# Q1 2016 Earnings Call

## Company Participants

- Roland Vogel
- Ulrich Wallin

## Other Participants

- Frank Kopfinger
- In-Yong Hwang
- Kamran Hossain
- Michael Haid
- Vinit Malhotra
- William Hawkins
- Xinmei Wang

## MANAGEMENT DISCUSSION SECTION

### Operator

Good morning, ladies and gentlemen, and welcome to today's Hannover Re International Conference Call on Interim Results Q1 2016. For your information, this conference is being recorded. At this time, I would like to hand the call over to your host today, Mr. Ulrich Wallin, Chief Executive Officer. Please go ahead, sir.

### Ulrich Wallin {BIO 4863401 <GO>}

Thank you. Good morning, ladies and gentlemen. I'd like to welcome you to our conference call presenting our result for the first quarter of 2016. As always, I'm joined by our CFO, Roland Vogel. Given that we also today have our AGM, we have this call rather early in the morning and we do hope that this would not cause any inconvenience to you.

Coming to slide number one, I'm pleased to report that we had a very good start to 2016 financial year. Group net income increased by 12.7% to €271.2 million. If you eliminate from last year's results the special effect from the termination fee of the financial solutions treaty, top line development is in line with expectation and gross premiums declined by 3.1%, forex adjusted by 2.1%. However, the net premium earned, in fact, increased by 3.2% due to a higher retentions on our life and health business and positive change in the unearned premiums for our P&C business.

The pleasing business development in the first quarter is driven by strong underwriting profit in property/casualty reinsurance as well as good and solid results of our life and health reinsurance business and on the investments side. This is a specialty gratifying against a well-known difficult business environment. This is a soft market, in particular, on the P&C side and the challenging investment environment with ever lower interest rates. At 13.2%, we were again able to achieve an attractive return on equity (02:38) by further strategic target and this was achieved despite a further increase of the IFRS capital base by about 4%.

The book value per share at the end of the first quarter stood at €69.42, and it's, as I said, increased compared to year-end of last year. Following four consecutive years of low major natural catastrophe losses and very good results, the property/casualty reinsurance business continues to be fiercely competitive. As a result, we continue to write our business highly selective in accordance with our profit-orientated underwriting policy, which is also reflected in slightly reduced premium volume.

I should remind you, however, that last year, we had a special effect on our facultative business where we accelerated the premium booking to the amount of around €100 million which, of course, is not recurring this year. The overall profitability of the business, so far 2016, is still good and certainly above our margin requirements. In the first quarter, we continue to see good business opportunities in particular in the U.S. but also in parts of Asia.

On the other hand, we also saw some decline in the premium income. This particularly refers to Chinese motor quota share business, which are bought for solvency relief reasons and for the new solvency regime, C-ROSS, does not really help those treaties because it reduced the capital necessary for motor business in China.

With the combined ratio of 94.7%, we achieved an increased underwriting result as compared to last year. This also then resulted in healthy growth of our EBIT to €300 million which, in fact, is a growth of 17%. You should, however, remember that the first quarter of 2015, the property/casualty result was a little bit below average. On the other hand, the life and health result in the first quarter of 2015 was extraordinary good.

We feel that the result is strong and this is particularly due to the fact that we didn't change our loss reserving policy, particularly regarding the large losses. And we did not do any active reserve releases. So, on the reserve development side, all you saw is the normally expected positive development.

In life and health reinsurance, we recorded a solid first quarter result. Gross written premium increased slightly by 0.3% on a forex adjusted basis. This is on the back of attractive opportunities, particularly, in Asia and also in our longevity business. At the same time, also here we have some lost transactions, which did not renew and in particular, refers to enhanced annuity business in the UK, some Australian group business and also some business that we have written in our Shanghai branch, which was single premium business and therefore the business is on the books. But of course the single premiums were booked last year.

Nevertheless, the favorable underwriting results resulted in an operating results of €106 million, which is a little bit higher than the average run rate of our quarterly EBIT. And we believe that signals that the underlying profitability of our life and health business continues to develop favorably. The drop compared to last year is, of course, due to the fact that we have the positive one-off effect last year, which I already mentioned.

Also our investment income developed entirely in line with expectations. ROI stood at 2.9%, in line with our target. And on that positive note, I would hand to Roland who is actually looking after our investments.

## Roland Vogel {BIO 16342285 <GO>}

Yes. Thank you, Ulrich. Good morning to all of you. As usual, I will try to keep my comments as brief as possible, which, on the one hand should be rather easy this time as the Q1 2016 results are fairly straight forward and do not include any material one-off effects. On the other hand, we this time have included some information about our solvency ratio at year-end which we have added to my part of the presentation.

As already mentioned, the slight decrease on the top line is within the range we are expecting for the full year. Net premium increased favorably. Ulrich mentioned that this is mostly due to the change in unwritten premium and not an increase in retention. Also, I would like to remind you that the very positive premium development in 2015 was significantly ahead of our expectations and therefore, the basis for growth for this year is actually very high.

