

**Title slide**

- Good morning everyone, and welcome to this supplementary presentation to our usual interim results webcast. As this is the first time we are reporting our results under IFRS 17, I thought it would be helpful if I went into deeper technical detail on some specific topics, so you can better interpret our half-year performance.
- I will be focused solely on accounting under IFRS 17. Along with Aki and Jo, I will cover business performance in our main results presentation.

Let me first summarise the agenda for today.

**Slide: Agenda**

- Building on my presentation in June, I will give you some more modelling tips on claims discounting, and how to think about the corresponding partial offset from movements in our bond portfolio.
- Then I'll move on to LPTs. Although these have a net nil impact on the income statement when combined with gross reserve movements under the LPT's protection, they distort various disclosures and income statement lines, and I want to explain what we are doing to help you understand underlying movements.
- On both these topics, I also want to acknowledge the modelling challenges they present, especially on LPTs. My presentation is unfortunately not going to give all the answers to help you model. However, it will explain why there is no perfect modelling solution and give you some practical suggestions on how to separate the noise they inject into the presentation of our results.
- Finally, the analysis of change is a new disclosure under IFRS 17, and I wanted to provide you with some pointers of what to focus on, and some of the pitfalls when analysing it.

So dust off your notes from my June presentation, and let's get started with discounting on claims.

**Slide: Claims discounting**

- As you know, the IFRS 17 accounting standard introduces discounting of claims liabilities which partially offset movements on assets, reducing volatility and creating better symmetry in the income statement.
- At our June restatements session, we outlined to you how we think about discounting claims liabilities in three steps, and I'll now go into this in more detail, using our actual half year numbers to explain each step:
  - step one: is the initial discount on recognition of the claim, and this element is recognised at the prevailing interest rate, which is a bottom-up approach. As a guide, our average weighted rate was 4.2% in the first half of 2023;
  - next, step two: the unwind of the discount, which flows through the IFIE. This unwind will be a combination of prior and current year claims, as they settle. Prior year reserves unwind using a 31 December 2022 yield curve which we published in our June restatements presentation. For current year reserves, use a 31 March yield curve, in other words, the mid-point of the period. As I've footnoted on the slide, in practice we use a ground-up approach here and the unwind calculation is done on a monthly basis using interpolated rates;
  - finally step three: the impact of rate change. To run this calculation, you need to do the following:
    - for prior period claims, multiply the prior period claims reserve on the balance sheet by the difference in rate from the start to the end of the period, so by 0.4% in H1 2023, as rates moved from 4.3% to 4.7%;
    - and for current-year claims, use the difference between the rate used in step one, 4.2%, and rate at the end of the period, 4.7%, so by 0.5%.
- Over the last 12 months interest rates have continued to increase. So, what does this mean for the discounting impact at half year?
- For step one, you can see the amount of \$70.2 million is \$42.2 million higher than prior year. For step two, the half year unwind of \$63.7 million is within our guidance of \$60 million–\$65 million, and our full-year guidance of \$110 million–\$140 million remains unchanged. As you would expect, step three has significantly reduced in quantum to \$25.9 million as we are currently seeing a more stable rate environment.
- It is worth noting that the sensitivity analysis we provided you in June checks out and you can continue to use this for your modelling. As a reminder, we said a 100 basis point rate movement would give a \$55 million impact to PBT. So the 40 basis point movement in rate this half gives a sensitivity of \$22 million, broadly in line with our actual figure of \$25.9 million. Please note that we have now issued our current sensitivity which is broadly unchanged.
- The net impact on profit across all three steps is positive \$32.4 million. However please do bear in mind that these are non-cash impacts; where we take a benefit from initial claims discounting, this will then have the opposite impact in future periods as the discount unwinds over the duration of our book.
- Finally, before I move on, I also wanted to cover off one other topic, which is the impact of a change in claims settlement pattern on discounting. The expected settlement pattern is locked in the discount unwind for the

entire year. The actual settlement pattern can often deviate from expectations, particularly in the big-ticket businesses which are exposed to larger more idiosyncratic loss events. The discounting impact of the difference between the actual and expected settlement flows through claims incurred – i.e. as part of step one.

- For example, if our actual claims settlement is slightly slower than expected:
  - the undiscounted reserve will decrease more slowly than we expected, and this means the actual discounting benefit, which goes through claims incurred, is higher than expected;
  - the unwind within the IFIE is locked in at the outset based on the expected settlement pattern;
  - so what this means is the discounted claims incurred is effectively understated but the unwind in the IFIE is overstated, and the discounted combined ratio absorbs the benefit of the higher than expected discounting.
- This ultimately has a nil impact on profit and is merely a timing difference, however this means there may be a bigger difference between the discounted and undiscounted combined ratios. For example, in H1 2023 the overall impact of discounting on the Re & ILS combined ratio is 4.9 percentage points versus 1.1 at full year 2022, as you can see in our June presentation. And of that, 3.5 percentage points is due to the impact of discounting on prior year claims, driven by the difference between actual and expected claims settlement pattern.

