NEW ZEALAND EQUITY RESEARCH | INSURANCE | GENERAL INSURANCE
24 NOVEMBER 2022

Tower Limited
FY22 Guidance Beaten But One-offs Impact

JAMES LINDSAY
James.Lindsay@forsythbarr.co.nz
+64 9 368 0145

Tower (TWR) reported a solid FY22 result, with underlying NPAT up +31% to NZ$27.3m from NZ$20.8m in FY21. Reported NPAT was flat at NZ$18.9m relative to NZ$19.3 in FY21 after including the higher Christchurch earthquake costs and one-off policy remediation provisions. The Board declared a 2H22 dividend of NZ4cps, the largest since 2016, bringing full-year dividends to NZ6.5cps, ahead of our NZ5.5cps expectations. In FY22, gross-written-premium (GWP) grew as management successfully passed on inflationary pressures, undertook the bancassurance acquisitions and via organic growth. A continued focus on achieving cost efficiencies meant FY22 exceeded earlier guidance of underlying NPAT between NZ$21m and NZ$25m. Management's intial FY23 guidance is for NPAT between NZ$27m and NZ$32m. We lift our FY23 forecast +2% to NZ$29.9m. Our blended spot valuation rises to NZ$0.80, from NZ$0.78.

NZX Code	TWR
Share price	NZ$0.69
Spot Valuation	NZ$0.80 (from 0.78)
Risk rating	High
Issued shares	379.5m
Market cap	NZ$262m
Avg daily turnover	124.4k (NZ$83k)

Financials: Sep/	22A	23E	24E	25E
NPAT* (NZ$m)	17.7	29.9	34.6	36.9
EPS* (NZc)	4.4	7.9	9.1	9.7
EPS growth* (%)	0.2	77.5	15.6	6.7
DPS (NZc)	6.5	6.5	7.0	7.5
Imputation (%)	0	0	0	50

*Based on normalised profits

Valuation (x)	22A	23E	24E	25E
PE	15.5	8.8	7.6	7.1
EV/EBIT	n/a	n/a	n/a	n/a
EV/EBITDA	n/a	n/a	n/a	n/a
Price / NTA	1.5	2.0	2.3	2.6
Cash div yld (%)	9.4	9.4	10.1	10.9
Gross div yld (%)	9.4	9.4	10.1	13.0

What's changed?

- **Earnings:** Underlying NPAT+2% to NZ$29.9m with our FY24 forecast rising by +1% and FY25 falling by -3%.
- **Spot valuation price:** Our spot valuation rises to NZ$0.80, +2cps, driven by higher investment earnings.

Positive core business and market improvements continue

TWR's core business showed improvements in several areas over the year. Customer numbers grew +5% from 304,000 a year ago to 319,000 in FY22. The company did well to pass on the inflation seen in its motor and dwelling claims costs, lowering the business as usual claims ratio to 48.9%. Management expense ratio fell to 36% in FY22 from 37% in FY21, demonstrating continued cost control and the benefits of scale. TWR's investment income was +NZ$1.2m, slightly above our expectations. A higher running yield on the investment portfolio will help future results, which was at 4.1% as of 30 September 2022.

Christchurch provisions again affect results

The result included two negatives, with a further NZ$5.5m after-tax Christchurch earthquake provision and one-off costs associated with an error in calculating multi-policy discounts of NZ$2.6m after-tax. The earthquake provision increased due to further inflationary impacts and new claims over the EQC cap. This is disappointing given prior comments from the company that they had worked with EQC to avoid further new claims. We have always taken a more conservative view of Christchurch claims costs. We retain our additional NZ$10m provision over and above that assessed by TWR in our valuation.

FY23 outlook improves

Management provided FY23 underlying NPAT guidance between NZ$27m and NZ$32m. Our prior underlying NPAT forecast was NZ$29.3m. In this update, we lift our estimates to NZ$29.9m following further rises in interest rates. At the midpoint of management's range, this is up +8% on underlying FY22 numbers, fueled by management forecasts of +10% to +15% GWP growth (excluding the sold PNG business). Management guided to a FY23 dividend flat on FY22 at NZ6.5cps (providing a ~9.4% gross yield, unimputed), and we lift our estimate to match this DPS number from NZ6.0cps prior.

Tower Limited (TWR)

Market data (NZ$)	
Priced as at 23 Nov 2022	**0.69**
52 week high / low	0.73 / 0.60
Market capitalisation (NZ$m)	261.8

Key WACC assumptions	
Risk free rate	4.50%
Equity beta	1.10
WACC	10.1%
Terminal growth	1.8%

Profit and Loss Account (NZ$m)	2021A	2022A	2023E	2024E	2025E
Sales revenue (GEP)	395.5	418.3	472.5	520.7	556.6
Normalised EBITDA	**n/a**	**n/a**	**n/a**	**n/a**	**n/a**
Depreciation and amortisation	n/a	n/a	n/a	n/a	n/a
Normalised EBIT	**n/a**	**n/a**	**n/a**	**n/a**	**n/a**
Net interest	n/a	n/a	n/a	n/a	n/a
Associate income	0	0	0	0	0
Tax	(9.1)	(7.5)	(13.8)	(15.9)	(16.9)
Minority interests	0.6	0.1	0	0	0
Normalised NPAT	**18.7**	**17.7**	**29.9**	**34.6**	**36.9**
Abnormals/other	0	0	0	0	0
Reported NPAT	**18.7**	**17.7**	**29.9**	**34.6**	**36.9**
Normalised EPS (cps)	4.4	4.4	7.9	9.1	9.7
DPS (cps)	5.0	6.5	6.5	7.0	7.5

Growth Rates	2021A	2022A	2023E	2024E	2025E
Revenue (%)	6.2	5.8	13.0	10.2	6.9
EBITDA (%)	n/a	n/a	n/a	n/a	n/a
EBIT (%)	n/a	n/a	n/a	n/a	n/a
Normalised NPAT (%)	57.1	-5.4	69.3	15.6	6.7
Normalised EPS (%)	55.4	0.2	77.5	15.6	6.7
Ordinary DPS (%)	n/a	30.0	0.0	7.7	7.1

Cash Flow (NZ$m)	2021A	2022A	2023E	2024E	2025E
EBITDA	**n/a**	**n/a**	**n/a**	**n/a**	**n/a**
Working capital change	n/a	n/a	n/a	n/a	n/a
Interest & tax paid	0	0	0	0	0
Other	0	0	0	0	0
Operating cash flow	**99.7**	**8.6**	**40.6**	**44.9**	**47.4**
Capital expenditure	(12.0)	(17.3)	(13.9)	(15.1)	(15.9)
(Acquisitions)/divestments	(14.4)	(6.1)	4.1	0	0
Other	(24.5)	(13.3)	(6.8)	(7.4)	(7.7)
Funding available/(required)	**48.7**	**(28.2)**	**24.0**	**22.4**	**23.7**
Dividends paid	(10.5)	(20.0)	(24.7)	(26.6)	(28.5)
Equity raised/(returned)	0	(30.6)	0	0	0
(Increase)/decrease in net debt	**38.2**	**(78.8)**	**(0.7)**	**(4.1)**	**(4.8)**

