

IAG announces FY08 result in line with July guidance and reports progress with implementation of operating model

Insurance Australia Group Limited (IAG) today announced a net loss after-tax of \$261 million (FY07: net profit of \$552 million) for the year ended 30 June 2008 including nearly \$400 million (after-tax) of restructuring and impairment charges.

This outcome is in line with the guidance provided at IAG's trading update in July. Key features of the result are:

- A 5.6% increase in gross written premium (GWP) to around \$7.8 billion;
- An insurance margin of 6.1% (FY07: 11.4%) and insurance profit of \$448 million (FY07: \$767 million), which were adversely impacted by:
 - Increased claims costs from natural perils, up 22% to \$502 million (FY07: \$411 million), well above allowances;
 - A \$122 million impact from widening credit spreads (FY07: nil); and
 - Lower reserve releases, down 16% to \$406 million (FY07: \$485 million).
- Significantly lower income on shareholders' funds, of \$24 million (FY07: \$301 million), reflecting weaker investment markets;
- A \$60 million restructuring provision in respect of the devolved operating model being introduced in Australia and in the corporate office; and
- A non-cash after-tax writedown of approximately \$350 million in respect of the UK assets, following the decision to narrow IAG's focus in that market.

As previously foreshadowed, the Board has declared a fully franked final dividend of 9 cents per share payable on 3 October 2008 to shareholders registered on 3 September 2008 (FY07: final dividend 16 cps). This takes the total dividend to 22.5 cents per share (FY07: 29.5 cps).

IAG Managing Director and CEO, Mr Michael Wilkins said: "This is a poor result. While we have been affected by the increased frequency of natural perils, widening credit spreads and soft cycles in key markets, we have acknowledged we need to do better. We've recently made some tough decisions to ensure we get the fundamentals right and set a clear course for the future. We are confident these measures will underpin improved future profitability."

"We're increasing our discipline and focus. In both Australia and New Zealand, rate increases are being implemented in line with rising claims costs and frequency, while in commercial insurance we have ceded volume to maintain price discipline. In the UK, we are shifting the mix of our portfolio towards the more profitable specialty motor classes."

Mr Wilkins confirmed that IAG is on track with the implementation of the initiatives announced in July, which are designed to improve both margin and profitability. In accordance with the refined strategy outlined last month, the Group has:

- Moved to a simpler operating model, which will drive improved performance of the Australian and New Zealand businesses;
- Commenced the restructure of its Australian operations and corporate office to deliver around \$130 million in annual before-tax (run-rate) savings;
- Continued to pursue select growth opportunities in Asia, including finalising arrangements with State Bank of India to form a joint venture, which is expected to be trading in 2009; and

- Commenced the staged exit of the private motor and mass market distribution operations of Hastings/Advantage and Equity Insurance Brokers in the UK, as well as the sale of the Alba and Diagonal reinsurance vehicles.

Business Segments

The Australian Direct Insurance business had underlying GWP growth of 3.8% for the full year (adjusted for the impact of the Lifetime Care & Support Scheme). The Queensland and Western Australian portfolios grew by around 10%, while the largest portfolio, NSW home and motor, grew 4.1%. The insurance margin for the year was lower at 11.1%, affected by storms and widening credit spreads.

GWP in the Australian Intermediated Insurance business (CGU) decreased 1.8% as the business maintained underwriting discipline and chose not to renew business where pricing was inadequate. The insurance margin was down from 9.4% to 7.4% due to higher storm costs, claims inflation, lower reserve releases and widening credit spreads. The June renewal season showed promising signs around the cycle, particularly in the SME market while in the middle market renewals were generally maintained at expiring terms.

The New Zealand business recorded an insurance loss of \$17 million due to an unprecedented number of claims from storms, an earthquake and other large losses. Revenue was up 2.4% in local currency terms, benefiting from rate increases, in particular in the commercial market where the cycle is hardening.

In the UK, Equity Red Star remained profitable while Advantage improved its performance in relation to the market and is now operating at close to break-even. The private motor market remained difficult. In response the Group implemented further rate increases and reduced exposure to private motor in favour of specialist lines. In line with the refined corporate strategy, the Group is now scaling back its UK operations to the specialist underwriter, Equity Red Star and associated specialist distribution.

In Asia, the Group's insurers in Thailand grew GWP by 5.1% in local currency terms while AmAssurance, in which the Group has a 30% interest, increased GWP by 15% in local currency terms. The profitability of both was affected by weak investment markets.

On 13 May 2008, the Group announced it was in exclusive negotiations with the State Bank of India, India's largest bank, to form a joint venture that will underwrite and distribute general insurance. The venture is expected to commence trading in 2009.

Capital and Investments

The Group continues to maintain a very strong balance sheet, with a Minimum Capital Requirement multiple of 1.62x as at 30 June 2008. IAG's key wholly owned insurers remain the highest rated of any Australian-based general insurer, with a Standard & Poor's insurer financial strength rating of 'AA-' (Stable).

