Zurich Insurance Group

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Operating and financial review (unaudited) 2017

Results for the six months to June 30, 2017

Operating and financial review

The operating and financial review is the management analysis of the business performance of Zurich Insurance Group Ltd and its subsidiaries (collectively the Group) for the six months ended June 30, 2017, compared with the same period of 2016.

Contents

The information contained within the operating and financial review is unaudited and is based on the consolidated results of the Group for the six months ended June 30, 2017 compared with the same period of 2016. All amounts are shown in U.S. dollars and rounded to the nearest million unless otherwise stated, with the consequence that the rounded amounts may not always add up to the rounded total. All ratios and variances are calculated using the underlying amounts rather than the rounded amounts. This document should be read in conjunction with the annual results 2016 of the Group and, in particular, with its consolidated financial statements and embedded value report for the year ended December 31, 2016.

In addition to the figures stated in accordance with International Financial Reporting Standards (IFRS), the Group uses business operating profit (BOP), new business measures and other performance indicators to enhance the understanding of its results. Details of these additional measures are set out in the separately published glossary. These should be viewed as complementary to, and not as substitutes for the IFRS figures. For a reconciliation of BOP to net income attributable to shareholders (NIAS), see table 13.4 in note 13 of the unaudited consolidated financial statements.

Certain comparatives have been revised as a result of reclassifications and other adjustments. For details refer to note 1 of the unaudited consolidated financial statements.

Group structure

The Zurich Insurance Group consists of Zurich Insurance Group Ltd and its subsidiaries (the 'Group' or 'Zurich').

Zurich's business is focused on providing best-in-class general and life insurance products and services to individuals, small businesses, mid-sized and large companies.

The operational group structure became effective as of July 1, 2016 and reflects both, the Group's businesses and geographical regions. The Group pursues a customer-centric strategy, with the Property & Casualty (P&C) and Life businesses which are managed through our regional structure. For details on the activities of the various businesses refer to note 13 of the unaudited consolidated financial statements.

The Group further divides its P&C and Life business into Retail and Commercial customer units.

The Group has identified the following 13 reportable and operating segments.

Group structure

Businesses	Property & Casualty (P&C)	Life	Farmers	Non-Core Businesses	Group Functions and Operations
Reportable segments	Europe, Middle East & Africa (EMEA) North America Asia Pacific Latin America Group Reinsurance	Europe, Middle East & Africa (EMEA) North America Asia Pacific Latin America Group Reinsurance	Farmers	Non-Core Businesses	Group Functions and Operations
Customer units	Commercial Retail				

Operating and financial review (continued)

Financial highlights

in USD millions, for the six months ended June 30, unless otherwise stated	2017	2016	Change[1]
Business operating profit	**2,167**	2,163	–
Net income attributable to shareholders	**1,503**	1,613	(7%)
P&C business operating profit	**1,020**	1,204	(15%)
P&C gross written premiums and policy fees	**18,005**	18,517	(3%)
P&C combined ratio	**99.5%**	98.1%	(1.4 pts)
Life business operating profit	**650**	562	16%
Life gross written premiums, policy fees and insurance deposit	**14,361**	14,842	(3%)
Life new business annual premium equivalent (APE)[2]	**2,275**	2,203	3%
Life new business margin, after tax (as % of APE)[2]	**25.3%**	23.9%	1.5 pts
Life new business value, after tax[2]	**503**	453	11%
Farmers business operating profit	**794**	766	4%
Farmers Management Services management fees and other related revenues	**1,438**	1,422	1%
Farmers Management Services managed gross earned premium margin	**7.0%**	7.0%	–
Farmers Re gross written premiums and policy fees	**772**	759	2%
Farmers Life new business annual premium equivalent (APE)[2]	**46**	46	–
Average Group investments[3]	**187,372**	188,564	(1%)
Net investment result on Group investments	**3,091**	3,651	(15%)
Net investment return on Group investments[4]	**1.6%**	1.9%	(0.3 pts)
Total return on Group investments[4]	**1.7%**	4.9%	(3.2 pts)
Shareholders' equity[5]	**30,717**	30,660	–
Z-ECM[6]	**134%**	125%	9.0 pts
Return on common shareholders' equity (ROE)[7]	**11.3%**	11.9%	(0.6 pts)
Business operating profit (after tax) return on common shareholders' equity (BOPAT ROE)[7]	**11.0%**	11.2%	(0.2 pts)