Investment income is in line with expectation excluding the €39 million positive one-off in life and health reinsurance in 2015. It is almost stable compared to the previous year, which I feel – can be seen as a success of the current year's environment. Other income expenses decreased mainly due to less positive currency effects in life and health, and just for the sake of completeness, the tax rate is back down on an expected level.

If we look at the capital side on the next slide, the level of hybrid is unchanged compared to the yearend. This is a level we feel comfortable with also as it gives us significant flexibility to issue more. We will come back to such potentials when discussing the composition of our economic capital later on.

Shareholders' equity increased by almost 4%. On the right hand side of this slide, you can see that the change is driven by asset valuations and the currency translation largely offset each other, therefore the increase is mainly driven by our positive earnings.

The cash flow, on the next slide, continues to be very positive mainly driven by good results on the underwriting as well as on the investment side. You might remember that we had shown an adjusted number for the cash flow in Q4 2015 when we received money from the Chinese financial solutions deal which was due to be forwarded only in Q1 2016. As expected, we have now paid out roughly €300 million to (11:43), depressing the reported number for operating cash flow in 2016. Adjusting for that, we had a favorable cash flow of €584 million. The remaining €200 million difference between the two effects will be paid out over the remainder of the year.

Assets under own management were rather stable at a level close to €40 billion. The negative impact from FX effects was around €900 million, offsetting rising valuation reserves of around €400 million plus the positive cash flow. In addition, the cash outflow that I just mentioned for the financial solutions treaty, of course, led to a reduction in cash and short-term assets.

P&C gross premium decreased by 3.7% on an FX-adjusted basis. This is the result of our strict margin-oriented underwriting approach and is fully aligned with our expectations following the extraordinary growth I already mentioned we had in 2015. Additionally, the previous year's premium was influenced by a non-recurring effect associated with the accounting of our facultative business where we booked almost €100 million in additional premium last year.

Moreover, we did not renew some Chinese motor quota shares as well as a specialty business from specialty lines, namely, aviation, where rates did not justify to continue. Nevertheless, net earned premium increased by 5.2% adjusted for currency effects. As mentioned, this is not the result of the higher retention, which actually decreased from 89% to 88%, but it's due to the change in unearned premium. This development is driven by the strong growth in 2015 which, as you will remember, was supported also by the strong U.S. dollar.

At 2.8% of net premiums, major losses were again well below the budget in the first quarter. The underwriting result is again on a very good level with a combined ratio of 94.7%, which as you might know is well below the target of 96%.

As in the previous years, we stuck to our practice and did not release the unused loss budget but kept it as IBNR for the remainder of the year. The run-off results in the first three months was unremarkable. And as in the first quarter of last year, we did not benefit from any extraordinary positive developments. The confidence level of the loss reserves should at least remain stable.

Ordinary investment income was in line with expectations. Realized gains were also within the normal range. These were mainly the result of structural changes within our private equity portfolio in the first quarter, which means that as in the past, we did not actively harvest unrealized gains from our fixed income portfolio.

Other income expenses improvement by €9 million mainly driven by currency effects. Altogether, net income for P&C business stands at €204 million, up by almost 20% compared to an already good first quarter in the previous year.

On the next slide, you can see that most lines of business showed good underwriting profitability. The main profit contributors in the first quarter were the target markets, as well as our worldwide treaty book and not surprisingly, our global cat business was an outstanding combined ratio.

Also, marine is significantly below the maximum tolerable combined ratio with – also benign loss experience shows good profitability. The good combined ratio of our aviation business was affected by a plane crash in Russia, which was around €10 million for our account. Additionally, we have been notified that the Chennai floods in India in the fourth quarter of 2015 resulted in a damage to a number of helicopters and aircrafts, which combined with a remarkable decrease in premiums, results in this unusual high combined ratio for the first quarter.

Our facultative business was particularly impacted by a few single large losses and that already leads us immediately to the large loss slide here on the next page. We can go through that next slide rather quickly because, as already mentioned, major losses were well below average on budget. Overall, the bulk of the €134 million in unused budget is to be carried forward for the remainder of the year. Still, we should bear in mind that the year has only just begun and we have already had two earthquakes; one in Japan and one in Ecuador in the second quarter. And those may show up on the large loss lists for the first half year then. And we will have to wait and see what the impact from the fires in Alberta will be. Still, these losses should be comfortably covered by the unused part of our Q1 large loss budget in addition to the budget for the second quarter.

Next slide, four losses made it onto the large loss list, all between €10 million and €20 million. Net cat losses, significantly below the expected level. Man-made losses, more or less in line with expectations.

With currency adjusted growth of 0.3%, the premium development is in line with our expectations for the full year in life and health. Adjusted for the already mentioned one-off effect and the extra ordinary positive currency gains within the other income, the result of our L&H business group is at the same good level as last year. Additionally driven by a favorable underwriting result, the overall strong EBIT of €106 million is a little bit above the normal quarterly run rate. What we have seen in the recent past that earnings here can be volatile from quarter to quarter and therefore, our expectations for the full year today remain unchanged.

