Q4 2015 Earnings Call

Company Participants

- George Quinn
- James Quin
- Kristof Terryn
- Tom de Swaan

Other Participants

- Andrew J. Ritchie
- Andy Hughes
- Dhruv Gahlaut
- James A. Shuck
- Michael I. Huttner
- Nadine van der Meulen
- Nick Holmes
- Paul De'Ath
- Peter D. Eliot
- Ralph Hebgen
- Sami Taipalus
- Stefan Schürmann
- Thomas Seidl
- Vinit Malhotra

MANAGEMENT DISCUSSION SECTION

Operator

Ladies and gentlemen, good morning or good afternoon. Welcome to the Zurich Insurance Group Annual Results 2015 Conference Call. I'm Sarah, the Chorus Call operator. I would like to remind you that all participants will be in listen-only mode and the conference is being recorded. After the presentation, there will be a Q&A session. The conference must not be recorded for publication or broadcast.

At this time, it's my pleasure to hand over to Mr. James Quin, Head of Investor Relations and Performance Management. Please go ahead, sir.

James Quin {BIO 18345789 <GO>}

Good afternoon, and welcome to our 2015 results call. On the call are our Chairman and ad interim CEO, Tom de Swaan; our Group CFO, George Quinn; and the CEO of our GI Business, Kristof Terryn. Tom will give a brief overview and then we'll take your questions.

Tom de Swaan {BIO 1702205 <GO>}

Thank you, James, and good afternoon, good morning. Our results for 2015 are disappointing. The issues are concentrated in our GI business, mainly in Global Corporate. GI had a full-year combined ratio of above 103% and this is principally due to a very high level of large individual losses, including claims arising from the Tianjin Port explosions, a number of major fire claims, a large credit and surety loss, and other events. In total, large losses were around 4 points higher than our expectations.

Due to GI performance, our earnings were well short of prior-year levels and BOP after-tax return on equity of 6% is a long way short of our target range of 12% to 14%. We have actions underway. Some have already started to show some positive signs as you have seen in the pack distributed this morning. And I'm confident that the new team under the leadership of Kristof, who is present here as well, deliver much improved results for 2016.

Good progress continues to be made in both Global Life and Farmers. Global Life is on track, having delivered good growth in both new business value and BOP in local currency. Growth in BOP was due to progress made in Bank Distribution and our in-force management initiatives, while growth in new business value was achieved mainly in our Bank Distribution and Corporate Life and Pension Pillars. Farmers continue on its trajectory with the sixth consecutive quarter of top line growth, and this shows that the transformation that Jeff Dailey and his team started is bearing fruit.

At the time of quarter three results, we announced that the group would take a decision on February 2016 on how it would deploy excess capital and that this would be communicated with the full year results. And in line with this timetable, the board of directors has carefully evaluated capital deployment options.

While the board is confident in the reserves, capital, cash generation and future earnings prospects for the group, it has concluded that it is important to maintain the group's capital strength and flexibility in the current circumstances and has, therefore, decided not to return addition capital to investors at this time. This, I realize, is not the outcome that was expected at the Investor Day nor indeed later in the year, but it is the right course of action.

In summary, the right actions are being taken to address General Insurance challenges. Zurich has an excellent team in place that will be further strengthened with the addition of Mario Greco, who will lead preparation for a new strategic cycle in 2017. As you know, we announced this morning that he will join on the 7th of March.

So, the group remains in very strong position in terms of balance sheet, cash generation and financial flexibility, and looks forward to a rapid recovery and profitability in 2016.

We would now like to take your questions. Thank you very much.

Q&A

Operator

We will now begin the question-and-answer session. The first question is from Dhruv Gahlaut, HSBC. Please go ahead.

Q - Dhruv Gahlaut {BIO 16209870 <GO>}

Good morning. Thanks for taking my question. I've got a couple of questions. Firstly, could you update what happened to Z-ECM post the nine-month stage, and what is the level of deployable capital against the €3 billion, which you had at that point? Secondly, in 2015, you've had as in both the issues from the large losses side as well as from the weather events, well, as in could you outline the changes which you've made in terms of reinsurance, retention levels, et cetera? Also then, in terms of these changes, what is the cost that would go up in the P&L next year for reinsurance? Could you just outline those as well? Thanks.

A - Kristof Terryn {BIO 17664174 <GO>}

You take the first one, George...

A - George Quinn {BIO 15159240 <GO>}

I'll take the first one and Kristof will take the second. So on the capital side of things, so we haven't prepared the full run. We typically do that in March as part of the cycle with (6:00), but we have done an update. So we would estimate that Z-ECM capital adequacy would have improved over the position that we reported at the end of September, slightly towards the end of the upper half of our range.

On the S&P side, which tends to be the more constraining of those capital measures at least currently. I mean, if you look at what we have projected with (6:33), which was in the $3 billion range, if you allow for what we set aside for the acquisitions, which is about $800 million, and you look at the short fall that we suffered in capital (6:46) in Q4, which is a loss of around $400 million (6:50), I guess we'll see a profit in the $700 million range. That gives you a relatively ready guide to where we would currently project we would be.

So on the large losses?

A - Kristof Terryn {BIO 17664174 <GO>}

I guess on large losses and particularly to the question of reinsurance. So, the number of additional reinsurance covers, the most important one is we put in place and I believe (7:20) has produced the volatility on the large losses. We've also put in place or increased the number of quota shares that would give us some time to address the underwriting (7:32). And that is in our Global Corporate and North American property portfolio.

Through the year we'll continue to (7:41) where it does make sense to sell (7:46) reinsurance.

Q - Dhruv Gahlaut {BIO 16209870 <GO>}

Sorry, I think you were breaking up. Could say what was the cost, as in for the exchanges, as in the cost of the increase in reinsurance?

A - George Quinn {BIO 15159240 <GO>}

Dhruv, it's George. So, we haven't broken out the cost of the new reinsurance programs that is included. Together with the expectations will it arrive (8:10) and overall combined ratio for 2016, that cost was fully reflected in those estimates.