Balance Sheet (NZ$m)	2021A	2022A	2023E	2024E	2025E
Working capital	146.9	183.2	171.7	186.3	196.4
Fixed assets	9.4	5.4	6.9	8.3	9.5
Intangibles	120.6	132.5	131.2	135.4	139.0
Right of use asset	25.6	23.3	20.6	17.9	15.2
Other assets	313.0	295.6	295.6	295.6	295.6
Total funds employed	**615.5**	**640.0**	**626.0**	**643.5**	**655.7**
Net debt/(cash)	(116.1)	(84.5)	(83.8)	(79.7)	(74.9)
Lease liability	39.4	35.1	28.3	20.9	13.2
Other liabilities	342.5	383.5	419.4	453.2	476.6
Shareholder's funds	347.0	306.0	262.1	248.9	240.7
Minority interests	2.7	0	0	0	0
Total funding sources	**615.5**	**640.0**	**626.0**	**643.5**	**655.7**

Spot valuation (NZ$)	**0.80**
PE relative	0.82
P/Book relative	0.79
DCF	0.77

DCF valuation summary (NZ$m)	
Total firm value	376
(Net debt)/cash	2
Less: Capitalised operating leases	(52)
Value of equity	326

Valuation Ratios	2021A	2022A	2023E	2024E	2025E
EV/EBITDA (x)	n/a	n/a	n/a	n/a	n/a
EV/EBIT (x)	n/a	n/a	n/a	n/a	n/a
PE (x)	15.6	15.5	8.8	7.6	7.1
Price/NTA (x)	1.3	1.5	2.0	2.3	2.6
Free cash flow yield (%)	38.1	3.3	15.5	17.1	18.1
Net dividend yield (%)	7.2	9.4	9.4	10.1	10.9
Gross dividend yield (%)	7.2	9.4	9.4	10.1	13.0

Key Ratios	2021A	2022A	2023E	2024E	2025E
Return on assets (%)	n/a	n/a	n/a	n/a	n/a
Return on equity (%)	5.4	5.8	11.4	13.9	15.3
Return on funds employed (%)	0.0	0.0	0.0	0.0	0.0
EBITDA margin (%)	n/a	n/a	n/a	n/a	n/a
EBIT margin (%)	n/a	n/a	n/a	n/a	n/a
Capex to sales (%)	3.0	4.1	2.9	2.9	2.9
Capex to depreciation (%)	n/a	n/a	n/a	n/a	n/a
Imputation (%)	0	0	0	0	50
Pay-out ratio (%)	113	146	82	77	77

Capital Structure	2021A	2022A	2023E	2024E	2025E
Solvency capital	155.9	150.5	179.4	136.4	167.7
Minimum solvency capital (MSC)	56.6	52.3	66.3	66.5	73.6
Total regulatory capital	106.6	102.3	83.3	91.3	91.3
Solvency ratio (%)	275	287	271	205	228

Operating Performance	2021A	2022A	2023E	2024E	2025E
Gross written premium	404.7	445.6	499.5	541.9	571.3
Gross earned premium	**395.5**	**418.3**	**472.5**	**520.7**	**556.6**
Reinsurance premium	(62.2)	(66.3)	(68.8)	(75.4)	(80.5)
Net earned premium	**333.3**	**352.1**	**403.7**	**445.3**	**476.1**
Net claims expense	(204.3)	(224.9)	(257.9)	(285.6)	(306.4)
* includes Large event claims of	(13.9)	(19.0)	(30.0)	(31.0)	(32.0)
Management & sales expenses	(123.3)	(129.9)	(142.9)	(152.1)	(158.5)
Underwriting profit	28.0	23.6	32.3	37.0	40.7
Investment and other revenue	0.2	1.2	12.3	14.4	14.1
Financing and other costs	(0.4)	(0.9)	(0.9)	(0.9)	(0.9)
Profit before tax	**28.5**	**25.2**	**43.7**	**50.5**	**53.9**
Tax expense	(9.1)	(7.5)	(13.8)	(15.9)	(16.9)
Profit after taxation (Reported)	**19.3**	**17.7**	**29.9**	**34.6**	**36.9**
Abnormals	(1.1)	0	0	0	0
Comprehensive profit	**18.2**	**17.7**	**29.9**	**34.6**	**36.9**

Key ratios					
Tower Direct GWP growth %	26.4%	17.2%	11.2%	9.0%	5.0%
Partnership GWP growth %	-30.0%	13.0%	14.0%	8.0%	7.0%
Total GWP growth %	7.3%	10.1%	12.1%	8.5%	5.4%
Total claims ratio %	54.3%	54.1%	56.6%	57.5%	58.2%
MER %	37.1%	36.0%	35.4%	34.2%	33.3%
Combined ratio %	91.4%	90.1%	92.0%	91.7%	91.5%

FY22 review showing good underlying progress

TWR's FY22 result delivered a reported NPAT of NZ$18.9m, relative to NZ$19.3m in the pcp. Underlying profit after tax was NZ$27.3m, up from NZ$20.8m last year. The difference between underlying and reported numbers was due to the provision of NZ$2.6m for remediation to multi-policy holders, who were overcharged, and an additional NZ$5.5m Christchurch earthquake outstanding claims provision.

At the top line, underlying gross-written-premium (GWP) was NZ$457m, up +13% on last year. The significant uplift in GWP was due to the strong growth TWR has experienced in NZ, with acquisitions plus inflationary impacts being passed on via pricing and new business growth helping. The reported GWP, which removes the now sold PNG operations and customer remediation charges, was NZ$446m, up +13% on the FY22 reported figure. TWR has seen a continued improvement in the management expense ratio (MER), falling to 36% in FY22 from the 37% seen in FY23. TWR's solvency position remains strong post recent acquisitions and divestitures. See Figure 7 below. The January 2022 volcanic eruption in Tonga, and the corresponding NZ$6.8m of claims, led TWR's Pacific Island insurance unit to report an NPAT loss of -NZ$4.3m for the period.

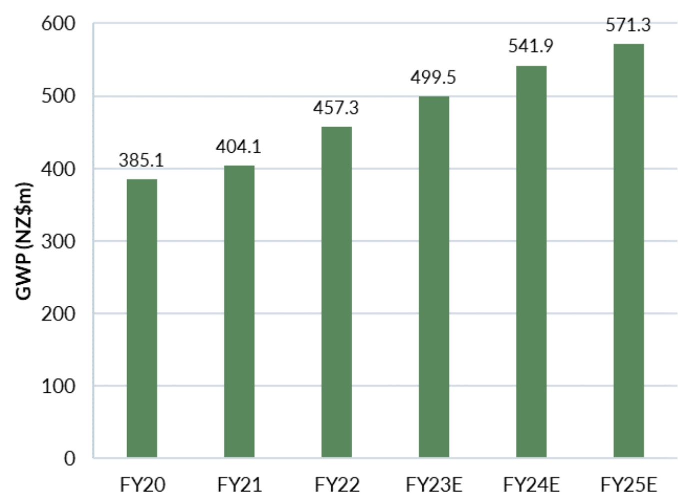
The company announced a final (unimputed) dividend of NZ4cps for payment on 1 February 2023, bringing the full-year dividend to NZ6.5cps. This was above our NZ5.5cps dividend forecast for the year.

