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Y 2019 Earnings Call

Company Participants

- George Quinn, Group Chief Financial Officer
- Mario Greco, Group Chief Executive Officer
- Richard Burden, Head of Investor Relations

Other Participants

- Andrew Ritchie, Analyst
- Farooq Hanif, Analyst
- James Shuck, Analyst
- Jon Hocking, Analyst
- Jonny Urwin, Analyst
- Michael Huttner, Analyst
- Niccolo Dalla Palma, Analyst
- Nick Holmes, Analyst
- Peter Eliot, Analyst
- Vinit Malhotra, Analyst

Presentation

Operator

Ladies and gentlemen, welcome to the Q&A Analyst Conference Call and our results 2019. I am Shai [ph], 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. The presentation will be followed by a Q&A session. (Operator Instructions). 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 Agencies. Please go ahead, sir.

Richard Burden {BIO 1809244 <GO>}

Good morning, good afternoon, everybody. Welcome to Zurich Insurance Group's Full year 2019 Q&A call. On the call today is our group CEO Mario Greco; and our Group CFO, George Quinn. As usual for -- the Q&A, we kindly ask you to keep to a maximum of two questions. And if we have time, we will come back to further questions later in the call.

But before we start with the Q&A, Mario will make a few introductory remarks to the results. Mario, over to you.

Mario Greco {BIO 1754408 <GO>}

Thank you, Richard. Good morning, good afternoon to all of you and thank you for joining us. Before we get into the questions, let me just give you a few remarks from my side. As you know in 2016, we set ambitious targets and we launched a bold new strategy and we have executed fully on them.

BOP is up 16% in the past year, and the BOPAT ROE of 14.2% is well above the target and so are the cost savings and the net cash remittances. In addition to the financial delivery, Zurich is now simpler, more efficient business, with the stronger operations worldwide, with more engaged employees and higher levels of customer satisfaction.

The performance of our Property & Casualty business has been particularly pleasing, with the business showing stronger growth in premiums as well as an improved underwriting performance and reduced volatility. The improvement in the accident year combined ratio before natural catastrophes shows the actions that we have taken to change the mix of the business and improve the quality of the portfolio were the right ones. These have also positioned us well relative to the industry, in terms of the current inflationary pressures. This is especially the case in our commercial business, where discipline and focus has driven significant improvement in profitability in contrast to many of our peers.

Looking forward, we see the pricing continuing to improve and exceeding loss cost inflation, which will support both further growth in premiums as well as further improvement in underwriting performance. Our life business continues to perform well, with further underlying growth with headline results only held back by the strengthening of the US dollar.

Against the backdrop of ongoing low interest, we remain well positioned for further growth as a result of our decision to focus on protection and capital efficient savings product, ready over a decade ago. Both the Zurich owned Farmers' businesses and the policyholder on Farmers' Exchanges continued to grow successfully in the first half of the year. And in particularly, the Exchanges continued to successfully execute against the objectives aimed at enhancing the business as set out at the Investor Day in 2017.

Our balance sheet remains very strong, providing us with significant flexibility to further develop our business while allowing us to continue to reward shareholders through a further increase in the group dividend to CHF20 a share, Over the past three years, we have laid the strong foundations, together with our customer-focused strategy, and the further strengthening of both our product and distribution capabilities.

This gives me great confidence in our ability to meet the even more ambitious targets for the next three years that we presented to you in November last year. Thank you very much for listening. And now, George and I are ready to take your Q&A.

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Questions And Answers

Operator

We will now begin the question-and-answer session. (Operator Instructions) The first question comes from the line of Jon Hocking, Morgan Stanley. Please go ahead.

Q - Jon Hocking {BIO 2163183 <GO>}

Hi there, good afternoon, everybody. I have got two questions please. Firstly on workers' comp in the US. It seems that the sort of market commentary's to that line is seeing some softer pricing. Could you comment on what you're experiencing on that book and whether you're confident that the reserve release passing [ph] we've seen in recent years can continue there. That's the first question. And then, secondly, on the -- on the Life business, looking at the investment income, the reinvestment yield for the discrete second half, looked pretty low (inaudible) 3%. I was just wondering whether there's something distorting those numbers or is that a new run rate we should be thinking about using going forward in particular, given the different yields, year-to-date. Thanks.