Q - Dhruv Gahlaut {BIO 16209870 <GO>}

Thanks for that.

Operator

The next question is from Andrew Ritchie, Autonomous. Please go ahead.

Q - Andrew J. Ritchie {BIO 18731996 <GO>}

Hi there. I had a question also on the reinsurance. I know maybe this is a bit simplistic, but just to give us a sense. If, horror of horror, 2015 was to happen again, let's hope it doesn't, what would the net benefit of reinsurance have been, just roughly? I appreciate you may have broken through some of the aggregates, but if there's any sort of sense as to what the benefit would have been, that would be helpful.

And the second question, could you just update us on reserves in terms of independent reviews? What has been done? Is there anything additional or special being done? I know you talked about some of this at Q3, but a recap would be helpful, anything additional you did in Q4. Thanks.

A - George Quinn {BIO 15159240 <GO>}

So, on the first one. Andrew, it's George. As you can imagine, given the experience we had last year, we would have had a significant recovery under the contract on a pro forma basis. And, again, in the discussions we've had with reinsurance partners, if they weren't convinced that we had changed what we were doing, we wouldn't have the coverage in the form that we've got. So I think if I gave you a number, it'd be potentially quite misleading. So I'm not sure it's helpful to do that.

On the reserving side of things, we've just been through the normal year-end process, which includes, obviously, reviews by third parties. There's nothing new that comes out of that. If you look into what's happened in detail at the year end, we have a relatively modest positive PYD overall for the group. From a positive and negative perspective, we had a large positive on a commutation, but that was in the legacy book. And, in fact, we took a charge also within the legacy book partly to offset that in the same breath, which is A&E-related.

But in the GI book, things are pretty stable. And, in fact, the headline number we reported for PYD would have in higher were it not for the fact that we've re-estimated premiums in one of the books during the year that had positive impact on premiums. But we've also recorded obviously the claims associated with that and that's recorded as PYD. So that artificially brings down the PYD number.

So overall and from a review perspective, we've done all (10:50) that we intend to do that was one-off and, in fact, it was all done prior to the Q3 results release in November. And now we're back to managing the reserve position as we always have done.

Q - Andrew J. Ritchie {BIO 18731996 <GO>}

Can you just remind us, is it you want 80% of your reserves to be reviewed externally over a rolling three years. Is that the rule?

A - George Quinn {BIO 15159240 <GO>}

So we have several rules within the reserving process. So we have a peer review, which is an internal peer review requirement. We have a requirement that some of the longer liability exposures are reviewed externally. And typically the frequency in the past has been every two years.

And if you look at what's happened to us over the last probably two-and-half years to three years and because of the general interest that regulators have in reserving, broadly for the industry, we've had several reviews, which are always targeted at higher risk areas around, say, workers' comp or other long-tail forms of liability. And I guess if you looked at the high risk parts of the reserve, they've all been reviewed over the course of the last two years and sometimes more than once.

Q - Andrew J. Ritchie {BIO 18731996 <GO>}

Okay. You answered the previous question saying the cost of reinsurance was included within your 2016 combined ratio expectations. Have you actually given a 2016 combined ratio expectation? I didn't see one.

A - George Quinn {BIO 15159240 <GO>}

Thank you for pointing that out. So what we've done today, we've tried to avoid giving another short-term target for 2016, given the things that we have to address during the course of this year. But at the same time, the ambition, the expectation, in fact, the plan we have has not changed. I think the challenge that we perceive today, given the weakness that we've still seen in Q4, I think we think it will take slightly longer in 2016 to get there, but we still expect to get there.

Q - Andrew J. Ritchie {BIO 18731996 <GO>}

So that would be what, 97.5 or something?

A - George Quinn {BIO 15159240 <GO>}

If you go back to where we were before, we had indicated at Q3 that we thought we were around 99.5. I think today we'd probably revise that up slightly and we still expect to see an improvement in the range that we previously discussed.

Q - Andrew J. Ritchie {BIO 18731996 <GO>}

Okay. Thank you.

Operator

The next question is from Peter Eliot from Kepler Cheuvreux. Please go ahead.

Q - Peter D. Eliot {BIO 7556214 <GO>}

Thanks very much. If I could first just follow-up on Dhruv's question on the Z-ECM ratio. I guess I was positively surprised by what you said about the current position because if I take the sort of 114% and then just naturally from the earnings, dividend accrual and RCIS acquisition, I reckon that's about a 5 point headwind. And then you had quite horrible markets recently. I appreciate some of your reinsurance actions will help a bit, but I'm surprised that you can get back up into the higher end of your range. So I was wondering if you could just elaborate a little bit there and what I'm missing.

And then the second question was back to the General Insurance division. So you said that you've put through rate increases of 5% to 10% in Global Corporate's worst-performing tiers, given the sort of high combined ratios you identified in some parts of the business in Q3. I'm just wondering if those rates are sufficient. And I guess given you've had a bit of experience year-to-date and know your intention on the reinsurance cover, I'm wondering whether you can also give us any guidance about the outlook for your net premium development that you expect. Thank you.

A - George Quinn {BIO 15159240 <GO>}

I'll take the first one and Kristof will handle the second. So I think the key difference between us is that I haven't given you a figure as of today. So what I'm giving you would be equivalent to the SST1 filing, which is a January 1 perspective of the view for this year.

So if you allow for some of the market volatility we've seen, it would certainly be lower. But I think the biggest difference in the positive that you probably included it but then knocked it back out because of what's happened since, is really the impact of markets in Q4 which were actually quite positive for us on Z-ECM.

A - Kristof Terryn {BIO 17664174 <GO>}

And maybe let me take the question on rate. So as we said earlier, we've been very disciplined in terms of how we push for rate, including in the bottom tiers. The rate increases that we're looking for have to be much higher. At the same time, we see the retention drop, retention in the bottom tier, so fourth tier has dropped in certain lines of business to as low as 60%. So it's not just grade that will improve the combined ratio. We talk about lift, which is basically the impact of the different parts of the book growing or retaining them at different levels. So that in itself will impact on the combined ratio as well.