[1] Parentheses around numbers represent an adverse variance.
[2] Details of the principles for calculating new business are included in the embedded value report in the annual results 2016. New business value and new business margin are calculated after the effect of non-controlling interests, whereas APE is presented before non-controlling interests.
[3] Including investment cash.
[4] Calculated on average Group investments.
[5] As of June 30, 2017 and December 31, 2016, respectively.
[6] Ratios as of June 30, 2017 and December 31, 2016, respectively. Ratio for June 30, 2017 reflects midpoint estimate with an error margin of +/- 5 pts.
[7] Shareholders' equity used to determine ROE and BOPAT ROE is adjusted for net unrealized gains/(losses) on available-for-sale investments and cash flow hedges.

Performance overview

The Group's business operating profit of USD 2.2 billion remained flat in U.S. dollar terms, but increased by 2 percent on a local currency basis compared with the same period of 2016. Adjusted for the Ogden discount rate change in the UK[1] (Ogden), with an overall negative impact of USD 289 million, BOP would have been higher by USD 293 million compared to the same period in 2016, with strong performance in Life with increases in all segments on a local currency basis and Property and Casualty being flat, with improvements to the loss ratio. Famers benefited from higher fee income and favorable prior year development at Farmers Re. In addition, expense savings of approximately USD 550 million against the 2015 baseline have been achieved.

Net income attributable to shareholders of USD 1.5 billion decreased by USD 110 million, or by 7 percent in U.S dollar terms and by 6 percent on a local currency basis. The decrease is primarily the effect of lower net capital gains.

Shareholders' equity increased by USD 56 million to USD 30.7 billion during the first half of 2017, with net income for the period and positive currency translation adjustments almost offsetting the cost of the dividend approved in March 2017 and net actuarial losses on pensions.

Business operating profit of USD 2.2 billion remained flat in U.S. dollar terms, but increased 2 percent on a local currency basis.

- **P&C** business operating profit decreased by USD 184 million to USD 1.0 billion. Excluding the effects of Ogden, P&C is USD 25 million or 2 percent above in U.S dollar terms and 6 percent on a local currency basis, reflecting improvements in the net underwriting result and higher investment income.
- **Life** business operating profit increased by USD 88 million to USD 650 million, or 16 percent in U.S. dollar terms and 18 percent on a local currency basis. On a local currency basis all segments showed increases, with the largest improvement driven by Asia Pacific, which benefited both from organic and inorganic growth. Overall business operating profit benefited from higher loadings and fees, as well as an improved technical margin and lower operating costs, partly offset by increases in acquisition costs and policyholder taxes.
- **Farmers** business operating profit increased by USD 28 million to USD 794 million. This was primarily due to an increase of USD 25 million in Farmers Re as a result of a 4.1 percentage point improvement in the combined ratio, partially offset by lower investment income.
- **Group Functions and Operations (GF&O)** business operating loss reduced to USD 301 million and benefited from favorable foreign exchange movements and underlying expense savings, partially offset by lower central charges.
- **Non-Core Businesses** reported a business operating profit of USD 3 million compared with a profit of USD 26 million in the same period of 2016, reflecting reserve strengthening as a result of Ogden discount rate changes and other one-off impacts.

[1] The discount rate reflected in the Ogden tables defined by the Lord Chancellor of the UK Ministry of Justice is used to calculate personal injury and accident claims in the UK. On February 27, 2017 this rate was changed from 2.5 percent to minus 0.75 percent.