Other income is back to normal or to more or less a normal level, which represents a swing of minus €24 million compared to the previous year's, almost entirely driven by lower currency gains. The overall result is also reflected in the EBIT margin for our four categories with financial solutions and longevity outperforming their respective targets. Mortality and morbidity came in only slightly below the 6% target which is nevertheless a significant improvement as compared to 2015.

Net investment income was in line with our expectations and just for the sake of completeness, the effect from our ModCo derivatives was minus €1.4 million in the first quarter.

So now looking at the investment, the development is satisfactory despite considerable volatility seen on the capital markets in the first three months, investment income is in line with expectations. The decrease in ordinary investment income is largely due to the last year's one-off effect from the termination fee in life and health. Low interest rates had the expected impact on the return from our fixed income book as we did not change our overall risk position here.

Realizations, at the same level as last year, with the majority driven by a structural changes within our private equity portfolio. Despite the high volatility in the first quarter, impairments are again on a very low level, mainly consisting of regular depreciation on real estate. Overall, the return on investment was 2.9%, which is exactly the figure we are targeting for the full year and as a result of decreasing yields, valuation reserves increased from year-end to reach €2 billion at the end of the first quarter. Credit spreads remained rather stable, at least when you compare the two balance sheet dates, as we all know, we have seen significant volatility in between.

The next slide shows an overview of how our different asset classes contributed to the ordinary investment income. The slide on the right hand side demonstrate that we've kept our asset allocation more or less stable. In the first quarter listed equities are now at 2% as we acted on the volatility in the first quarter to buy another tranche of around €400 million continuing the moderate reentry into this asset class.

At 42%, corporates have the highest share in our investment income. The contribution from government bonds is not surprisingly a lot lower than their share in our portfolio. On the other hand, 12% income from - 4% real estate investment is a remarkable performance even adjusted for real estate specific costs, which are excluded here. The contribution from private equity is a little bit below our expected run rate, also because the development is somewhat seasonal depending on the distributions from our funds.

So now, as usually or usually Uli is the one to comment on the target metrics, but this time the honor falls to me as I will also be presenting a few slides on our capitalization according to Solvency II afterwards. So excluding the one-off effect in the first quarter 2015, earnings per share increased by 12.7%, meaning that we were successful in achieving all Group targets in the first quarter of 2016. I'm not at all concerned about the premium development of our two business groups as these targets are to be achieved over the cycle and for furthermore a year with less growth is absolutely in line with our strategic target, especially in light of the strong growth of the previous year. Profitability is favorable in those business groups.

So before going into more detail on our capitalization, I would like to make a few general remarks on our Solvency II reporting. The figures we provide on the following slides are for the Hannover Re Group. As a former subgroup of Talanx, the Hannover Re Group legally is not subject to group regulation. Still, we did apply form and we received approval for a full internal group model in addition to the Hannover Re SE model. This group model will also be audited in line with the legally required audit for the Hannover Re SE. We do that to give all stakeholders and clients the information they need and they are used too in our industry.

To a large extent, the risk profile and the capital position for the Hannover Re SE can be seen as an equivalent to the Hannover Re Group. From an economic point of view, it is equivalent to the group excluding minority interest.

The Solvency II ratio, as the of 2015, for the Hannover Re SE stood at 231% compared to the 221% for the group. And this is unchanged from the figure we reported for the end of the third quarter 2015.

So on this slide, you can see the different metrics we use to calculate the capital adequacy of the group. Firstly, we – or first, we distinguish between the internal view based on our full internal model, which is a framework for our actual risk management within the group.

We also show such numbers on the basis of the Solvency II confidence level of 99.5%. And the number below, they're having (26:11) solvency do consider two former Solvency II requirements, and insofar, lead to the approved capital solvency ratio of 221%. On the following slide, I will explain where the differences come from.

Here, beginning with our internal model at 99.97% Value at Risk, we start with a translation to the 99.5% quantile as required by Solvency II, leading to a reduction in the capital requirement of €4.6 billion. We have already discussed the next two steps last year. Firstly, the haircut for minorities reduces the available capital due to the limited transferability of the minority's interest under Solvency II rules. Secondly, the required capital increases due to the calculation of the capital requirements for the operational risk according to the standard formula as against our own internal approach to measure operational risk.

As you can see, each of the two effects accounts for roughly half of the difference between the capital adequacy ratio derived from our full internal model relative to the regulatory view.

The next slide should not be new to you, since we have merely adjusted it to the Solvency II regulatory view as of December 2015. As one of the large global reinsurers, we do benefit from a significant diversification between the different risk categories. The market risk and the underwriting risk continue to be the main risk factors for Hannover Re.

On the next slide, we show the bridge from the IFRS shareholders' equity to the basic own funds. The adjustments for assets under own management largely reflect the other comprehensive income, the OCI. The adjustment for technical provision give rise to the biggest difference between the accounting and the economic view. They mainly consist of the effect from the discounting of technical provisions for P&C and reserve redundancies, as well as the value in-force from our Life & Health business minus the risk margin.

