3Q 2022

Santiago

Good morning and thank you for joining Qualitas third quarter and nine months of the year earnings call: I'm Santiago Monroy, Qualitas' IRO. Joining us today are our CEO, Jose Antonio Correa and our CFO and International CEO, Bernardo Risoul to walk you through our quarter results and performance.

As a reminder, information discussed on today's call may include forward-looking statements regarding Qualitas´ results and prospects, which are subject to risks and uncertainty. Actual results may differ materially from what is discussed here today, and the company cautions you not to place undue reliance on these forward-looking statements. Qualitas undertakes no obligation to publicly update or revise any forward-looking statements, whether because of new information, future events, or otherwise.

Let's turn it over to Jose Antonio, our CEO, for his remarks.

JOSE ANTONIO

Thank you, Santiago. Good morning, everyone, great to be with you all. Volatility and uncertainty have been part of 2022 daily context and third quarter has been no exemption; nevertheless, Qualitas has shown its ability to keep on growing in terms of written premiums and insured units while being profitable. We are pleased with top line performance of our business, but recognize profitability is not where we want it to be. To better understand this third quarter results, we should break them into the three main buckets: Mexico auto underwriting, international subsidiaries, and Financial Income where we had an important one-time impact. By diving into each one of them, you will have more clarity on where we are and most importantly what we are doing to ensure all of them are headed to the profitable growth path.

I will expand on the first one, our core, Mexico auto insurance business, which makes up for 90% of our premiums, while letting Bernardo walk you through the others. In Mexico, premiums are up 15%, adding 230 thousand of new vehicles quarter over quarter and reaching a new watermark of 4.6 million Mexican insured units; this is the largest quarterly growth in the past couple of years. Equally important, despite several headwinds, we have posted resilient underwriting results during these first 9 months of the year. As all of you well know, the auto insurance industry has historically followed cyclical trends, and Qualitas has navigated the cycle during 28 years of history; this time there are some particularities to consider:

- First, a high inflation environment not seen in Mexico in the past 2 decades; it has reached 8.7% while inflation for the new cars is up 14.6%, heavily impacting our costs,
- Second, supply chain constraints and shortages caused by the pandemic and now geopolitical conflict. Despite early signs of recovery, with YTD new car sales posting a 3% growth they are still down -19% vs pre-pandemic levels and certainly below demands needs; the signs of a future recovery are in the map, but not until mid-2023.

While impossible to be certain, as it will also depend on the evolution of macroeconomic variables and competition behavior, I expect that we will peek the cycle in the next 3-6 months with sequential recovery as we continue to adjust tariffs during 2023.

As talked before, we have been disciplined on pricing, seeking balance between recovering inflation while staying competitive; we are also relying on our scale and innovation to mitigate some costs and relying on our endless journey for excellence in service to ensure our value proposition remains unmatched. These actions have allowed us to maintain a profitable underwriting performance; according to latest industry figures, in current environment, Qualitas Mexico had a better combined ratio than the Top 5 companies and the industry overall, proving the health of our Mexican subsidiary and our strong fundamentals.

I would also like to share that, during September, we celebrated an important milestone for Qualitas Controladora´s future. After several years of working on it, our Qualitas Salud subsidiary is now a reality and has issued its first premium. With a talented team, a differentiated product and the unique Qualitas DNA, we are confident this will become an important pillar in the next years, creating value and becoming an engine of growth for the long term and the sustainability of our results.

We will be providing updates on the evolution of this business regularly but let me remind you all that our entry into the market is gradual; this is not expected to be meaningful to the holding company performance in the short term; we are following the launch, learn, adjust, and then expand strategy ensuring we can create value to all stakeholders.

Overall, despite short terms challenges our company is stronger than ever. The consistency of results and solidness of all subsidiaries that compose the holding company was recognized by S&P, which maintained our BB+ rating and stable outlook.

Finally, Qualitas' sustainability commitment was reinforced by signing SBTi initiative, "Science Based Targets" to establish goals and targets to reduce our Greenhouse Emissions, looking for a Net Zero emissions' scheme towards 2050. Qualitas will continue to implement measures and processes, that also make sense for the business of course, to mitigate emissions and keep with the never-ending journey towards sustainability.

Before I hand it over to Bernardo let me reiterate that our mission remains to create long-term value for all stakeholders. Our strong balance sheet supports our leadership position and the commitment of our experienced management team lead us to navigate through this challenging environment, which is reflected in the execution of our strategy.

We understand low ends of the cycle are never fun, but they bring along an opportunity for reinvention and to further stand out. I am certain of our ability to overcome the challenging environment, and optimistic about the future for Qualitas ahead.

Let's move now to review financial details and a deeper dive on the quarter results. Bernardo, please.