So, overall, Gen one (15:58), we saw in overall Global Corporate business positive rate on the overall book with some very strong differentiation between the different years. On your question on the NEP side, the actions that we've taken in terms of exits of books, I mean that's about $400 million in premium. That's about 1% of the top line that we will lose.

In addition, I expect most of the businesses to remain flat roughly which is a combination growth in some areas and slight declines in others. Global Corporate, as a whole, will likely see a slight decline in the top line. So, if you combine that together with the exits and a higher level of reinsurance, I mean, the net premium will see a slight decline as well at the overall level.

Q - Peter D. Eliot {BIO 7556214 <GO>}

Okay. Thanks a lot.

Operator

The next question is from Michael Huttner from JPMorgan. Please go ahead.

Q - Michael I. Huttner {BIO 21417183 <GO>}

Thank you. Thank you very much. On the cash flows of $3.9 billion, we have about $0.5 billion from Farmers Re and $0.5 billion one-off in Life. So, that gives me an underlying run rate of $3 billion. So, these are obviously coming out of 2014 profits which are quite good. Can you talk us through the variances which would kind of help us gauge the cash flow for – the coming cash flow? And I'm assuming you have a lot of visibility because you have all the results and these are just dividends from the subsidiaries.

And then my other question is on Global Life. I have in mind, but I get very confused that – and it's me. I'm not saying anything more, but the – that previously, the expectation was that the Life results would rise to above $350 million a quarter. And from my reading or my understanding of the release today, you seem to be happy with profits of about $300 million. And I'm just wondering if that's the new number which I should use going forward. Thank you.

A - George Quinn {BIO 15159240 <GO>}

Michael, its George. I mean for 2015, I think you've captured, I mean, almost all the key items that are the significant one-offs and the 2015 cash flow. So, $3.9 billion we've reported today. Approximately $0.5 billion from Farmers, which is installment number one of what we expect to see from Farmers Re and the steps that we started to put in place about a year ago there.

And Global Life, which is a combination of the annuity transaction in the UK and the sale of an investment manager that we had last year, which is a bit less than $0.5 billion, which leaves us with around $3 billion is more or less the underlying element for last year. So we will have a negative impact next year principally because of the impact of the GI earnings impacting the statutory outcomes and therefore the statutory dividends that get cleared.

At this stage, what we're telling the market is that we still expect to see total cash flows, total net remitted cash flows for the group next year that will leave us above the $10 billion mark. So from that you can see we're allowing for the possibility we'll see a fall from the normal or the targeted $3 billion level, but not a significant fall and not a fall at this stage. But at least from a cash perspective, I would expect to leave the dividend uncovered.

Q - Michael I. Huttner {BIO 21417183 <GO>}

I understand. Just before you go on, (19:50) what's the balancing figure to get to $10 billion? What's the difference? No, no. I'm just asking. It's mathematical. You've got the years in front of you, I don't. That's all.

A - George Quinn {BIO 15159240 <GO>}

Yes, so it's $3.7 billion, $3.9 billion. $2.4 billion would be the minimum required.

Q - Michael I. Huttner {BIO 21417183 <GO>}

$2.4 billion. Got it. That's really helpful. Thank you.

A - George Quinn {BIO 15159240 <GO>}

Just before someone takes away that as a headline, that's not the expected cash remittances for 2016. We expect the number to be higher than that.

Q - Michael I. Huttner {BIO 21417183 <GO>}

And that includes the another half – if I understand your comment on Farmers Re, that would include another installment of about the same amount.

A - George Quinn {BIO 15159240 <GO>}

Approximately. Slightly less.

Q - Michael I. Huttner {BIO 21417183 <GO>}

Slightly less.

A - Kristof Terryn {BIO 17664174 <GO>}

Let me take the Global Life question. So, the run rate that we're guiding towards for 2016 of $350 million a quarter, I mean, we said back in 2013. So in 2014, there was already an impact of FX but in spite of that, we stuck to the target of $350 million. If you look at the result for 2015, I mean, at 2014 FX levels, that's a $1,478 bump. So, we actually achieved the $350 million a quarter in 2015.

Q - Michael I. Huttner {BIO 21417183 <GO>}

Right. But that's looking backwards. What's the figure which I should be – with all the changes that's happened in FX and stuff, what's the changes – what's the figure which is equivalent to this $1,478?

A - Kristof Terryn {BIO 17664174 <GO>}

I mean, the figure has changed. I mean, the figure that we gave in 2014 was that we were aiming for a quarterly run rate of $350 million plus

Q - Michael I. Huttner {BIO 21417183 <GO>}

Yes.

A - Kristof Terryn {BIO 17664174 <GO>}

In 2016, that's at 2014 FX levels.

Q - Michael I. Huttner {BIO 21417183 <GO>}

And the FX if I – from your disclosure. The FX took about 15% off, is that right? If I compare the $1,478 with the $1,300?

A - Kristof Terryn {BIO 17664174 <GO>}

I think more or less, Michael. More or less 15%.

Q - Michael I. Huttner {BIO 21417183 <GO>}

Yeah. Okay. More or less 15%. That's really helpful. Thank you very much.

Operator

The next question is from Paul De'Ath from RBC. Please go ahead.

Q - Paul De'Ath

Hi there. Couple of questions, please. And on the OOB line, there was a bit of a difference there from what we were expecting there and due to a number of one-off factors. And if you could give us any more feel as to what those one-offs were and what we should be thinking about for that flat line going forward? That would be great.

And the second point was on the cost-savings targets. So targeting sort of $300 million plus for 2016, which, if I'm reading it right, are going to cost around $420 million something to implement and, you're looking for $1 billion in total after 2018. Is that the cost per pound of cost saves that we should thinking about for the rest of the $1 billion going forward and/or any guidance around that would be great. Thanks.

