Q3 2017 Earnings Call

Company Participants

- George Quinn, Group Chief Financial Officer
- Richard Burden, Head Investor Relations & Rating Agency Management

Other Participants

- Andrew J. Ritchie, Analyst
- Andy Hughes, Analyst
- Arjan van Veen, Analyst
- Farooq Hanif, Analyst
- James A. Shuck, Analyst
- Johnny Vo, Analyst
- Michael Huttner, Analyst
- Nadine van der Meulen, Analyst
- Thomas Seidl, Analyst
- Vinit Malhotra, Analyst

MANAGEMENT DISCUSSION SECTION

Operator

Ladies and gentlemen, good morning or good afternoon. Welcome to the Zurich Insurance Group Q3 Results 2017 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. Richard Burden, Head of Investor Relations and Rating Agency Management. Please go ahead, sir.

Richard Burden {BIO 1809244 <GO>}

Good morning, good afternoon, everybody, and welcome to Zurich Insurance Group's third quarter 2017 Q&A call. On the call today is our Group CFO, George Quinn. But before we start with the Q&A, George will just make a few introductory remarks. I'll pass it over to you, George.

George Quinn {BIO 15159240 <GO>}

Thanks, Richard, and good morning and good afternoon, everybody. And thank you, again, for joining for this Q3 call. So before we move to the Q&A, just a few initial remarks.

First, as you know from our comments at the half year results, we've changed disclosure for Q1 and Q3, with the emphasis now on revenue trends and some qualitative commentary on the performance of the business. We'll refer to a customer (01:22) level of detail the full year and the half year.

Over the third quarter, we've continued to address our group strategy, despite the challenging backdrops of the natural catastrophe events that we've seen this quarter. I'm pleased to say that our focus on underwriting discipline and the use of re-insurance to manage our overall exposure have served us well on the quarter with the pre-tax losses from the three hurricanes coming in at $700 million, a level which we see as positive for a group of our size in the U.S. market.

Looking forward, we expect the industry losses to drive improvements in pricing across our business. As we highlighted in the previous press release, these losses will only have a relatively limited tax offset, which will naturally lead to a one-time increase in the overall effective tax rate for the year.

Away from the hurricane-related losses, we continue to see improvements in retention and new business across all of our businesses. P&C, the business has returned to growth with gross premiums up by 1% on a like-for-like basis, and we continue to make progress on costs while continuing to focus on further underwriting improvements.

Our Life business continues to deliver on our strategy of focusing on capital life and protection business, with this continuing to support good growth and new business value. Farmers continues to deliver steady positive performance in terms of top line development as the focus on rates continues to drive premium growth. The quarter has also confirmed our very strong capital position with a Z-ECM ratio further improving to 136%, providing us with significant capital flexibility.

We continue to review the capital levels of the business in light of growth opportunities and the macro outlook. However, our near-term primary focus remains on delivering on a dividend policy and growing the dividend over the planned period.

Before turning over to Q&A, I'll just also highlight that as we had communicated the first half results, we expect approximately $150 million of the $500 million anticipated restructuring charge for this year to come through (03:51) with this largely impacting the P&C non-technical result.

With that, over to Q&A.

Q&A

Operator

We will now begin the question-and-answer session. The first question from the phone is from Vinit Malhotra from Mediobanca. Please go ahead.

Q - Vinit Malhotra {BIO 16184491 <GO>}

Yes. Good afternoon. Thanks for taking my question. Just, George, there was this comment in the press release, which said additional efforts required on underwriting goals, is this – and in the context of your comments just now, should we interpret it that is all things are same as they were at 1H or are they better or are they worse? Any commentary on the underlying trends linked to that?

And second question is just on the Life. I mean, there's been two or three quarters now as Life's delivered and beaten consensus and our expectations on operating profit, and new business value looks a very high growth as well in the third quarter. Could you just comment a bit about how we should think about the Life as well (05:20)? Thank you.

A - George Quinn {BIO 15159240 <GO>}

Thanks, Vinit. So, on the first point, I think the challenge here is simply that at a (05:30) relatively late press release today that focuses mainly on revenue trends. And I think this comment, I think, has been picked up by a number of people and probably given significantly more weight than we had intended.