A - George Quinn {BIO 15159240 <GO>}

Jon, it's George. So on the workers' comp topic, of all the lines of business, workers' comp in the US is the only one that really exhibits any kind of weakness. I guess, we'll come on to the others in some point later in the call. I mean, we still see a 1% to 2% reduction with an inflation both experience and overload [ph] that continues to be very benign. So I think I've said before on one of these calls, I mean, actually at this stage we would anticipate inflation, maybe slightly negative still around workers' comp. In terms of the fundamental trends that we've talked about on prior calls, I guess over the last 12 months to 18 months, no change on the workers' comp topic.

On reserve releases, so I mean we've, this has been another strong year for workers' comp for us is one of the drivers, but not the sole driver of the Group's overall positive reserve development. I mean, I could not promise you could extrapolate all of these positives into the future. I mean clearly the more recent years because of the pricing trends are going to be a bit more competitive and we need to see how the claims' partners develop.

But I mean, we've had a strong releases both last year, last year being '18 and '19. We've reinvested -- reinvested -- recycled most of that to strengthen reserves elsewhere. And our perception of our current workers' comp position at the end of 2019 is that the reserve position continues to be extremely strong. On the investment income topic, what happened, I guess, Germany interest rate thing happened, in general. So it has distorted a bit, because you did see a bit of a bounce back towards the end of the year.

But given the -- the book has a bit of a European bias to it, I mean, those kind of income -- those kind of interest rate moves can have an effect, although, where they typically relate more to what happens in the policyholder side of things than they do for the shareholder.

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Q - Jon Hocking {BIO 2163183 <GO>}

All right. Thank you very much.

Operator

Next question comes from the line of Andrew Ritchie, Autonomous. Please go ahead.

Q - Andrew Ritchie {BIO 18731996 <GO>}

Hi, there. First question, I think this is the same question I asked at the half year. When I look at the footnotes in the financial statements, you see a very, very low contribution on a pro forma basis from OnePath. Again, especially the second half. Could you just clarify -- appreciate there might be some restructuring in there, were there some reserve adjustments in there. Maybe just update us on the status of OnePath, actions you've taken and does -- what means for the future profitability.

Second question. On the commercial business, the clean combined ratio ex-cat, ex-POID [ph] was running about 98.6%[ph], I think in the second half. It's still improved year-on-year from the second half '18, will be at about 80 bps. Was there anything in the second half commercial? It was -- was there unusually high large losses or was there any -- did you take any opportunity to do maybe a bit more current year true-up on some of the more pressured lines by way of sort of additional conservatism. Thanks.

A - George Quinn {BIO 15159240 <GO>}

Thanks, Andrew. So on the first one and I think, I'm going to give you a very end of the answer I gave you when you asked me that question at the half year. So on one part, I mean we took over control of it at the end of May. I mean, we're in the process of integrating, it will require more restructuring than I think we anticipated.

Certainly, when we did the -- announced the transaction back in December of '17. I mean, at that point we had anticipated some deterioration in DI, but the market has seen more so that requires more activity by the team locally to bring it back to the profitability levels that we anticipated. There is a restructuring cost in it. There isn't any impact of reserve strengthening because the business is so new to the extent that we've seen any of that that's on the opening balance sheet.

Now in terms of forward guidance, no change to what I told you before. So I mean, we still expect to bring the business back to the path that we had indicated at the time that we did the deal back in December of '17, because it requires us to take certain actions. It will be a bit second half loaded again in 2020, as I mentioned last year. I mean the overall expectation that we have for it is the same.

The -- I mean I think that -- you know there is -- it's a more challenging environment than we anticipated. There are -- excuse me, we have a bit noise in the room. There are some other environmental factors that I think are actually quite positive. So, I mean, you'll be aware what APRA [ph] has been doing and the pressure that exerts around the whole DI topic. And in an overview, anything that encourages the market to separate DI from lump sum, and price each appropriately is a significant positive step. So we think that, I mean, actually the environment is conducive to the kind of changes that are required. But guidance on our expectation for OnePath for '20 remains unchanged.

On the commercial topic, so there is no real current year true up. We didn't go back and do the kind of things that we used to do three or four years ago, which is to adjust the entire year in the last quarter of the year. I mean the real -- I mean the things that cause challenges in the second half are actually, mainly property topics. So the the commercial business in more than one market has been impacted by property events and of course then that can happen.