Figure 1. TWR – comparison of FY21 and FY22 results

	FY21	FY22	Change (%)
Gross written premium	404.1	457.3	13.2%
Gross earned premium	394.9	430.7	9.1%
Reinsurance Expense	(62.2)	(69.5)	11.7%
Net earned premium	**332.7**	**361.2**	**8.6%**
Net Claims Expense	(166.8)	(176.5)	5.8%
Large event claims expense	(13.9)	(19.0)	36.7%
Management expenses	(112.0)	(120.6)	7.7%
Net Commission Expense	(11.3)	(9.3)	-17.8%
Underwriting profit	**28.7**	**35.8**	**24.8%**
Net Investment Income	0.2	1.2	480.0%
Other costs	1.4	1.3	-7.1%
Profit before tax	**30.3**	**38.3**	**26.3%**
Tax expense	(9.5)	(10.9)	14.7%
Underlying Profit after tax	**20.8**	**27.4**	**31.6%**
Canterbury impact on outstanding claims	0.9	(5.5)	
Multi-policy holder discount remediation	-	(2.6)	
Other non-underlying items	(2.4)	(0.4)	
Reported Profit after tax	**19.3**	**18.9**	**-2.2%**

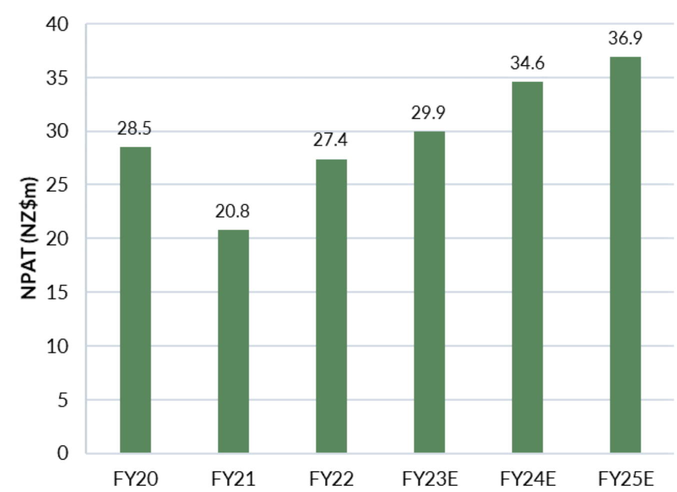
Source: Company, Forsyth Barr analysis

Figure 2. TWR – Underlying GWP (NZ$m)



Source: Company, Forsyth Barr analysis

Figure 3. TWR – Underlying NPAT (NZ$m)



Source: Company, Forsyth Barr analysis

Earnings revisions

We lift our FY23 NPAT forecast by +2% to NZ$29.9m while slightly increasing our FY24 forecast by +1% and reducing our FY25 forecast by -3%. In more detail, our earnings revisions include the following:

- Across the forecast horizon we make material upgrades to investment income, given the recent upward interest rate movements. TWR invests its investment portfolio, NZ$259m at FY22, in 6-month government bonds, with approximately half the cash position of NZ$85m invested at or near the prevailing OCR. The six-month NZ Government Bond yield has risen from 0.83% as of the FY21 balance date to 4.20% at the FY22 balance date. The current yield on the six-month Government bond is 4.87%. TWR exited FY22 with a 4.12% running yield, implying a slight mark-to-market loss for FY23, however, more than offset by higher interest income.
- We change a mix of management expenses and claims costs.
- We forecast a return to profit for TWR's Pacific Island operations in FY23, given that the costs of the Tongan eruption were the largest in 100 years.
- We forecast a more modest MER ratio improvement than in FY22 with a continued cost-efficiency focus and good top-line GWP growth further helping economies of scale. See Figure 8 below.
- CFO said, "*Post balance date we have an approximate gain on sale of NZ$2.1m [on the PNG business]; however, as we announced in September we also have the purchase of the Kiwibank legacy book completing in December. So these two factors will approximately equal and offset themselves during 1H23*".

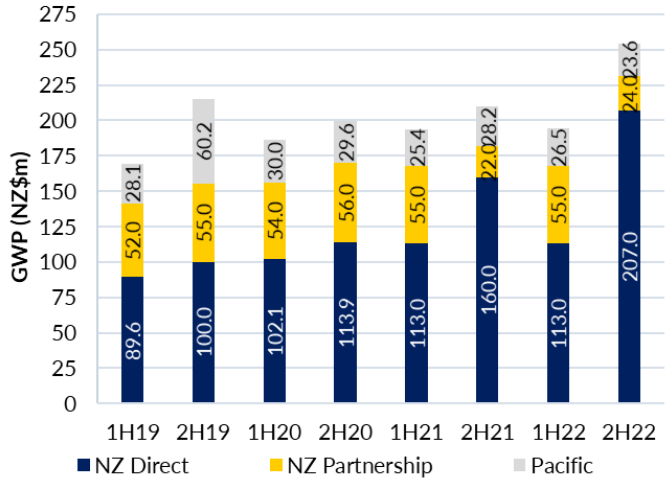
Figure 4. Underlying earnings revisions

	FY23E			FY24E			FY25E		
	Old	New	Change	Old	New	Change	Old	New	Change
Gross written premium	**499.8**	**499.5**	**0%**	**542.0**	**541.9**	**0%**	**571.5**	**571.3**	**0%**
Gross earned premium	474.2	472.5	0%	520.9	520.7	0%	556.8	556.6	0%
Reinsurance expense	(68.6)	(68.8)	0%	(75.5)	(75.4)	0%	(81.1)	(80.5)	-1%
Net earned premium	405.5	403.7	0%	445.4	445.3	0%	475.7	476.1	0%
Net claims expense	(206.9)	(198.5)	-4%	(233.0)	(225.2)	-3%	(253.1)	(245.0)	-3%
Large event claims expense	(30.0)	(30.0)	0%	(31.5)	(31.0)	-2%	(33.0)	(32.0)	-3%
Management and sales expenses	(134.9)	(142.9)	6%	(139.4)	(152.1)	9%	(143.6)	(158.5)	10%
Underwriting profit	**33.7**	**32.3**	**-4%**	**41.5**	**37.0**	**-11%**	**46.0**	**40.7**	**-12%**
Investment and other revenue	11.4	12.3	8%	11.1	14.4	30%	11.7	14.1	21%
Financing costs	(0.9)	(0.9)	n/a	(0.9)	(0.9)	n/a	(0.9)	(0.9)	n/a
Underlying profit before tax	**44.2**	**43.7**	**-1%**	**51.7**	**50.5**	**-2%**	**56.8**	**53.9**	**-5%**
Income tax expense	(14.9)	(13.8)	-7%	(17.3)	(15.9)	-8%	(18.8)	(16.9)	-10%
Underlying profit after tax	**29.3**	**29.9**	**2%**	**34.3**	**34.6**	**1%**	**38.0**	**36.9**	**-3%**
Reported profit / (loss) after tax	**29.3**	**29.9**	**2%**	**34.3**	**34.6**	**1%**	**38.0**	**36.9**	**-3%**

