

Genworth Mortgage Insurance Australia Limited First Half 2020 (1H20) Earnings Update

Key Points:

- Statutory net profit after tax (NPAT) of \$90.0 million loss (1H19: \$88.1 million profit) and underlying NPAT¹: \$85.5 million loss (1H19: \$43.1 million profit).
- 1H20 result affected by anticipated economic impacts of COVID-19 that led to a \$181.8m Deferred acquisition costs (DAC) write-down in 1Q20, and additional \$35.5 million loss reserving (pre-tax).
- Gross written premium (GWP) up 30.0% to \$239.3 million (1H19: \$184.1 million), reflecting housing market recovery pre-COVID-19, ongoing low interest rates and strong lender customer performance.
- Net earned premium (NEP) increased 2.2% to \$150.8 million (1H19: \$147.6 million), in line with seasoning of current and prior book years and higher GWP.
- Loss ratio increased to 67.0% (1H19: 54.1%), due to the COVID-19 related increase in loss reserving.
- Strong liquidity and capital position, with a solvency ratio of 1.77 times Prescribed Capital Amount (PCA), above the Board's target capital range of 1.32 to 1.44 times on a Level 2 basis and representing surplus capital of \$276.5 million above the top of the range.
- Net tangible assets of \$3.37 per share (1H19: \$4.14).
- Interim ordinary dividend of Nil (1H19: 9.0 cents per share).

SYDNEY 30 July 2020 – Genworth Mortgage Insurance Australia Limited (Genworth or the Company) (ASX: GMA) today reported its financial results for the half year ending 30 June 2020 (1H20)².

Genworth Chief Executive Officer and Managing Director, Ms. Pauline Blight-Johnston said, “Genworth’s first half performance reflects the sound fundamentals of our business which, along with a strong capital base and leading market position, has set us up well to manage the impacts of COVID-19. We responded quickly to the pandemic and have adapted our ways of operating in a manner that prioritises the well-being of our people and supports our lender customers and their borrowers in these challenging times.”

Genworth’s first half result has been affected by the anticipated economic impacts of COVID-19 that led to a deferred acquisition cost (DAC) write-down of \$181.8 million (pre-tax) at 31 March 2020 and a \$35.5 million (pre-tax) increase in loss reserving.

Genworth delivered higher volume in its core Lenders Mortgage Insurance (LMI) business, with new insurance written (NIW) up 8.1% to \$13.5 billion (1H19: \$12.5 billion), reflecting housing market growth in the major capital cities pre-COVID-19 and the benefit of a low interest rate environment. Volumes continued to grow over the second quarter, with strong lender customer performance accompanied by improving consumer confidence as COVID-19 restrictions began to ease. The fixed income and equities portfolios also benefited from tightening credit spreads and a rally in fixed income and equity prices, reversing first quarter losses.

Government restrictions to suppress the spread of COVID-19 led to a slowdown in lender customer loss management processes with legal moratoriums and repayment deferrals that reduced the incidence of new delinquencies and cures. Net claims incurred increased to \$101.1 million reflecting additional COVID-19 loss reserving which resulted in a loss ratio of 67.0%.

¹ Underlying NPAT is based on Statutory NPAT but excludes the after tax effect of (a) unrealised losses of \$3.2 million on the investment portfolio (1H19: \$45.4 million gain); and (b) foreign exchange rates (net of hedge) on Genworth’s investment portfolio (1H20: \$1.3 million loss; 1H19: \$0.4 million loss).

² The financial result of Genworth and its subsidiary companies (the Group) is prepared in accordance with the Australian Accounting Standards (AAS) adopted by the Australian Accounting Standards Board (AASB), which are consistent with those under the International Financial Reporting Standards (IFRS).