Operating and financial review (continued)

The Group achieved good progress on an underlying basis against its financial targets in the first six months of 2017. **BOPAT ROE** on an annualized basis stood at 11.0 percent. Excluding the effect of Ogden, annualized BOPAT ROE would have amounted to 12.5 percent, which is in line with the Group's target of 12 percent and growing over the 2017–2019 period.

The Group's capital and solvency position remained strong. Solvency measured on an economic basis as determined under the **Zurich Economic Capital Model (Z-ECM)** was 134 percent as of June 30, 2017, well above the target range of 100–120 percent, and increased by 9 percentage points from January 1, 2017.

Following **expense savings** in 2016, the Group has made further progress and has delivered additional savings in the first six months of 2017, reflecting measures the Group has taken to meet its expense target of USD 1.5 billion against the baseline of 2015. Accumulated savings total about USD 550 million as of June 30, 2017.

Cash remittances in excess of USD 9.5 billion over the cycle are on track to be achieved.

The **net investment result on Group investments**, before allocations to policyholders, of USD 3.1 billion decreased by USD 561 million, or by 15 percent in U.S. dollar terms and 14 percent on a local currency basis, resulting in a **net investment return on average Group investments** of 1.6 percent (not annualized) compared with 1.9 percent in the same period of 2016. **Net investment income**, predominantly included in the core business results, of USD 2.6 billion decreased by USD 214 million, or 8 percent in U.S. dollar terms, and 6 percent on a local currency basis as a result of the continued low-yield environment. **Net capital gains on investments and impairments** included in the net investment result decreased by USD 346 million to USD 489 million, mainly due to a negative revaluation result from derivatives compared with the prior period. **Total return on average Group investments** was 1.7 percent (not annualized), compared with 4.9 percent in the same period of 2016. Total return includes the net investment result, net capital gains and the favorable impact from net unrealized capital gains before allocations to policyholders reported in shareholders' equity, which were USD 134 million compared with USD 5.6 billion in the same period of 2016. This decline was due to rising bond yields in Europe compared to falling yields in the same period of 2016.

The **shareholders' effective tax rate** increased to 32.5 percent for the period ended June 30, 2017 compared with 29.9 percent for the same period of 2016. The effect of Ogden, changes in the geographical profit mix and several other non-recurring charges in 2017, which did not attract tax relief accounted for this change.

ROE decreased by 0.6 percentage points to 11.3 percent largely due to the reduction in net income attributable to shareholders and a higher effective tax rate. **BOPAT ROE** decreased by 0.2 percentage points to 11.0 percent despite a lower average equity primarily as a result of a higher tax rate.

Property and Casualty (P&C)

in USD millions, for the six months ended June 30	Total			Of which Commercial[1]		
	2017	2016	Change	**2017**	2016	Change
Gross written premiums and policy fees	18,005	18,517	(3%)	8,222	8,400	(2%)
Net earned premiums and policy fees	12,498	13,227	(6%)	5,414	6,059	(11%)
Insurance benefits and losses, net of reinsurance	8,389	8,900	6%	4,000	4,212	5%
Net underwriting result	62	252	(75%)	(148)	222	n.m
Net investment result	1,026	936	10%	644	560	15%
Business operating profit	**1,020**	**1,204**	**(15%)**	**506**	**843**	**(40%)**
Loss ratio	67.1%	67.3%	0.2 pts			
Expense ratio	32.4%	30.8%	(1.6 pts)			
Combined ratio	**99.5%**	**98.1%**	**(1.4 pts)**			

[1] Excluding Group Reinsurance and intersegment eliminations.