Bernardo

Good morning, everyone; glad to be with you all again. As Jose Antonio eluded, it has not been an easy year for auto insurance nor financial investment companies, neither in Mexico, nor worldwide. As a high-level summary, this quarter top-line was better than expected, Qualitas Mexico, our main subsidiary loss ratio was in-line with what we had anticipated while financial income and Qualitas US undelivered.

Going directly into our underwriting results, top line grew 14% for the quarter and 7% YTD, driven once again by the strong performance of the traditional segment in Mexico which increased 18% in the quarter and is up 13% for the year. The better-than-expected top line reflects our ability to reach more consumers through more agents; new car sales early signs of recovery helped as well, growing quarterly, but still down -5% in the year. Just as a reference, had the new car sales been at 2019 level, our top line fair share would yield two and half points of additional growth.

Top line was driven both by pricing and volume; on the latter, we are happy to share we reached a new record high for the holding company, with 4.8 million insured units, an increase of almost 300 thousand units vs year-end 2021; when compared against same period year ago, insured units are up 6%. In terms of pricing, relative to the lowest point of 2021, our tariffs are up 14% on average. However, relative to cumulative inflation, tariffs still have some catch up to do being 2 percentage points below.

Also, international operation is up 4% in the quarter and 11% YTD in US dollars, which stands at 10% YTD. When breaking down our US subsidiary vs rest of LATAM markets we see two different behaviors which we can expect to continue. On one end, our US business, the largest one representing 5% of the total holding company underwriting, with over $100 million dollars in premium, this subsidiary slowed down this quarter and will stay flattish seeking to balance top and bottom line profitability; and on the other hand, the rest of LATAM, constituted by El Salvador, Costa Rica and Peru, which are growing 20% YTD and are expected to continue fueling the growth considering they are already profitable and with large potential replicating Qualitas' model with a local touch in each market.

Let me elaborate on the United States subsidiary, a company that started operations back in 2014 in California and Arizona, and soon after expanded into Texas. This business came to light as a way to satisfy an unmet need of Mexican customers needing coverage in the US and vice versa; due to demand and opportunity, it started expanding into domestic US as well. Over the past quarters and given the long-tail litigation processes and legal particularities mainly in Texas, we have been impacted by some older claims – up to 6 years old– that have closed in a much higher cost than initially reserved; this also forced us to relook at all historic claims reserves, resulting in the need to increase them significantly. At this time, we are finalizing the assessment, together with an external actuarial firm and will share conclusions in the next quarter.

We know there is a large market potential in the US; incentives for nearshoring to Mexico remain high for companies serving the US market and being THE ONE insurance company that can provide unique service on both sides of the border is a competitive advantage that we want to continue exploiting. Of course, we need to ensure on-going profitability, therefore among several actions we will slow down growth, we will refocus on the cross-border business while reducing weight of US domestic; as well as increase prices since last year and strengthening our team, mainly on the claim management where new experienced people have joined the organization.

So, let me now move back to Qualitas results. Earned premiums posted an 11% increase, reflecting our strong top line growth and a mild reserves release, commonly seen during every year second and third quarter. For reference, during the quarter we released $75 million and for the year we have released $92 million in reserves, this relates to the duration of our portfolio which is now composed of more annual policies, which naturally earn faster.

Shifting gears into our operating performance, third quarter loss ratio was 71.4% for a cumulative of 68.5%, above our desired 62-65% technical range target, but already expected considering the part of the cycle we are in, and that changes take time to fully reflect. Let me provide a few highlights:

- The inflationary environment has a direct impact in our claims' costs related to material damages and medical expenses which have increased around 10% vs. same quarter 2021, and up to 20% vs. same period 2019. To cope with these increases, we are not only relying on pricing but looking at cost saving opportunities which include our vertically integrated operation that allows for more than 10% reduction vs market prices and is now expanding into other business lines; we have also leveraged our salvage recovery process by which we sell vehicles declared total losses; the percentage of salvage recovery is now at an all-time high at 47%, resulting from the used cars prices peak and being able to streamline the auction process. Recognizing we do not control inflation, what we will aim is to always stay ahead of competition in terms of cost advantages.

- Also relevant to mention is the expected peak of mobility and impact on frequency; now that all COVID restrictions have been lifted, people go out more, mobility is up from pre-pandemic levels and, not only is this affecting traffic, but higher number of claims.
- Another important component of our claims are theft and robberies, which have reverted its 3-year downward trend and are entering an inflection point which could impact our costs. As Qualitas has the largest volume of the market, actions towards addressing this include our unique pricing model, which considers zip code, and the strengthening of our theft prevention and recovery process through partnerships with third parties' suppliers and in which we expect to improve our current 47% recovery rate, that despite being ahead of competition is below our historic 52%.
- Finally, third quarter is a heavy rainy season for Mexico, with cyclones, tropical storms and hurricanes. As a reference third quarter claims ratio has historically been 2 percentage points higher than rest of the year due to this seasonality.