We then have to consider deferred tax on these items. And in the next step, also deduct foreseeable dividends, not only those paid to Hannover Re shareholders, but also, to the minority shareholders of E+S Rück. Finally, we already discussed haircut on minorities has to be deducted and all-in-all resulting in the unrestricted Tier 1 capital.

On top of this, we add our subordinated debt, the two-dated hybrids are classified as Tier 2, the perpetual reissued in 2014 as restricted Tier 1 capital. As you can see and I've pointed out this earlier, we have substantial headroom for further Tier 2 issuances under Solvency II, leaving us with a high degree of flexibility to improve our overall capital position or to act on upcoming business opportunities in the future. Overall, the composition of our own funds as defined by Solvency II is of a very high quality with 87% being unrestricted Tier 1.

As you know, we have stopped the full reporting on MCEV this year, because of the reporting – because the reporting will be full substituted by the Solvency II for the three reporting going forward. Therefore, we have also no longer applied the 4.5% cost of capital as suggested by the CFO. But we have instead changed it to the 6% cost of capital as required by the Solvency II calculations.

On this slide, you can see the development of the MCEV based on those metrics, also with a view to providing a transition from one reporting basis to the other. Based on the 4.5% cost of capital we have applied in the past, the MCEV is up by 3%, mainly driven again by the very favorable development of the new business value in 2015 and reflecting a further increase in the off balance sheet value that we carried.

Next slide. If we now go one step further in the reconciliation from MCEV methodology to Solvency II, you can see that there is actually only rather small differences in the result from the valuation of our life and health technical provision. This is also one reason why we have discontinued with the MCV reporting and switch directly to Solvency II. The main difference between two methodologies is based on minor differences in the capital allocation and a few assumptions regarding the diversification.

Other differences are (32:00). And this should be – so our entry I'm sure there are also into the Solvency II reporting. This concludes my remarks, and I'll leave the outlook to you, Ulrich.

## **Ulrich Wallin** {BIO 4863401 <GO>}

Thank you, Roland. This slide really shows you the renewal at first week of April, with which we are quite satisfied and if renewals for our traditional (32:33) reinsurance business from Japan and also to some extent from Australia, New Zealand, Korea, and North America.

Despite the prevailing competitive market conditions, we managed to increase our volume by 9%. And if you look at the sources of their increase, you can see that the price and volume changes were rather minimal, which also shows you that the rating level maintained quite well with the exception of some of the natural catastrophe business where the rate reductions were in line with what we have seen at 1/1, but largely less pronounced than a year ago. The growth came especially from the Asia-Pacific region. And here, in particular, also, from Japan that we managed to grow our non-cap (33:50) business. Also, in North America, based on our very broad portfolio with more than 600 insurance companies we are doing business with, we were able to increase our business from existing clients.

I would say that when you look into the new and cancelled and restructured business, new business of €77 million, you can see that we have not written any very large new treaty (34:33), but the growth is mainly the result of a number of new treaties from various regions. We have, in particular, been – continue to be very cautious when it comes to proportional treaties on U.S. excess and umbrella business, mainly because of our experience from the last soft market where these treaties, which are very long tail in nature, eventually resulted in some undesirable results.

We also had some growth on our credit and surety business, which again is with existing large clients where there were some additional proportional reinsurance being purchased. And with our market position, we were able to grow our shares there.

Also, our natural catastrophe business, we wrote some new business, which is a diversifying business. And that actually resulted in – also an increase in our cat business, but only very small increase.

I should probably mention, again, that we haven't changed our overall risk appetite for cat, where our market share continues to be below our market share on the non-cat business. We have continued to see significant pressure on aviation and also the marine business. We managed to defend our good position on the marine excess of loss business, where we could keep the volume at acceptable rate. This is not true on aviation where we further reduced our volumes.

Lastly, also from proportional business, where the underlying rates at our view (36:45) rather low, and you have a better chance to lose money with those rates than make money. And at the same time, our clients wanted to increase the commissions, we actually reduced our involvement.

So if you look at the renewals so far here, we had 1.5% reduction in the first quarter and a 9% increase in the smaller AAA for renewals. Overall, that means that our premium volume on a currency-adjusted basis on the renewed season so far, on the traditional property and casualty treaty business has been flat. And this is much in line with our guidance for the entire year.

I said I would come to the guidance. As you can see, the guidance is unchanged. You may remember that when we reported on the full year results 2015, we changed the group net income target from – in the region of €950 million to at least €950 million. And I think the result of the first quarter fully supports this change.

As far as the dividend payout ratio goes, you can see here our strategic payout of 35% to 40%, which allows us to self-finance our growth ambitions. However, with the current situation being much like it were the last two years, if we are not seeing any new business opportunities of a large scale, if we are not seeing the large losses being well above our large loss budget, and if the capital markets behave, we would most likely again consider an extraordinary dividend for 2016, even though I have to say it's early days, and a lot can happen between now and year-end.

If you look at our non-life business, you can see that we continue to seek good opportunities in North America. We already have seen that so far this year. And we also believe that we will earn the cost of capital.