BOP by segment

in USD millions, for the six months ended June 30	Business operating profit (BOP)			Net underwriting result		
	2017	2016	Change	**2017**	2016	Change
Europe, Middle East & Africa (EMEA)	316	682	(54%)	52	355	(85%)
North America	564	465	21%	10	30	(67%)
Asia Pacific	114	131	(13%)	89	105	(14%)
Latin America	133	179	(26%)	43	31	41%
Group Reinsurance[1]	(107)	(252)	57%	(133)	(269)	50%
Total	**1,020**	**1,204**	**(15%)**	**62**	**252**	**(75%)**

[1] Including intersegment elimination.

Business operating profit decreased by USD 184 million to USD 1.0 billion as a result of the Ogden which led to a reserve strengthening in EMEA and Group Reinsurance of USD 209 million. Excluding this, Property and Casualty BOP was USD 25 million or 2 percent higher in U.S dollar terms and 6 percent on a local currency basis. Apart from the impact of Ogden, **EMEA** was further impacted by adverse losses in the UK and weather events in Switzerland and Spain, partially offset by improvements in Germany. In **North America** BOP increased to USD 564 million, primarily driven by improved hedge fund results reflected in the net investment result. In **Asia Pacific** BOP declined by USD 16 million, due to the impact of weather in Hong Kong and the disposal of the Group's operation in Taiwan in January 2017. This was partially offset by an improved loss development and growth in Japan. The acquisition of Cover-More, a provider of travel insurance and assistance solutions contributed positively to the non-technical result for the first time in the second quarter 2017. **Latin America** declined by USD 46 million as foreign exchange gains in Venezuela due to the devaluation of the bolivar, though still positive, were smaller compared to the same period of 2016. **Group Reinsurance** benefited – compared to the same period of 2016 – as negative developments in loss reserves established in prior years reduced.

BOP for **Commercial** Insurance has been impacted by reserve strengthening related to Ogden and other lines of business in EMEA, and lower prior year reserve releases for Property in North America and the UK. In addition, foreign exchange gains in Venezuela included in non-technical result were lower compared to the same period of 2016. These negative effects were partially offset by a relatively benign level of catastrophes and weather related events in EMEA and North America compared to the same period of 2016.

Gross written premiums and policy fees decreased by USD 512 million to USD 18.0 billion, or 3 percent in U.S. dollar terms or 1 percent on a local currency basis. Excluding businesses exited in South Africa, Morocco, Taiwan and the Middle East over the last twelve months, gross written premiums and policy fees decreased by USD 249 million or 1 percent in U.S. dollar terms but increased slightly on a local currency basis as a result of the continued focus on profitability and the impact of soft market conditions. Overall, rates rose by around 1 percent in the first six months of 2017.

The **net underwriting result** decreased by USD 190 million to USD 62 million, with an overall combined ratio of

Operating and financial review (continued)

99.5 percent, 1.4 percentage points higher than in the same period of 2016. Adjusted for the impact of Ogden, the net underwriting result was USD 20 million higher, resulting in an improvement of the combined ratio by 0.2 percentage points. The loss ratio improved by 1.8 percentage points, reflecting lower catastrophe and weather events, an improvement in underlying loss experience and the favorable development of loss reserves established in prior years. The expense ratio increased by 1.6 percentage points, with the commission ratio increasing across all segments reflecting changes in the business mix. The other underwriting expense ratio remained flat compared with the same period of 2016, with the effect of a lower expense base as a result of initiatives to reduce costs offset by lower premium volumes.

On a segmental basis, the net underwriting result in **EMEA** decreased by USD 303 million, and adjusted for Ogden by USD 87 million. This development was attributable to the negative impact of weather and large loss events in Switzerland as well as higher commissions including an accounting adjustment in the UK. **North America** decreased by USD 20 million with improvements in the current accident year loss experience, despite several large hailstorms in Texas and Colorado, offset by a lower favorable development in loss reserves established in prior years and higher commissions due to changes in business mix and growth in financial lines & surety. **Asia Pacific** was USD 15 million lower than in the same period of 2016 due to adverse experience in Hong Kong and Malaysia for attritional and large losses partially offset by positive development in loss reserves established in prior years in Australia. The underwriting result in **Latin America** improved by USD 12 million, reflecting a significantly improved underlying current accident year loss ratio and a benefit from a one-time settlement of premium taxes in Brazil.