A - George Quinn {BIO 15159240 <GO>}

On the first one, on the OOB, so we have a couple of relatively significant one-offs that's flattering the OOB number for particularly Q4. As we have some sustainable items around the financing cost. We got some benefits earlier in the year around FX which again are one-off in nature. It's actually quite hard to build anything from the Q4 number. I think the gains I would give you at this stage is that we would expect to see OOB cost. I mean, depending on things like the foreign exchange, but assuming that things are reasonably stable there, I mean in the $800 million range for 2016.

On the second question, so the – I guess the cost per dollar of cost saves. And I mean, we're looking again about how we can accelerate some of the changes that we're making. Obviously, Kristof and his team have pushed ahead much quicker than we had originally anticipated in the fourth quarter. So, that significantly increased. I think because of the nature, some of the things that – some of the areas that we tackled in Q4. I'm not convinced that the cost per dollar in the future will be quite as high. So, I think it might be slightly lower, but we're going to exceed the Investor Day guidance that we gave back in May which was for – if you hit the midpoints of what we said, for something around $1.1 billion in total.

I think we may, I mean, we're doing more work as we come up to Q1, I'll give you a much clearer sense. But at this stage, I mean, we could easily see a run rate of say another $500 million reaching for the next two years, where we complete the program, but we'll give you more information in Q1.

Q - Paul De'Ath

Great. Thanks.

Operator

The next question is from Nick Holmes from Société Générale. Please go ahead.

Q - Nick Holmes {BIO 21515144 <GO>}

Hi there. I have two questions. First is on expenses. With the expense ratio in the GI business, I wonder, could you give us a bit of color on how rapidly you expect improvement? And why I'm asking is because I wonder do you think it could actually get worse before it gets better? And I'm thinking of the pruning that you're doing in the group.

You're exiting business in the U.S., and the Middle East and I just wondered whether the top-line reduction is going to be a problem for the expense ratio for reducing expenses in line with the top line. And then, second on the reserves, I wondered, I mean, you've given us some additional disclosure on the NAC business, I just wondered what's sort of reassurance you can give us that the losses in commercial auto and property are not going to be repeated? I mean, what sort of comfort would you draw our attention to in the numbers that you disclosed? Thank you.

A - Kristof Terryn {BIO 17664174 <GO>}

Okay. Let me tackle the first question on the expenses. And maybe, first of all, we did have some one-offs in the Q4 expense ratio. So, it should probably normalize that back. On your question on the expense progression into 2016 and the impact of the top line, I mean, overall we are looking at an absolute expense reduction going to 2016. And that is target that we have set for the businesses as well. We've moved away from an expense ratio target to make sure that what people focus on is on the profitability and the quality of the business, as well as an absolute expense reduction.

Now, as I said in the – as an answer to a previous question, I mean, it is likely that we see some slight top line. The focus at this point is really on the quality of the portfolio. So, that's really what we're targeting. But you should see an absolute expense reduction going into 2016.

Q - Nick Holmes {BIO 21515144 <GO>}

I'm sorry. If I may follow-up. I just asked because in the past, the trade-off between loss ratio and the expense ratio perhaps hasn't been managed as effectively as it could have been and what sort of reassurance would you give us, that that's the key focus for you going forward?

A - Kristof Terryn {BIO 17664174 <GO>}

Look, the primary focus for this business is to improve the absolute combined ratio. And so, the key improvement that you should see next year is in the loss ratio, and we will not make any trade-offs between top-line growth and loss ratio. We've been clear as to where the priority is. It is on the underwriting quality of the book and the rate and (28:01) that we need to see.

Q - Nick Holmes {BIO 21515144 <GO>}

Okay.

A - George Quinn {BIO 15159240 <GO>}

On the second part of your question, we have provided additional disclosure today on the reserve triangles so you can see it by the major GI segments. And we've also given some (28:20) information. I hope the information today is helpful. I think it's quite hard unfortunately to use this to actually drill in and look at, say, an individual line and an individual territory, like commercial auto.

What I would say on commercial auto, though, of course, is that our big challenge was in Q4. We've had several gos at trying to get commercial auto in the right place, starting already in Q4 last year. We did that again in Q2. And following the review that Kristof and I conducted with Q3, we moved it significantly as a part of the pre-announcement of the Q3 earnings.

We've made a conscious decision there to move ahead of the normal actuarial indications, so we've moved away from a technique that we felt would lag experience and moved to one that gave far more weight to the far more recent, far more negative experience. And that's held up well in Q4 (29:18).

So I'm afraid I think the answer to this question is that it will take several more quarters of us demonstrating that we have no further adverse on the commercial auto I think for all of us to take a more substantial comfort. But the first quarter after the reserve increase, which was Q4, has performed well.

Q - Nick Holmes {BIO 21515144 <GO>}

Thanks very much, George. Just one follow-up. Commercial auto obviously part of more of an industry phenomenon. But with the proxy book, the construction book in the U.S., can you tell us a little bit more what went wrong with that book and why it went wrong and what you're doing to prevent that recurring?

A - George Quinn {BIO 15159240 <GO>}

I think on commercial auto in general, I think it starts with the industry-wide issue around the pricing dynamics, the trends and the loss cost. And I think for us, as Kristof has mentioned several times, we were slow to the trends and should have acted faster. So I think there's a broader industry issue, but our failure here was to see it coming and to address it swiftly.

I think on some of the other lines of business where we've had challenges, so you pointed to this sub-line of tractors book we have in the U.S. That's a book that for several years was very, very profitable for us. What we've seen more recently is that we've had exposure to events that we had not anticipated and we've taken steps to make sure that that's reflected in the way the contracts are awarded. It's a relatively long tail line of business and it typically carries the large individual exposures. So we still carry some significant exposure going forward.

But I think on commercial auto, we've certainly reacted. You've heard from Kristof on what we're doing on the GI review. On the other areas, we need to make changes to lines of business that we believe to be profitable for us, we've made those changes.