Source: Company, Forsyth Barr analysis

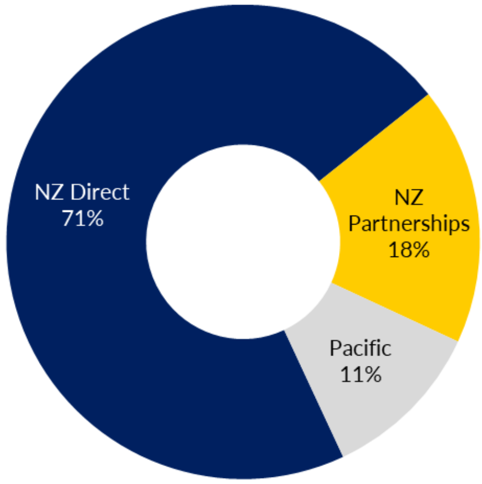
Key TWR related charts

Figure 5. TWR — GWP by division (half-on-half)



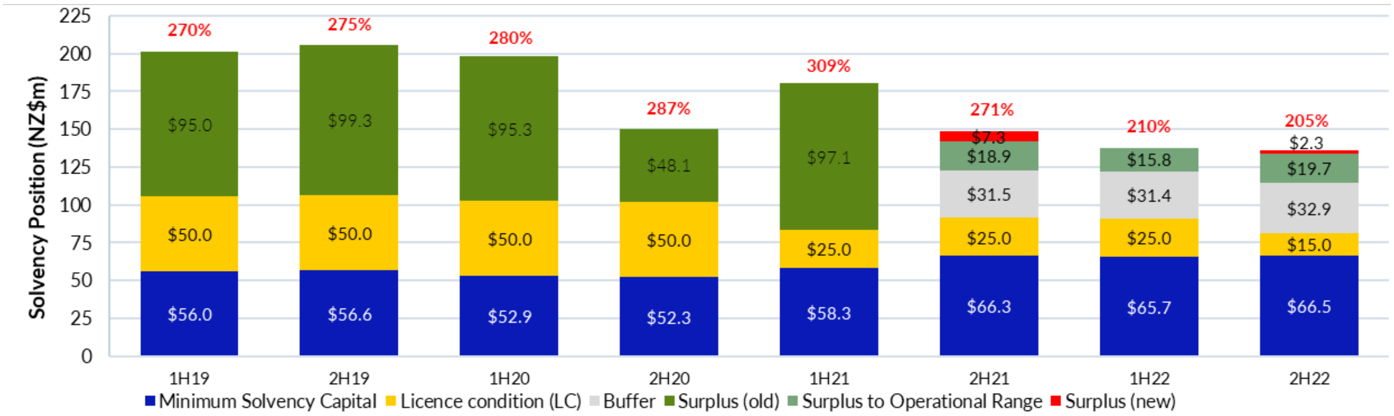
Source: Company data, Forsyth Barr analysis

Figure 6. TWR — GWP segmental split (FY22)



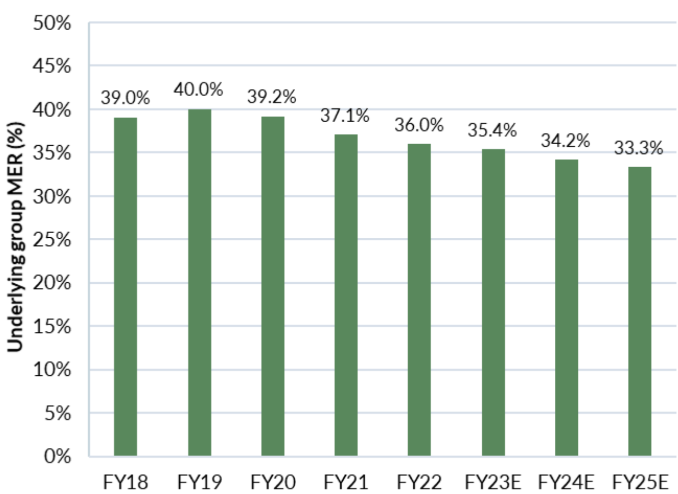
Source: Company data, Forsyth Barr analysis

Figure 7. TWR — Solvency position over time (NZ$m)



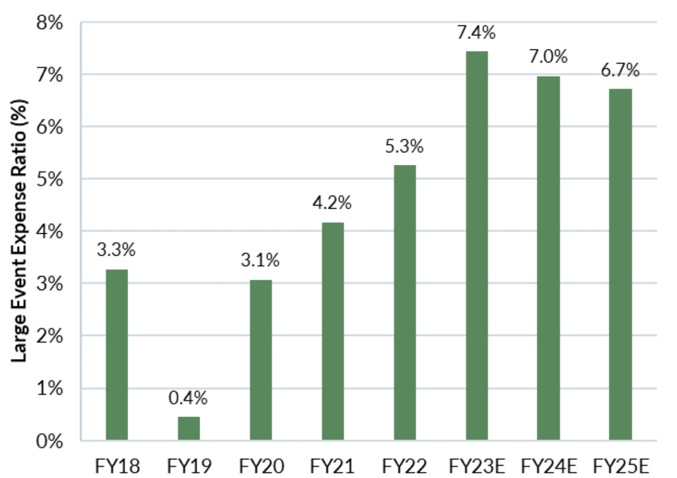
Source: Company data, Forsyth Barr analysis

Figure 8. TWR — Underlying group MER (%)



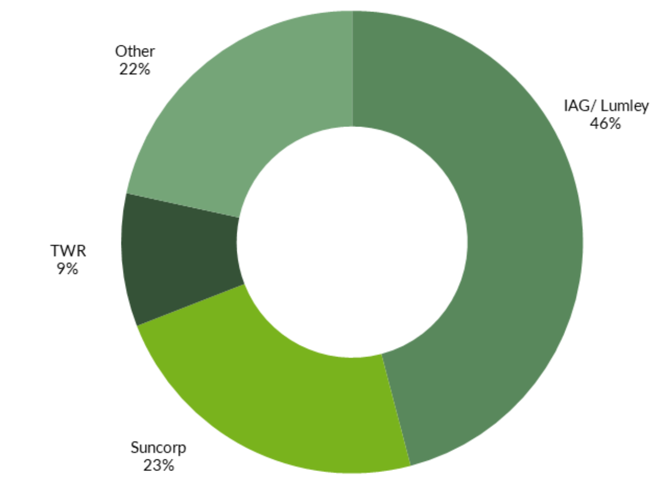
Source: Company data, Forsyth Barr analysis

Figure 9. TWR — Large event expense ratio (%)