So I mean, I think commercial continues to make progress, you commented on the fact that there is an improvement over the prior year. We expect to, given the price and loss cost outlook, that we have to continue to improve into 2020. I'm sure I'll come back to that question very soon.

Q - Andrew Ritchie {BIO 18731996 <GO>}

Sorry, George, would you say that the large loss, I mean, I think you've always been cautious of talking about large losses now, which is, the large loss is above a sort of normalized level or you don't want to go that far?

A - George Quinn {BIO 15159240 <GO>}

I'm not sure I'd go that far. I think the -- and I definitely don't want to talk about large. We just have more space through the -- in the second half of the year, we see more property coming through than we had. But I think that's quite a bit more than we saw in the first half and that's the real driver of, I mean, what you've seen from commercial. I guess the key point to reiterate is that we haven't done a current year true-up from the initial picks.

Q - Andrew Ritchie {BIO 18731996 <GO>}

Okay, thanks.

A - Mario Greco {BIO 1754408 <GO>}

And on the other side, Andrew, this is, let's say what is sustaining the further price increases in property. Property hasn't yet rebalanced, and so that's why prices continue to grow and keep moving up.

Q - Andrew Ritchie {BIO 18731996 <GO>}

So -- great, thank you.

Operator

The next question comes from the line of Peter Eliot, Kepler Cheuvreux. Please go ahead.

Q - Peter Eliot {BIO 7556214 <GO>}

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Thank you very much. The first one is on the Z -- the Z-ECM ratio. I mean I guess your framework still says that sort of add up between 120% and 140%, and you should consider increased risk taking. But you seem to have done the opposite this quarter. So I was just wondering if you could sort of square that and say, how we should think of your risk appetite from here at this level.

And the second one was on the crop business. I just think -- when you think about 2019, should we just sort of put that down to bad luck and move on, or are there any other sort of pricing or other implications for that business going forward.

A - George Quinn {BIO 15159240 <GO>}

Thanks, Peter. So you're absolutely right about what the -- the Z-ECM framework says, but it doesn't say that you have to do that. So we have a choice. So I mean, as you can imagine in the environment that we've been in, I mean if anything we'd like to reduce the extreme sensitivity that we have. I mean, that's why you see some of that reduced risk taking that you referred to earlier.

I mean the capital level is clearly very strong but again the -- I mean, we obviously, we actively look at the portfolio that we have, we look at the risks that we currently run, we look at the trends and the expectations that we have for the future.

And I mean, we feel comfortable with where we are at the moment just given the the external environment. I mean, it gives us the ability, I mean in order to give additional assurance around dividends, but I mean if opportunities arise. It also gives us that capital flexibility that can be a huge benefit.

On the coal business, I think having had three really, really good years, it would be -- it'd be a bit cheap of me to say it was bad luck, that last year, because I mean at some point, we actually have to pay people, claims on this business. So I mean, we've had combination of events last year, we had the prevented planting topic that we talked about in the first half, it wasn't really in the first half results, it came in the second half. And then very late in the year, we had the freeze on the sugar beet.

I mean, I think that one of the really asking things for me was the efforts that farmers made, especially on the sugar beet topic, to try and mitigate losses. So, I don't think we see it as bad luck, it doesn't change our view of the line of business. We like it. We think that we can manage it well. We're happy to have it as part of the portfolio.

Q - Peter Eliot {BIO 7556214 <GO>}

Right. Thanks very much.

Operator

Next question comes from the line of Jonny Urwin, UBS. Please go ahead.

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Q - Jonny Urwin {BIO 17445508 <GO>}

Hi guys. Thanks. Just two-piece, so on P&C rate versus claims inflation basically. So rates -- rate's gone up 4% across the P&C book, 9.6% in North America. Just wondering, can you give us an indication of where loss trend is running currently, the cost of the whole book and for North America. And then secondly, what's your pricing versus loss trend expectation for 2020. I know you flagged positive margin draws, but I'm just trying to gauge the constant. Thank you.

