

## **Annual Results 2013**

Remarks by Martin Senn (slides 4 to 7), CEO, and Vibhu Sharma (slides 9 to 22), CFO ad interim of Zurich Insurance Group

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### **Slide 4: Solid results underpin high cash returns**

Welcome to Zurich Insurance Group's results presentation for the two thousand and thirteen financial year.

Business operating profit for the year rose 15 percent to 4.7 billion U.S. dollars, while net income attributable to shareholders was up 4 percent at 4.0 billion dollars.

The annualized return on equity for the year based on business operating profit after tax was 10.5 percent and on net income attributable to shareholders, it was 12.0 percent.

Cash flows remained strong with net cash remittances to the holding company of 2.9 billion dollars. Zurich remains well capitalized with a Zurich economic capital model ratio of 120 percent as of September 30. That is at the upper end of our double A-target range.

Overall, I would characterize these as solid results which have given our Board the confidence to propose a dividend of 17 Swiss francs per share, unchanged from the prior year.

Vibhu Sharma, our interim CFO, will expand on these numbers in detail in his presentation, but I will explain some of the key drivers of our performance in two thousand and thirteen and what this means for us in the future.

### **Slide 5: Drivers of our 2013 performance**

In General Insurance, we grew gross premiums in our priority markets by 5% in local currency, mainly driven by improved rates but with some exposure growth outside of Europe.

Improved profitability was mainly due to lower catastrophe losses and the one-off charges related to reserve strengthening in Germany in 2012, though this was partly offset by an increase in large and weather-related losses as well as lower investment income.

We are continuing to see the benefit of rate increases ahead of loss cost inflation, as well as ongoing expense discipline, and we view most of the portfolio as being in very good shape.

However, as we discussed at the investor day, there are areas that are clearly not meeting our expectations and where we will take remedial action. As a case in point, our Q4 results include a write down of goodwill of around 200 million dollars in our business in Russia, and we are exploring our options for our retail operations in this country.

Global Life benefited from strong growth in the protection business, particularly in emerging markets. From an operating profit perspective, expansion of the protection business resulted in an increase of roughly 50 million dollars in net risk margins, which was more than offset by lower investment margins and build-out costs related to growing our operations in the U.S. and Asia.

At the Farmers Exchanges, which we manage but do not own, rate and underwriting actions begun in 2012 led to a decline in both new business sales and retention, mainly in relation to non-standard auto and small commercial insurance business, but also in the core Farmers auto and home business. 2013 was a challenging year for Farmers, and the business is going through a transitional period as its new consumer strategy is implemented. That being said, the business continues to deliver resilient margins and strong cash earnings, and an improved underwriting performance is clearly visible in a better underwriting result at Farmers Re.

These results demonstrate that, as we said at our Investor Day in December, while much of our business continues to perform well there are areas which need improvement. We are taking firm action in this respect, and I have set my team clear priorities for two thousand and fourteen that are aligned with the three cornerstones of our strategy for the next three years.

#### **Slide 6: Priorities for 2014**

In terms of prioritizing investment in distinctive positions, the first of our strategic cornerstones, we will continue to invest in growing our corporate, commercial business and select retail businesses

In the corporate space, we aim to strengthen our combined Global Corporate and Corporate Life & Pensions “go-to-market” approach. We are in the process of ramping up our data and analytics capabilities in North America Commercial which will eventually allow us to better serve commercial mid-market customers around the world. And we have completed our field work on customer segmentation within three retail markets where we believe our brand strength and reputation give us a competitive advantage and are currently analyzing the data from that process.

The second cornerstone of our strategy relates to businesses that we are managing for value. In our European life operations, which account for the bulk of the capital allocated to the manage for value group, our priority for two thousand and fourteen is to explore opportunities to improve our distribution model and, in the current low interest rate environment, there is increased focus on in-force management. We are setting up a new in-force management team to enhance our global capabilities in this area and to support the business units in extracting more value from our existing in-force portfolios.

We have moved quickly to execute our strategy for turning around or exiting underperforming businesses. In our General Insurance business, we combined the regional management of the Middle East and Africa with Europe to allow for economies of scale in running the business. Global Life recently announced a plan to simplify its management structure and has exited an underperforming distribution channel in Hong Kong. We will continue to take decisive action, and intend to have largely completed our evaluation of underperforming operations by the end of this year.