I mean, probably the most important thing I'll say on the call today is that our targets and our expectation of achieving them is unchanged. I mean, that comment simply reflects the fact that we're nine months through the year with three more months to go.

On the Life side, I'm going to apologize in advance, and this may happen a few times during the call that, I mean, obviously, you'll understand that I cannot talk about our Q3 performance. Life had a strong six months, we've seen very good performance in new business value during nine months. If you look at the drivers, I mean, certainly the mix has helped this growth, particularly in some of our higher growth markets, has been an important contributing factor. So I mean, we're very happy with the progress that Life had made. But again, just to remind people that at the half year, the guidance that we gave for our quarterly operating profit expectations around Life was, I mean, somewhere in the high $200 million to around $300 million per quarter mark.

Q - Vinit Malhotra {BIO 16184491 <GO>}

All right. Thank you very much.

Operator

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

Q - Thomas Seidl {BIO 17755912 <GO>}

Yes. Thank you. Good afternoon. Three questions. First is on the cat losses. Could you give some color what were the main sources for those cat losses in terms of type of clients, was it SME, was it the large corporate space? That will be quite helpful, I would say. Secondly, and maybe related to that, you say you expect price increase across the business. So, precisely in what segments and what magnitude of price increases would you expect?

And thirdly, on Farmers. Obviously, Farmers got a big help from the re-insurers, which what one can hear in the market, leads to very high price increases in the re-insurance. Does this mean that Farmers has to significantly up its prices for 2018?

A - George Quinn {BIO 15159240 <GO>}

So the last piece, Thomas, what was the question?

Q - Thomas Seidl {BIO 17755912 <GO>}

The last piece was Farmers got, of course, a huge protection from reinsurance, and this would lead to substantial rise in the reinsurance cost, my question is in order to sustain margins, does this not mean Farmers needs to dramatically increase prices into 2018?

A - George Quinn {BIO 15159240 <GO>}

Great. Thank you. So on the first one on cat losses, I mean, very much across the board, the main source for all three of the events is the large corporates, I mean, probably as you would expect. I mean, we don't have a lot of SME business in the U.S. book, but depending on a particular event, you'll find significant amounts of large corporate and mid-market and some alternative market business in all three of the loss events.

On the price increase topic, so, as you saw on the press release this morning, I've commented that, I mean, we expect this to drive improvement across the business. I think if you look at it in terms of, I mean, where will you see it most, where will you, probably, see it less, I mean, within our U.S. business, we've already issued a new target guidance certainly for all the property underwriters and we have price increase expectations that start with even non-cat, non-loss-affected lines of business. And again, as you imagine, as you go up to the categories that was (09:22) loss affected, we have expectations of much more substantial rises.

If we look at actual price action in the market, I mean, we do see price increase start to go through already. I mean, certainly for that top group, I mean, both for what we see of us and what we see of other activity in the market, I mean, pretty substantial double-digit rate increases already going through. There is some anecdotal evidence that it already has an impact on other non-property lines. My expectation is the further you move away from, I mean, the precise source of the loss, the less pronounced the impact will be on pricing, but we do expect to see price improvements.

On Farmers, where the speculation in the market is that, obviously, Farmers hasn't said (10:17) so there's no official announcement from Farmers about their reinsurance program. So I won't comment on, I mean, the extent to which the market speculates, on what the rate increase may or may not be for Farmers. What I will say is this. I mean, Farmers from a cat perspective, if you look at the premium they spend on cat cover as a proportion of the total premium volume, it's a relatively small number.

So even if you apply quite a large percentage to that, you end up with a large percentage of a relatively small number, which in itself is a small number. So, I mean, we'll see how things turn out for Farmers, but certainly I don't have signals from the exchanges of the team there. They expect this to be, in any way, a challenge for them.

Q - Thomas Seidl {BIO 17755912 <GO>}

Okay. But the premium spend is small, but - I mean, can you remind us what the recovery was for Farmers, was very substantial now from a reinsurance?

A - George Quinn {BIO 15159240 <GO>}

Yeah. I mean, you used to work for reinsurance companies. You know how it works, Thomas.

Q - Thomas Seidl {BIO 17755912 <GO>}

Yeah.