Investment income from shareholders' funds reduced during the period as a result of weak markets globally. The Group's return from shareholders' funds was \$24 million, which included a \$69 million revaluation benefit from the RES exchange right embedded in the Group's fully funded off balance sheet contingent capital arrangement. This compares with an investment return of \$301 million in FY07.

Outlook¹

Mr Wilkins said the actions the business was taking to increase its efficiency, maintain pricing discipline and improve the customer experience should give shareholders confidence that the current financial year will bring an improved performance.

He said the Group expected to generate underlying GWP growth of 3–5% for the year ending 30 June 2009, while reported GWP is expected to grow around 0–2% due to the Group's change in its UK strategy and the introduction of six-month CTP policies in NSW.

The Group's FY09 insurance margin is expected to be above 10%, and now includes corporate expenses and the NSW Insurance Protection Tax, which were previously reported separately and are equal to about 1% of the reported margin.

"IAG is a unique asset with leading franchises and iconic brands," Mr Wilkins said.

"We are confident that our revised strategy and actions will improve shareholder value in FY09 and beyond."

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About Insurance Australia Group Limited

Insurance Australia Group Limited (IAG) is an international general insurance group, with operations in Australia, New Zealand, the United Kingdom and Asia. Its current businesses underwrite more than \$7.5 billion of premium per annum. It employs more than 16,000 people of which around 11,000 are in Australia. It sells insurance under many leading brands including NRMA Insurance, CGU, SGIO, SGIC and Swann (Australia); NZI and State (NZ); Equity Red Star (UK); and NZI and Safety (Thailand). For further information please visit www.iag.com.au

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¹ Subject to no material movement in foreign exchange rates, no catastrophes or large losses beyond the Group's allowances and no material changes in credit spreads.

FACT SHEET

22 AUGUST 2008



INSURANCE AUSTRALIA GROUP RESULTS FOR THE 12 MONTHS TO 30 JUNE 2008

| Summary information | 12 months to 30 Jun 2007 \$m | 12 months to 30 Jun 2008 \$m |
|--|---------------------------------|---------------------------------|
| Gross written premium (GWP) | 7,381 | 7,793 |
| Net earned premium (NEP) | 6,743 | 7,295 |
| Net claims expense | (4,474) | (5,155) |
| Underwriting profit/(loss) | 407 | 16 |
| Investment income on technical reserves | 360 | 432 |
| Insurance profit | 767 | 448 |
| Net corporate expenses ¹ | (69) | (125) |
| Profit from fee based business / share from associates | 83 | 25 |
| Investment income on shareholders' funds | 301 | 24 |
| Amortisation ² | (55) | (407) |
| Net profit/loss after tax attributable to holders of ordinary shares | 552 | (261) |
| Group combined ratio | 94.0% | 99.8% |
| Immunised Group combined ratio | 95.1% | 100.3% |
| Group insurance margin (before tax) | 11.4% | 6.1% |
| Dividend per share (cents, fully franked) | 29.5 | 22.5 |

1: Includes \$60m provision for restructuring costs

2: Includes \$342m of write-downs of goodwill and identifiable intangibles

Group Summary

- **Operating environment** characterised by continuing soft cycles in the Australian commercial and UK motor insurance markets, another year of high claims from natural perils and volatile investment markets. The natural perils are summarised below.

| FY08 NATURAL PERILS AND ASSOCIATED CLAIMS COSTS | | |
|---|---------------|----------------------|
| Event | | Net Cost (A\$) |
| NZ Northland storm | July 2007 | \$32 million |
| UK floods | July 2007 | \$49 million |
| Lismore (NSW) hailstorm | October 2007 | \$68 million |
| Western Sydney (NSW) hailstorm | December 2007 | \$110 million |
| Melbourne (VIC) storms | December 2007 | \$21 million |
| NZ Gisborne earthquake | December 2007 | \$9 million |
| Mackay (QLD) storms | February 2008 | \$51 million |
| Victorian windstorm | April 2008 | \$20 million |
| Other small events | | \$142 million |
| TOTAL | | \$502 million |

- **Net loss after tax** of \$261 million, which includes nearly \$400 million in restructuring and impairment charges.
- **Gross written premium** growth of 5.6% to \$7,793 million, mostly attributable to the inclusion of a full year's business from the UK operations.
- **Insurance margin** of 6.1%, affected by a \$91 million increase in claims from natural perils (to \$502 million), a \$122 million impact from widening credit spreads (or a 1.7% margin impact) and a reduction in prior period reserve releases from \$485 million to \$406 million.
- **Final dividend** of 9 cents per ordinary share, fully franked, bringing total dividends for the year to 22.5 cents per ordinary share.
- **Balance sheet** strength maintained, with a Minimum Capital Requirement coverage of 1.62x as at 30 June 2008.
- **Refined corporate strategy** introduced, with a focus on margin and profitability.

