

Q3 Results 2014

Remarks by George Quinn, Chief Financial Officer of Zurich Insurance Group.

November 6, 2014

Slide 2: Key messages

Good morning or good afternoon. My name is George Quinn and I am the Chief Financial Officer of Zurich Insurance Group, and I would like to welcome you to our Q3 results presentation.

Let me start by making a few short introductory remarks on our results.

First, in our General Insurance business, we continue to see good improvement in our accident year profitability due to a combination of earned rate increases in excess of loss cost trends and other profit improvement initiatives.

Second, our life results are in line with our expectations, with strong progress in bank distribution in terms of both BOP and new business value.

Third, after 6 quarters of decline, the Farmers Exchanges' top-line was back in positive territory in Q3, with growth in gross premiums written of 0.6 percent overall. Excluding businesses in transition – namely, 21st Century and Business Insurance sold through Independent Agents – the picture is even more encouraging.

And last, our solvency capital continues to be very strong across all key metrics, with our Z-ECM ratio at 126 percent at the end of June.

Overall, this is a solid set of results. While we continue to make progress in executing our strategy, we recognize that the environment is getting tougher. The pricing environment in GI may be about to enter a phase of softer pricing and interest rates remain at very low levels. As a result we will have to work even harder to reach our targets. The good news is that we have the levers to get us there. We will continue to optimize our portfolio, taking action on underpriced risks and allocating our capital to those areas offering the most attractive returns. We also have the ability to meaningfully improve our efficiency and our high cash remittances and strong capital base afford us significant flexibility when it comes to our previously stated capital management priorities. We are confident in our ability to achieve our financial and strategic goals.

Turning back to Q3, I will now take you through some of the results of our business in more detail.

Slide 3: Group – Business operating profit

Business Operating Profit of 1.2 billion dollars in Q3 is down 6 percent compared to the prior year quarter. Within this, the result of our core operations are largely unchanged, with the main driver of the difference being a swing in the result of non-core businesses. Viewed on a year to date basis, Business Operating Profit is up 7 percent in comparison to the prior year, and 9 percent in local currency.

I will cover the operating performance of our segments shortly, but I will briefly highlight three points on this slide.

First, as you can see in the BOP to NIAS reconciliation, we have a high tax rate for the third quarter, of around 33 percent. This reflects the fact that we now expect the full year tax rate to be slightly over 29 percent, above the 27.5 percent we indicated at the time of Q2, driven mainly by mix effects. As I've mentioned before, the effective tax rate we expect for the full year is negatively distorted by a number of items that we view as non-recurring. That said, and in part due to the growing importance of our business in Latin America, we also think it is more prudent to plan for a higher future effective tax rate, of around 25 percent for the group overall.

Second, also in the BOP to NIAS reconciliation for the third quarter, we had quite a high level of realized gains. This was due to a positive revaluation of real estate in Switzerland and Austria, as well as gains on equities and fixed income securities.

And third, we show restructuring and accounting charges of roughly 60 million dollars for Q3, broadly in line with what we indicated we would take at the time of our Q2 results.

Previously, we'd expected to close the sale of our Russian retail business in Q3, but as you will have seen from our recent press release, this is now a Q4 event. While the numbers are still being finalized, we expect this disposal will generate a loss through net income of around 300 million dollars, in line with what we'd previously announced, to be included in our Q4 results. As we've mentioned before, most of this loss is due to realization of previously unrealized currency losses, and consequently, will have only a very small impact on our shareholders' equity.

Slide 4: General Insurance - Topline

Excluding the impact of a large discontinued fronting contract, gross premiums in local currency were up 2 percent for both Q3 and for the first nine months.

Rate increases on renewal across the book as a whole were also 2 percent for Q3. Pricing in both Global Corporate and in Europe was up by around 2 percent, with NAC essentially flat in the discrete third quarter.

In terms of top-line development overall, Global Corporate reported a Q3 decline of 2 percent compared to the prior year. This includes some seasonality and timing effects and we would see the 2 percent growth for the nine months as more indicative of current trends. We have seen higher retention and better new business production in the US, while within Global Corporate in Europe, premiums are slightly down, mainly driven by our underwriting actions.

Elsewhere in the business, NAC's gross premiums were up 2 percent for the quarter, excluding the discontinued fronting contract, and our European business grew top-line by 1 percent in local currency. As mentioned last quarter we continue to see growth momentum in some key European markets such as in the UK and personal lines in Switzerland and Germany. Also as was the case in prior quarters, there was some top-line pressure in Italy, where the market is shrinking, as well as in some of our turnaround markets, such as South Africa.

In International markets, premiums increased by roughly 4 percent in local currency. We are still expanding the business but our underlying growth rate has slowed, mainly due to some selective re-underwriting in LatAm and market softening in Australia.

Standing back from the detail, and consistent with much of what you've heard already, market conditions are not that different to what they were in the second quarter. Pricing is broadly running in line with loss cost trends, and our retentions are very good, although clearly at the margin we do see signs of increased competitive pressures in some areas, and with fairly limited overall exposure growth in most markets.