A - George Quinn {BIO 15159240 <GO>}

You know what the capacity is. You can play a guess what a reasonable rate online (11:32) is, and you could determine a reasonable number for the premium, and then you could tell your view of what the market rate increase will be. I mean, (11:39) the premium volume that Farmers raise (11:41) I wouldn't expect that to be a massive number.

Q - Thomas Seidl {BIO 17755912 <GO>}

Okay. Thanks a lot, George.

Operator

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

Q - Michael Huttner {BIO 1556863 <GO>}

Thank you very much. The - I was thinking to say (11:58) great results but then no results today. So what I would like to say is my disappointment to do the (12:02) level of disclosure? And then my view as you compete with (12:07). Anyway, on my question - I have three. The first one, you just said there was a - this new (12:16) book. And I just wondered what the impact is in terms of Solvency and profit?

The second is on tax. I think we've had this in the past that high losses create high tax charge or less tax recoveries however you look at it, and there seems to be an asymmetric problem and an asymmetric issue (12:37) good years of taxes average and bad years in terms of no profits, the tax rise, the tax goes up, the tax rate or the lack of tax recovery works against you. And I just wondered if you're planning to do anything about it or is this something which will continue as a trend (12:55)?

And then finally, you highlighted the return to growth in Q3 in (13:03) and I just wondered whether you can say a (13:05) where it is and how much is pricing and how much is mix kind of to get a feel for the improvement there. Thank you.

A - George Quinn {BIO 15159240 <GO>}

Thanks, Michael. It was a wee bit hard to hear you at the start, but I think you asked me about the Solvency and profit impact from the recent bank (13:24) book transaction.

Q - Michael Huttner {BIO 1556863 <GO>}

That's correct, yes.

A - George Quinn {BIO 15159240 <GO>}

The perceived tax asymmetry of the cat events (13:26) and then the source of growth that we've reported towards that.

Q - Michael Huttner {BIO 1556863 <GO>}

Yes. Exactly. Thank you.

A - George Quinn {BIO 15159240 <GO>}

So, on the – the German transaction was announced yesterday morning. I mean, relatively immaterial impact for both. I mean, the book is relatively small, diversifies well within our overall portfolio. I mean it's not going to be particularly material either from an operating profit perspective, nor from a capital perspective.

On the tax asymmetry issue, I think the challenge here is I don't think a tax asymmetry actually exists. And what you see at the moment is, I mean, principally because of some of the things we're doing from a restructuring perspective and the fact that most of that falls on the parent company here in Switzerland, our tax rate is elevated because of that, we don't get full recovery of that restructuring cost. And what that does mean at the moment is that, I mean, anything unusual that pops tends to attract that same zero tax rate.

If you look at the cat component on its own and you look at it over longer periods, I mean that part of our structure does exactly what we expect it to do. I think I'm less concerned about the asymmetry, maybe slightly more concerned about the volatility that it drives. I mean, we have the challenge that, I mean, in most circumstances, tax will act as a dampener on our results overall. And in our case because of the structure we have, it doesn't do that. And that is something we do intend to look at.

On the growth topic, so if you look at the movements, I mean, the headline number is really quite small. So it's – I mean, you don't have the impression of businesses growing very rapidly. But if you break it apart, though, I mean – but personally, I see a much more positive picture. Within that, we have been trimming some of the more challenged line of business, which would be typically more in the North American commercial corporate side of things. And through the year, we've been growing some of the businesses that are more stable, that tend to have lower loss ratio, tend also to have a higher commission ratio, but in general more profitable and more predictable than the business they replace.

So, from a growth perspective, we see more of that in the alternative markets side of things, so the F&I book in the U.S., we've seen it in Latin America in mass consumer. I mean, in this quarter, one of the contributions comes from us, recapture some of the premium from the Cover-More travel deal. So the headline number up modestly within there, actually much more activity, and more importantly a mix shift that, from a longer-term perspective, is beneficial for us (16:07).

Q - Michael Huttner {BIO 1556863 <GO>}

Okay. And in terms of the mix shift, is it captured in your 1% rate increase number?

A - George Quinn {BIO 15159240 <GO>}

So the mix shift is caught and the – so the rate increase that we quote for the quarter reflects the book that we have. It's not a market view.