A - Kristof Terryn {BIO 17664174 <GO>}

Maybe let me just add one point in terms of lessons learned. So, if there's a lesson learned, it's around the speed of reaction. And I think we took the right actions in Q3. Also I want to make sure that people understand that when we talk about the GI review, both the commercial motor book and the sub-part of the construction liability book, those are actually relatively isolated reserve-strengthening movements.

By and large, what came out of review is a current accident year profitability issue, not a reserve issue. So the broader lessons around addressing the current accident year profitability go much more back to underwriting discipline, growing in the right areas making the right actions.

Q - Nick Holmes {BIO 21515144 <GO>}

Okay. Thank you very much.

Operator

The next question is from Sami Taipalus from Berenberg. Please go ahead.

Q - Sami Taipalus {BIO 17452234 <GO>}

Hi. Good afternoon, everyone. Thanks for taking my question. On the first one, I just wanted to go back, you gave a slide at nine months where you showed that 15% of the business was flat, giving a combined ratio of 143% and that 85% was giving a combined ratio of 94% to show that the problem was quite isolated within your book. I was wondering if you could give an update on that slide and whether you still feel that the problems are quite isolated. That's the first question.

The second question I had was on the excess capital. You said that you've decided not to return it, but you haven't excluded M&A from the agenda. So I was wondering if that's still a possibility. Thank you.

A - Tom de Swaan {BIO 1702205 <GO>}

This is Tom de Swaan. I'll take the M&A question. We have always said that we will use any excess capital for organic growth, inorganic growth, or capital actions vis-à-vis the shareholders. That still stands.

As I said in my introduction, the board has extensively discussed this. We believe that under the present circumstances, it is not warranted to return capital to the shareholders. Obviously, the arrival of the new CEO also plays a big role in this and he will also, together with the other members of the management team and the board, look at this very carefully. But the present posture we have that we will use the excess capital for these three items remains valid.

Q - Sami Taipalus {BIO 17452234 <GO>}

Okay. So there is still excess capital available for M&A. Is that the right interpretation or did I misunderstand that?

A - Tom de Swaan {BIO 1702205 <GO>}

Excuse me?

Q - Sami Taipalus {BIO 17452234 <GO>}

There is still excess capital available for M&A, should you need it. Or did I misunderstand that?

A - Tom de Swaan {BIO 1702205 <GO>}

Well, as George explained earlier in the call, he gave you an impression of the amount available and that amount is available for these three purposes.

Q - Sami Taipalus {BIO 17452234 <GO>}

Okay. Perfect. Thank you.

A - George Quinn {BIO 15159240 <GO>}

And maybe back to your first question on the 15 portfolios that we highlighted at the third quarter. So to make a comparison with Q4 is just very difficult because of the cats that we experienced in Q4 and then some of the isolated large losses. But maybe a couple of points in terms of where we see the actions coming through.

So some of the exits that I talked about, the $400 million of GWP that we exited or are non-renewed as of January 1, are clearly within bottom 15 portfolios. We are also seeing that on January 1 renewals, we are getting slightly more rate in those 15 portfolios than in the rest of our book. But I would also like to reiterate that the actions we have taken are not just on the bottom 15 portfolios. What we did see in 2015 is that the attritional did not move and stayed relatively flat year-over-year. So some of the actions we're taking are much broader than just in those bottom 15 portfolios.

Q - Sami Taipalus {BIO 17452234 <GO>}

All right. Okay. Thank you.

Operator

The next question is from James Shuck from UBS. Please go ahead.

Q - James A. Shuck {BIO 3680082 <GO>}

Hi. Good afternoon. Thank you for taking my questions. I have three quick questions, please. Firstly, I just like to understand a bit more about what the earning risks are as we go into kind of Q1 and Q2. I appreciate some of the action that you're taking to get control of the volatility in the business and reduce the large losses, it might take some time. And I just like to kind of hear what your thoughts are about the experience year-to-date and what the risk is of those large losses recurring in the first half of the year? That's my first question.

Secondly, obviously, Solvency II doesn't directly impact your business, but it will indirectly. And a lot of your Life operating capital generation comes from countries that are under Solvency II. I think the guidance you've given previously was for $500 million of capital generation on an inflection point trending upwards sharply from 2016. So could you just give a little bit of insight into whether that's still the case under Solvency II as other territories go live with that regime?

And then thirdly, around the dividends, Tom, I've seen some comments that the maintained dividend shows belief and sustainable dividend going forward. And could you just clarify those comments? Because, obviously, the payout ratio based on IFRS earnings and on capital generation is quite high. It's easily affordable. A new CEO might take a different view in terms of that policy. So I just came to understand your comments in that context please.

A - Tom de Swaan {BIO 1702205 <GO>}

Thank you. Well, I think that what I said is something we have been expressing quite some time. Clearly, the dividend over 2015 has, to put it mildly, a very high payout ratio. But we also said that we believe that 2016, we'll see a progressive improvement in the results of 2016, as far as GI is concerned, we see continued good performance in the Life and the Farmers business. So that was a major part of the discussions in the board about the dividend and whether we should maintain our traditional – position that we are there to pay a sustainable and attractive dividend.

So I think that maintaining the dividend at CHF 17 for 2015, combined with repeating our general policy and this shows that the board has a substantial trust in the development in the company in 2016. That is clearly our opinion and I'm pretty much convinced that the new CEO will look at it in the same way. Obviously, it depends on the performance of the company going forward, but it doesn't take away that we believe that we can continue to pay sustainable and effective dividend.

A - George Quinn {BIO 15159240 <GO>}

So on the other two topics you had, so one was around, I mean, earnings risks in general and then the Solvency II capital cash generation topic for our Life company. So on earnings risks let me give you an update on what we see for Q1, maybe just I'll explain some of the caution that we have.