So that's the liabilities taken care of, now let's turn to assets.

#### Slide: Bond movements

- I appreciate that most of you know how our bond portfolio moves with interest rates as you have been modelling this for several years, but let me briefly cover key points for completeness.
- I've set the slide out with the same structure as claims, to help you understand the offsetting components which I will cover on my next slide. You'll notice there are only two rows in the table, each representing how our investment result from bonds moves with interest rates. The initial discounting of claims has no corresponding offset on the asset side, as the amount we have available to invest is determined by the amount of premiums we have collected, rather than the present value of claims we expect to pay.
- Taking each row in turn:
  - bond income comprises the coupons from our bond portfolio. When we reinvest bonds on maturity, their coupon will increase or decrease depending on the change in yield, which of course changes with interest rate. Our coupon increased significantly in the first half of 2023 to \$84.0 million. Bond income is included in the investment return line within the income statement;
  - secondly, we have the mark-to-market movements on our bond portfolio. There are various drivers of mark-to-market movements as I've set out in the slide. In the first half, we had a net mark-to-market gain of \$6.5 million. Although there was a modest increase in yields in the first half of the year which resulted in a negative MTM movement equivalent to the sensitivity we disclosed in June, this was offset by a combination of reduction in spreads, manager alpha and any credit rating changes. As with liabilities, we have also released an updated sensitivity which is broadly unchanged, however as you can see, there are many other moving parts when you model the MTM component of the investment result.
- So overall in the first half we had a net positive movement on the bond portfolio of \$90.5 million.

So let's now marry the assets up with the liabilities so you can see the overall reduction in volatility in the income statement.

#### Slide: Income statement volatility reduced

- In the old IFRS 4 world, we only had the grey bars on this chart, meaning our bottom line, as for all insurers, was sensitive to interest rate movements.
- With the introduction of claims discounting, represented by the purple bars on the chart, there is now better symmetry and as a result income statement volatility is reduced.
- The offset is not a perfect match as you can see, and I wouldn't expect it to be, for three reasons:
  - firstly, our bond portfolio of circa \$5.8 billion, is larger than our net claims liabilities of circa \$3.3 billion, so rate changes will naturally have a larger impact on the asset side as you can see in the chart.
  - Secondly, there are differences in the rates used for discounting claims versus those used for assets. Also worth mentioning, these rates differ slightly to those used to calculate our BSCR, as we are mandated to use prescribed rates published by the BMA.
  - And lastly as I've just explained, the bond coupon is not exactly matched to the liability discount unwind.
- So a key takeaway here is that, yes, there is less income statement volatility, but it is not fully eliminated.

Now let me move onto our second topic, LPTs.

**Slide: LPTs – reminder of treatment in the financial statements**

- I thought it would be useful to firstly set the scene and remind you of how LPTs are treated in the financial statements.
- Do bear in mind this is purely a worked example, the numbers are not real, as I wanted to create a simplified explanation to help your understanding.
- This is quite a busy slide, and I'm not going to talk to all of it. But there are three key takeaways I wanted to draw out:
  - firstly, after initial recognition, LPTs have no impact on profit when combined with gross reserve movements under the LPT's protection, they simply create noise in various income statement lines throughout their lifetime;
  - secondly, LPTs are initially recognised as an unearned asset under IFRS 17. Therefore, they run-off, or earn, throughout their coverage period. In the example on the slide, you can see the LPT runs-offs at 50 in year one, 30 in year two, and ten in year three. In rough terms, the typical run-off period for our LPTs is circa five years in line with the expected payment pattern of the gross claims they are protecting. In the income statement, this is recognised as equal and opposite entries in allocation of reinsurance premium, and amounts recoverable from reinsurers. This grosses up these two income statement lines, artificially inflating them even if the impact on the insurance service result is nil; and I'll show you this on the next slide.
  - Lastly, there may well be a change to our initial expectation of recoveries from the gross claims under the LPT's protection. In the example of the slide, there is a deterioration of gross reserves of two in year three, partially offsetting the run-off of ten, meaning the unearned portion of the LPT only decreases by eight in the period. While the deterioration of gross reserves is intuitively recognised in the insurance service result, the offsetting LPT recovery that the deterioration triggers is recognised in a reduction of reinsurance premium, rather than an increase in reinsurance recoveries as one might expect. So in summary, there is an additional LPT recovery of 2 to offset the gross reserve deterioration meaning the impact on the insurance service result is nil, however it is not recognised as a reinsurance recovery. This treatment is frankly confusing, but we are required to account for LPTs like this under the new standard.

Staying with LPTs, let's take a look at what we're doing to try and remove the noise LPTs create in our combined ratio.