Q - Michael Huttner {BIO 1556863 <GO>}

I know it's an effective book that you have, but the book has changed. So I did do economics, but I forgot completely how you change (16:55) things where your basket changes. Clearly, the basket has changed (17:01), so I'm asking not relative to the same basket but relative to Zurich, has it – is that an improvement more than the 1%?

A - George Quinn {BIO 15159240 <GO>}

The rate change is like-for-like, so it's the retained book. So that won't include the impact of new business. So to the extent that we are – we're shedding business that is less profitable and adding business that we see as more profitable, that's not reflected in the rate change.

Q - Michael Huttner {BIO 1556863 <GO>}

And could you maybe give a feel for that?

A - George Quinn {BIO 15159240 <GO>}

Not here right now, I couldn't.

Q - Michael Huttner {BIO 1556863 <GO>}

Okay. Thank you.

Operator

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

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

Oh, hi, there. Back to the exciting topic of tax, George, I wonder if you've looked at the proposed tax reform. I appreciate it's a long journey from proposal to finality. Obviously, there is a sort of (17:56) bill hidden within them. Do you have a view as to what potentially that could mean for Zurich or what mitigating actions you may have to take?

The second question, the U.S. P&C result season has been littered with quite a lot of volatility in underlying loss experience, ex-cat across a number of lines, continued problems in areas particularly like commercial auto. Maybe you could just sum up how you're seeing the underlying loss experience ex-cat across the commercial books especially North America, and I wonder if that's requiring even more aggressive action or does it change any of your views on PYD. Thanks.

A - George Quinn {BIO 15159240 <GO>}

Yeah. Thanks, Andrew. So first of all, on the tax reform topic, I mean, you're absolutely right that the topic is clearly developing and potentially (18:53) changing before we reach some conclusion. I think, I mean, overall we would support tax reform. It's important to recognize that together, Zurich and Farmers, employ more than 30,000 people in the U.S., so we have a keen interest in what takes place there.

From an overall perspective, I mean, we'll see how it all aligns. But, I mean, I would say here what you would expect to hear from me, and that's that to the extent that final proposals adopt features that make the manufacturer of the product, in our case, insurance protection, which, of course, is an important enabler for economic growth, I mean, that's problematic. I mean, we would prefer not to see that. I think today, I mean, it's too early to reach any conclusions at this stage. We'll have to see how the – that proposal develops, and then at the end of that process, we can draw conclusions.

On P&C and the performance reported by Q3 peers or Q3-Q4 peers (20:07), I can't talk about our other (20:07) performance in the quarter. Maybe what I can reflect on is, I mean, what we see from a rate perspective and what that means, if anything, for the future.

I mean, overall, if you look at rates for the group, we've actually seen an improvement, I mean, a relatively small one and rate change in Q3, so a slight improvement over where we were at Q1 – Q2, slightly behind Q1.

Within that, I mean, where you see the strongest improvement is Europe. LatAm and APAC also much stronger rate than we saw in either Q1 or Q2. Where things are weaker is North America. So, we would see rate in North America, as of Q3, as slightly negative.

If you look at the lines of business, Property, if anything, is actually slightly better; liability, slightly worse. Motor, better than Q2, similar to Q1, still not really a level that is transformational for motor. Specialty, I mean, around the same type of level, and workers' comp is the one that, again, has shown further slippage over where things were at Q2.

Within the other businesses, within Europe, I mean, the improvement is actually mainly driven by the UK, so we see commercial business and in particular, motor, showing strong improvement. I mean, the other European businesses, generally, are in similar places to where they were at Q2. LatAm and APAC both slightly up to reasonably strongly up. So overall picture for us as a global P&C business, slightly better than it was at Q2. But the U.S. has suffered, while our other markets have improved over the period. From a PYD perspective, today, I don't see any of that driving any change in PYD expectations.

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

Okay. Great. Thank you.

Operator

The next question comes from James Shuck, Citigroup. Please go ahead.

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

Oh, hi. So, yeah, it's James Shuck here from Citi. I had two questions, please. George, I appreciate you can't speak about the third quarter but I just wanted to come back to the issue of the large losses. You kind of moved to this kind of approach with large losses and saying it's kind of up a bit or down a bit versus the prior year. That's what you did at Q1, which was a bit better. I think in Q2, that was a bit worse.