Life

in USD millions, for the six months ended June 30	**2017**	2016	Change
Insurance deposits	7,313	7,664	(5%)
Gross written premiums and policy fees	7,048	7,177	(2%)
Net investment income on Group investments	1,449	1,554	(7%)
Insurance benefits and losses, net of reinsurance	(4,932)	(5,480)	10%
Business operating profit	**650**	**562**	**16%**
Net policyholder flows[1]	2,715	4,249	(36%)
Assets under management[2, 3]	272,328	248,899	9%
Total reserves for life insurance contracts, net of reinsurance, and liabilities for investment contracts (net reserves)[3]	220,553	203,037	9%

[1] Net policyholder flows are defined as the sum of gross written premiums and policy fees and deposits, less policyholder benefits.
[2] Assets under management comprise on balance sheet Group investments and unit-linked investments plus assets that are managed by third parties, on which fees are earned.
[3] As of June 30, 2017 and December 31, 2016, respectively.

BOP by segment

in USD millions, for the six months ended June 30	**2017**	2016	Change
Europe, Middle East & Africa (EMEA)	438	448	(2%)
North America	(16)	(19)	14%
Asia Pacific	78	12	nm
Latin America	149	121	23%
Group Reinsurance[1]	1	–	n/a
Total	**650**	**562**	**16%**

[1] Including intersegment elimination.

Business operating profit increased by USD 88 million to USD 650 million, or 16 percent in U.S. dollar terms and 18 percent on a local currency basis, with increases in all segments on a local currency basis. The majority of the improvement occurred in **Asia Pacific**, which benefited both from organic and inorganic growth, as well as the effect of positive market movements. In addition, business operating profit in the same period of 2016 included the effects of expenses related to the acquisition of the retail life insurance protection business of Macquarie Group in Australia. In **EMEA**, the improvement on a local currency basis arose due to lower overall costs, though was offset by a deterioration in the investment margin and lower fee revenue in Germany. In **Latin America**, higher overall volumes and the positive effect of a one-time settlement of premium taxes in Brazil were the main contributors on a local currency basis. In **North America** improved claims experience and investment margin were the main drivers behind the increase.

Gross written premiums, policy fees and insurance deposits decreased by USD 481 million to USD 14.4 billion, or by 3 percent in U.S. dollar terms, but remained flat on a local currency basis. On a local currency basis, improvements occurred in Latin America, from higher sales of individual protection products in Zurich Santander and a large corporate contract in the Zurich-branded business in Chile, coupled with growth in Asia Pacific. These positive effects were offset in EMEA, following a reduction in sales of individual savings products in Germany and Spain.

Net policyholder flows were positive at USD 2.7 billion, though USD 1.5 billion lower compared with the same period of 2016. The majority of the reduction occurred in the retail business in EMEA driven by lower sales of individual savings products in Spain. **Assets under management** increased by 9 percent in U.S. dollar terms and 3 percent on a local currency basis compared with December 31, 2016. The local currency increase was driven by favorable market movements and positive net policyholder flows. In U.S. dollar terms, a further improvement was driven by the impact of the weaker U.S. dollar against the euro and the British pound, compared to December 31, 2016, on investments denominated in euro and British pounds.

Operating and financial review (continued)

Source of earnings[1]

in USD millions, for the six months ended June 30	2017	2016	Change
Loadings and fees	1,654	1,669	(1%)
Investment margin	252	258	(2%)
Technical margin	492	397	24%
Operating and funding costs	(655)	(660)	1%
Acquisition costs	(1,187)	(1,191)	–
Impact of deferrals	94	89	6%
Business operating profit	**650**	**562**	**16%**

[1] Each line represents the Group's interest after deducting non-controlling interests, amounting in total to USD 145 million in 2017 and USD 122 million in 2016 in business operating profit.