The third cornerstone of our strategy is to grow our operating earnings. Here, I have set three priorities.

First, we have a project in the pipeline to reduce complexity and thereby reduce overhead burdens across the Group. I intend for this project to have been completed, and actions implemented, by the end of this year.

Second, I will also be pushing for renewed focus on improving the profitability of a number of our General Insurance portfolios which are currently under-performing, with a clear plan to address these issues within the next 18 months.

And third, we will implement our plan to diversify our investment portfolio into less liquid assets in line with our disciplined investment approach.

At the Farmers Exchanges, the priorities are to improve the customer experience, roll out omni-channel capabilities and to begin tailoring propositions for the target customer base, the “confident planners”. The goal here is to make real progress in the transition of the business by the end of the year, with improvement in new business and retention visible in the second half.

In recent months, we have also strengthened our Group Executive Committee with the addition of George Quinn as Chief Financial Officer and Robert Dickie as Chief Operations and Technology Officer.

With a full-strength management in place, and the great depth of talent in our Group, I am confident that we will have the right team in place to deliver on our strategy.

To summarize our priorities, this is a year in which we are taking firm actions in relation to each of the three cornerstones of our strategy. We expect some of the benefits of these actions to become visible this year, as we lay a strong foundation for the delivery of our strategic targets for 2014 to 2016.

I look forward to updating you on our progress on these priorities at the half-year when we will also publish the first of our report cards.

#### **Slide7: Key messages**

In closing, Zurich has delivered robust results for 2013 with solid operating profits in all our core businesses.

We have delivered good growth in our priority General Insurance and Life markets, while the transition at Farmers continues.

The Group continues to generate strong cash flows and remains well capitalized with solvency at the high end of our double-A target range giving our board the confidence to propose a very attractive dividend of 17 francs per share.

Lastly, we have set out a clear strategy for 2014 to 2016, with priorities identified for 2014 and actions already underway, and we are well positioned to deliver on the goal we set out at the investor day of delivering strong total returns to our investors

Thank you for your attention and your continued trust and interest in Zurich.

### Slide 9: BOP by segment

Good morning and good afternoon ladies and gentlemen.

In 2013, we achieved solid operating results with good growth in both General Insurance and Global Life priority markets. We delivered strong cash remittances to the holding company and maintained our excellent capital position.

At a segment level, let me highlight the following key points

In General Insurance, our business operating profit increased by 35 percent compared to 2012, mainly due to lower catastrophe losses and the charges we took in Germany in the prior year. We continue to see good momentum on rates, and expect to see improvements in our underlying margins in our 2014 results.

Global Life BOP is slightly down in 2013, due to lower investment margins, but we see a positive trend. We are growing in our protection business and are very pleased with the progress of Zurich Santander. We are seeing these positive indicators having a favorable impact on our operating earnings.

Farmers BOP is up 8 percent from the prior year, due to much improved results at Farmers Re.

And our 2013 Other Operating Business loss was around 100 million dollars higher than the prior year, principally due to lower investment income. Our Headquarters costs in the discrete fourth quarter were higher than in the previous quarters, reflecting the timing of media spend that I referred to with our Q3 results, as well as the timing of some other expenses.

In aggregate, we achieved a 15 percent increase in our BOP in comparison to 2012.

### Slide 10: Reconciliation from BOP to NIAS

While our BOP increased by 15 percent, our net income of 4 billion dollars increased by 4 percent in comparison to 2012. There are three main points I would highlight.

First, while we had a high level of realized gains in 2013, mainly due to the sale of our investment in NCI, total realized gains were still lower than in 2012.

Second, we have taken roughly 300 million dollars in restructuring costs in the fourth quarter of 2013. While 30 million dollars of this amount is included within BOP, the majority of these costs were taken "below the line". The biggest item relates to our decision to write down the goodwill relating to our Russian retail General Insurance business. This decision is an example of the increased scrutiny of underperforming businesses that we highlighted at our investor day.

And third, our tax rate is roughly 1.5 points higher than the 23.5 percent we expect on an ongoing basis, mainly due to one-off factors relating to mix and the settlement of a local tax audit.

#### **Slide 11: General Insurance – Key performance indicators**

The key highlights for General Insurance can be summarized as follows.