If I kind of roll back a bit and look at what Tom de Swaan mentioned in 2015, he mentioned that large losses were 4 points above normal in 2015. So, if I take 2016, which was 160 bps better than 2015, then the implication is that 2016 is about 240 basis points above trend. And then, kind of H1's overall still seems to be running a bit high. So, my question is kind of can you give a little bit more clarity please about where the large losses are versus a normal run rate at H1 without necessarily commenting on Q3? That's my first question.

Secondly, on your own reinsurance protection, so you, obviously, exhausted the aggregate cover as a result of the hurricanes. Could you give a little bit of insight into what your outlook is for reinsurance buying, whether the structure of it is as you would want it to be, whether the cost of it is as it might be? And kind of connected to that, you're effectively running naked into Q4 in terms of large losses with no aggregate cover or did you buy more? Thank you.

A - George Quinn {BIO 15159240 <GO>}

Yeah, hi. Thanks, James. The first question was a bit complicated. It may require actually for us (24:26) to be face to face or (24:28) in my head. I think on large losses, I mean, through the first half, I'm not sure I saw any significant deviation from roughly where we would expect to be. There's been a huge improvement over that part of the performance compared to 2015.

I think I talked about it a bit on the Q2 call, and in fact it's something I plan to say a (24:58) bit more about at the Investor Day. Maybe I'll cover in a bit more detail later if you don't mind, and I'll save the response for when I actually have something concrete in front of me that I can discuss with you.

But I mean today, I think I said on the Q2 call that I don't worry about large loss per se. I mean, it's more focused on driving the overall underwriting improvement that we want across the entire loss experience that we have, including attritional.

On our own reinsurance protection, from an outlook perspective, I mean, I think the most important thing in this market is to try and be reasonably consistent over time. I think in the past, you've seen that one of our challenges has been that we've typically bought reinsurance protection for the balance sheet and very little from an income statement perspective.

One of the changes that we made starting at the end of 2015-2016 was both around trying to protect against some of the volatility that we saw, but at the same time, making sure that we reinvested the savings that we saw from relatively softer reinsurance market by taking core (26:14) participation, dropping retentions and doing those kind of anti-cyclical things that over time will benefit the company.

I think the good news is, you can see the positive impacts of that already in the Q3 losses that we've reported for the three hurricanes. I mean beyond that, there's also a risk appetite topic reflected in there that, I think, has been clear for some time that property cat (26:42) in the U.S., has been problematic. And I mean, we have substantially reduced our exposure to that topic either incoming (26:48) or through these tactical reinsurance before we even get to the cat program.

So we would look for stability around the main cat programs, so I look as far as possible to renew it in a similar structure to the one that we have today. I think the area of question mark that we still have in our own minds is the volatility cover that we have, well, from a good news perspective, it hasn't attached, so that won't always attach, but I think we like to look at that to make sure that that money is working effectively for us most (27:28) effectively as it can.

So I mean as we run into the renewals, we're not (27:35) looking to shift the program significantly. We'll see what the market offers. But – I mean, the program we have to today reflects mainly our preferences and more or less, that's what we'll be looking to buy as we go through the process.

On the aggregate topic, I mean we're not looking to try and (27:56) at this point in the year. I mean, we, obviously, still have cat parallel (28:01) protection. The covers that we have, I mean, are typically one plus one (28:07) reinstatements. I mean, so only two of them (28:11) programs. One of them, it may do, I mean, we've set the expectation on that loss, which is Maria at the attachment point for the time being. So I think we still feel that we have reasonable amounts of protection in place for the remainder of the year.

But what it would mean is, for example, if we see a substantial U.S. event, we obviously have a substantial retention before it will attach the cat program.

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

That's very helpful. Thank you, George.

Operator

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

Q - Andy Hughes {BIO 15036395 <GO>}

Hi. A couple of questions, if I could. This - can I try the large claims on a different way, which is if we look at what everyone else has said about core London market business in Q3, they've all talked about the sort of AIG, QBE, RSA, also about lots of large claims in Q3 through London market and large commercial particularly ex the weather stuff. Is there any reason why you would be any different to this? And do you think this is just the market seeing what you've already seen in the first half of the year?