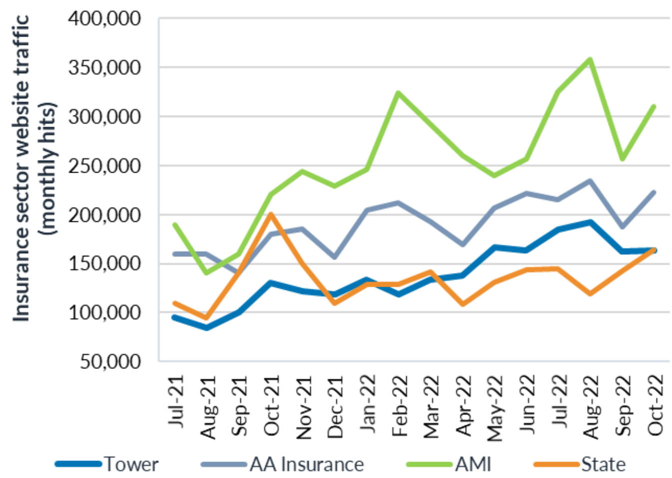
Source: Company data, Forsyth Barr analysis

Figure 10. NZ Personal lines insurance market shares (30 September 2022 estimate)



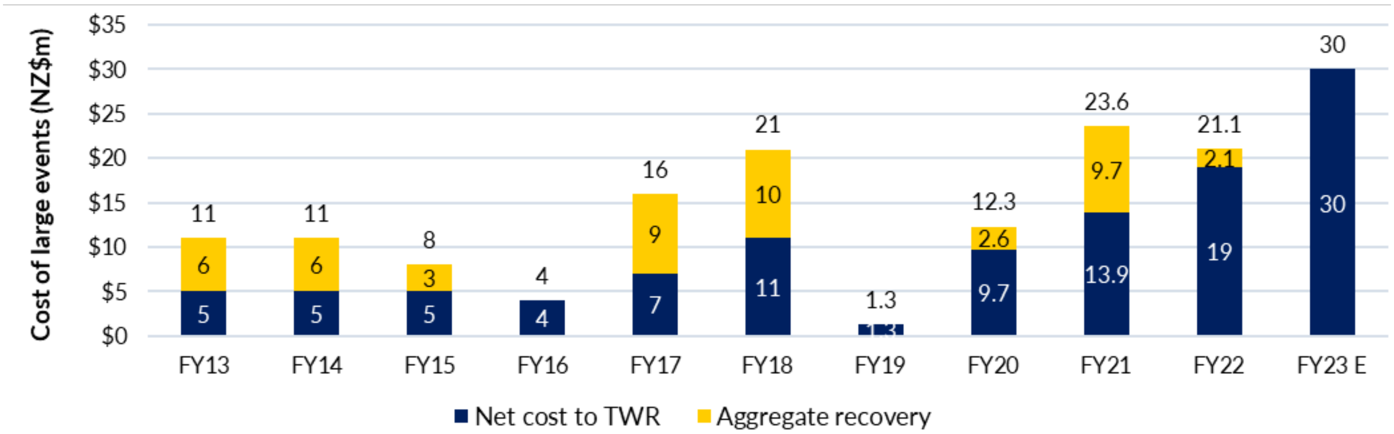
Source: Company data, Forsyth Barr analysis

Figure 11. TWR — Website traffic of combative insurance brands



Source: Company data, Forsyth Barr analysis

Figure 12. Ultimate estimated cost of large events (NZ$m) — excluding reinsurance premium costs



Source: Company data, Forsyth Barr analysis

Figure 13. TWR — Core investment portfolio running yield

Source: Company data, Forsyth Barr analysis

Figure 14. Six-month NZ Government bond yield

Source: Refinitiv, Forsyth Barr analysis

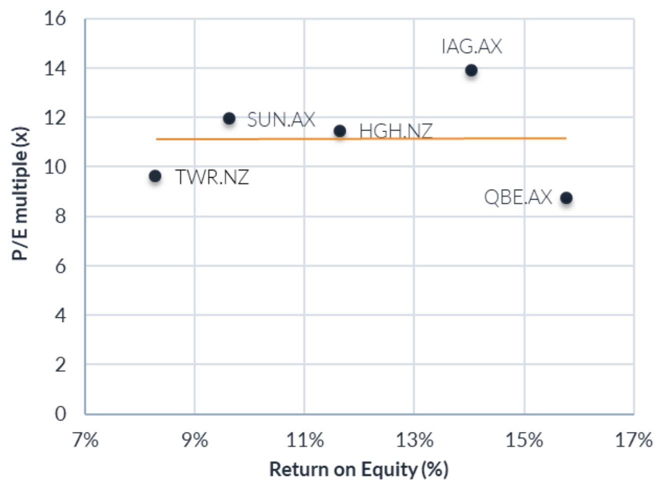
Sector ratios (of relevant peers)

Figure 15. TWR — Comparables table

Ticker	Next Bal Date	Company	Share Price	Market Cap (NZ$m)	PE (x) 1-yr fwd	PE (x) 2-yr fwd	Gross Div Yield (%) 1-yr fwd	P/B (x) 1-yr fwd	P/B (x) 2-yr fwd	ROE % 1-yr fwd	ROE % 2-yr fwd
TWR.NZ	30/09/2023	Tower	0.69	262	9.6	8.5	7.6	0.8	0.8	8.3	9.1
IAG.AX	30/06/2023	Insurance Australia	4.89	13,114	13.9	13.0	2.5	1.8	1.7	14.0	13.8
SUN.AX	30/06/2023	Suncorp Group	11.90	16,285	11.9	11.7	4.8	1.1	1.1	9.6	9.2
QBE.AX	31/12/2022	QBE Insurance	12.85	20,366	8.7	8.0	2.3	1.3	1.2	15.8	15.9
HGH.NZ	30/06/2023	Heartland Group	1.86	1,305	11.5	10.8	8.3	1.2	1.2	11.7	11.3
		Peer Median			**11.9**	**11.3**	**3.7**	**1.3**	**1.2**	**12.8**	**12.6**

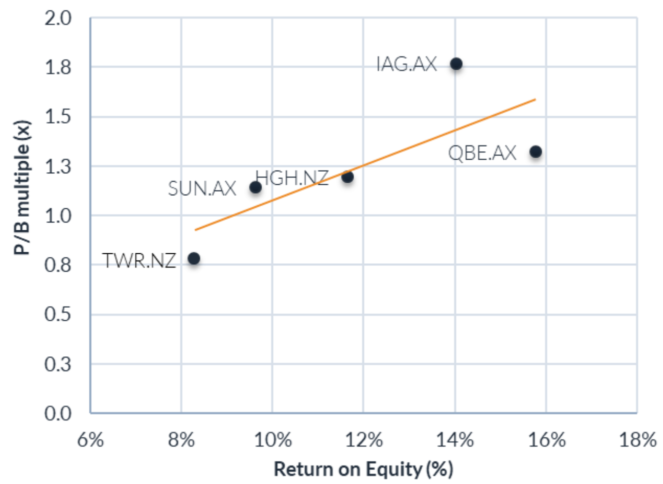
Source: Refinitiv, Forsyth Barr analysis