Viewed by profit sources and on a local currency basis, business operating profit benefited from higher loadings and fees, as well as an improved technical margin. In addition, an improvement in operating costs was more than offset by increases in acquisition costs and policyholder taxes.

Loadings and fees deteriorated by 1 percent in U.S dollar terms, but improved 2 percent on a local currency basis. In local currency, growth in Asia Pacific was the main driver of the increase, which benefited from the recent acquisitions of MAA Takaful Berhad insurance company in Malaysia and the retail life insurance protection business of Macquarie Group in Australia. Higher volumes in Latin America and the positive effect of market movements on fund values in EMEA further contributed to the increase. These were partially offset by a reduction of fee revenue in Germany due to decreasing volumes of single premium business. **Investment margin** deteriorated by 2 percent both in U.S. dollar terms and on a local currency basis. Improvements from positive market movements in Asia Pacific and higher spreads in North America, were more than offset by a deterioration in Germany. **Technical margin** improved by 24 percent in U.S dollar terms and 25 percent on a local currency basis, predominantly driven by the growing life insurance protection books of business in Asia Pacific, predominantly Australia and Japan, and improved claims experience in North America and Latin America.

Operating and funding costs improved by 1 percent in U.S dollar terms, but deteriorated by 3 percent on a local currency basis. In local currency, the positive impact of expense reductions across EMEA was offset by investments in Asia Pacific, largely resulting from growth initiatives and the cost of integrating the recently acquired businesses. **Acquisition costs** remained flat in U.S dollar terms, but deteriorated by 2 percent on a local currency basis. The increase on a local currency basis reflected higher volumes of business in Asia Pacific and in Latin America, with a partial offset in EMEA primarily due to a reduction in volumes of single premium business in Germany. The positive contribution from the **impact of deferrals** increased by 6 percent both in U.S. dollar terms and on a local currency basis, driven by the effect of positive market movements, deferrals of higher acquisition costs where business has been growing and lower deferrals of fees in Germany, resulting from the decrease in single premium business.

NBV, APE and NBM by segment

in USD millions, for the six months ended June 30

	New business value, after tax (NBV)[1]		New business annual premium equivalent (APE)[2]		New business margin, after tax (as % of APE) (NBM)[3]	
	2017	2016	2017	2016	2017	2016
Europe, Middle East & Africa (EMEA)	328	335	1,596	1,621	21.6%	22.3%
North America	17	15	25	36	67.5%	42.8%
Asia Pacific	78	47	87	73	90.9%	65.2%
Latin America	80	56	566	473	22.4%	19.4%
Total	**503**	**453**	**2,275**	**2,203**	**25.3%**	**23.9%**

NBV, APE and NBM by Line of Business

in USD millions, for the six months ended June 30

	New business value, after tax (NBV)[1]		New business annual premium equivalent (APE)[2]		New business margin, after tax (as % of APE) (NBM)[3]	
	2017	2016	2017	2016	2017	2016
Protection	389	342	787	689	63.5%	64.2%
Corporate Pensions	49	88	632	618	7.8%	14.3%
Unit Linked	78	39	607	484	14.2%	8.9%
Annuities and Savings	(14)	(16)	250	411	(7.1%)	(5.2%)
Total	**503**	**453**	**2,275**	**2,203**	**25.3%**	**23.9%**

[1] New business value is calculated on embedded value principles net of non-controlling interests.
[2] APE is shown gross of non-controlling interests.
[3] New business margin is calculated using new business value as a percentage of APE based on figures net of non-controlling interests for both metrics.