A - George Quinn {BIO 15159240 <GO>}

Thank you for the question. So I think on Europe -- so I mean, Europe and the US being the two major components. I mean, no real change around where we see Europe. So relatively small margin expansion in Europe in the -- if you look at the full year, they are about 2.2%. It was stronger towards the end of the year, we are anticipating that it maintains that strengths into 2020. So we were more -- just over three level, at the very end of the year. Loss cost inflation, probably running at something like about two-thirds of that level in Europe.

In the US, I mean obviously, the US is for all the the interest lines currently from a price perspective, I'll come back to loss costs topics in a second. I mean, generally, sequentially each quarter has improved last year, so Q4 is the strongest you've seen in the slides, already, today, that close to 10% overall in the US book. On the three major lines of business. Property, Liability and Motor, they're all in double-digits. I think we then look at trends -- certainly, if we think about trend coming into 2020, I think from a price perspective, we don't see this slowing down, so which is a change to we were at the half year.

So I think we were a bit more cautious. I think today, we expect this to continue through 2020. Loss cost trends across those different lines of business, our focus on Liability and Motor because those are the two that are most heavily affected. So in Liability, you really need to look at primary distinct from excess. Excess is where most of the action seems to be I mean we will have loss cost trend picks. I mean, probably high single just into double-digit level, so significant margin expansion.

But obviously not as much as the -- you would expect, given the pure price topic. And on Motor, which again is in double digits. We expect, based on the studies, that we've done, I mean we expect to add about a point to the loss cost trend pick for 2020, taking us to somewhere between five and six overall. So on both of these, I mean, the margin expansion is attractive. They come from totally [ph] different places in terms of current profitability. I mean they both offer an attractive opportunity.

Having said that, I think we said at the Investor Day that we're not chasing share. So part of the reason for the loss cost trend choices that we're making is I guess to contain appetite around these topics.

I think we're quite happy to see the growth that we anticipate for 2020 driven by rate rather than exposure, but that's broadly how we see it. Hope that's helpful.

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Q - Jonny Urwin {BIO 17445508 <GO>}

Thank you very much. Very helpful.

Operator

Next question comes from the line of James Shuck from Citi. Please go ahead.

Q - James Shuck {BIO 3680082 <GO>}

Hi, good morning -- afternoon, everybody. Two questions from me. On the EPS growth target, so the capital market today is greater than 5%, 2019 to '22. You've delivered a strong set of results in these numbers, but there was a very high level of capital gains in those numbers, around $145 million, I'm presuming that those capital gains will trend down over the next couple of years or so, closer to the $400 million level.

Sorry, my question is kind of, where is the rest of the growth coming from, you're fighting against lower investment income on the P&C side. I'm presuming it's all coming from the combined ratio improvement and a little bit in life, but that's going to be low-single digit, but perhaps you could just square that kind of implied underlying growth that now looks a little bit stronger given the higher base delivered in 2019.

Second question around the capital position. So the changes to the model that you've made and the reduction in the investment risk. Could you just clarify, is there more to come on that side of things. I can see that you haven't published updated Z-ECM sensitivities to credit, 100 basis points increase, loss reported was negative 17 points, which is obviously a very big number and I appreciate you don't benefit from any of the buffers under long-term guarantee package, but do you have a target level for reducing that sensitivity for credit. And can we expect further developments on the Z-ECM from management action.

Thank you.

A - George Quinn {BIO 15159240 <GO>}

Thanks, James. So as you started that question, I was trying to anticipate where you were going. You took it to a different place from the one I was expecting. So, on EPS growth, I'm going to answer the question. I wanted to answer and I'm going to answer you at the same time. So just for everyone's benefit, the starting point of course is the as published number, as you point out, there is quite a high level of gains, there is a -- I mean, there is also a reasonably high level of realized losses in there which are main really related to some of the disposals that we did last year.

So either the transaction in Venezuela, or the sale later in the year, which is yet to complete, but will complete in the first half of the retail wealth platform, and in the UK. In terms of where does the growth come from. So I think as we approach the Investor Day, we had a pretty clear sense of I mean what we anticipated in terms of the outcome around our net income for the year. So that's already baked into the positions that you see there. I mean if you look at that, again, I know you're familiar with the -- the main

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driver is going to be the P&C business. We do expect Life to attribute, I think your number is right over the period. Probably Life growth into 2020 will be slightly stronger than that. That lower -- that lower -- lower mid single-digit type level, will be a bit higher than that. I think especially as the the OnePath business comes on stream fully this year. But those are the two key drivers. There are other things. I mean, Farmers will continue to grow. But, of course you're aware -- the growth rate we anticipate there is. We've got some expense action that we'll undertake.