1H20 DETAILED FINANCIAL PERFORMANCE

Financial performance measures (A\$ million unless otherwise stated)			
	1H19	1H20	Change
New insurance written ³	12,480.0	13,487.7	8.1%
Gross written premium	184.1	239.3	30.0%
Net earned premium	147.6	150.8	2.2%
Statutory net profit/(loss) after tax	88.1	(90.0)	(N.M.) ⁴
Underlying net profit/(loss) after tax	43.1	(85.5)	(N.M.)
Loss ratio (%)	54.1%	67.0%	12.9%
Total portfolio delinquencies (#)	7,891	7,614	(3.5%)
Portfolio delinquency rate (%)	0.60%	0.62%	2bps

New insurance written (NIW) increased 8.1% to \$13.5 billion (1H19: \$12.5 billion). **Gross written premium (GWP)** increased 30.0% to \$239.3 million (1H19: \$184.1 million). The NIW and GWP growth reflected the increase in LMI business written by lender customers arising from the pre-COVID housing market recovery supported by a low interest rate environment.

Net earned premium (NEP) increased 2.2% to \$150.8 million (1H19: \$147.6 million), in line with seasoning of current and prior book years and higher GWP. Genworth's **Unearned premium** was \$1.3 billion (1H19: \$1.2 billion).

Statutory NPAT of \$90.0 million loss includes the \$127.3 million DAC write-down (after tax) at 31 March 2020 and the COVID-19 \$24.9 million (after-tax) increase in loss reserves.

Underlying NPAT of \$85.5 million loss, excludes the unrealised losses of \$3.2 million (after tax) on the investment portfolio and the after-tax impact of foreign exchange rates (net of hedge) on Genworth's investment portfolio (\$1.3 million loss).

The **delinquency rate**⁵ increased 2 basis points to 0.62% (1H19: 0.60%). This increase reflects continued policy cancellation activities reducing the insured loans in-force exposure.

New delinquencies were down 9.6% to 4,988 (1H19: 5,515) as lender customer loss management processes slowed with legal moratoriums and loan repayment deferrals. Similarly, **cures** were down 6.0% to 3,904 (1H19: 4,154).

The number of **paid claims** was up 12.4% to 691 (1H19: 615) reflecting borrowers taking advantage of the improved property market earlier this year while the \$94,900 average paid per claim was similar to 1H19 (1H19: \$94,200).

Net claims incurred was \$101.1 million (1H19: \$79.8 million). This reflected the additional COVID-19 loss reserving. The **loss ratio** was 67.0% (1H19: 54.1%) as a result of the increase in COVID-19 loss reserving.

The **expense ratio**, excluding the net impact of the DAC write-down⁶ of 35.6% (1H19: 34.7%), reflected increased underwriting and operations costs due to higher workloads resulting from repayment deferrals and closer scrutiny of applications.

³ Excludes excess of loss insurance.

⁴ N.M. Not Meaningful (increases / decreases > 200%).

⁵ Delinquency rate is the number of delinquencies divided by policies in force, excluding excess of loss insurance.

⁶ \$181.8m DAC write-down in 1Q20, less associated 2Q20 DAC amortisation benefit of \$12.3m.

Investment income was \$49.8 million (1H19: \$114.9 million) with \$58.6 million earned in 2Q20 mainly due to tightening credit spreads and a rally in fixed income and equity prices. 1H20 net interest and dividend income declined to \$27.2 million (1H19: \$42.4 million) due to the low interest rate environment. During the half year, \$29.0 million of realised gains (1H19: \$8.2 million) and \$4.6 million of unrealised losses (1H19: \$64.9 million gain) resulted from declining interest rates, widening credit spreads and increased volatility in equity markets.

The 1H20 annualised investment return⁷ was 1.7% p.a. (1H19: 2.6% p.a.) with returns continuing to be pressured by the low interest rate environment.

As at 30 June 2020, the value of Genworth's cash and investment portfolio was \$3.2 billion, of which 81% was held in cash and fixed interest securities with a rating of 'A-' or better. The Company had \$84.5 million invested in equities together with \$636.9 million of the investment portfolio invested in non-AUD income securities⁸.