In Continental Europe, first quarter was pretty good. We saw increased volume at good profitability. Overall for the year, we continue to believe a slight decrease in volume for this business, particular outside (40:09) Germany is fairly competitive. But we still, with our selective underwriting approach, would expect that we earn the cost of capital.

On the specialty line, overall declining premiums, because specialty lines are particularly competitive on the marine side. We believe that we have rather high-quality (40:44) portfolio. Therefore, we believe that the profitability will be well above the cost of capital. However, this profitability we will only achieve if we forego some of the premium volume.

Aviation, is a class I originally started my career. And it's fair to see that it's in a rather dismal situation at this point in time. I won't spend much time on it. Credit and surety, we now believe that maybe we even can see a slight increase in the volume and continued profitability. And the same is true for the UK and Ireland where we particularly see some growth in our rather modest primary insurance business. And on the facultative side, of course, the one-off effect that we mentioned will not be there again this year. Therefore, we see some reduced growth. But for the full year, we still believe that profitability will be good.

On the global reinsurance overall, situation is reasonably favorable, particularly on the worldwide treaty, where we see good development, particularly in Asia and Latin America. There's good profitability. You can see here that on the property tax we say that we're not earning the cost of capital fully. That's, of course, only the case if we have major losses to the tune of the expected losses.

Of course, if we have situation like in the first quarter and the previous years, even at the very slim rate that we are currently getting, we will see good profitability. However, at the expense of significant volatility and therefore we curtail our exposure to property catastrophe, structured reinsurance and ILS, that is where we have the Chinese (42:55) shares and therefore we expect reduced premium volumes there, but earnings and cost of capital.

If I come to the life and health side, we continue to see good business opportunities on our financial solution segment. And also, expect the profitability here to be very attractive. Also, on the longevity business, we see further growth opportunities, despite the fact that this business, particular on the pension blocks has become increasingly competitive.

In the area of mortality and morbidity, we expect some reduced volume due to large transactions not to be renewed. However, I would say that this will mainly affect the growth premium and to a much lesser extent the net premium, because we have relatively high retrocession on these large transactions, which are subject to non-renewal.

When we look at the overall business, we believe that we will continue to see increased underlying profitability, of course, in particular, on the, our U.S. mortality business due to our measures to reduce collateral costs and even due to some successful initiatives to increase rate on some underperforming YRT business.

I will then come to our rationale for the profit guidance for 2016 and beyond. We continue, as we explained to believe that the underlying profitability of our Life & Health business is increasing, of course, in 2015 due to the termination fee, with a little bit of spikes here. But if you exclude that, the underlying increase in profitability should prevail.

On our P&C business, we entered 2016 on a very strong position with even increased confidence levels of our loss reserves, which gives us very good and comfortable buffers, so that we are quite confident that we will be able to keep the combined ratios below 96%, maybe even quite a bit below 96% as long as the large losses stays in the large loss budget. Also, on our retrocession side, we bought little bit more retrocession, but conditions also have improved for us.

On the investment income, in absolute terms, again, outside one-off effects, we expect rather stable development. I would say if you look at the last – at the five-year average from the last year, in absolute terms, we should be able to continue at those levels. And this is despite the continued low interest rate or in some cases, even a no interest rate environment.

And on the admin expenses, it's (46:46) that we maintain our competitive advantage. Indeed, in the first quarter in absolute terms, our admin expenses actually declined, but we not necessarily think that this is a trend for the whole year.

With that, this ends the presentation we are giving you today. And, of course, we are now more than happy to answer your questions.

# Q&A

## Operator

Thank you. The first question is from In-Yong Hwang, Goldman Sachs

## Q - In-Yong Hwang {BIO 18784369 <GO>}

Hello. I'm In-Yong Hwang here from Goldman Sachs. I've got two questions. Firstly, on the combined ratio improvement by one percentage point, it doesn't – with your NatCat budget is still booked and full, and the one-offs doesn't seem to be anything special about that. So should we interpret this as kind of underlying improvement on one percentage point, we are seeing quite strongly given the pricing pressure that's still going into the market. So just a comment on how we should see this underlying combined ratio improvement would be helpful?

And secondly on the April renewals, could you give us some idea what you're seeing on pricing. I think one of the competitors today is saying that pricing decline is slowing down. Obviously, it splits out of volume and the pricing development for your newer data (48:07), but just some idea what you're seeing in the market would be helpful? Thank you.

## A - Ulrich Wallin {BIO 4863401 <GO>}

Yeah. I mean, if I come to the improvement in the combined ratio, I would say that we continued to benefit from relative favorable development on the attritional losses. And I mean, we've largely kept our policy to not release the unused budget profit, and that for - I mean, if we keep the loss ratio (48:57) stable for the newest accident here and (49:04) are not happening, our IBNR reserve has actually increased in the first quarter quite significantly.

I mean, you may be a little bit puzzled by the very low combined ratio of our Bermuda subsidiary, but bear in mind that Bermuda largely writes property catastrophe business, meaning, it's a very short-tail business. And, therefore, I mean, we tried to be very conservative on (49:44) loss reserving. But of course, as it is a short-tail business, there are always some relief (49:55) from previous years, because the limited time you can keep those reserves.