Figure 16. TWR — Relevant Australasian financials — P/E versus ROE one-year forward



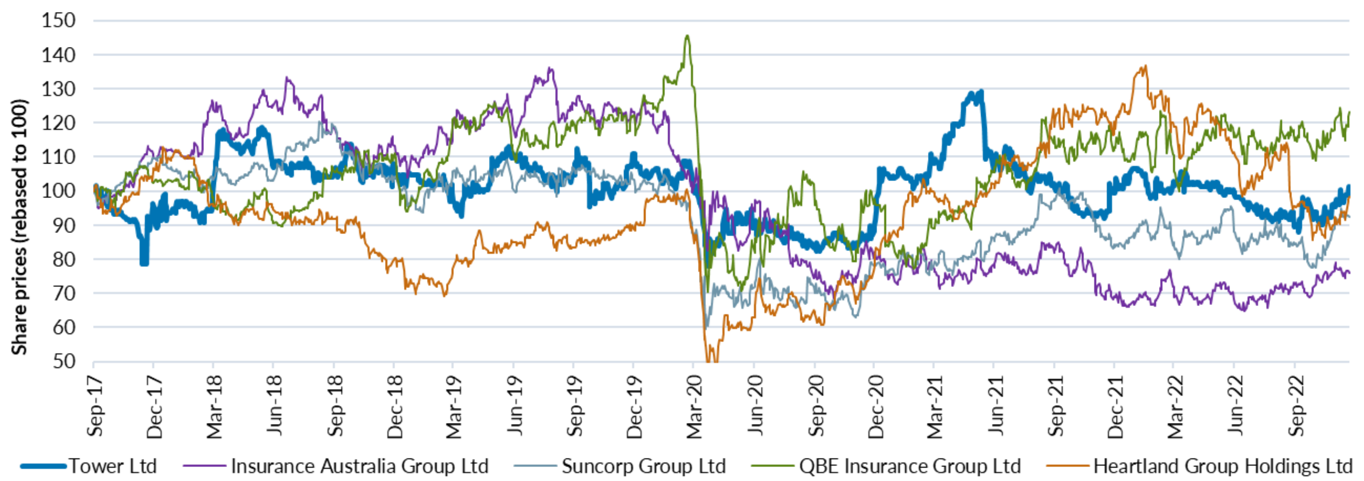
Source: Refinitiv, Forsyth Barr analysis

Figure 17. TWR — Relevant Australasian financials — Price to Book versus ROE one-year forward



Source: Refinitiv, Forsyth Barr analysis

Figure 18. TWR — Sector performance of relevant comparables



Source: Refinitiv, Forsyth Barr analysis

Appendices

Appendix 1: Upcoming IFRS-17 accounting standard

A new global accounting standard will soon come into effect that establishes new principles for the recognition, measurement, presentation and disclosure of insurance contracts. It becomes effective for reporting periods beginning on or after 1 January 2023. The new insurance standard (IFRS-17 or NZ IFRS 17) in summary:

> "*IFRS 17 establishes the principles for the recognition, measurement, presentation and disclosure of insurance contracts within the scope of the standard. The objective of IFRS 17 is to ensure that an entity provides relevant information that faithfully represents those contracts. This information gives a basis for users of financial statements to assess the effect that insurance contracts have on the entity's financial position, financial performance and cash flows. IFRS 17 was issued in May 2017 and applies to annual reporting periods beginning on or after 1 January 2023.*"

An entity shall apply IFRS 17 Insurance Contracts (IFRS 17:3) to:
1. Insurance contracts, including reinsurance contracts it issues
2. Reinsurance contracts it holds
3. Investment contracts with discretionary participation feature, provided the entity also issues insurance contracts.

We understand the outcome of these new standards will be mostly presentational, but they are significant presentational changes. Investors will notice material differences in how income statements and balance sheets are displayed. The legislation applies to all insurance companies so investors may need some education. We highlight this impending standard change as part of that. There are further changes to the valuation of assets and its flow through to profit and loss, albeit likely less material.

We understand that TWR has started work on implementation, and is engaging with its auditors. We estimate that TWR will report under these new standards in its FY24 result (released in November 2024).

For more information, see: https://www.xrb.govt.nz/standards/accounting-standards/for-profit-standards/standards-list/nz-ifrs-17/

Appendix 2: Upcoming RBNZ solvency standards

Solvency standards set out the Reserve Bank of NZ's (RBNZ) risk appetite and how insurers like TWR should calculate the minimum capital required and value the 'solvency capital' held. The solvency standard is designed to ensure insurers hold enough capital to pay claims despite quite adverse future events. There are currently five solvency standards on issue in NZ, however, the RBNZ is in the process of reviewing and replacing these due to:
1. Accounting changes to IFRS-17
2. Their sub-optimal structure and inconsistencies
3. Shortcomings found in recent reviews
4. A desire to become more highly compliant with the Core Insurance Principles.

The RBNZ issued an Interim Solvency Standard in October 2022 to address many of the above issues. Insurers will need to implement the new standard at the same time they implement IFRS-17. In coming years the RBNZ intend to replace this with a more comprehensive Final Solvency Standard. Consistent with the existing standard, the new standard aims to ensure that insurer's capital is adequate for contingencies in 199 of 200 years for most risks and 999 out of 1,000 years for seismic risk. The significantly more conservative approach for seismic risks taken by the RBNZ reflects NZ's unique major earthquake risk and the importance for insurers to be able to pay out if a further major earthquake was to arise.

The Interim Solvency Standard, which we expect TWR to adhere to in FY24, establishes an operational risk capital charge. It is designed to make insurers more resilient by providing a capital buffer against operational risk events, such as cyber risks. This will be developed in the final standard to be sensitive to each insurer's risk environment, with an incentive to reduce these risks. This operational risk will be in addition to capital charges around possible adverse market movements or the event of more claims than expected. The operational risk capital charge will be phased in over a four-year period to 2026.

For more information, see: Review of the Insurance Solvency Standards — Reserve Bank of New Zealand — Te Pūtea Matua (rbnz.govt.nz)

Appendix 3: QBE Insurance Group Limited (QBE) 3Q22 update

QBE released, on 21 November 2022, a trading update for the third-quarter of its FY22, cited elevated weather claims and reinsurance renewals hurt its results and offset any benefit from higher bond yields. QBE mentioned "*elevated catastrophe activity*" and said it expects to incur FY22 catastrophe losses of around A$1.06 billion, which is above its catastrophe allowance for the year of A$962 million. Up until October, being 10 months of QBE's FY22, the company said that total catastrophe net claims cost were ~A$880m. Extrapolating this into November and December QBE said its catastrophe allowance is ~A$180m.