And then, the next question, I guess, is on the restructuring costs. So have you got quite a lot of restructuring costs still to spend in Q4, or have you done a lot of these changes already and should we expect a lot of announcements between now and the end of the year? Thanks.

A - George Quinn {BIO 15159240 <GO>}

So on the last one, first of all, Andy, so I can't say for (29:47) Q4. Also, I'm not talking about Q3 yet, (29:52) Q4 today. I think, I mean, just to give clear guidance of where we stood at the half year, I mean, we've indicated to people that we would expect to be no more than $500 million for the full year. That's still our expectation today. And of that $500 million, as I mentioned in the introduction, $150 million of that will drop into the operating results for P&C, within non-technical, just to keep it separate from the remainder.

Q - Andy Hughes {BIO 15036395 <GO>}

Sorry. The reason I was asking that one was just because I haven't seen any of kind of huge scale announcements in Q3 unless I've missed something, where you sort of (30:32) indicated a large amount of restructuring cost occurred in Q3.

A - George Quinn {BIO 15159240 <GO>}

I could only restate the answer I gave you to the question.

Q - Andy Hughes {BIO 15036395 <GO>}

All right, okay. No problem.

A - George Quinn {BIO 15159240 <GO>}

On the large claim topic, I mean, I can't comment on Q3. And it's, obviously, relatively difficult for me to do the relative comparison because I don't know what the others have in their portfolios. I think on the Q3 topic, I'd go back to what I said to James a few moments ago and say that, I mean, obviously, large losses were a real problem for us in 2015.

As I said in Q2, I mean, we've had - as James put it, I think, a bit up, a bit down, or maybe even a bit down and a bit up to get the right order. But we've seen a huge improvement over where we stood in 2015.

Again, I will talk about this a bit at the Investor Day. I'll look back over some of the historical experience and certainly recap where we were at the end of Q2 and give a view of how we intend to manage the topic going forward without talking about Q3 and Q4. I'm afraid that's the best I could do to you today on large claims.

Q - Andy Hughes {BIO 15036395 <GO>}

All right. Thank you.

Operator

The next question is from Arjan van Veen from UBS. Please go ahead.

Q - Arjan van Veen {BIO 5197778 <GO>}

Thanks. George, a couple of questions on, firstly, the legacy sales. You mentioned before the German legacy medical mal portfolio wasn't particularly material, but can you comment a bit more holistically about this portfolio?

And so, firstly, is there more of a plan to offload more of these? Obviously, there's one large one in Europe that's been in the press (32:17). And also is there capacity for executing on these deals to free up some capital?

And then second question, just a bit more sort of dig down into the European. You commented on the U.S. quite - just quite a lot. Could you comment a bit about volume trends in some of your core markets in Europe? In particular does (32:42) the comment that you made about pricing improvements across the portfolio going forward, how much of that applies to Europe?

A - George Quinn {BIO 15159240 <GO>}

Yes. Great. So, on the legacy topic, I mean, our aim for the legacy (32:58) it. It's obviously not causing us issues currently, but it ties up capital that we would quite happily redeploy somewhere else for a more attractive return.

Again, there's been a lot of press speculation, which I'm going to avoid commenting on, other than to say that I think you guys have a reasonable sense of what's in there. So we have a number of typically long-tailed lines, the largest of which is the UK EL book. I mean, none of these things are there to be (33:35) to the expiry of the last claim. But we're rather (33:38) looking for better homes for this business, if we can find it. I mean, we'll take our time to try and maximize the trade-off between price certainty and all of the key drivers.

But it's certainly our intention that we will dispose off all of this. We're not looking to retain any of it. So, I would expect over the course of the next year, 18 months or so, that you'll see more activity. I'm not expecting that to cause any significant P&L volatility. But I do hope to see some reasonable capital release from it.

On the European topic, so maybe just on the pricing topic to begin with, so, again, on the various markets, I mean, compared again to where we were, say Q1, Q2, I mean, Switzerland is similar to where we were at Q2. Germany is similar, slightly better. UK is the one that stands out. As I mentioned earlier, we're seeing a pretty substantial pick-up, particularly driven by the motor side of the book. Italy is slightly stronger. Spain, similar to what it was, maybe slightly weaker, but again, a relatively high level. I mean, Spain is one of our top three markets from an overall perspective.