We also had an extraordinary effect on Bermuda, because we had treaties that had been commuted that we had to put €10 million reserve on the Tianjin explosion in China. And as the treaty has commuted and we had - I mean, we have no liability, and the loss hasn't been recognized, because it was rather remote. And, therefore this is (50:32), of course, immediately €10 million positive development in previous year loss ratio, which was entirely unavoidable.

## Q - In-Yong Hwang {BIO 18784369 <GO>}

Okay.

## A - Ulrich Wallin {BIO 4863401 <GO>}

If you then come to the pricing at April 1, mixed picture, I would say. I mean, still, on a non-proportional side, this is easier to comment on. We saw a slowing down in the declines, but still, declines in most of the property catastrophe business. But overall, I would say, the property catastrophe business is maybe down 4% to 5%.

On the non-cat business, situation was more stable. This also have to do with the fact that there are risk losses in the market, and they have an effect on the business. So I mean as shown in our slide, if you take it all together, I would say great quality decline is low-single digit. So not dramatic.

If you look at the demand side for reinsurance the first quarter, quite a lot on the proportionate side, where clients also from the U.S. were seeking pro rata cover. We are happy to involved in that as long as there is reasonably short-tail business, meaning property classes or claims made casualty classes.

As I already mentioned on the excess and umbrella business, where a lot of reinsurance is being sought. We have been trying our ways overall (52:30).

## Q - In-Yong Hwang {BIO 18784369 <GO>}

Okay. Great. Thank you very much.

## Operator

Thank you. The next question is from Xinmei Wang, Morgan Stanley.

## Q - Xinmei Wang {BIO 17860767 <GO>}

Hi. Good morning. I've got two questions. So the first is on the solvency ratio. Could you give us an update on your conversations with the regulator? I know in the past you talked about getting approval for the modeling of operational risk under the approved internal model. So just an update on your conversations there.

And then, the second is on reserve development. Given some comments from your peers over the last couple of weeks, I was wondering if you also had any impact from premiums – reinstatement premiums or commissions given the low to benign (53:24) loss environment of that being less than expected and whether that's affected your run-off results in the quarter or in the last year. Thank you.

## A - Roland Vogel {BIO 16342285 <GO>}

Well, I mean, if you look at the Solvency II internal partial model that's just excluding operational risk, as far as model changes are concerned, that has been rather stable in the first quarter. On the operational risk, we have projects to improve our operational risk model to an extent that our regulators are able to approve that as well, and that is on a good way. I mean, we expect at the latest in the first quarter 2017, at least that's the goal. Of course, it depends on our regulator in the end. But that's a goal that at that time, we'll also get our operational risk model – modified operational risk model being approved. That should then hopefully also further improve the Solvency II ratios.

On the reserve development, I would say, I mean, 2015 reserve development was quite positive, because the redundant reserves actually increased quite remarkably, and the confidence level increased.

On the first quarter, uneventful, no particular changes there I would say. Of course, we are not having done, I mean, first quarter full actuarial calculation here. As far as reinstatement premiums are concerned, well, I would say, of course, due to the lack of natural catastrophe losses, we haven't got any reinstatement premiums on the NatCat business.

On the risk business, I would say the risk losses are at or even slightly above the expected levels, and therefore the reinstatement premiums there, at least on our books, are pretty much in line with expectations. I mean, it's nothing extraordinary there.

Commissions. Of course, commissions increased on pro rata treaties as the results are good, because you have to pay out profit commissions and, yes, it has an effect also on our results. So the commission level is higher compensating in part for the low loss ratios. But this is what you always have on pro rata business.

The profit and losses are not attributed on the metric basis, but rather there is a profit commissions that is mitigating for the client. The effects are very good, you see that results from pro rata treaties.

## Q - Xinmei Wang {BIO 17860767 <GO>}

Okay. Thanks a lot.

## Operator

Thank you. The next question is from William Hawkins, KBW.

## Q - William Hawkins {BIO 1822411 <GO>}

Hello. Thank you. The Hannover Re SE Solvency II ratio of 231%, could you tell me what the numerator and denominator are for that ratio? Apologies if it's disclosed to someone. And could you also tell me, would you apply the same 180% to 200% threshold range for that entity or would it be different from the Group level?

And then secondly, on quarterly earnings, you made some comment about 2Q events, but could you just be clearer, there've always been a number of headlines. Do you think those – from your early plans, still are within the 2Q budget or would be enough to slip in to the carried over first quarter P&L (57:46)? Thank you.

## A - Ulrich Wallin {BIO 4863401 <GO>}

Unfortunately, we haven't got those number on the SE Solvency II ratio. But I can tell you that the difference is mainly the haircut which we haven't got on the SE. And otherwise, I mean, the compile (58:04) the SE Solvency ratio based on so-called look-through approach, which means that, therefore, it is very similar to the Group ratio and the difference as I said is the haircut on the minorities.

## Q - William Hawkins {BIO 1822411 <GO>}

So, can I infer from that, that 180% to 200% is also a fair...