So if you look at Q4, the main challenge we had on large loss is all about the second half of December. Our large loss expense roughly by a month (39:23) is just more than $100 million for October. It's about $160 million-ish for November. And it's well over $350 million excluding the UK storms in December. And the steps that the GI teams are taking will clearly have an impact on that. But again, because we have contracts that were written before the changes took place, we still have some exposure to large individual events.

The second thing is that, while the reinsurance business will attach to all the risks in the 2016 accident year, there's a deductible. And again, because of the way that looks and even if we have another high year for large losses, the benefits of that contract will be a bit back end loaded. So you would experience it, maybe later in the year rather than earlier. So that's why we're just a touch cautious around the very beginning of the year.

On the capital generation topic, so we don't see any need to change the guidance on what we expect from the Life businesses. I mean you're aware that – the figures already anticipate having to address, I think, some fairly substantial issues in Germany around ZZR. So I mean it's already, I think, a tough target for the Life team. But given what we see, we see no reason to revise the guidance we've given previously.

Q - James A. Shuck {BIO 3680082 <GO>}

Okay. That's very helpful. Thank you.

Operator

The next question is from Thomas Seidl from Sanford Bernstein. Please go ahead.

Q - Thomas Seidl {BIO 17755912 <GO>}

Yeah. Thank you. Good afternoon. Three questions please, first, again on reserves. I appreciate, of course, that the audits confirm the reserve adequacy. But my question is more about the reserve buffer and what comfort it can provide there. We just observed that the development of the accident year is flattening and you have a number of metrics which point and indicate reducing reserve buffer. So my question is can you give us any indication about the level of reserve buffer you have? And hence, how much you are able to compensate future reserve uses in one of the other business area?

Second question is on the top-line. I must say, I'm a bit surprised about the rather benign top-line changes you are planning. It even sounds like 2 percentage points, 3 percentage points, 4 percentage points. When I first looked at the North American commercial business, commercial auto, commercial multiple, workers' comps is about one-third of the business that runs at negative or very low margins and that includes combined ratio and investment income. So I wonder is this not – are we not going to see much bigger change in order to improve performance in the P&C space?

And my last question goes to Tom on the CEO's selection. As you pointed out in the release, you know Mario Greco very well. He runs the P&C business from 2010 to 2012. But then when you look at the periods, the performance was not that good in P&C and one could argue that as the issue started already at that time and at the end of 2013, it was P&C which mainly didn't deliver. So my question is why does the board feel comfortable that Mario Greco is the right choice to turn around the P&C business of Zurich?

A - George Quinn {BIO 15159240 <GO>}

I'll go ahead first.

A - Tom de Swaan {BIO 1702205 <GO>}

Yeah.

A - George Quinn {BIO 15159240 <GO>}

Can I make a request to everyone that if we can try and keep ourselves to two? I promise that when we get to the end, if everyone with two will come back, (42:56) anyone with extra questions.

On the reserve position, Thomas, again, we have given some additional information today. I think it will take time for those to have a look at it and form conclusions and ask some new questions. As far as buffer goes, I mean, we don't disclose an absolute level of buffer within the reserves. We made it clear in the past that our reserving policy requires us to reserve in the right-hand side of the range. And I mean that includes the loans for the non-mathematical issues that can emerge in the portfolio over time. Unfortunately – I mean, more than that I don't want to repeat the answer I gave to the question earlier. Kristof?

Q - Thomas Seidl {BIO 17755912 <GO>}

Maybe just a follow-up on this, if that was the case, why does Zurich need to report a relatively small reserve increase of $300 million on a reserve portfolio of some $55 billion? That doesn't really fit together I think.

A - George Quinn {BIO 15159240 <GO>}

Again I could repeat what I said in Q3. So Q3, Kristof and I did a review of reserves and we looked at vulnerabilities. So we didn't spend our time worrying about the areas where the company was in a strong position for reserve, but we focused on those areas where we are concerned that we see the deterioration or in fact in some cases continued deterioration. And we felt it was important to address them and that's what you saw us do in Q3.

Top line, Kristof?

A - Kristof Terryn {BIO 17664174 <GO>}

So on the top-line, I mean as I said before, I mean the main objective is that the team has been given more around the underwriting profitability that is where we're focusing with a very strong focus on the tiering of the risks. I mean we have some very good quality risks on the book. We'll absolutely keep. We'll also be very differentiated by the business and as I said, you're likely to see some marked differences looking down the Global Corporate book and some of the better performing personal lines and commercial lines of books.

At the end of the day, we will hold the line on profitability and see where the market will let us absorb that. But, again, I'm not that negative on the outlook. We have some very good parts of our book that continue to perform, but we will push for growth and we'll be very differentiated on where we pursue that.

Q - Thomas Seidl {BIO 17755912 <GO>}

Maybe just to follow-on. You basically with (45:13) 3% to 5%, you're expecting still to improve the combined ratio underlying here (45:20) by 2 percentage points.

A - Kristof Terryn {BIO 17664174 <GO>}

So the thing that I said as well is that when you look at the differential retention rates that we're likely to see and what we are actually seeing at Jan 1. When you see retentions in some lines of business, and our bottom tiers is only 60% and the key more than 90% in the top tiers, I mean just to lift would actually be amazing contributor to that uplift in combined ratio.

A - Tom de Swaan {BIO 1702205 <GO>}

Thomas, as far as the CEO selection is concerned when we discussed the profile and the word about of the new CEO, we basically set two preconditions. We want somebody with a long and strong insurance background and we want a seasoned CEO who has led a large insurance company. And I think that Mario clearly lives up to both parts of the profile. So we're very pleased that he is coming over and he is very enthusiastic to start working for Zurich.

Q - Thomas Seidl {BIO 17755912 <GO>}

Okay. Thank you.

Operator

The next question is from Stefan Schürmann from Bank Vontobel. Please go ahead.

Q - Stefan Schürmann

I just have two questions. The first one is basically on the asset management strategy. You do sort of increased the part of liquid assets, can you maybe just update here what has been done and what will be done? And I think that's infrastructure and real estate. But just how much in fact and what the impact is on the new money yield?