APE improved USD 73 million to USD 2.3 billion, or 3 percent in U.S. dollar terms, and 7 percent on a local currency basis. On a local currency basis the largest improvement occurred in EMEA, driven by higher corporate sales across most countries, and higher retail sales of unit-linked products in the UK, Ireland and Italy, more than offsetting reductions in sales of individual savings products in Spain and Italy. Latin America also improved, largely driven by higher sales of corporate protection business in the Zurich-branded business in Chile. In Asia Pacific the increase reflects the impact of MAA Takaful Berhad in Malaysia, which was acquired in 2016. These positive impacts were partly offset by lower new business sales in North America.

New business value increased by USD 50 million to USD 503 million, or 11 percent in U.S. dollar terms, and 14 percent on a local currency basis. On a local currency basis, the largest improvement occurred in Asia Pacific, mostly benefiting from positive changes to operating assumptions in Japan. In addition, EMEA benefited from the effect of higher volumes of new business. Favorable product mix drove increases in Latin America and North America, the latter offset by reductions in sales.

New business margin improved by 1.5 percentage points to 25 percent, with improvements in all segments except EMEA. The most notable improvements occurred in Asia Pacific following the positive effect of assumptions changes in Japan. In Latin America reducing interest rates in Brazil resulted in an improved margin on individual protection business. In EMEA, improvements in Italy and Spain, resulting from a shift in sales from individual savings to unit-linked business, were more than offset by the effects of an overall increase in sales of lower margin corporate business.

Operating and financial review (continued)

Farmers

in USD millions, for the six months ended June 30	2017	2016	Change
Farmers Management Services (FMS)	700	697	–
Farmers Re	6	(19)	nm
Farmers Life[1]	87	88	(1%)
Total business operating profit	**794**	**766**	**4%**

[1] Reflects management view and contains the ongoing business and certain closed books of Farmers New World Life Insurance Company (FNWL)

Farmers business operating profit increased by USD 28 million to USD 794 million, or by 4 percent. **Farmers Management Services** business operating profit increased by USD 3 million to USD 700 million, driven by growth in gross earned premiums of the **Farmers Exchanges**[1] partially offset by higher expenses. **Farmers Life** business operating profit remained in line with the same period of 2016. **Farmers Re** business operating profit increased by USD 25 million to USD 6 million due to a 4.1 percentage point improvement in the combined ratio, partially offset by lower investment income.

Farmers Management Services

in USD millions, for the six months ended June 30	2017	2016	Change
Management fees and other related revenues	1,438	1,422	1%
Management and other related expenses	(750)	(746)	(1%)
Gross management result	688	675	2%
Managed gross earned premium margin	7.0%	7.0%	–

Management fees and other related revenues of USD 1.4 billion increased USD 16 million, or 1 percent, due to growth in gross earned premiums of the Farmers Exchanges across most lines of business. **Management and other related expenses** increased slightly to USD 750 million.

The **managed gross earned premium margin** remained unchanged at 7.0 percent.

Farmers Re

in USD millions, for the six months ended June 30	2017	2016	Change
Gross written premiums and policy fees	772	759	2%
Net underwriting result	(23)	(54)	56%
Loss ratio	71.0%	75.1%	4.1 pts
Expense ratio	32.0%	32.0%	–
Combined ratio	**103.0%**	**107.1%**	**4.1 pts**

Gross written premiums and policy fees increased by USD 14 million to USD 772 million, or by 2 percent, as a result of an increase in gross written premiums at the Farmers Exchanges. Participation in the All Lines quota share reinsurance agreement remained unchanged at 8 percent.

The **net underwriting result** improved by USD 30 million to a loss of USD 23 million driven by a 4.1 percentage point improvement in the combined ratio. The **loss ratio** decreased 4.1 percentage points as a result of favorable development of loss reserves established in prior years, improved underlying loss ratio and slightly lower catastrophe events. The **expense ratio** remained flat at 32 percent.

[1] The Farmers Exchanges are owned by their policyholders. Farmers Group Inc., a wholly owned subsidiary of the Group, provides certain non-claims administrative and management services to the Farmers Exchanges as attorney-in-fact and receives fees for its services.

