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Calliden Group Limited today reported net profit of \$1.3 million for the year ended December 2007, compared with a loss of \$2.4 million for the previous year. Excluding costs of \$2.8 million relating to the integration of the Australian Unity general insurance businesses (since renamed Calliden Insurance), which you acquired on 1 August 2007, the group made a profit of \$4.1 million. How did the actual 2007 result compare with your expectations?

CEO Nick Kirk

At the time of the acquisition we expected that, in our hands, the AU businesses would produce annual profit of \$7.5 million to \$8.5 million before integration costs. We estimate that their normalised contribution was in line with that expectation. It's worth stressing that there are further integration costs to come, particularly on IT, as we rationalise systems over the next 18 months. Also, our existing business reached break-even point in the last quarter of 2007, as expected.

However, since the acquisition the operating environment has changed. We've moved from a period of benign weather for insurers into a La Nina cycle, bringing increased storm activity and floods. Investment markets which had been producing record returns have become very volatile on the back of a credit crunch that's pushed up interest rates. At the same time, prices in the commercial insurance intermediated market have continued to soften. This has meant that, as we integrate our recent acquisitions and joint ventures, we've focussed on protecting the Group from this harsher environment.

Therefore, we've combined the reinsurance treaties of Calliden Insurance and Calliden Limited into one wider and more comprehensive programme. This protected us well against the many weather incidents in 2007. We've also exited a number of non-performing portfolios post the acquisition and increased the non-risk bearing part of our business by doubling CSA's claims management business and acquiring the Lloyds underwriting agency Mansions of Australia as part of the AU deal. On the investment side, we've maintained our conservative approach and reduced our exposure to equities so they now represent less than 5 percent of our total investments.

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Calliden Insurance made a \$0.5 million contribution to net profit in the five months since acquisition. Given the normalised full-year contribution of the businesses was \$7.5 million to \$8.5 million, this implies a relatively weak performance in the months since acquisition. What were the reasons for this?

CEO Nick Kirk

Firstly, the \$0.5 million was after one-off integration costs of \$2.8 million, \$1.2 million of which related to overheads and \$1.6 million to the consolidation of our reinsurance arrangements. The second half of 2007 saw four major weather events: the Lismore and Sydney hail storms and two storms in Melbourne. In addition the regional and rural business ARGIS, formerly FMG, always has increased claim activity in the summer months. This summer, on top of the weather events, ARGIS in common with other rural insurers has seen increased large fire losses. Many of the fires have been caused by the spontaneous combustion of hay, reflecting the timing of the hay cutting and the humid conditions.

The Calliden Insurance portfolios are more short tail than the Calliden Limited portfolios so they were always going to bring an increased exposure to weather related losses. For both the regional and rural book and the home insurance portfolios, premium prices are already adjusting to reflect the increased incidence of loss.

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The group's gross written premium (GWP) was \$124.4 million in 2007, up from \$51.8 million, reflecting GWP contributions of \$59.0 million from Calliden Insurance and \$65.4 million from Calliden Limited. Annualising the five-month GWP contribution from Calliden Insurance suggests a 12-month contribution of \$142 million and therefore a group GWP of over \$200 million. In this light, your expectation of GWP "approaching" \$200 million in 2008 seems conservative. Can you comment?

CEO Nick Kirk

The Calliden Insurance book is seasonally skewed towards the second half of the year. Therefore, you can't just annualise the five months to December. Our estimate of annualised GWP for 2007 is \$180 million to \$185 million. I'd point out that our real focus this year will be to make sure the portfolio is profitable. That will mean organic growth is going to be very much secondary.

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In the second half, Calliden Limited had GWP of \$37.1 million, up 14 percent year-on-year, compared with growth of 48 percent in the first half. To what extent did the slowing of growth reflect internal factors such as management distraction as a result of the AUGIL acquisition?

CEO Nick Kirk

There's no doubt that in a company of our size, purchasing a company twice your size needs a lot of management focus which will then detract from the new business effort. However, one of the main reasons for the slower growth in the second half was that our increased scale with the addition of the AU portfolios gave us the opportunity of exiting a number of portfolios in Calliden Limited that were performing below expectations. The benefits of these actions will show in the second half of 2008.

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You've indicated that the first steps of the integration have been completed. What steps remain, and what's the expected level of integration costs over the current year ending December 2008 and over the 18-month period during which you plan to consolidate the group onto one IT platform?

CEO Nick Kirk

Our plans for the integration are aimed at protecting and developing the long-term value of the business. In the case of the AU businesses, and many of our other acquisitions, we've bought successful companies with skilled and motivated teams. We aim to extract any synergies carefully over time to ensure we don't damage the business or customer relationships.