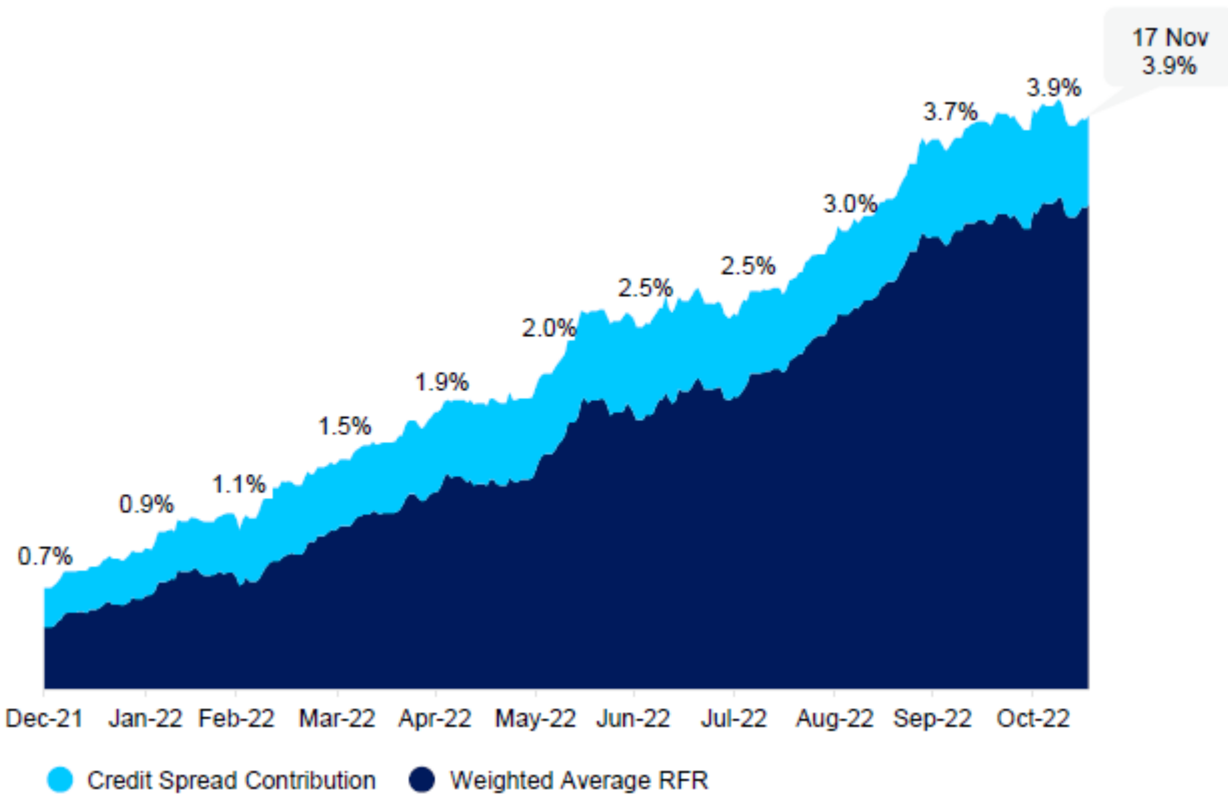
In terms of GWP growth, QBE said that GWP rose +6% in 3Q22 against pcp, and +12% for the nine months in 2022 over pcp. This was higher than the guidance given in August of +10% growth, although management has retained this estimate for the full year. QBE stated that *"we expect the supportive premium rate environment should continue into 2023"*. We await the outcome of its reinsurance renewal on 1 January 2023 covering the period for FY23.

On investment returns, QBE said that interest rates continuing to rise had meant A$461m of market-to-market losses in 3Q22, which was broadly offset by the claims liability discount falling by A$413m. See Figure 19 below.

Management comments included:

- *"challenging operating conditions have persisted into the second half, and while performance remains resilient across many facets of our business, higher than expected catastrophe costs have introduced some risk to our original full year outlook"*
- *"QBE continues to expect FY22 Group constant currency GWP growth of around 10%, and we expect the supportive premium rate environment should continue into 2023."*
- *"Based on our assessment of underwriting performance to date, we now expect a FY22 Group combined operating ratio of around 94%. As outlined at the 1H22 result, QBE's FY22 combined ratio outlook excludes the impact of the Australian pricing promise review."*

Figure 19. QBE's fixed income running investment yield



Source: QBE, Forsyth Barr analysis

Appendix 4: FY23 reinsurance programme — catastrophe reinsurance cover secured but aggregate cover dropped

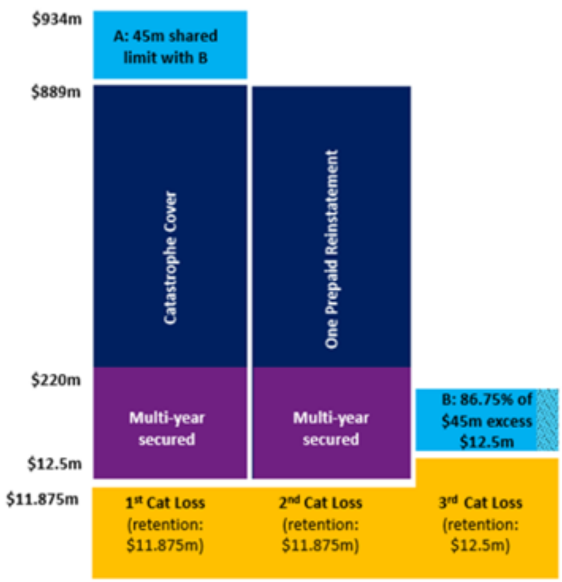
TWR recently updated the market on its FY23 reinsurance programme with savings obtained for comprehensive cover. TWR's CEO said he was "*very pleased with the reinsurance programme*" with "*excellent coverage*". TWR will pay a lower proportion of reinsurance going forward as a result of this renewal. Our prior research had signalled that global reinsurers were pulling away from providing aggregate cover. As such, news that no aggregate cover was taken as part of the reinsurance programme has not come as a complete surprise, albeit we had envisaged that cover would be in place for several more years. TWR's CFO commented that this is "*one of the most challenging reinsurance markets we've seen in over 40 years*". TWR has allocated a conservative NZ$30m to large claims events in its budgets for FY23, which provides support to its earnings guidance. Management has said this is part of TWR continuing to drive towards consistency in an attempt to lower the variability of outcomes in NPAT and dividends.

TWR has increased its catastrophe upper limit to NZ$934m to reflect expectations for business growth. This is a ~+7% lift on the NZ$873m upper limit of catastrophe taken in FY22. The catastrophe cover excess of NZ$11.8m is in line with prior years. For FY22 and FY23 TWR has purchased catastrophe reinsurance at the 1:1000 level (one in one thousand year) for the whole portfolio. TWR's reinsurance premiums for FY23 have increased by +6.7% relative to FY22 (after adjustments), with book growth and the hardening global reinsurance market taking effect. We consider this a good outcome in a challenging reinsurance environment. TWR will pay proportionally less for its reinsurance cover in FY23 at 13.6% of total income or Gross Written Premium (GWP), compared to 15.9% including the aggregate programme.