I mean, all of these in combination and roughly the same proportions that you saw at the Investor Day are anticipated to be the driver of growth and it doesn't assume the same level of gains. Just to be clear.

On the capital model, I mean it's a really good question. I think the challenge right there is the -- I mean if the -- I mean, Peter Giger and I are -- he's our Chief Risk Officer, and we've had several conversations since the moves that we saw in Q3, Q4. I think on the one hand is it just a dramatic real world perspective to this whole thing that, I mean, on the -- in the asset risk continuum. Well, as you all know, we're not risk free, we're equally not the riskiest either and for us to do substantial derisking around fixed income, I mean, it's always taking a pretty significant bay in the other direction, and I think we would rather be consistent around this area, even if it still brings volatility to the reported number.

I think the approach Peter and I have agreed is that I mean we will look through some of the temporary volatility, we will look at kind of what the market does elsewhere around UFR. We want to maintain the model that we have because we think it gives a pretty clear picture of what's really going on. And if you want to take the view that the interest rate risk can be paid down over a long period as the UFR tends to do. I mean, we can take an active decision to do that at that point in time.

But reducing risk taking around trade is not high on our list of priorities, other than the comments we made earlier this year, around capping credit exposure.

Q - James Shuck {BIO 3680082 <GO>}

And just on the point around, are there further benefits to Z-ECM model, that you would expect through 2020 from either changes to the risk allocation or in the model changes?

A - George Quinn {BIO 15159240 <GO>}

So, at this point, there's nothing material planned. But I mean, I know that the SST [ph] only has an agenda to take a look at the whole thing and just make sure that it has all of the -- the most modern thinking in it, I don't think that will cause material changes either positive or negative. I mean the model has been pretty stable over a longer period. So I think, you could assume that will continue through this year.

Q - James Shuck {BIO 3680082 <GO>}

Yeah. Thank you very much.

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Operator

Next question comes from the line of Michael Huttner, Berenberg Bank. Please go ahead.

Q - Michael Huttner {BIO 1556863 <GO>}

Thank you so much. It's really one question, it's a bit complicated. And congratulations on achieving all your targets. And so, you know, on Life company, If I look at the capital allocation, 54% and on that lovely slide at the beginning, where you show the split of gross written premiums in Life, most regions are overwhelmingly in your preferred segments except EMEA which I guess is due to Germany. And also, in the risk report, you showed a figure for the interest rate sensitivity jumping from $2 billion for the life segment to $3 billion, for minus 100 bps negative. So these are big numbers, and I just wondered what your thinking is here whether you're -- you would be planning maybe to sell off your German Life unit, or what would the obstacles be to maybe running itself or transferring the portfolio. Thank you.

A - George Quinn {BIO 15159240 <GO>}

Thanks, Michael. I was going to say, welcome back.

Q - Michael Huttner {BIO 1556863 <GO>}

Thank you so much.

A - George Quinn {BIO 15159240 <GO>}

We -- so I mean, so I think you correctly analyze the challenge that we face for the change in capital that you see, that is -- actually has nothing to do with something that changed in the business. We didn't go out and suddenly become more risky. Of course, the financial markets moved quite a bit, and the asset Intensive elements of the portfolio, which are all in Life passively consume substantially more capital.

I mean, I think we talked about a bit before, around, I mean, how do we best manage this. I think if we saw ways that were in our interest and interest of all of our partners and our clients to improve it. I think, I mean you could assume that we would do that.

I mean the German situation is a bit tricky, and being, for reasons I think you understand and are aware of. I mean we do look to ways in which we can improve the capital consumption, the returns on capital that we achieve, and in fact, I think I'd mentioned already, it may have been at the Investor Day, maybe it was at the half year that if you look at the German business actually on a local -- to a local capital basis, the funded basis, I mean, the returns are -- I mean, not so bad doesn't sound like a glowing recommendation.

But I mean the returns are not bad. The challenges when we overlay that model that James referred to a second aog, and I know, that you understand, I mean that's where the challenge comes from. So I mean we continue to look at ways in which we can improve it. In Germany, currently, we actually have a little not few things that are probably

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higher priority, that are more about where the business is headed. And trying to make sure that we can take advantage of the market opportunities that continues to be I assume both for us and for the -- our leaders in Germany to try and find a way to address this, but I don't have a further update beyond that today.