Company's efforts to address cost are broad based and a priority for all functions. In doing so, we have also found ways to improve service, which build on strengthening our value proposition, our ultimate goal. As an example, the remote express claims which continues to increase and has now reached 26% for the quarter; that means serving 26% of claims remotely; the upcoming launch of Qualibot strengthens our customer experience and has a better seen rate than text messages or e-mails. We also now implement a brand segmentation for claim officers and valuation teams, so they will become our experts within the specialization seeking for faster and more accurate valuations and hence, improve cost control.

I would like to be very transparent regarding loss ratio, the factors before mentioned, have and will continue to impact our costs during the next quarters. We have talked about pricing taking time to fully reflect and there is still a lot of uncertainty on inflation and spare parts supply restitution. This is very dynamic, thus what I can assure you, is that we will continue to further accelerate on what we can control and to ensure that our value proposition remains competitive.

Our acquisition ratio and operating ratio are in line with historical range standing at 23% and 4% for the quarter and YTD respectively.

All of the above, resulted in a combined ratio of 98% for the quarter and 96% YTD. As we have mentioned, in a tough operating environment, these results continue to outperform Mexico and many of our global peers.

Now, moving into the other important pillar of the business, our financial income for the third quarter stood at $52 million which cumulatively speaking represents an ROI of 1.6%. These results are well below our initial expectations and prior year let by two main reasons:

First, a one-time impact of around $200 million in the quarter and $650 million for the year behind an important equity position in UNIFIN, which we still hold. As you are aware, this Company is currently undergoing a restructuring process which has eroded 95% of the stock price in the year, with an important dive in this third quarter. While we do not disclose equity specifics, this was one of our largest standalone names; at this point no single investment represents more than 2% of our total equity portfolio.

Secondly, the overall financial behavior that has impacted capital markets with general hikes in interest rates. On the latter, our initial expectation for Mexican reference rate was closing at 6.5% by year end, standing now at nine and a quarter, with projection to be at 10.5% or slightly above. While our portfolio is short in duration, this delta has had a negative effect on current positions.

Recognizing the disappointing result on the financial income and the effects they have had in the overall performance of Qualitas, let me share that I believe our portfolio is well set to deliver good news and high returns in the next quarters. Main reason to support this is that by the end of the third quarter, 88% of our portfolio is invested in fixed income with a duration of 0.6 years, the lowest we have been in decades, which means we will start benefiting from the high rates cycle as soon as of next quarter. We will also start taking longer terms positions at double digit rates; important to highlight that our current yield to maturity rate of the fixed income portfolio stands at 7.9%.

Equities represent 13% of our portfolio, excluding UNIFIN, they are down -14% in the year. At this point ~90% is in the Mexican market and the balance in the US. For the short term, we do not plan to increase equity position significantly. Important to highlight that most equity positions are held at the holding Company level, while keeping fixed income – with higher liquidity and lower risk – at the insurance entities, thus from a solvency standpoint we are solid and well covered.

Again, the way our $35 billion pesos portfolio is set represents a unique opportunity in the current high interest rate market. The investment team, together with the investment committee are close to this and will ensure the right actions are taking to capitalize its full potential.

All in all, we posted a $211 million net income for the quarter, taking our cumulative profits to $1,600 million. Regarding our financial ratios, our 12-month ROE stands at 12.6%, reflecting our YTD performance and capital position; 12 months Earnings per Share stands at $6 pesos, Price to Earnings stand at $13.8 pesos and finally Price to Book Value at 1.8.

Regulatory capital requirement, stood at $3,694 million at the end of third quarter, with a solvency margin of $15 billion pesos, equivalent to a solvency margin ratio of 498%. As eluded by Jose Antonio, this strong capital position together with our strong DNA and business model, has been recognized by rating agencies, maintaining a stable outlook for the holding company and subsidiaries.

On the capital allocation front, and in addition to start of operations for Qualitas Salud which will require around $10 million dollars of capital for the next year, we have started a due diligence processes to assess two business opportunities within the insurance ecosystem. Further to that, just as a reminder, during November we are going to pay a $2.5 pesos cash dividend as the second exhibit of our declared 2022 dividend, which totals $6.5 pesos for the year and around 8% dividend yield.

Cash returned to our investors and shareholders remains a priority, and Qualitas' has had the ability to consistently deliver dividends as signal of its durable business model that is well positioned to outperform throughout the business cycle. Although it is too early to forecast 2023 dividend, we will fully comply with our dividend policy.

Before opening the line for Q&A, let me once again share that while we are not satisfied with these quarterly results, we have full understating on what led to them. We have and will continue to take actions to overcome the cycle where we are facing strong macroeconomic volatility and competitive pressure; we are encouraged to see that fundamentals in our core business are strong, that the financial income portfolio is poised for a strong 2023, and that executing against the strategy will allow for value creation to all stakeholders which include policy holders, agents, employees, and shareholders.

Now, operator please open the line for questions.