a huge portfolio diversification happening because of the small granularization of the risk. Overall, when you build a large portfolio it becomes very profitable for us.

Prakhar Sharma: What edge do you have vis-à-vis competition and can 40% kind of a growth continue for a year or two? Will this book continue to outgrow your overall premium growth?

Bhargav Dasgupta: We will continue to outgrow our overall growth because if you remember even when we did the IPO, this was one segment that we said that we are investing in and we have been seeing more than 30% growth for the last two years. This fast growth has been happening due to multiple factors. Firstly, there is migration of quality distribution. It is a focused strategy and we are consciously seeing how we can build a quality agency distribution.

We are also seeing shift of business to private sector and a lot of these businesses are coming in the SME segment. Thirdly, we have done a lot of work in terms of claim service which is reasonably well known. Finally, what we have kind of invested for the last year, year and a half has been on the distribution technology. So these are assisted sales, where an insurance agent can actually issue a policy for fire without interacting with the underwriter using this robotic process assessment tool that we have built. Similarly, on our agent portal or agent app for SMEs we have added lot of functionalities and lot of flexibility over the years. A lot of that is still ongoing work that we are doing to make the issuance process and the empowerment for the agent significantly superior to what probably others have..

Prakhar Sharma: How big would this be in proportion to the overall premiums?

Bhargav Dasgupta: It is ₹300 crores for the quarter.

Prakhar Sharma: Do you think, motor third-party loss ratios would they have bottomed out or there is hope because on one side you are realigning your loss or reserving and on the other hand the tariff hikes for your segments have been pretty low this year.

Bhargav Dasgupta: Difficult to estimate, but I think from a combined perspective we are reaching a good place, because we are seeing some amount of motor own damage pricing corrections which is less than the benefit that we got from the distribution cost. So it will also depend on some of the lines that we end up writing. So for example, group health by design will be a higher loss ratio business. The sourcing cost is less but the loss ratio is high. So on combined front it may work but loss ratio optically might look high. Overall, we will be happy to retain the combined ratio of 98%I rather than try to take it down further.

Prakhar Sharma: Actually, I meant to check on the motor TP.

Bhargav Dasgupta: We think that the number should hold for the motor TP segment If we do not get a hike next year, what we do as a company is by design assume an inflation. So, by design the reserving that we will do be at an elevated level compared to what we will have this year. So, it is all subject to what price increases we get next year.

Prakhar Sharma: Any material impact on the underwriting losses due to the recent Mumbai rains?

Bhargav Dasgupta: No, nothing to speak of.

Moderator: Our next question is from Gaurav Nigam from Catamaran. Please go ahead.

Gaurav Nigam: I understand, ICICI Lombard generates lot of business from the agents directly and there have been change in regulation last year wherein IRDA introduced the regulation wherein brokers can appoint these agents. We have been hearing from the market is that these agents of individual insurers are going out and becoming agents of brokers. What is you view on that and do you think because of that thing your direct business which is coming from agents is now going to the brokers who might have a higher pricing power over time because of this?

Bhargav Dasgupta: We are not seeing that, there may be little bit of movement here and there. One or two of the brokers are trying to do that. The new regulation is a very positive development for us as an industry and we are in fact actively building up the number of such agents that we have. If you see the numbers, 14% - 15% increase in our agency base in one year is a pretty decent growth for us. So we are not seeing the heat of this issue at all. In fact, we are seeing agency migration towards us as we speak.

Gaurav Nigam: But is this a threat that agents are not remaining exclusive now?

Bhargav Dasgupta: Agents are never exclusive. Theoretically they are always tied but most agents, at least large agents would have a license in the name of relative. So effectively they would be tied as per that license, but they would go and offer three, four company solutions to a client.

Moderator: Thank you very much. I would now like to hand the conference back to the management for any closing comments.

Bhargav Dasgupta: Thank you, everyone. We are always available to explaining more if you need to understand separately. Please feel free to reach out to us. Thank you again and look forward to talking to one quarter later.

Moderator: Thank you very much. On behalf of ICICI Lombard General Insurance Company Limited, that concludes this conference. Thank you for joining us, ladies and gentlemen. You may now disconnect your lines.