Gross written premiums increased in local currency by 3 percent, with growth of 5 percent in priority markets, adjusting for the discontinuation of a large fronting contract.

We delivered a solid combined ratio of 95.5 percent for the full year, roughly 3 percentage points better than in 2012, due to the lower impact from major catastrophes and positive underlying loss and expense trends, partially offset by higher claims from mid-size weather events and large industrial losses.

Investment income continues to reflect the persistent low yield environment, declining by roughly 300 million dollars in 2013. But, as indicated previously the decline was much lower towards the end of the year, with the fourth quarter declining by roughly 30 million dollars versus the prior year. The fact that new money yields are still below the running yield on the portfolio points to a further decline in investment income, but at a much slower pace compared to 2013, and we are starting to expect a flattening out in the next few years.

Further I would like to highlight two factors in our full year results: first, our BOP includes roughly 170 million dollars in realized gains on our hedge funds and other investments; and second, lower non-technical expenses, driven by roughly 100 million dollars of non-recurring items in 2013.

#### **Slide 12: General Insurance – Rate change monitor and GWP performance**

We continue to see good rate increases across the book, 3.7 percent for the full year and 4.2 percent for the fourth quarter. This is particularly the case in our Global Corporate and North America Commercial business, where we achieved rate increases of 5 percent and 4 percent, respectively, in the fourth quarter.

As I said before our gross premiums in local currency grew by 3 percent, with the fourth quarter flat against Q4 2012. The lower figure for discrete Q4 is mainly related to currency and non-recurring items such as the catch-up of the quarter in arrears for Zurich Santander in 2012, and the impact of the fronting contract I mentioned before.

Global Corporate and North America Commercial grew by 6% on an adjusted basis, and we also continued to expand in our International Markets.

In our European retail and commercial business, we experienced a decline in gross premiums. However, the shortfall in Europe slowed towards the end of the year, with some signs of improvement in the

fourth quarter. On a stand-alone basis in the fourth quarter, we grew by 1 percent in local currency, driven by growth in UK commercial and personal lines in Germany.

### **Slide 13: General Insurance – Combined ratio trends**

On this slide, we give you a breakdown of our combined ratio into the key elements.

You will find the usual details on our loss and expense ratio in the appendix of the 2013 analysts' presentation.

Over the last four years, we have improved the accident year loss ratio, including all catastrophe and large losses, by 5.2 percentage points, due to our focus on increasing rates and on portfolio management.

This improvement is mainly visible in our underlying loss ratio which improved by 6 percentage points to around 60 percent in 2013.

While the fourth quarter underlying loss ratio was a touch higher, at 61 percent, we would not draw any conclusions from just one quarter, particularly since this was partially driven by the crop business in North America Commercial which earns the majority of the premium in the fourth quarter and runs at a higher underlying loss ratio.

Looking at 2013 more closely, our catastrophe and large losses were 10.3 percentage points, slightly higher than the five year average. While last year was a quiet year for big catastrophe losses, it was an active one for mid-size weather events. Our large losses were also above recent experience.

Consistent with our nine month results, while there has been an increase in large losses since 2010, roughly half of the change is due to mix, with the balance being the inherent volatility in our portfolio. As we said before, we investigate and learn from each major loss and this will continue to be a focus for us in 2014 as we look to ensure that we leverage our insights and risk engineering capabilities.

The last piece of the loss ratio detail is our prior year development. This was 2.4 percentage points for 2013, with positive run-off experience in most parts of our portfolio.

In terms of our expense ratio, this has been flat over the past four years and we were able to compensate for the investments in our international growth markets with the focus on expense management in our mature markets.

### **Slide 14: General Insurance – BOP and CoR by business**

In Global Corporate, we were able to grow our business and we delivered good results despite an increase in weather related and individual large losses especially in Europe. The growth was achieved through solid rate increases but also through some exposure growth in all our markets. We are very

well positioned to further capitalize on our key strengths in this business and we are investing to support this.

North America Commercial made some further progress and achieved a combined ratio of 95.3 percent. The improvement was driven by lower catastrophe losses, a further reduction in our underlying loss ratio and tight expense management offset by lower prior year releases. In 2014, we will be focusing on pockets of business where we see improvement potential, and we continue investing in data analytics capabilities to further enhance our market position.