Slide 5: General Insurance – Combined ratio

Our accident year ex-cat combined ratio was 95.4 percent for the third quarter. This is 1.4 percentage points better than in the prior year and at a similar level as the first half, excluding the one-off pension gain in Q1.

The driver of the improvement in comparison to the prior year is a 2.3 percentage point lower accident year ex-cat loss ratio, with the trends in Q3 essentially unchanged from Q2. In other words, we have seen a more normal level of large industrial losses compared to what we experienced in 2013, as well as around a 1.5 percentage point improvement in our underlying loss ratio, especially in NAC and Europe.



While large losses were slightly higher in the third quarter than in Q2, mainly due to an increase in very large individual claims in Global Corporate, experience is essentially in line with expectations both for the quarter and for the year to date.

Our overall expense ratio for the quarter of 31 percent is roughly 1 percentage point higher than in the third quarter of last year and the second quarter of this year. As we had previously flagged, we had some non-recurring benefits in the prior quarters, which explains about half the difference, with the remainder due to the cost of investments we are making in priority markets.

The impact from catastrophes was 3 percent in Q3, including a 90 million dollar impact from Hurricane Odile in Mexico, mainly in our commercial business and in Global Corporate. While hard to put this in an industry context, we'd expect to have a reasonably high market share of any major cat loss in the region given that we are a leading insurer of hotels, which were significantly impacted by this event.

In terms of prior year development, the result for the quarter and the 9 months is a 0.6 percentage point benefit to our combined ratio. This is again slightly lower than the indicated range of 1-2 percentage points that we talked about in our Q1 results. For the specific quarter we had a 'normal' level of reserve releases in a number of European markets offset by additions in specific and identifiable areas, such as our APH liabilities in the UK and a discontinued line in Global Corporate North America. There is no change to our indication on this topic but I expect that we will continue to see fluctuations in PYD between quarters.

Turning to the performance by region, the Global Corporate Q3 combined ratio includes the impact from Hurricane Odile of roughly 2 points. Within the results we saw a good improvement in the accident year ex-cat loss ratio, especially in Europe, with a small overall level of adverse development in one specific area, as I just mentioned.

NAC and EMEA have both significantly decreased the accident year ex-cat combined ratio, by a little less than 2 percentage points respectively, and benefitted from lower catastrophe losses compared to the third quarter of last year. While this is partly a function of fewer large losses in the quarter, we continue to see some improvement in the underlying performance of these businesses.

And lastly, the combined ratio of our International business includes a roughly 5 percentage point impact from Hurricane Odile. While our Asia Pacific business is doing pretty well, and the results of our LatAm business improved compared to Q3 2013, there is still much to be done in Brazil to improve our underlying profitability.

Slide 6: General Insurance – BOP components

GI BOP was 724 million dollars in the third quarter, down 4 percent compared to the same quarter last year. This is mainly driven by the lower level of prior year reserve releases, partly off-set by the 1.4 percentage point improvement in the accident year ex-cat combined ratio I mentioned before.

The BOP contribution from investment income and hedge fund investments is roughly 10 million dollars higher in comparison to the prior period, with Q3 benefitting from a 17 million dollar non-recurring positive item. Overall, based on the 9 months numbers, we are trending close to flat for investment income, as we expected.

And lastly, the non-technical result for the third quarter is a loss of 14 million dollars. This benefitted from roughly 30 million dollars in currency gains mainly from our LatAm business. Excluding this item, the underlying non-technical result was broadly in line with our quarterly expectations.

To summarize on our General Insurance business, there are plenty of encouraging trends in these results but we have already started to evaluate the actions that we will need to take given what is likely to be a tougher market environment in the next few years.

Slide 7: Global Life – New business

Q3 discrete APE volumes were broadly flat compared to Q3 2013. Growth in the US, Santander and Spain was offset by lower volumes of pensions business in the UK compared to a particularly strong prior period, and where very large pension contracts can create timing differences between individual quarters.

For the year date, APE is up 9 percent in local currency. Our main growth areas include North America, where our IFA strategy and agent productivity initiatives helped us expand new business volumes by 34 percent, Santander, with 18 percent local currency growth, and Spain, where the extension of our bank distribution joint venture with Sabadell helped us to more than double our APE.

As expected our year to date new business value was slightly down year on year, as expense allocations and lapse assumption changes mask an improving underlying picture in the regions. Adjusting for these changes NBV would have grown by around 5 percent.

And finally, net inflows were again slightly positive in the quarter, primarily driven by our US and Latin America businesses.

Slide 8: Global Life – BOP by region

Q3 business operating profit increased by 13 million dollars to 331 million dollars compared to the prior year quarter.

Zurich Santander life BOP of 54 million dollars for the quarter is 20 million dollars higher than in the prior period quarter and the business continues to deliver good growth, with year to date BOP 14 percent above the prior year despite local currency devaluation.

