Chambre de commerce et d’industrie
du Québec métropolitain

INDUSTRIAL ALLIANCE AND THE RENEWAL OF THE FINANCIAL SERVICES SECTOR

Notes for a speech by

Yvon Charest
President and Chief Executive Officer
Industrial Alliance
Insurance and Financial Services

Château Frontenac, Quebec City
Tuesday, December 18, 2001

INDUSTRIAL ALLIANCE
INSURANCE AND FINANCIAL SERVICES

I would like to start by thanking the Chambre de commerce and its partners for voting Industrial Alliance the Visionary Company of the Year for 2001 at the Vision Awards. All Company employees and agents are very proud of this award, which crowns a number of remarkable years for Industrial Alliance.

I would also like to emphasize that the Chambre de commerce had somewhat of a sixth sense a few months ago, when they invited the president of an insurance company to deliver a speech the day after one of the largest transactions in the world of insurance in Canada was announced. As you probably know, yesterday Sun Life announced that it intended to acquire Clarica, to form the largest insurance company in Canada.

This announcement fits in with the environment that has prevailed in the insurance and financial services sector over the last few years, especially:

- Aborted bank merger projects;
- The conversion of 5 major mutual insurance companies into stock companies;
- Changes that will be made, starting January 1^{st}, to ownership regulations for financial institutions;
- And, of course, the merger and acquisition rumours involving banks and insurance companies.

Informed observers have every right to be asking themselves what kind of evolution will we continue to see in the financial services sector? Is Sun Life's acquisition of Clarica the beginning of a new round of consolidation? And, closer to home, what does the future hold for mid-sized companies, especially Industrial Alliance?

Despite the great respect I have for the media, I have always said that if you depend on the headlines in the newspaper to follow the evolution of a market, you will probably miss 90% of what is really going on.

I will therefore attempt today to present my vision of the financial services sector and the role Industrial Alliance intends to play.

But, as always, you have to see where we're coming from before you can see where we are going, so allow me to give you a brief background on recent Industrial Alliance history.

Without fanfare…

When I started writing this speech, I wanted to call it "without fanfare." Like humans, every company has its own personality. In the case of Industrial Alliance, this personality was forged over the past 100 years based on two strong values: discretion and efficiency.

Without fanfare, we became the seventh largest life insurance company in Canada. In the nerve centre that is the individual insurance sector, our strongest area, we are first in Canada with respect to sales. Over the past four years, we have sold more individual insurance contracts than Sun Life, ManuLife, Great-West, Clarica or Canada Life or even Sun Life and Clarica combined. We have developed the largest insurance product distribution network in Quebec, with over 1,200 agents.

Without fanfare, we set in place a Canada-wide expansion strategy about 15 years ago that resulted in the acquisition of three major life insurance companies. Currently, half of our income is generated outside of Quebec. Without even realizing it ourselves, we have become the Quebec financial institution with the most geographically diverse activities in Canada.

Without fanfare – and you will no doubt be surprised to learn this – half of our business has nothing to do with insurance. Over the past few years, 50% of Industrial Alliance's income and profit has come from savings and investment products. The logic behind this is simple – we seek to offer the most complete range of financial products possible in order to help people reach greater financial freedom. And financial freedom means not just protection products such as insurance but also savings and investment products too.

What types of savings and investment products do we offer? Let me give you four examples.

- We offer mutual funds, called segregated funds in the insurance industry. Segregated funds did not exist at Industrial Alliance in 1994. Today we manage over 3 billion dollars worth. Our family of funds includes over 40 investment funds. Two thirds of the amounts invested by our clients are managed internally by our own managers, most of whom work right here in Quebec City at our Head Office. In the past year, over 80% of our funds performed better than the median.

- In addition to segregated funds, we distribute mutual funds through our Investia subsidiary. As a result of the purchase of the Groupe Financier Concorde – a Quebec City company – earlier this year, Investia's assets tripled to 300 million dollars. Almost half of our insurance agents now hold a licence to distribute mutual funds.

- Still in the savings and investment family of products, we offer registered retirement savings plans (RRSPs) just like the banks. I say just like the banks because the majority of people in Quebec know that banks offer RRSPs but roughly less than half know that insurance companies offer RRSPs too. We currently manage some 6 billion dollars in RRSPs at Industrial Alliance.

- We also offer two versions of a registered education savings plan. Perhaps you have seen our recent ad on television about our registered education savings plan or even heard it on the radio.

In order to reflect this extended vocation, we decided to change our commercial name last year to Industrial Alliance Insurance and Financial Services. As you can see, over the years the distinction between insurance company and bank has become quite tenuous.

While we have developed without fanfare, it was with a roar that we demutualized close to two years ago. Almost 700,000 insureds, mostly in Quebec, shared in some 550 million dollars, in their choice of cash or Industrial Alliance shares.