This reflects:

1. Changes to the EQC cap moving from NZ$150k +GST to NZ$300k +GST per household from 1 October 2022
2. The risk-based pricing work programme
3. Increasing confidence in TWR by reinsurers
4. The removal of the aggregate cover
5. All previous reinsurers plus one new prominent global player on TWR's reinsurance panel.

Figure 20. TWR — reinsurance programme overview



Source: Company data, Forsyth Barr analysis

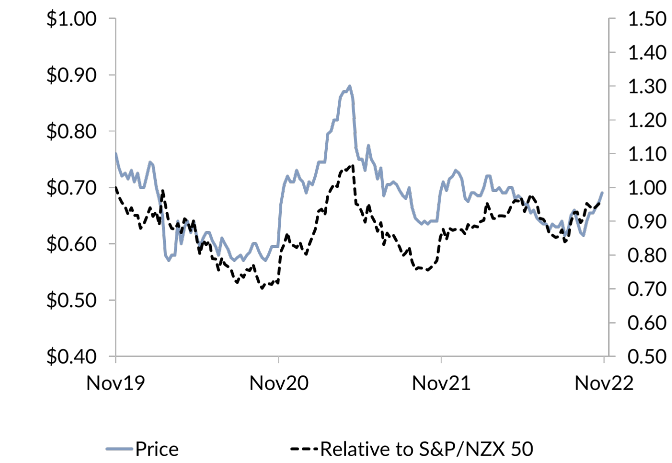
Appendix 5: Papua New Guinea (PNG) country sale

TWR sold its PNG subsidiary to Alpha Insurance Ltd for an estimated gain on sale of NZ$2.1m. The deal was announced on 10 June 2022 and **settled on 28 October 2022**, after TWR's balance date. Alpha Insurance is a PNG insurance company providing a range of personal and business insurance products. We understand the sale was for PGK$22m, approximately NZ$10m at current exchange rates. Alpha Insurance will utilise the Tower brand as it undertakes a rebranding process for up to three months. TWR will also provide transitional services to Alpha Insurance for up to six months after completion.

Appendix 6: Kiwibank insurance portfolio acquisition

TWR announced on 6 October 2022 the acquisition of the rights to the Kiwibank portfolio of insurance policies for NZ$5.9m. These policies have been underwritten by TWR since 2006 and contributed NZ$12m to TWR's GWP in FY22. Ongoing these risks will form part of the Tower Direct channel rather than the Tower Partnerships channel. The deal is expected to settle during 1H23, **on 1 December 2022**. TWR's CEO said, *"the completion of this deal brings an end to our strategy of acquiring legacy insurance books and migrating them to Tower Direct. Since February 2021 Tower has agreed to purchase books for a total price of NZ$26m from ANZ, Westpac, TSB and Kiwibank, ending commission payments and enabling us to have a direct relationship with these customers, who represent more than 88,000 risks. Previously, Tower paid total commission to these partners of around NZ$11m per annum"*. TWR continues to focus on the progressive partnership model building on existing partners, which now include TradeMe Insurance, TSB, Ray White, NZ Financial Services Group and the NZ Defence Force.

Figure 21. Price performance



Source: Forsyth Barr analysis

Figure 22. Substantial shareholders

Shareholder	Latest Holding
Bain Capital Credit LP	20.0%
ACC	9.6%
Salt Funds Management	7.0%
Investment Services Group	5.4%
NZ Funds Management	5.2%

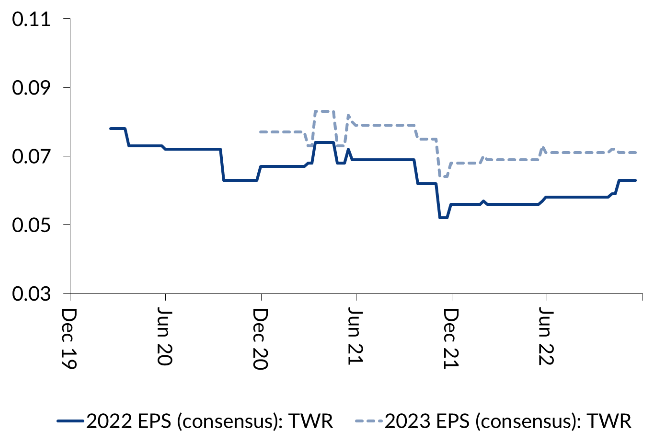
Source: NZX, Forsyth Barr analysis, NOTE: based on SPH notices only

Figure 23. International valuation comparisons

Company	Code	Price	Mkt Cap	PE		EV/EBITDA		EV/EBIT		Cash Yld
(metrics re-weighted to reflect TWR's balance date - September)			(m)	2023E	2024E	2023E	2024E	2023E	2024E	2024E
Tower Ltd	**TWR NZ**	**NZ$0.69**	**NZ$262**	**8.8x**	**7.6x**	**n/a**	**n/a**	**n/a**	**n/a**	**10.1%**
Heartland Group Holdings *	HGH NZ	NZ$1.85	NZ$1,305	11.3x	10.6x	n/a	n/a	n/a	n/a	6.8%
Insurance Australia Group	IAG AT	A$4.91	A$12,104	14.2x	12.9x	n/a	n/a	n/a	9.3x	5.9%
Suncorp Group	SUN AT	A$11.89	A$15,030	12.1x	11.8x	n/a	n/a	n/a	48.6x	6.6%
QBE INSURANCE GROUP	QBE AT	US$8.41	US$12,485	10.6x	7.9x	n/a	n/a	n/a	7.1x	6.7%
			Compco Average:	**12.1x**	**10.8x**	**n/a**	**n/a**	**n/a**	**21.7x**	**6.5%**
EV = Mkt cap+net debt+lease liabilities+min interests-investments			**TWR Relative:**	**-27%**	**-30%**	**n/a**	**n/a**	**n/a**	**n/a**	**56%**

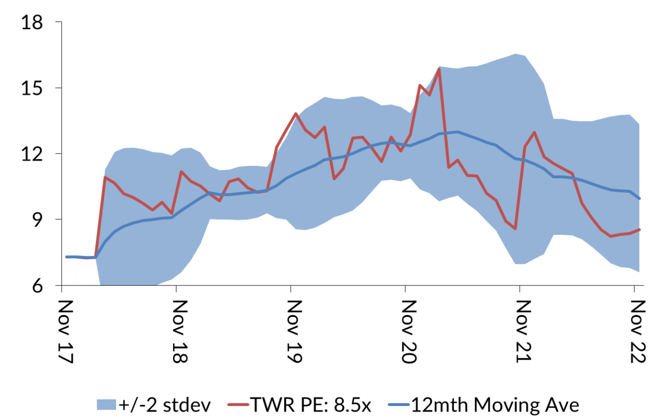
Source: *Forsyth Barr analysis, Bloomberg Consensus, Compco metrics re-weighted to reflect headline (TWR) companies fiscal year end

Figure 24. Consensus EPS momentum (NZ$)



Source: Forsyth Barr analysis

Figure 25. One year forward PE (x)



Source: Forsyth Barr analysis

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