Additionally, net favorable impacts from assumption updates and claims experience helped to improve BOP in North America and Europe.

These positives are partly offset by a reduction of BOP in the 'Other' region due to higher one-off expenses associated with strategic growth and in-force management initiatives. These central expenses reflect the investment in our strategy of manage for value, turnaround or exit and in-force management, which continues to be a high priority.

Further, we experienced slightly negative overall currency impacts as the dollar strengthened against local currencies in September. Looking forward, assuming current exchange rates remain unchanged, we'd expect the recent weakness of the Euro against the US dollar to have a modestly negative impact on our Q4 results.

Overall we see this as a solid result from our life business, and we look forward to showing further tangible progress on the execution of our strategy in the coming quarters.

On the next slide I will give you an update on the Farmers Exchanges, which we do not own but are relevant to the performance of our Farmers business segment.

Slide 9: Farmers Exchanges – KPIs

After six quarters of declining premium volume I'm pleased to report that the Farmers Exchanges returned to growth in the third quarter of 2014.

Improved retention and better new business helped the Farmers Exchanges to increase gross premiums by 0.6 percent in Q3. In addition, looking at the core business – in other words, excluding 21st Century and Business Insurance sold through Independent Agents – gross premiums were up by 2.6 percent in Q3 compared to the prior year period.

This was due to strong growth at Bristol West and in the Specialty business, as well as Business Insurance sold through Exclusive Agents. A further positive sign is the slight increase in Standard Auto

vehicles-in-force sold through Exclusive Agents, and with Farmers branded homeowners policies in force very close to flat in Q3.

In terms of the Farmers Exchanges' profitability, Q3 turned out to be a fairly light quarter for catastrophe losses, with only one severe event, in Arizona and Colorado, costing 75 million dollars.

This relatively quiet quarter for cat losses helped the Farmers Exchanges report a combined ratio of 97.2 percent for Q3, 1.4 percentage points better than in the prior year quarter. Around 0.5 percentage points of the year on year improvement was due to low cat losses, with around 1 point due to improved ex-catastrophe loss and expense ratios.

In terms of capital, the Farmers Exchanges surplus ratio of 36.7 percent at the end of September was more or less unchanged from 30 June. Operating profits for the quarter were offset by the redemption of 100 million dollars of surplus notes during Q3.

Since the end of the third quarter, Farmers Exchanges issued 500 million dollars of new surplus notes. The main purpose of this debt issue is to redeem outstanding surplus notes owned by Zurich, with 200 million dollars callable by the end of this year. This will have a positive impact on the financial position of the Farmers Exchanges, and it will lower their financing costs.

Slide 10: Farmers – KPIs

Farmers Management Services revenues were 1 percent lower than in Q3 2013, in line with the 1 percent decline in the gross earned premiums of the Farmers Exchanges.

In terms of operating profits, Farmers Management Services earnings were slightly lower than in the first two quarters of the year, as well as in Q3 of last year, all of which benefitted from some positive one-off expense items. The Managed Gross Earned Premium margin of 7 percent for Q3 discrete is in line with what we have previously said is likely to be the sustainable level over the longer term.

And lastly, Farmers Re benefitted from the low level of catastrophe losses incurred by the Exchanges in Q3.

Slide 11: Group – Balance sheet and capital

Shareholders' equity slightly increased in Q3, with net income and unrealized gains partially offset by negative currency translation adjustments, as the US dollar strengthened against major currencies.

In terms of our capital position, we signaled back in August that we expected the Z-ECM ratio to decline by 3 to 5 points when we updated our model for Q2 movements, which reflect the actions we

took in the second quarter to add incremental risk to the investment portfolio. In the event, the reduction from the end of Q1 to the 30 June position shows a slightly smaller decline, due to positive market movements in Q2 and a minor reduction in capital requirements.

With a Z-ECM ratio of 126 percent and an SST ratio of 215 percent at the end of Q2, our economic capital position remains very strong. We are also very pleased to note the recent action of Standard & Poor's, in putting our AA- rating on a positive outlook.

Slide 12: Key messages

First, our Q3 results show that we continue to make good progress in improving our General Insurance current year profitability.

Second, our life results are on track with expectations, and with strong progress from our bank distribution channel.

Third, the Farmers Exchanges are back to positive growth again.

And last, our solvency capital continues to be very strong across all key metrics.

Overall, we continue to make good progress in executing the strategy that we set out last December, and we also look forward to giving you more insights into how we are doing in two of our priority businesses, NAC and Farmers, at our investor update on 5 December.

That said, we know that there is more to be done. When we set out our strategy, we didn't rely on improved capital markets to help us achieve our targets, and neither did we assume a favorable tailwind from improved GI pricing either. But we are more than aware of the fact that we will need to be proactive in ensuring that our strategy can cope with potential headwinds as well. Our targets are our number one priority, and we will be taking all necessary steps to make sure that we deliver them.

Thank you for watching.



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