STRONG CAPITAL POSITION WITH FLEXIBILITY

Genworth's regulatory solvency ratio was 1.77 times the Prescribed Capital Amount (PCA) ratio on a Level 2 basis at 30 June 2020, above the Board's target range of 1.32 to 1.44 times representing surplus capital of \$276.5 million above the top of the range.

At 30 June 2020, the Company had \$800 million of excess of loss reinsurance cover with a well-diversified panel of over 20 reinsurers with a minimum rating of 'A-'. The program was renewed on 1 January 2020 and provides a one-year cover with an option to extend to a full term (6-10 years depending on the layer).

At 30 June 2020, Genworth's wholly owned subsidiary, Genworth Financial Mortgage Insurance Pty Limited (GFMI) held \$200 million of Tier 2 subordinated notes. During the period GFMI successfully exchanged \$146.6 million of these existing 2015 subordinated notes into new subordinated notes and issued \$43.4 million additional new subordinated notes, both settling on 3 July 2020.

Following these transactions, GFMI had \$243.4 million subordinated notes on issue comprising \$190 million of 2020 Tier 2 subordinated notes that will receive full Regulatory Capital credit for the next 5 years, and \$53.4 million of 2015 Tier 2 subordinated notes that continue to receive full Regulatory Capital credit until 2 July 2021, subsequently reducing by 20% (\$10.7 million) annually until maturity on 3 July 2025. Genworth has APRA's approval, valid to 30 September 2020, to repurchase \$43.4 million of the 2015 Tier 2 subordinated notes to ensure the total Tier 2 subordinated notes on issue remain at \$200 million. Subject to APRA approval the 2015 Tier 2 subordinated notes may be partially (or fully) called at each quarterly coupon date.

Due to the ongoing uncertain economic outlook, and APRA's recent guidance, the Company believes it is prudent to preserve capital to sustain its strong capital position. In these circumstances [the Board has decided not to pay an interim ordinary dividend in 2020]. Any future dividend will be subject to economic conditions, retaining a strong capital buffer and may require APRA approval.

RATINGS AGENCIES RECOGNISE CAPITAL ADEQUACY STRENGTH

Following an assessment of the impact of the COVID-19 pandemic, in May 2020, ratings agencies revised the insurer financial strength (IFS) rating of the Company's operating subsidiary GFMI.

Genworth's rating was affirmed by Standard & Poor's at 'A'; with the outlook changed from 'stable' to 'negative'. Fitch revised its rating from 'A+' (Strong) to 'A' (Strong); with the outlook maintained as 'negative'. Both agencies acknowledged the capital strength of Genworth and strong competitive position. The change in these ratings has no impact on the contractual arrangements that exist between Genworth and its lender customers.

⁷ Investment return is net interest and dividend income / average of opening and closing total cash and investments for the period.

⁸ The bulk of foreign exchange (FX) exposures of the non-AUD investments are hedged through forward FX derivative contracts.

ECONOMIC ENVIRONMENT

The road to economic recovery continues to be supported by an unprecedented level of fiscal stimulus, accommodative monetary policy and lender support programs. Genworth welcomes the Government's recent decision to extend the JobKeeper Payment by six months, with new eligibility criteria and tapered payments supporting a gradual transition to economic recovery. Genworth also welcomes the recent extension by four months of the mortgage repayment deferral programs offered by lenders and we are working closely with them to provide ongoing support to borrowers.

Unemployment arising from the lockdowns and structural changes to industries directly and indirectly impacted by the closures, are expected to weigh on the medium-term economic outlook. House prices are moderating in the metropolitan centres, and the short to medium term outlook for the national housing market will ultimately depend on the continued containment of COVID-19 and the sustained return of consumer confidence. The latest economic and housing indicators are broadly consistent with Genworth's Central Estimate scenario assumptions underpinning the DAC write-down in 1Q20 and the Company considers these assumptions continue to be reasonable.

Genworth has been analysing lender customer data on repayment deferrals since March. At 30 June 2020, we had received over 48,000 payment deferrals from our lender customers, representing circa 4 per cent of our insured loans in force. We expect the volume of repayment deferrals has peaked notwithstanding the program being extended, as lenders are actively segmenting and managing the deferrals resulting in increasing numbers of borrowers opting out or being taken off the program.