**Slide: LPTs – economic benefit unchanged but some lines in income statement distorted**

- I've set out at the top of the slide another illustrative example of the income statement distortion I talked about on the previous slide.
- In this example, we'll assume that no new LPTs were entered into during the period, and thus there is no impact on profit as you can see from the unchanged insurance service result of 20. LPTs are also discounted in reality, but again I have ignored this impact to simplify the example.
- The dark grey middle column on the slide shows the income statement as it gets reported under IFRS 17, however this is distorted by the LPT treatment. Let me explain this for you.
  - The run-off of the LPT artificially inflates reinsurance premium and reinsurance recoveries by ten as you can see in the second column in the table.
  - Moving to the third column, reinsurance premium is being further distorted by the gross loss experience movement. You might expect the increased recovery to come through reinsurance recoveries, but in fact the benefit of two comes through reinsurance premium. This artificially understates reinsurance recoveries by two, and therefore the net claims position looks worse than it actually is, as there is no offset to the gross claims deterioration.
  - Having said all this, I'll reiterate my message from the previous slide, the net impact on the insurance service result is still nil reflecting the economic benefit of the LPT protection.
  - So to have a more economic view of the income statement, it helps to reclassify LPT movements from reinsurance premium and put them into reinsurance recoveries where they would more intuitively sit. I've highlighted this in the penultimate column of the table, where eight is reclassified to reinsurance recoveries. Notice again, this has not impacted the insurance service result, just the geography of the income statement.
- Changes in the gross loss experience of the LPT are dependent on the claims development trend and are not easily predictable. This presents an unfortunate modelling challenge, and to my frustration, there is no hack or top-down approach I can provide you with to accurately predict this.
- As I outlined in June, we have therefore adjusted our COR definition to remove the impact of LPTs, to reduce volatility and offer better comparability period on period. The Group LPT adjustment, which we will disclose by

segment, for the first half of 2023 was \$24.3 million. This is equivalent to the adjustment of eight in the worked example, so your view of the income statement for the COR calculation is the far right-hand column.

- Despite all of the complexity IFRS 17 has created for LPT accounting, my final message on this slide is an important one. That is to say there is no change to the economic benefit of LPTs; the noise and volatility is purely from the accounting the new standard requires.

Moving to my third topic the new analysis of change disclosure.

**Slide: Analysis of change**

- I'm not going to spend too long on this slide, however for those of you still grappling with the new disclosure, let me briefly summarise what it is as I didn't cover this off in my June presentation.
- The AOC provides a walk of technical balances from the opening to closing balance sheet, by presenting movements in both the income statement and cash flows. It is a Group level disclosure, and it is not required to be presented for each of our segments, much to the relief of my financial reporting team given the complexity involved in creating it.
- Movements in the insurance service expense, are split between current and prior accident years, and are further dissected by best estimate (labelled as 'estimates of present value of future cash flows' in the disclosure), risk adjustment, and onerous contracts. So there's a lot of granular detail in the AOC, however I've given you a simple high level view of the overall construction here on the slide.
- The disclosure is long, complex, and contains some figures that are more helpful than others. I've set out on the right-hand side of the slide some tips for analysing the new disclosure. I won't talk to all of these, however there are three points I want to draw out.
  - Firstly, because the AOC splits claims between current and prior year, you will be able to read off our prior year claims development, though I'll cover this in more detail on my next slide as there are some adjustments that you will need to make.
  - Secondly, please do take care when analysing discounting and LPT treatment in the AOC. LPTs are only included within the asset for remaining coverage. Also, the risk adjustment is not discounted but the best estimate is. This leads nicely into my final point on confidence level.
  - Confidence level is the IFRS 17 measure of reserve conservatism and this will be disclosed in our results. So do use this to compare our reserve adequacy period on period, rather than the ratio of risk adjustment to best estimate; the impact of discounting on this ratio as I just outlined means it will not give you a good view of underlying trends in our reserves.

There's one more thing I wanted to cover off on the analysis of change, and that is how to read our prior year claims development numbers.

**Slide: LPTs – additional disclosures to show underlying trend in PYD**

- You will be familiar with our usual PYD slide in our results presentations. Our PYD figure is also now presented in the new analysis of change disclosure.
- However, there are two key things to remember in order to reconcile between the PYD figure you see in our results presentation of \$62 million at half year, and that presented in the analysis of change of \$105 million. This is that the analysis of change includes discounting, but does not allow for LPTs, which is the opposite to our management presentation. I've set out the reconciliation here for you on the slide.
- We use the management presentation view internally, as it removes volatility and offers better period on period comparability. We have added extra disclosures to the analysis of change so that you can reconcile these numbers, however we recommend you use the undiscounted view allowing for LPTs when analysing our period on period reserve development.

I've now reached the end of my presentation, and I hope it has provided you with a good understanding of how discounting and LPTs have been treated under IFRS 17 within our interim results; and that you also have a good lead in to understanding the new analysis of change disclosure. Thank you for listening, and I look forward to speaking to you all again soon.