In Europe, we continued to face challenges from the economic downturn in some of our markets. Headwinds remain in 2014, especially in Spain and Portugal. However, with the exception of our Russian business, we are delivering good performance in our main markets.

Our performance has not lived up to expectations in some of our International Markets. While the high combined ratio is in part a reflection of our investments in this region, and we continue to take market share, our focus in the next two years will be on improving profitability.

Clearly this focus is not limited to International Markets only but to give you a sense of what we mean here, achieving breakeven for our operations in Latin America and Middle East and Africa, would have increased our reported BOP by 6 percentage points.

To summarize on our General Insurance business:

On the positive side, we continue to get good rate increases, we are growing in our priority markets, the decline in investment income is slowing, and the majority of our portfolio is in very good shape.

Equally, there are businesses that are not performing up to expectations. and we are taking actions to address this.

#### **Slide 15: Global Life – Key performance indicators**

Protection sales combined with growth strategies in Latin America, and Asia Pacific and Middle East, are an increasingly important part of the global life story and are the key elements that shape the results that I share with you today.

Protection not only plays a major factor in the growth strategies in these regions, particularly in retail distribution, but also in Europe through our bank distribution and corporate life and pensions pillars.

As a reminder, protection is a low volume higher margin business, which is the opposite to the dynamics of a fee based business, and becomes self-evident when we look at our Global Life KPIs.

Starting with APE, the slide shows that the full year 2013 APE reduced by 6 percent over the prior year. This was due to a couple of factors in the prior year that did not reoccur in 2013. The first of which was a major one-off contract in Chile, and the second, lower sales of an investment product in the UK.



These two items accounted for 638 million dollars in the 2012 APE, but had a small impact on new business value.

Where we see the impact of our focus on protection is in the 17 percent increase in new business value and the 5.5 percentage point improvement in new business margin.

Almost all of the growth in new business value was from the priority markets we identified at the investor day. The most significant contribution came from Zurich Santander, included in the comparative year for the first time, where APE grew 26 percent to 821 million dollars, and with new business value growing by 52 percent. This was predominantly due to significant growth in protection sales, particularly in the core markets of Brazil and Mexico. The short payback, high return nature of the business is illustrated in a 25 percent improvement in the local statutory profit before tax. We show more information on Zurich Santander in the Appendix to our results presentation.

While Zurich Santander is doing very well, we are also encouraged by our progress in the US IFA market, Latin America excluding Zurich Santander and the Middle East. We have fully integrated our 2012 acquisition in Malaysia and have built our distribution capabilities in Indonesia. These actions provide a solid platform for growth in 2014.

#### **Slide 16: Global Life – Business operating profit: Profit by Source**

The headline business operating profit came in just above the middle of the previous guidance range for the full year, averaging out at approximately 320 million dollars per quarter. The high level themes driving our earnings have remained consistent throughout the year, but to recap

First, and reflecting the product focus outlined on the previous slide, the combined expense and risk margins increased by 258 million dollars, or 183 million dollars when including the change in acquisition deferrals. The majority of this improvement came from Europe, partially driven by our expense program.

Second, we continue to see a growing contribution from Zurich Santander, the result of which is reported in other profit margins. This business contributed 387 million dollars before non-controlling interests, or 182 million dollars after non-controlling interests, to our life BOP for the full year 2013. Overall this results in an increase of 77 million dollars compared to the prior year.

Third, and partially offsetting these favorable developments, was a 138 million dollar reduction in the investment margin, as low yields continued to affect spread business and returns on capital, particularly in the US, Asia Pacific and Middle East, and Germany.

Fourth, there was a roughly 200 million dollar increase in costs flowing through other profit margins relating to statutory reserve movements in Germany and investments in priority markets.

And finally, we incurred 30 million dollars of accounting charges booked in special operating items in the fourth quarter, relating to the closure of the tied agent channel in Hong Kong.

So in conclusion, our investments in Latin America, and Asia Pacific and Middle East, combined with our focus on product profitability and the expense savings program in Europe have enabled us to deliver profits within our guidance. We will continue to invest in our priority markets and build on our successes. In addition, as we set out at the investor day, we are focused on enhancing our in-force management and improving profitability in our manage for value markets.