## A - Ulrich Wallin {BIO 4863401 <GO>}

Yeah.

## Q - William Hawkins {BIO 1822411 <GO>}

... target range? Right.

## A - Ulrich Wallin {BIO 4863401 <GO>}

Yeah. There's a target range that we have said (58:32) as well. (58:35) large losses in Q2. I would say, from what I see now, of course, very early days, I mean, they could slip into the carried over unused large loss budget. It's still early days. I mean, if I look at the Japanese quake, early reports are more – are quite encouraging that the losses might not be that large for our book. (59:07) on Ecuador that we have the largest market share of all the reinsurers, which of course, means that we might have an over proportionally large loss there. But, I mean, nothing too concerning. And as the McMurray fire, slightly different Canada on the cat business like in all our cat business we're a little bit underway. However, it's really early days there. I mean, today's report are a little bit more encouraging, but we really have to wait there.

## Q - William Hawkins {BIO 1822411 <GO>}

Thank you.

## Operator

Thank you. The next question is from Kamran Hossain, RBC.

## Q - Kamran Hossain {BIO 17666412 <GO>}

Hi. I've got – I guess, just one question from the life and health business. Clearly, that financial solutions business is exceeding target enormously. So 18% EBIT margin versus your expectation of your target of 3%. Can you talk a bit about why we're seeing such fantastic margins in financial solutions?

And then the second part of the question is, overall in life and health, you're seeing premium growth of pretty much flat. But obviously, that's somewhat down to reduced longevity from the UK and from Australian product. Can you talk about kind of the trajectory of kind of how much you're seeing financial solutions business grow? Any color on that would be really helpful. Thank you.

## A - Ulrich Wallin {BIO 4863401 <GO>}

Well, I mean, first of all, why do we have 2% target that we achieved the double-digit EBIT margins? The 2% target is a little bit more from what we traditionally used to write in the financial solutions business, which has been cash financing business. And on cash financing business, of course, you financed through, I mean, commissions on quota share treaties and in some cases, you have to write the fee – the seeding company has to seek quite a lot of premiums in order to generate enough embedded value that the pre-financing is being expected to be paid back to see necessary certainty.

In recent years, however, particular in the U.S., some of our business has changed from cash financing basically to covering tail end exposures on largely mortality and to some extent less exposures on policyholder behavior exposures.

These treaties are partly not booked as premiums under IFRS. And even if they are, the premium is normally the same as the profitability because the loss expectancy to these treaties on actual method is close to zero, but they are still capitalization efficient on a statutory basis. That's the reason why the margins are so high then compared to the IFRS premium.

When we look at the development of the IFRS premium, if that growth – I think it will grow this year mainly because there are re-emergence of relatively attractive cash financing opportunities, which will, of course, boost the premiums a bit, will also lower the EBIT margin on an IFRS basis.

And your second question, you were wondering on the...

## Q - Kamran Hossain {BIO 17666412 <GO>}

It's just a different – the growth of the two businesses, so growth of financial solutions business underlying because (01:03:28) all the moving parts.

## A - Ulrich Wallin {BIO 4863401 <GO>}

Well, I think – I mean, the business is still growing. You may not necessarily see that in the premiums only if it's cash financing because some of them may be deposit accounted. But I would say if you measure at a covered value enforced, you will probably see a pretty good growth on that business. And the underlying profitability, more importantly, is growing as well. So that business continues to be very favorable for us.

As far as the longevity business is concerned, yes, on the enhanced annuities in the UK, for the reasons that have (1:04:09) we see a reduced premium volume and we also had, I think, some last single premium treaties in China where we also see a reduced volume after – I think if you exclude those, I think, the underlying growth is still there. You may not see much of this, this year but I think if you look on a five-year time horizon, we will – I'm very confident that we will achieve our growth objectives.

## Q - Kamran Hossain {BIO 17666412 <GO>}

Fantastic. Thanks very much. I appreciate the color. Thank you.

## Operator

Thank you. The next question is from Frank Kopfinger, Deutsche Bank.

## Q - Frank Kopfinger {BIO 16342277 <GO>}

Yes. Good morning, everybody. I have two questions on your Solvency II reporting. First of all, could you walk us down from your 253% from last year to the 221% as of the end of 2015? What were the drivers? Obviously, it's higher volumes but also, could you comment on the diversification benefit that you're applying?

And secondly, could you provide some figures in respect to sensitivities? And especially I'm looking for your credit spread sensitivity for Solvency II. I appreciate you have some sensitivity for the P&L and the shareholders' equity, but as this is based on a relative basis, it says it's 50%. Could you also provide some sensitivities with respect to absolute numbers, so let's say, if credit spreads widens by 100 basis points.

## A - Ulrich Wallin {BIO 4863401 <GO>}

I think Roland, if you want to take the second one.

## A - Roland Vogel {BIO 16342285 <GO>}

Yes. I would do that.

## A - Ulrich Wallin {BIO 4863401 <GO>}

Yes.

## A - Roland Vogel {BIO 16342285 <GO>}

Should I start with it or...