And second question, quite simply, should we expect any further restructuring charges, or is everything done now? So nothing to come in 2016?

A - George Quinn {BIO 15159240 <GO>}

It's George. So on the liquids, we'll give you the exact numbers after the call. I mean we've been through most of what the team have intended to do. I think there's more we can do potentially around the real estate side of things. But we've done most of what we intended, it's a relatively small shift overall for the portfolio. And thinking about the answer to that question, I forgot the second one already. Can you repeat?

Q - Stefan Schürmann

Yeah. Can you just talk about new money yields as they are linked to that strategy, where do you stand in life and non-life?

A - George Quinn {BIO 15159240 <GO>}

I can't break out the individual components for you, but I can give you a sense of the overall. So for the group overall, for everything, for GI and GL, we have a gap of about 70 basis points between the accounting yield and the reinvestment yield. If you focus on GI, which of course is the biggest driver for the shareholders' side of it, it's much less than half of that. That's based on year-end figures.

Q - Stefan Schürmann

Yes, okay. And the other question was just on the restructuring charges. Is there any more to come in 2016?

A - Tom de Swaan {BIO 1702205 <GO>}

So on the restructuring charges, I apologize if you didn't hear what I said earlier. There is more to come. If you look at the things that we focused on last year, again, GI have made big steps on their program, but we have still more to do in GI and across the rest of the group.

We incurred more than we expected last year. At the time of the Investor Day, the guidance I gave was to anticipate something in the $1 billion to $1.2 billion in total. We're not quite through; we're about halfway through that. I suspect in total it will cost us more to get to the very end.

And as I said earlier, I think you could assume for the time being that perhaps another (48:54) may be required. But I'll provide a further and more detailed update when we do the Q1 release.

Q - Stefan Schürmann

Okay. Thank you.

Operator

The next question is from Andy Hughes from Macquarie. Please go ahead.

Q - Andy Hughes {BIO 15036395 <GO>}

Hi. Thanks so much. A quick question on the top line again on GI. It sounds like you're quite positive about the tiering and how that's going to work in terms of the growth. Is there any data in terms of tiering that you can share with us so far on the progress of that that might help (49:28) continue only growing certain parts of the book (49:30) others. Is there any way you can break down maybe the renewal price number into (49:36)?

And the second question was on the asset slide, slide 65. I'm just wondering, you've got quite a lot of financial exposure on that slide. Could you talk through what it is and is it mainly senior and what kind of (49:51) looking at? Thank you.

A - Tom de Swaan {BIO 1702205 <GO>}

Maybe let me answer the tiering question and George can break that information out. But to give you some indications, what we're actually seeing is, as I said, on the overall book and particularly the one book that's important here is the Global Corporate European book. That has a Jan 1 renewal that is more than 40% of the book. But overall on Jan 1 renewals, so we have seen positive rates.

If I have to give an indication on the rate differentials between the different tiers, in the first and second tier, which are at best risks, we see rough flat rate development. And, again, these are very good risks and we want to keep on the book. The bottom tier, we see rates between 5% and 10%. We also see huge differentials in retention, about 60% retention in some bottom tier and the lines that we're targeting for improvement. And we see retention as high as 90% in the top tier. So the improvement of the portfolio and the underlying loss ratio will come as much on the differential and retention by tier as it will come from the differential in rate.

Q - Andy Hughes {BIO 15036395 <GO>}

Thank you.

A - George Quinn {BIO 15159240 <GO>}

So on the split of assets by the industry concentrations, you pointed to the slide that contains it for corporate bonds. I guess that would generally reflect the market, so I think it's probably close to equal weight. So given where we were at the end of last year, we hadn't taken a position certainly from a strategic or even a tactical position at that stage as regards the broader market.

Our instruments here will be a combination of what you'd expect, a combination of senior and hybrid in the portfolio. I don't have a precise breakout of which is which, but we'll have a look and we can certainly share that on request.

Given the volatility of the last few days, obviously the banking sector is a bit more in focus. It's a topic that we continue to monitor. But our general outlook (52:00) Q1 and certainly Q2, there's still relatively benign economic environment. And so at this stage we don't feel the immediate need to take dramatic action around the strategic asset allocation. But on the more detailed side of financial institutions, we'll come back via IR, if that's okay with you.

Q - Andy Hughes {BIO 15036395 <GO>}

Great. Thank you very much.

Operator

The next question is from Nadine van der Meulen from Morgan Stanley. Please go ahead.

Q - Nadine van der Meulen {BIO 15200446 <GO>}

Yes. Hi. Good afternoon. Firstly, the decision to keep the dividend stable. I was wondering to what extent was the new CEO, Mario Greco, involved in that decision, given that he's joining very shortly.

And secondly, you already talked a lot about the reserves. You've released some reserves in the fourth quarter, but still clearly well below the 1 percentage points to 2 percentage points target which George has emphasized as sustainable quarter-after-quarter in the past. Can you give us some concrete guidance on this part going forward? That's it. Thank you.

A - Tom de Swaan {BIO 1702205 <GO>}

This is Tom, Nadine. Mario was only released from Generali on Tuesday, which is less than 36 hours ago. So he was not involved in the decision and he should not have been involved in the decision on 2015 dividend.

Q - Nadine van der Meulen {BIO 15200446 <GO>}

Right. Sorry to interrupt, but you did mention that you're highly confident that the new CEO will look at things the same way. I think it's the comment you made earlier.

A - Tom de Swaan {BIO 1702205 <GO>}

As I said, we have looked for a seasoned insurance executive and a seasoned CEO. So I assume and I'm very confident actually that we hired somebody who understands the insurance business, who understands you and understands the market. So that's why I'm confident how he looks upon these things. But it doesn't mean that we have consulted him on the dividend, because we should not have to consult him, because he was still employed by Generali.

Q - Nadine van der Meulen {BIO 15200446 <GO>}

Thank you.

A - Tom de Swaan {BIO 1702205 <GO>}

You're welcome.