Farmers Life

in USD millions, for the six months ended June 30	2017	2016	Change
Insurance deposits	80	83	(4%)
Gross written premiums and policy fees	438	439	–
New business annual premium equivalent (APE)	46	46	–
New busines value (NBV)	49	42	16%
Assets under management[1, 2]	5,335	6,823	(22%)
Total reserves for life insurance contracts, net of reinsurance, and liabilities for investment contracts (net reserves)[2]	4,537	6,080	(25%)

[1] Assets under management comprise on balance sheet Group investments and unit-linked investments plus assets that are managed by third parties, on which fees are earned.
[2] As of June 30, 2017 and December 31, 2016, respectively.

Insurance deposits decreased by USD 3 million to USD 80 million. **Gross written premiums and policy fees** decreased by USD 1 million to USD 438 million.

APE remained unchanged despite lower cross-sell opportunities. **NBV** increased mainly due to improved persistency, expense assumptions and sales mix, partially offset by the negative effect of higher interest rates on certain individual protection business.

Assets under management decreased by USD 1.5 billion to USD 5.3 billion and **total reserves** decreased by USD 1.5 billion to USD 4.5 billion. Reductions in both items were driven by an agreement signed in the second quarter of 2017 with Reinsurance Group of America to reinsure a portion of Farmers Life's closed U.S. annuity book.

Farmers Exchanges

Financial information about the Farmers Exchanges, which are owned by their policyholders, is proprietary to the Farmers Exchanges, but is provided to support an understanding of the performance of Farmers Group, Inc. and Farmers Re.

The Farmers Exchanges are owned by their policyholders. Farmers Group, Inc., a wholly owned subsidiary of the Group, provides certain non-claims administrative and management services to the Farmers Exchanges as attorney-in-fact and receives fees for its services.

in USD millions, for the six months ended June 30	2017	2016	Change
Gross written premiums	10,047	9,883	2%
Gross earned premiums	9,846	9,652	2%

Gross written premiums in the Farmers Exchanges increased by USD 164 million to USD 10.0 billion, or by 2 percent. Growth in most lines of business from continuing operations was primarily driven by rate increases in Auto and was partially offset by decreases in the discontinued 21st Century operations.

Gross earned premiums in the Farmers Exchanges increased by USD 194 million to USD 9.8 billion, or by 2 percent.

Operating and financial review (continued)

Group Functions and Operations

in USD millions, for the six months ended June 30	**2017**	2016	Change
Holding and Financing	(217)	(293)	26%
Headquarters	(84)	(103)	18%
Total business operating profit	**(301)**	**(395)**	**24%**

Holding and Financing business operating loss of USD 217 million is an improvement of USD 76 million or 26 percent in U.S. dollar terms and 23 percent on a local currency basis. This was primarily driven by favorable foreign exchange impacts and savings in administration costs, which were partly offset by an increase in external debt expenses.

Headquarters recorded a business operating loss of USD 84 million, USD 19 million lower compared to the same period of 2016, or 18 percent both in U.S. dollar terms and in local currency, as a result of net underlying expense savings.

Non-Core Businesses

in USD millions, for the six months ended June 30	**2017**	2016	Change
Zurich Legacy Solutions	(44)	2	nm
Other run-off	47	25	91%
Total business operating profit	**3**	**26**	**(89%) %**

Zurich Legacy Solutions, which predominantly comprises P&C run-off portfolios, reported a business operating loss of USD 44 million. A reserve strengthening of USD 80 million in a UK legacy book as a result of Ogden was partially offset by releases in other run-off portfolios.

Other run-off, which largely comprises U.S. life insurance and annuity portfolios, reported a USD 23 million increase in business operating profit. This arose primarily from the release of long-term reserves as a consequence of in-force management activities in a closed Life book, and market value volatility.

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