## A - Ulrich Wallin {BIO 4863401 <GO>}

Well, then I may give the reasoning from the 253%. Of course, it's the increased business volume and on the reserves, of course, the increased volume of reserves had increased the cap requirement. Also, we saw in that period a significant strengthening of the U.S. dollar. And still, I mean, we are a little bit overweighed on our capital on euros that also have an effect. It had mainly an effect in boosting the volumes that create the SCR in euro terms. Those were the main drivers there. Diversification is slightly unchanged, I would say, because the increases in the SCR drivers developed relatively homogenously.

## A - Roland Vogel {BIO 16342285 <GO>}

Yeah, so, I will – I must admit I don't have an actual sensitivity based on an absolute basis points increase or decrease in credit spends available. We may take that up. The question here is, of course, if we would do that on a non-relative basis and you say, let's assume 50 basis points or 100 basis points, so of course, for German bonds, 100 basis points will be a very drastic increase.

And if you look at that (1:07:35), might not make that much sense. If you then look at 100 basis points on our high-yield portfolio that may be something which occurs a few times a year. And in that regard, I'm a little bit skeptical with these absolute terms sensitivities.

Well, if you, for instance, look at the numbers we give you for the 50% range and I would also say that this develops rather proportionally. So, if you then say, if a 100% increase in credit spreads would, in rough terms, result in double the number of the sensitivity and you apply that then to the approximately €5 billion in required capital, that then should give you a little bit of an indication. Still, we feel very comfortable and even such a sensitivity of potentially 100 basis points would not result in a sensitivity, which would immediately give alter to our solvency ratio.

## Q - Frank Kopfinger {BIO 16342277 <GO>}

Okay. Thanks.

## Operator

Thank you. The next question is from Michael Haid, Commerzbank.

## Q - Michael Haid {BIO 1971310 <GO>}

Morning. Two questions. So just one clarification. You've mentioned the reserving movements that we have seen no particular effect in the first quarter. Does that mean zero reserve releases or does it mean the expected level of reserve releases, something like €50 million or so?

Second question, on the April renewals, can you give us an explanation why you were able to increase the volume to such an extent in a very competitive environment? Is it because the underlying market growth or do you have better access to the market, i.e., is it Hannover Re specific, or why does this business show up in the reinsurance market?

## A - Ulrich Wallin {BIO 4863401 <GO>}

Would you take the first one, Roland?

## A - Roland Vogel {BIO 16342285 <GO>}

Yes, of course. So I think if we say there were no extraordinary developments to our loss reserves that means that we have the normal run rate, so it should be around the positive effect of the number which I have mentioned.

## Q - Michael Haid {BIO 1971310 <GO>}

Thank you.

## A - Ulrich Wallin {BIO 4863401 <GO>}

If I then come to the why we could increase on April 1. I think overall, we have seen a slight increase in demand for reinsurance at the April 1 renewal, particular also from proportional treaties. I don't think that this growth of the business is evenly spread among the reinsurers. It appears that the larger reinsurers benefit from that a little bit more maybe than the smaller reinsurers.

For us, I mean, we had quite good opportunities to grow the business at 1/4, actually to a larger extent than we actually did because we recognize that the market is still soft and reinsurance pricing overall is certainly a lot lower than it was like three years ago. And, therefore, I mean, we have to be very careful because some of that additional reinsurance buying might also be a little bit defensive.

So, from that point of view, we looked at a broad-based growth rather than very concentrated growth out of that, and we were able to achieve that. I think it's also fair to say that the overall volume renewed at 1/4, of course, is significantly less than what you see at 1/1.

## Q - Michael Haid {BIO 1971310 <GO>}

Okay. Thank you very much.

## Operator

Thank you. The final question is from Vinit Malhotra, Mediobanca.

## Q - Vinit Malhotra {BIO 16184491 <GO>}

Hi there. Morning. So most of my questions have been addressed. Thank you. But just one, if I can ask. In the MtCR on the European side, there is a rather low or a nice 88.9%. And I'm just wondering because one of the larger peers have mentioned German motor needed some longevity adjustment in their case. Have you noticed anything that should be highlighted here from (01:12:42) perspective below 90%. This level usually indicates a good level, but I'm just curious. Thank you.

## A - Ulrich Wallin {BIO 4863401 <GO>}

Okay. You don't think about the 88.9% (01:13:00) on Continental Europe. Well, I mean, this is certainly not for the German motor business where it's close to 100%. I mean, this refers to a large extent to the motor access of loss business that we have in that class because that is a very lucrative business. It is quite heavily exposed to volatility. And there, really the MtCR has dropped very significantly this year, decreasing interest rates because the value of money is coming down so much. And the other is, of course, on the pro rata and (01:13:55) business that is quite a bit of natural catastrophe exposure within that book. And this is the reason why we see this little bit surprisingly low MtCR.

## Operator

Thank you. We currently have no further questions.

## A - Ulrich Wallin {BIO 4863401 <GO>}

Okay. If there are no further questions, I would then thank you very much for listening, and thanks for your questions.

## Operator

Ladies and gentlemen, thank you for attending. This call has been included. You may now disconnect.