If you're looking at growth, I mean, Europe overall, from a GWP perspective, headline number is down 5%, so that's local currency. If you adjust for the disposals that we announced last year, down 2%, and the main reductions there are small movement in Switzerland, small movement in the UK given that the market was weaker earlier this year and, of course, a slightly more competitive environment in Italy around some of the retail lines. But, I mean, good rates and slight reduction in volume.

Q - Arjan van Veen {BIO 5197778 <GO>}

Okay. Thanks, George.

Operator

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

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

Good afternoon. Thanks for taking my questions. You've been asked this many times, but the Z-ECM continues to improve and strengthen. It's now at 136% and it's over $6 billion above the upper end of the target range. Could you once more (36:13) comment on the potential use of excess capital? Could you comment on that? Should the range be revised upward, perhaps, if you're more comfortable with the higher level?

And in that light, just asking about the dividends, to the extent that you can or will comment on it, the policy of 75% earnings payout or CHF 17. You commented in the past that the dividend is based on forward-looking earnings. And given this group capital strength that continues to get stronger and expected earnings growth, is there a possibility of having a temporary payout ratio above 75% even this year despite the large loss that we've seen this year?

And then lastly a quick one on the Ogden rate. Should there be a revision of the Ogden rate next year from minus 0.75% to between 0% and 1%, what would be the impact of that in light of the additional reserving (37:16) that you did earlier in this year? Thank you very much.

A - George Quinn {BIO 15159240 <GO>}

Thanks, Nadine. So on Z-ECM, we've seen a relatively modest move up. We estimate around 136% end of the quarter. I mean today, no change in the commentary that you had from us in Q2. So a key priority for us remains operating performance and what the improvement in operating performance will do for the dividends. That's priority number one, two and probably three and four as well. We'll evaluate capital positions as we (37:55) the end of the year, but the priority is operating performance and ordinary dividend.

On the dividend growth topic, I mean this is an important point. I've said a couple of times this year already that when the PR (38:10) policy needs to reflect sustainable earnings, I mean, it can't be based on earnings that are temporarily boosted by an absence of natural catastrophes nor should it be depressed by the temporary occurrence of excess natural catastrophes. Also, frankly (38:29), restructuring impacts such as Ogden and associated tax effects, I don't believe are relevant in assessing the group's ability to move the dividend. So what matters for us is that underlying sustainable level, so that when we move the dividend, that becomes the new floor for the group.

On the Ogden topic, I mean, it's another great question. So it's not entirely clear at least today, I mean, when any change might take effect. But in any event, as you point out, I mean we've absorbed a significant part of the impact of Ogden through the six months either through reserve strength and – or through offsetting stronger PYD. That would mean that in the event that we see a positive sort of a reversal of all the part (39:35) of the Ogden change, you should not anticipate to see that impact the P&L. So I would return that to the group's overall reserve strength.

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

Thank you.

Operator

The next question is from Johnny Vo from Goldman Sachs. Please go ahead.

Q - Johnny Vo {BIO 5509843 <GO>}

Yeah. Hi. Just a couple of quick questions. Just in regards to – obviously, you've shown improvement this year and you said that you feel like the underlying combined ratios is around about 98%. And given the fact that rate increases are improving across the book, particularly in the U.S. and it's providing a bit of a tower end (40:12), do you see these rate rises as sustainable or more transient? That's the first question.

Just coming back to capital as well. Obviously, the capital is - or the Z-ECM is at 136%, the organic capital generation is 3% to 4% (40:27) per quarter. So you're going to be rolling north of 140%. And not in relation to dividend, as you said, dividends are more linked to sustainability, but if the capital position is very, very strong, do we look beyond dividends to other forms of capital returns above 140%?

And then, the final question, just in terms of the UK. I noticed that you've disposed of the workplace pensions sort of business. You have some other chattels and platforms in the UK. Does this mark an exit from the UK sort of discretionary wealth market? And what are your thoughts on that? Thanks.