But quietly and without fanfare, our stock has risen since demutualization from $15.75 when we were first listed on the Toronto Stock Exchange to over $44.00 at the close of the market yesterday. Industrial Alliance stock is now part of the prestigious TSE 300 and TSE 100 indices. Our market capitalization places us among the 100 largest public companies in Canada, among the 20 largest in Quebec and first in the Quebec City region. And our market multiples are currently higher than those of the Canadian banks.

This is what Industrial Alliance has become today. From an essentially Quebec company to a Canada-wide company. From an insurance company to a financial institution. And from a mutual company to a stock company.

We owe Industrial Alliance's success to all those who preceded us at the company, from the very first president to the most recent – Mr. Raymond Garneau, who joins us here today and who I would like to acknowledge right now. Mr. Garneau was at the company's helm during the 1990s and successfully led us through the delicate demutualization process.

The most tangible proof of Industrial Alliance's success, and our deep roots in Quebec City, is the expansion of our head office. Because of past and anticipated growth, we decided last year to expand our head office, located on chemin Saint-Louis. This large-scale project for the region – and they tell me that it is the second largest construction site in the Quebec City region after that of the CHUL – is scheduled for completion early next year.

What does the future hold for the insurance industry: *megadeals* or "*piecemeal*"?
What does the future hold for the insurance industry? Will we witness a new wave of consolidation in the financial services sector? Will the large institutions, especially the major banks, continue to buy everything that moves? And what will be Industrial Alliance's role in all this?

When we talk about the future of the financial services sector, we are mainly talking about ownership of financial institutions. You have no doubt heard that the federal government passed a bill earlier this year setting out a new set of regulations for the financial services sector. This bill greatly changes the ownership regulations for federally chartered institutions.

So, as of January 1st (in exactly two weeks), a shareholder may acquire a maximum of 65% – and in some cases up to 100% of the stock in a medium-sized company. Four companies are affected by these measures: two insurance companies – Clarica and

Canada Life, and two banks, both from Quebec – the National Bank and the Laurentian Bank. Sun Life's announcement that it was acquiring Clarica falls under these rules.

You may have noticed that I didn't mention Industrial Alliance among the institutions affected by this bill.

In fact, Industrial Alliance isn't affected since it doesn't operate under a federal charter; it is a Quebec chartered company. The ownership regulations that govern Industrial Alliance are defined by a private bill, specific to Industrial Alliance, which was adopted in the National Assembly during the company's demutualization process. And this act stipulates that no shareholder may own more than 10% of the company's stock – with no time limit.

In order to amend a private bill, it takes a process that differs slightly from a public act. Any amendments to a private bill have to follow five steps:

- The agreement of the company's Board of Directors;
- The support of the shareholders;
- The approval of the insurance regulatory authorities;
- The assent of the Department of Finance; and
- The consent of the National Assembly.

Our action plan, which we have tirelessly repeated to our shareholders since February 2000, is to pursue the Company's development. The ownership regulation that is contained in our bill gives us the flexibility, at all times, to decide our own future, in the best interests of our shareholders.

What about the other financial institutions targeted by the federal government's new ownership regulations?

Obviously, no one knows for sure what the future holds for them, except Clarica of course, and it certainly would not be a wise move on my part to feed the rumour mill. However, I would like to warn you against doomsday scenarios where all medium-sized institutions disappear.

Even though everyone loves a good Hollywood ending, market rules are such that companies usually find a way to come up with new and original solutions that no one really thought about before. And this is what is currently taking place in the world of insurance and financial services. Let me give you two examples.

First of all, with respect to acquisitions in Canada, six mid-sized insurance companies have been taken over since 1999, not including yesterday's announcement. And where you would expect that the five dominant insurers or even the major banks would have split the proceeds, out of the six transactions, only one was carried out by a major insurer. To everyone's surprise, the acquisitions were made by so-called "group 2" insurers – insurers ranking from 6^{th} to 10^{th} – and one was carried out by an American insurer that had decided to deploy a portion of its capital in Canada.

Industrial Alliance didn't just sit back and watch it all happen. We put in offers for four of the six institutions. We managed to get our hands on Seaboard Life, a major Vancouver life insurance company, which we then merged with our other Vancouver subsidiary to create what is known today as Industrial Alliance *Pacific*. This was a 257 million dollar transaction. More recently, we lost by a hair at the finishing line to one of our competitors and in two other cases, after carrying out a due diligence, we decided to place a modest bid on the two other institutions, saving our money for other opportunities.

Secondly, mergers and takeovers are, by their very nature, sensational, but consolidation has taken a new form over the past few years in the financial services sector, that of strategic agreements.

Over the past few months, an unprecedented number of distribution agreements have been reached between financial institutions. These agreements may take the form of direct sales of one institution's products by another, or even that of client referrals between financial institutions.