Our first step was to create one management team and organisational structure across the group, which is now in place. The second was to combine the reinsurance programmes, which was finalised on 1 October 2007. The major area of current and future integration activity is IT. We identified this very early on as a big investment in time and money but one that would produce many cost and business benefits down the track. We're moving onto one modern and flexible system from four systems and will carry out those conversions sequentially as that's the best way to manage the risk. This means we'll have the costs of the conversions plus the cost of maintaining duplicated architecture for a period of time. Our IT budget for 2008 is \$7 million and we'd expect to make significant savings when the work is complete.

In the meantime we're also moving Calliden Advantage, the ex-AUGIL commercial broker business, onto an electronic trading platform. This will significantly streamline the business and make us a more attractive business partner for brokers.

In addition we're consolidating our office accommodation in Sydney and Melbourne in the coming months. We'll move to two offices from four in Sydney and to one from two in Melbourne.

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The group's main underwriting exposure is to public and product liability, householders and commercial property. You've indicated you expect a general firming in premium prices. How do you expect premiums in your main areas of exposure to respond?

CEO Nick Kirk

From a market perspective, public and products liability is performing very well and is profitable. Householders has been a very stable market for a period of years, but was very much impacted by the weather during 2007. And commercial property is an area we believe is now unprofitable.

So in public and products liability we'd expect little or no price rises, and perhaps a slight softening. Householders is a very rational market and prices will increase to reflect the adjusted longer-term weather pattern.

Commercial property is the big question. We have some very profitable commercial portfolios including portfolios in the former AU general insurance book. But with the sector now unprofitable within the market, prices have got to start to firm during 2008. It's now a question of when rather than if. I believe we stand to make considerable gains when that firming starts to occur.

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The insurance loss ratio was 60.4 percent in 2007, excluding the one-off costs of \$1.6 million relating to the consolidation of the reinsurance programmes of Calliden Insurance and Calliden Limited. How will the reinsurance consolidation impact and what's the outlook for the loss ratio going forward?

CEO Nick Kirk

The consolidation of our reinsurance programmes has had a positive effect on the net loss ratio. Had we faced the weather events we had in the second half of 2007 with two separate reinsurance programmes, we would have had two separate net retentions for each incident.

We expect the loss ratio to reduce in 2008, resulting from a firmer pricing environment in home insurance and the regional and rural portfolio together with continued tighter underwriting of our commercial portfolios. I'd also note that in 2008 we'll book a further one-off cost, of a similar size to the cost incurred in 2007, relating to the reinsurance consolidation.

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The group's expenses were \$14.2 million in 2007, excluding overhead costs relating to the integration, and the expense ratio was 47.6 percent. To what extent is this indicative of the level of expenses in the shorter term?

CEO Nick Kirk

As we get the benefits of scale and a full-year contribution from Calliden Insurance in 2008, we expect the expense ratio to drop further.

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Net investment income was \$8.2 million in 2007, up from \$5.9 million. Investments totalled \$165.0 million as at the end of December, up from \$98.4 million a year earlier. Listed equities accounted for 5.3 percent of the portfolio, the bulk of which comprises securities rated A1/AA or above. How might your investment strategy change in an increasingly inflationary environment?

CEO Nick Kirk

We'll continue with our conservative investment policy which we believe has been a significant support to the business during these more volatile times. Our asset allocation is focussed on producing stable investment earnings to conserve and grow our capital. Following the acquisition of the AU businesses we reduced the Group's equity market exposure and we have no direct exposure to the US sub-prime issue. Equities are now less than 5 percent of our investment funds.

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As at the end of December, the group had \$40.0 million surplus to its minimum capital requirement of \$31.9 million. What's the expected minimum capital requirement of the group following your planned consolidation into one insurance license and what is the expected time line for this?

CEO Nick Kirk

As and when we go ahead with merging the two insurance portfolios and consolidating our licenses into one, subject to the approval of the Australian Prudential Regulation Authority (APRA), we'd expect the amount of surplus capital released to be in excess of \$10 million.

In terms of the timing, our priority is to make sure we're following the best strategy for the portfolio transfer, bearing in mind the amount of administrative effort that needs to be put into it and ensuring we have continuity of customer service.

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You've indicated that the Group will continue to seek acquisitions. What balance sheet capacity do you have to pursue acquisitions, and with the integration of Calliden Insurance underway, where do you see the most attractive growth opportunities for the group?

CEO Nick Kirk

It's worth emphasising that our first priority is to make sure we've properly integrated the businesses we've acquired.

Should attractive opportunities arise then we would of course consider them provided any integration would not put at risk the integration work we're currently engaged in.

In terms of attractive areas, the personal lines market continues to be of interest. We believe it's a rational market where prices will move to reflect increased claims exposure. We'd also consider portfolios that have a specific

niche or added value that enables them to withstand the pressures of an otherwise cyclical market. We have significantly increased our fee earning business in 2007, with non-risk bearing business being over 10 percent of revenue, and we'd consider further opportunities to increase that further.

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Thank you Nick.

For more information about Calliden Group, please visit www.calliden.com.au or call Nick Kirk, on +61 (2) 9551 1102.

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