Australia

Direct Insurance

- Total GWP growth of 3.8% on FY07, after adjusting for the impact of the NSW Lifetime Care & Support Scheme. Short-tail GWP growth of 3.9% on FY07.
- Measured by registrations, CTP market share in NSW maintained at 38% and increased to 6.4% in Queensland.
- Insurance profit of \$312 million, or a 11.1% insurance margin, reflecting the impact of wider credit spreads on investment income, adverse weather, lower levels of releases and increased costs.
- Customer satisfaction index at 84.
- Growing focus on managing expenses and claims costs, and underwriting discipline.

| | |
|-----------------------|-----------------|
| Gross written premium | \$2,941 million |
| Net earned premium | \$2,806 million |
| Underwriting profit | \$108 million |
| Insurance profit | \$312 million |
| Insurance margin | 11.1% |

Intermediated Insurance (CGU)

- Integration of Business Partnerships division into CGU, which now includes all products sold through intermediaries, such as brokers and authorised representatives, motor dealerships and financial institutions.
- Continued soft cycle in commercial overall, with promising signs around the cycle in some classes.
- GWP decrease of 1.8%, in line with decision to lead the market in introducing price increases, but retention rates on existing business steady at around 80%.
- Continued impact of weather events, with the Mackay storms and the Victorian windstorm as the most significant events in 2H08.
- Pricing discipline maintained, with some loss of business as a result. Expense control and productivity focus continues.

| | |
|-----------------------|-----------------|
| Gross written premium | \$2,553 million |
| Net earned premium | \$2,363 million |
| Underwriting profit | \$31 million |
| Insurance profit | \$174 million |
| Insurance margin | 7.4% |
| Fee based business | \$33 million |

International

UK

- Operating environment challenging, with the private motor market remaining soft and the influence of aggregators continuing to grow. However, specialist motor classes continue to trade profitably and rate rises are holding.
- Insurance profit of \$28 million, with Equity Red Star maintaining its profitability track record and Advantage reporting further losses. Equity Red Star is withdrawing capacity from underperforming elements of private motor and substituting with premium in specialist classes.
- Equity insurance margin of 10.6%, affected by poor investment market returns in the second half.
- Integration benefits of \$60 million before-tax.
- Revised strategy implemented, with scale-back of operations planned, and only Equity Red Star and specialist broker Bennett & Bennett being retained.

| | |
|--|-----------------|
| Gross written premium | \$1,125 million |
| Net earned premium | \$999 million |
| Underwriting profit/(loss) | \$(33) million |
| Insurance profit | \$28 million |
| Insurance margin | 2.8% |
| Fee based business / share from associates | \$(4) million |

New Zealand

- Premium rate environment improving, with early signs of a bottoming out of the commercial market, but claims growth outpacing rate increases.
- GWP growth in local currency terms of 2.4%, reflecting progress in the intermediated channel.
- Net claims expenses up \$73 million due to higher catastrophe costs, abnormally large claims losses and an increase in underlying claims frequency and average claims costs.
- Customer retention levels steady despite significant rate increases in certain classes.
- Conversion to new IT system for direct insurance completed, improving underwriting capability and data access.

| | |
|----------------------------|----------------|
| Gross written premium | \$974 million |
| Net earned premium | \$845 million |
| Underwriting profit/(loss) | \$(39) million |
| Insurance profit/(loss) | \$(17) million |
| Insurance margin | (2.0)% |

Asia

- Growth in Thailand and Malaysia more subdued than in recent years, reflecting economic circumstances, declining consumer confidence and currency weakness.
- Thailand GWP growth 5.1% in local currency terms, primarily driven by Safety Insurance.
- AmAssurance GWP growth 15% in local currency terms, helped by further penetration of AmBank network and introduction of new products using IAG's capability transfer, but profitability affected by lower investment returns and claims trends.
- IAG selected as preferred partner by State Bank of India for a general insurance venture.
- Progress made with planned increase of IAG's holding in AmAssurance to 49%.

| | |
|--|---------------|
| Gross written premium | \$174 million |
| Net earned premium | \$132 million |
| Underwriting profit/(loss) | \$(1) million |
| Insurance profit | \$3 million |
| Insurance margin | 2.3% |
| Fee based business / share from associates | \$(4) million |

Strategic Priorities

- Improvement of the performance of the Australian and New Zealand businesses.
- Pursuit of international growth opportunities in Asia and other select segments of the Group's existing markets.
- Completion of the devolution to end-to-end responsibility for the businesses, with a corporate office acting as portfolio manager.
- Driving of operational performance, execution and accountability.
- Return on Equity of at least 1.5x Weighted Average Cost of Capital and top quartile shareholder return through the cycle.

Group Outlook for FY09*

- Underlying GWP growth of 3-5% targeted in FY09, with reported growth expected around 0-2% taking into account the planned exit from part of the UK operations and the impact of the introduction of six-month CTP policies in NSW.
- FY09 insurance margin of 10%+, including previously excluded corporate expenses.
- Reduction of operational costs by \$130 million per annum before-tax, with approximately 75% of the annual savings to be realised in FY09.
- Dividend expected in line with revised policy to pay out 50-70% of reported cash earnings.

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* Subject to no material movement in foreign exchange rates, no catastrophes or large losses beyond the Group's allowances and no material changes in credit spreads.