For example, the Investors Group, Great-West and London Life distribute CIBC banking and brokerage products. Clarica and TD Waterhouse reached an agreement that allows Clarica to refer to TD Waterhouse those clients who would like to buy or sell securities. ManuLife and Zurich signed an agreement that allows ManuLife to supply a wide range of insurance and group pension products to Zurich distributors, and Zurich to provide auto, home and business insurance to ManuLife distributors.

Industrial Alliance hasn’t been sitting this movement out either. For example, we manufacture and administer TD Bank life insurance products through our Toronto subsidiary. We also manufacture and administer credit insurance products for the Laurentian Bank. As well, we signed agreements allowing two insurance companies to distribute our star product – our universal life insurance policy.

And just yesterday, we announced that we have reached an important agreement with the National Bank. Through this agreement, we will administer the group pension plans distributed by National Bank Trust. We will thus administer some 1,400 group plans for National Bank Trust, on behalf of 33,000 members with a value of over 430 million dollars.

A financial analyst recently said: "While conventional wisdom has, up until now, suggested that consolidation/convergence will necessarily take the form of mergers between financial service providers, (the distribution agreements that have been announced over the past few months) suggest that there may be less costly symbiotic alternatives, at least in the medium term." I wholeheartedly agree with that analysis.

As you can see, even though everyone is expecting mega-mergers, we shouldn’t be surprised to see partnership agreements flourish too. I personally prefer the *piecemeal* approach to the *megadeal* one.

In my opinion, these strategic agreements meet a need for efficiency. Nowadays, companies cannot excel in all areas. To succeed, they have to specialize. This is why they do not hesitate to offer their competitors' products, if these products can better meet their clients' needs.

We often hear that, within the current context of market globalization, the large financial institutions hold the advantage over smaller companies. While this may be true when serving large companies that operate around the world, I do not believe that the large institutions have an advantage over the smaller ones when it comes to serving the needs of the retail market.

Competitiveness is not just a question of size, it is also a question of culture and strategy. For the local market, success is measured more in terms of dynamism and the ability to innovate and adapt rather than in terms of actual size.

I believe that the consumer will benefit from much healthier competition if the market is made up of a large number of institutions, of varying sizes, each with their own strategies.

A growth strategy for Industrial Alliance

In this constantly changing world, what will Industrial Alliance be like in three or even five years?

When the company demutualized, the Board of Directors gave Industrial Alliance a clear mandate: to pursue, indeed accelerate its growth, both on an organic level and through acquisitions, and to continue to extend its financial services operations, related to those of life and health insurance.

With respect to acquisitions, we came out ahead over the past three years by purchasing – and I touched on this earlier – Seaboard Life, an insurance company, the Groupe Financier Concorde, a mutual funds dealer, Mécagroupe, a credit insurance provider for Quebec automobile dealerships, and Aegis, a Saskatchewan insurance company that also operates in the credit insurance sector through automobile dealerships.

We also expect to continue expanding the range of financial products offered by our agents. It was in this spirit that we started distributing mutual funds last year as well as creating a trust company that just received its licence to operate in all Canadian provinces.

And the latest news is that the Board of Directors just gave their approval to the company to develop a full-service securities brokerage operation.

With respect to products, we also expect to take advantage of the federal government's recent authorization for insurers to become members of the Canadian Payments Association. This membership means that insurance company clients will be able to access their funds through automatic tellers using a debit card. There is a real need for this for all insureds since, in our industry, 90% of benefits are paid while the person is still living and only 10% of benefits are paid after a death.

Conclusion

This is where we are at right now. And this is where the values of discretion and efficiency have led us: to an energetic, forward-looking company.

Industrial Alliance is an important company for the region. And it wants to remain so. We employ over 1,000 people in the region, not including hundreds of agents. Even though we are not labelled a “new economy” company, over 150 people, most of them quite young, work in the technology sector.

We also own real estate assets in excess of 400 million dollars. In the Quebec City region, we are 3rd in terms of office building ownership. We own the ministère du Revenu building, at Pointe Sainte-Foy, a ministry which, unfortunately for you, the taxpayer, is growing rapidly! In Montreal, we contributed to the revitalization of the downtown core by purchasing and renovating the former Simpsons building, which is home to the very popular Maison Simons.

My objective for the next few years is to stick to our initial game plan of becoming a major player in the Canadian insurance and financial services sectors. And I will dedicate all my time and energy to it.

I have spent my entire working life at Industrial Alliance, and I will do my level best to follow the mandate dictated by my predecessors, emphasizing the values that have made us the success we are today.

Without fanfare, and in the tradition of Industrial Alliance, I will remain faithful to the maxim “Don’t seek admiration, strive to create something admirable instead.”

Thank you.