#### **Slide 17: Farmers - Key performance indicators**

Farmers overall posted good profitability for the quarter and the year as strong improvements at Farmers Re more than compensated for a small decline in FMS earnings. This reflects a significant improvement of the policyholder-owned Farmers Exchanges underwriting result due to the rate and underwriting actions we started taking in mid-year 2012. However, these actions have also negatively impacted new business sales and retention.

Before we get to the Exchanges I will first talk about Farmers Management Services and Farmers Re.

For FMS, management fees and other related revenues decreased by 1 percent over the year. While management fees slightly increased as the premium growth achieved in 2012 earned through and higher margin specialty business continued to grow strongly, this was offset by a decline in fees on new business.

For the fourth quarter on a discrete basis, management fees showed a modest decline, however, the attrition through other related revenues slowed as new business counts stabilized in most business lines.

While expenses remained basically flat adjusting for some positive one-off items, lower net investment income contributed to the overall decline in FMS BOP over the year and in the fourth quarter.

Overall, the Managed Gross Earned Premium margin finished the year at 7.2%, closer to the 7.0% which we've previously indicated is likely to be the sustainable long term level.

For Farmers Re, we saw a significant increase in business operating profit for both the full year and the fourth quarter, driven by a much better underlying loss ratio and, for the fourth quarter on a discrete basis, lower catastrophe losses.

#### **Slide 18: Farmers Exchanges - Key performance indicators**

The Farmers Exchanges results in the fourth quarter of 2012 were impacted by the Fogel and the State of Texas settlements. In my comments on growth and combined ratio I will refer to adjusted numbers for better comparison.

The year-on-year drop in Gross Written Premiums of 2 percent compares unfavorably with the 4 percent gain achieved in 2012 with some acceleration in the decline in gross written premiums in the fourth quarter.

Before I go into this in more detail let's look at the combined ratio first.

There is a significant improvement in the loss ratio amounting to 5 percentage points for the year and 8 percentage points for the quarter. In the fourth quarter, low catastrophe losses clearly helped. In a year-to-year comparison, however, catastrophe losses remained at 1.1 billion dollars which is above historical levels. As Jeff showed at Investor Day, there was significant progress in cutting Loss Adjustment Expenses. This reduced the loss ratio by about 2 percentage points for the year and the quarter with the balance being attributable to the underlying loss experience.

The expense ratio remained largely flat for the year and the quarter when adjusting for some one-off expense savings that occurred in the fourth quarter of 2012.

In summary, from a combined ratio perspective there is a significant improvement due to the rate and underwriting actions underway since mid-year 2012.

However, this had a negative impact on the top line as new business sales and retention decreased. Compared to the previous year, Farmers Exchanges GWP declined by 366 million dollars with almost half the decline coming in the fourth quarter.

There are two main factors here.

First, the repositioning of non-standard Auto, Independent Agent Business Insurance and Independent Agent personal lines. These books lost 435 million dollars in Gross Written Premiums or 22 percent of their total volume.

Second, in the fourth quarter premiums in standard Auto declined, and we experienced a slowdown in growth in the Farmers Homeowners business. This was due to further rate increases and the repositioning of 21st Century Direct in the context of the new consumer strategy outlined at the investor day.

In terms of where we are now:

For the books that have been subject to major repositioning, there are some signs of improvement. Non-standard Auto, by far the largest of the books showed increased new business sales and a slightly improved retention in the fourth quarter.

And in the standard Auto and Homeowners business, excluding Direct Auto, there are encouraging signs that retention and new business sales have stabilized.

Lastly, Farmers Exchanges surplus has grown during the quarter and the year and the surplus ratio according to the revised calculation excluding Farmers Reinsurance Company increased to 37% at year-end compared to 33% a year before. This is slightly above the target range indicated to you at the Investor Day and a reason to be confident that the reliance of the Farmers Exchanges on Quota Share reinsurance can be significantly reduced over time.

While the overall capital support for the Farmer Exchanges through the two Quota Share reinsurance treaties for the time being remains unchanged, the Farmer Re participation has been lowered to 18% from 18.5% for the All Lines Quota Share reinsurance treaty and to 900 million dollars from 925 million dollars for the Auto Physical Damage reinsurance treaty.

As Martin mentioned we see 2014 as a transitional year for Farmers Exchanges as its new consumer strategy is implemented. We are confident to see further improvement of the Farmers Exchanges underwriting result barring major catastrophes as well as its growth momentum to gradually pick up again throughout the year.