The extension beyond September of the government stimulus and lender initiatives beyond September 2020 will delay and help to cushion the effect of COVID-19 on Genworth's claims experience. Genworth's ultimate COVID-19-related claims will depend on the pace of the ensuing economic recovery, that will influence loss experience following the repayment deferrals.

VALUED CUSTOMER PARTNERSHIPS

Genworth is the market leader in LMI with 50% market share by GWP⁹. In the first half, Genworth renewed its largest customer for a further three years; and renewed other lender customers including an exclusive LMI relationship with a non-major bank, and extended its relationship with a mutual lender, for the first time on an exclusive basis, for a three-year period.

In June, NAB advised the Company that it would not renew Genworth's LMI supply and services contract that expires in November 2020. The revenue impact of the loss of this contract will be offset to some extent by continuing business growth from other lender customers.

WELL POSITIONED TO SUPPORT CUSTOMERS

Commenting on the first half result, Ms. Blight-Johnston said, "The anticipated impacts of COVID-19 on Genworth are playing out broadly in line with our 1Q20 assumptions at this stage, although there remains a long road ahead of us. The strengthening of reserving for the first half reflects this, and we will continue to consider the adequacy of our reserves as more information comes to hand. Notwithstanding early encouraging signs in Australia, significant global economic uncertainty remains, and the risk of deterioration in Australia's health and economic position is ever present.

"We are working closely with our lender customers and in these challenging times we are maintaining our high service level standards. Our people have transitioned seamlessly to a new way of operating, largely due to the investment over the past few years in enhancing our core capabilities and investing in technology and data.

⁹ Based on APRA Quarterly Authorised Deposit-taking Institution Property Exposures Statistics at 31 March 2020. Australian LMI market by GWP includes bulk portfolio loans and loans covered by excess of loss insurance, excludes retained risk and waived LMI loans.

“We have expanded our Natural Disaster Policy and adapted our processes to manage the increased transaction volumes, whilst prudently managing underwriting risk. We continue to respond with appropriate loss mitigation activities to work in tandem with the various stimulus packages, income support and repayment deferrals, to ensure that the Company is able to assist lenders and borrowers both at this time of need and over the longer term.

“Genworth’s capital strength along with the flexibility we have built with our reinsurance programs, positions the business well at this time. We will continue to work closely with our lender customers to support Australian borrowers to stay in their homes wherever possible.”

ENDS

For more information, analysts, investors and other interested parties should contact:

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Conference Call

Date: Thursday 30 July 2020 – 10.00am (Sydney time)

Conference name: Genworth Australia First Half 2020 Financial Results

Conference ID: 4556683

Australia dial-in details: 1800 123 296 (toll free) or +61 2 8038 5221 (toll)

International dial-in details

These numbers are toll-free dial-in numbers for each country listed below. For countries not listed below, the Australian participant toll number listed above can be dialled.

Canada	1855 5616 766	New Zealand	0800 452 782
China	4001 203 085	Singapore	800 616 2288
Hong Kong	30082034	United Kingdom	0808 234 0757
Japan	0120 994 669	United States	1855 293 1544

About Genworth

Genworth Mortgage Insurance Australia Limited (Genworth), through its subsidiary companies Genworth Financial Mortgage Insurance Pty Ltd and Genworth Financial Mortgage Indemnity Ltd (together, the Genworth Group or the Group), is the leading provider of Lenders Mortgage Insurance (LMI) in the Australian residential mortgage lending market. The Genworth Group has been part of the Australian residential mortgage lending market for over 50 years since the Housing Loans Insurance Corporation was founded by the Australian Government in 1965 to provide LMI in Australia. Genworth is currently a subsidiary of Genworth Financial, Inc. and part of the Genworth Financial, Inc. group of companies. The Genworth Financial, Inc. group of companies’ current ownership interest in Genworth is approximately 52% of the issued shares in Genworth.

The release of this announcement was authorised by the Board.