A - George Quinn {BIO 15159240 <GO>}

Thanks, Johnny. So the - on the rate increase topic, I mean, just to remind everyone that, I'm talking about the rate side of it. We haven't discussed the inflation topic. Normally Thomas will ask me about what's happening on the inflation side of things. We would still see even with this improved rate performance in Q3 that margin is eroding. And in fact, that's what we allowed for when we put together the targets last year. So it's a - I guess, maybe it's a smaller negative...

Q - Johnny Vo {BIO 5509843 <GO>}

Yeah.

A - George Quinn {BIO 15159240 <GO>}

...and to try and characterize it correctly. On the UK - sorry, the capital topic, I mean, that's (41:44) asking the same question that was asked earlier. I'm not going to say more on that topic than I've said already. I can't add anything to the comments that I have made particularly to Nadine.

And then on the UK topic, I think it's the first time I've had the UK business described as having chattels. I haven't used that word in any conference call so far in my career. I mean, this book in particular was one that suffered from a scale issue, obviously, the buyer has that scale, can benefit from the additional volumes that it brings. So I mean, I wouldn't look at this as signaling some broader read across. If you looked at our portfolio in the UK, that corporate savings business, not just for us, but for the entire market, has been particularly competitive and that's what led to that decision on the transaction.

Q - Johnny Vo {BIO 5509843 <GO>}

Okay. Thank you.

Operator

The next question is from Faroog Hanif, Credit Suisse. Please go ahead.

Q - Farooq Hanif {BIO 4780978 <GO>}

Hi, there. Thanks very much. I was going to ask the inflation question. So I might stop with just one (42:58). Just on everything you said, so inflation rate, change of mix, are you still looking for basic outstanding (43:11) the underlying loss ratio or do you think we will – we could, I mean, without making specific forecast but we could see some improvement in underlying loss ratio if current conditions persist? That's question one.

Question two, going back to capital, at H2, you gave some sort of math on the constraining capital with the rating agency and how that's aligned with Z-ECM a little bit. Obviously, some of the Z-ECM move is pension-related and it might be Life-related. I'm just wondering whether you think any of that math has really changed. So, I recall at 2Q you talked about a $2.5 billion surplus versus the real constraints that you have.

And last question, very quickly, what's happening to earned premium? So, we've got the GWP. Are there any sort of things we need to take into account in 3Q qualitatively? Thanks.

A - George Quinn {BIO 15159240 <GO>}

Thanks, Farooq. So, on the inflation topic, this issue – I mean, what can we expect? I mean, I think it's difficult for me to make any predictions other than the ones you've heard from me in the year so far. I mean, Richard and the team asked our U.S. team last night to provide updates on what they see in the market. So, I mean, of the (44:42) anecdotal information, that would imply something more positive. But I don't really have something that's systematic in my hands yet. So, therefore, I'd be cautious about predicting the scale of what we might be able to see from the market movement in the UK.

But I think, I mean, if I look at it objectively, given what we've seen from the hurricanes, given the comment that we made this morning in the press release, you would expect to see tailwinds around the technical performance, which probably replaces, I mean, the headwind trend that we saw, too early to quantify that in any way meaningful, I think, today.

It's a good question on the capital topic. I think I said on the Q2 call that this was a capital equivalent of a solar eclipse, and have been like a solar eclipse, it doesn't last forever. So I think (45:40) back to the commentary I gave you at Q2 for a sense of roughly where we are from a flexibility perspective. On the end (45:51) premium side of things, I mean, no change to guidance, so we expect the end (45:53) premiums to be broadly flat for the year.

Q - Farooq Hanif {BIO 4780978 <GO>}

And, sorry, just following up on that. That's broadly flat in like-for-like terms ex-FX or just broadly flat numerically?

A - George Quinn {BIO 15159240 <GO>}

Broadly flat numerically.

Q - Farooq Hanif {BIO 4780978 <GO>}

All right. That's brilliant. Thank you very much.

A - Richard Burden {BIO 1809244 <GO>}

Thank you. That was our last question on the call today. Thank you very much, everybody, for dialing in. If you do have further questions, please don't hesitate to call the Investor Relations team, and we'll be happy to answer them. Thank you and goodbye.

Operator

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