### **Slide 19: Investment performance of Group investments**

Net investment income further declined but at a slower rate compared to previous quarters. As we highlighted earlier, we expect this trend to continue for 2014. However, new money yields continue to fall short of running yield overall. Thus some pressure on net investment income will persist.

Net capital gains realizations for the quarter were largely on equity securities, and principally driven by the sale of all of the Group's remaining shares in NCI. The total realized gains for the year were significantly lower compared to the previous year and were the main driver of our lower net investment result.

Finally, the rise in government bond yields as well as the sale of NCI further reduced unrealized capital gains on Group investments. Overall, unrealized gains included in shareholders' equity declined by roughly 3 billion to 1.8 billion dollars.

### **Slide 20: Cash and capital**

Net cash remittances from our local businesses for the full year came in at 2.9 billion dollars, after funding our investments in priority markets, and deducting central costs. This demonstrates the Group's ability to convert local earnings into cash and is one of the key factors that gives us confidence that we can continue to pay an attractive and sustainable dividend.

In terms of the capital position, this remains very strong. The ZECM ratio at the end of September was at the top end of our target range at 120 percent, essentially unchanged from the half year.

The fact that our cash and capital positions remain strong is important in providing us a solid platform from which to execute on our strategy.

In future, we will report our ZECM ratios each quarter with a one quarter time lag, we will provide an update on cash remittances with full year and half year, and we will give you an update on free cash generation for 2013 with our half year results.

**Slide 21: Outlook for 2014**

In General Insurance, we look for continued improvement in the combined ratio due to better underlying profitability in our core business and improvement from our turnaround or exit operations. The headwind from low yields should be a much smaller issue in future years, although non-technical expenses will likely be higher and hedge fund gains lower.

In Global Life, the trends seen in our earnings in 2013 are likely to continue. In other words, growth in our risk margins and Zurich Santander and a decline, if at a slower pace, in the investment margin.

For Farmers, this is likely to be a transitional year. There are indications we should see a turn in top-line momentum at the Farmers Exchanges during the year. From a profitability perspective, we expect Farmers Re results to improve but with a modest decline in Farmers Management Services revenues.

For OOB, our current run rate is around 250 million dollars per quarter. While we will be taking actions to reduce complexity and overhead burdens in 2014, we would expect to see more benefit from this in 2015, partly in OOB, but mainly in the segments.

Across our priority markets, we will be investing in our Corporate, NAC and select Retail initiatives. This will come at a near-term cost, but from a P&L perspective we will also have a one-time pension gain in Q1, which as we see it today, is likely to be between 100 and 200 million dollars.

On restructuring costs, it is likely that we will incur the full 600 million dollars of charges we signaled in December, less of course the roughly 300 million dollars we took in Q4.

All these aspects show that we are starting to implement the strategy we outlined at the investor day in terms of where we invest, our manage for value priorities, and our focus on growing our operating earnings.

Finally, I want to highlight some reporting changes we will make. First, we will introduce the sources of earnings reporting for life in Q1. And second, we will simplify how we report our combined ratio, and include some of the non-technical costs in the expense ratio, most likely with our first half reporting.

**Slide 22: Key messages**

So let me summarize our 2013 results.

First, while not without headwinds, we delivered solid operating profits in each of our core segments.

Second, in terms of growth we take some clear positives from last year, especially in our priority markets, where we grew our gross premiums in General Insurance by 5 percent, and our life new business value by 15 percent. While this will be a transitional year for Farmers, we should see tangible progress in 2014.

Third, the strong cash remittances to the Group and a very solid capital position underpin our 17 Swiss Franc dividend per share proposal.

And lastly, as Martin has made very clear our focus now is on generating momentum in the execution of our strategy.

Here, we will be investing in our priority markets where we have distinctive positions. For 2014, this means Corporate Customers, NAC and three Retail markets.

We will continue to take decisive actions on our turnaround or exit operations, and we will implement in force management initiatives in a number of our Global Life "manage for value" markets.

And we will focus on growing our operating earnings through reducing complexity and overhead burdens, extracting more value from some of our General Insurance operations, and a modest increase in investment risk.

In short, we have a very clear sense of our priorities and what we need to do to deliver the targets we set out at the investor day.

Thank you for your time.



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