A - George Quinn {BIO 15159240 <GO>}

On the second point. Nadine, it's George. So on the reserve release, the guidance that we've given is still the same guidance today. So we still expect to see 1 percentage points to 2 percentage points. I pointed to one of thing that slightly depresses that number in Q4 and that's what we will refer to as audit premiums. So we have a premium catch-up. So we've re-estimated premiums in one of our businesses that leads to a more premium being recognized. And with that, comes an expectation that there are some additional claims. And the claims fall into PYD. I'm not sure that economically you would think of it as PYD, but that's the way it's commonly presented. But going forward, we expect to see 1% to 2% redundancy.

Q - Nadine van der Meulen {BIO 15200446 <GO>}

Thank you.

Operator

The next question is from Ralph Hebgen with KBW. Please go ahead.

Q - Ralph Hebgen {BIO 6297020 <GO>}

Hi, guys. Thanks for taking my question. I've got two things. One is going back to the Z-ECM ratio. George, it would be helpful if you could give some additional color perhaps on the sensitivities there. I'm still surprised to see the ratio actually going up from the level you reported. And equity markets haven't been good in the fourth quarter. The spreads have slightly increased. So that would be helpful.

And also perhaps if you could do that in the context of slide 123 disclosed at the Investor Day in May, where you put the retention of excess capital into the context of the Z-ECM ratio? And there you basically say that any Z-ECM ratio below 115% would urge you to retain excess capital in the company which, of course, you have just done.

So the second part of the question is looking at the current market turmoil and the commensurate volatility of the Z-ECM ratio, are you planning to take any of the actions outlined on the slides which are moderate de-risking and moderate hybrid issuance?

And second is just a simple confirmation. You were breaking up earlier. I couldn't quite understand when you were outlining your estimates of the building blocks of how much excess capital might be available now. I'd appreciate if you could just perhaps repeat that assessment. Thank you.

A - George Quinn {BIO 15159240 <GO>}

Yes. Forgive me, (56:42). I'll try and do this later, I think, page 123 from the Investor Day from memory. I mean it really wasn't intended to signal that 115% as the new threshold. What that slide was intended to do, if I remember it correctly, was give you a sense of how resilient we are to particular moves.

So to what you extent if there was a given market correction or a given combination of events, how might the company respond to maintain. It's strange, but it wasn't intended to signal that 115% was the new 110% or the new 100%.

On Z-ECM, just to give you a bit more color. What's the caveat is what we're talking about now is an estimate rather than the official number.

From what we've seen, we see a relative small increase on the available financial resources, and we have a reduction under required capital size. So, I guess the required capital is a bit – I guess it would be much more difficult for you guys to see clearly from an external perspective. And obviously, some of what Kristof has been discussing already is part of what contributes to that.

So, I mean, without me being particularly precise, we expect to see to see a Z-ECM ratio when we print the SST1 for 2016. It's higher than the last number of 114%. Again, up a half of the range. It will be impacted by what happens in this year. So, for example, the volatility in the markets that we've seen. Again, you have sensitivities on equities and spreads at the back of today's investor presentation.

So, again, assuming that that stage is/was, you see it come back down again. But I'll try to give you a sense of where we were end of last year. As far as flexibility goes, the – I mean, the way to think of that is that S&P is still the constraining factor. We've indicated that we were projecting in excess. We've given all the things that we have done and are planning to do of $3 billion. We've obviously spent part of that on the two acquisitions that took place in the fourth quarter, the largest by far being the acquisition of RCIS, in combination is about $800 million. And on top of that, the capital generated by the group in Q4 was much less than expected. And that's a combination of the performance in GI and thus, accelerating some of the restructuring.

And then, if you look at that, I mean, roughly – and we produced our lowest for shareholders of around $400 million versus, let's say, a broader expectation that it should have been around the $700 million mark. If you take both of those and compare it to the $3 billion, it gives you a very good sense as to where we currently project the flexibility to be.

Q - Ralph Hebgen {BIO 6297020 <GO>}

That's great. Thank you very much, George.

Operator

The last question is from Vinit Malhotra from Mediobanca. Please go ahead.

Q - Vinit Malhotra {BIO 16184491 <GO>}

Hi. Good afternoon. Thank you very much for this opportunity. The first question is just, I noticed the NAC has grown quite strongly in fourth quarter as well. And then also – and also in 3Q, is this what, Kristof, you meant by saying that while GC is going to not grow, but there are other areas which are strong? And I'm just wondering how comfortable you are that we're not creating another problem a few years later, so just how the NAC growth?

And second thing is just the – sorry to come back – but clarification on this comment that excess capital is not to be returned. In a situation that the turnaround happens to what you would like, is that opportunity, is that going to come back as a sort of a way to deal with that excess capital? Thank you.

A - Tom de Swaan {BIO 1702205 <GO>}

Right. As far as the last question is concerned, I find it very difficult to predict these kinds of things over a long-term ahead. But I will look at this year, clearly, this decision not to return capital stands where we move in the next couple of years, we'll see how the business develops. And what that means for as far as capital is concerned.

Q - Vinit Malhotra {BIO 16184491 <GO>}

All right. That's very clear. Thank you.

A - George Quinn {BIO 15159240 <GO>}

Just very briefly on NAC. I know we're showing a headline number of 7% growth for the full year 2015. All of that growth was driven through captives. Top-line number – the underlying number is closer to 3% which is a number that I'm comfortable with.

Q - Vinit Malhotra {BIO 16184491 <GO>}

All right. Thank you very much.

Operator

I would now like to hand over to Mr. James Quin. Please go ahead.

A - James Quin {BIO 18345789 <GO>}

Okay. Well, thank you very much to everybody for dialing in. Of course, if you do have any questions, then do call Investor Relations, and that we'll see some of you next week. Thank you.

Operator

Ladies and gentlemen, this concludes today's Q&A session. Thank you for participating and wish you a pleasant rest of the day. Good-bye.