Q - Michael Huttner {BIO 1556863 <GO>}

Thank you so much. And again, congratulations, amazing results.

Operator

Next question comes from the line of Farooq Hanif, Credit Suisse. Please go ahead.

Q - Farooq Hanif {BIO 4780978 <GO>}

Hi, everybody. Slightly simplistic question first. So if pricing is accelerating and going into double digits in some of the areas that you are growing in and this is widening jaws, or quite wide jaws on claims inflation. What is stopping your kind of underlying loss ratios plummeting down, is that the mix change?

So can you talk about the dynamics around the mix change that you want to do and how much further to go. And then secondly, on on cash flow. I can see the explanation of why it's lower here, primarily because of Life, lack of capital to release. But I'm just thinking, if going forward, what you see is the growth rate in that Life cash flow. So for example, is -- can we look directly at the OnePath earnings growth in Life, and directly assume that, that kind of will contribute to higher cash flow? Thank you.

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A - George Quinn {BIO 15159240 <GO>}

Thanks, Farooq. So on the first thing, and I mean, it would be fabulous if the combined ratio would simply plummet. I think the thing to remember, like there's my fault rather than yours, I mean, the comments that I made earlier, you need to sub-divide the portfolio, so the -- I mean if we're achieving, for example, and we take the liability -- if we've got a near 15% rate increase in liability in Q4, that's only on one particular part of portfolio. If the loss cost trend around the excess component of that particular book has say, 9%, 10%, again it's on an even smaller part of the portfolio.

So, they -- we are seeing the -- as you describe, I guess, the jaws open, I'm not -- I'm trying to work if that's a good analogy or a bad one. But we are seeing that positive margin develop, and -- but it's in particular parts of the portfolio.

I think if you look at the US, last year, just the US part of our business, and if you are prepared to put crop to one side, we do see a very significant move in the loss ratio. And of course, that's partly driven by this trend. So I think we are seeing it turn into improved performance, but I don't think it's going to plummet. And this is the point I'm trying to make (multiple speakers).

Q - Farooq Hanif {BIO 4780978 <GO>}

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Okay. I know -- just a comment and a question around that very quickly. So obviously, you're shifting mix as well. So not really -- more of a question really. So, I mean, if you, I mean, how much further have you got to go on this sort of 52% in specialty, and shorter tail lines.

A - George Quinn {BIO 15159240 <GO>}

So I think, if you think of how we manage mix from here, I mean if you look at on a written basis. I think the portfolio that we have -- I mean, ideally we want have a bit more specialty in the portfolio in the long run, but for reasons that we talked about recently, doing that in the short run would be completely kind of productive. And so, from a short-term perspective, I don't expect major shifts in the portfolio from written perspective. Now obviously, it's the earning through, the liability change has been earning through for the last couple of years, so from an aeons perspective, this will be the first year in which we see the full impact of that.

So I think, I mean, mix will have some effect on it, but I don't expect mix to have a significant negative offset to what you're seeing on rate and loss cost. I mean the benefits that we talked about earlier, allowing for some normal randomness around the claim incidents we expect to see in 2020. On the cash flow topic and growth rates, so I mean you referred to last year, so I won't rehash 2019. And obviously, there are a number of things that will drive it as we come into this year.

And as since some of the interest rate volatility will not be unhelpful to Life business, as we begin 2020. The (inaudible) OPL impact, and just a reminder for people who may have forgotten what we said in December of '17, we actually have a higher expectation for cash and earnings because of course this is quite a large in-force component to the portfolio.

So I mean Life will come up a bit from where it was last year. We talked -- talked about in the past that we're expecting to see something north of $1 billion for life, and OPL, well, an impact there. The remainder will be driven by earnings growth. We do expect, as you remember from the Investor Day, and things I discussed earlier with James, to see 5% compound annual growth that will feed into what should be a higher base starting point for 2020.

Q - Farooq Hanif {BIO 4780978 <GO>}

Okay, thank you very much.

Operator

Next question comes from the line of Nick Holmes, Societe Generale. Please go ahead.

Q - Nick Holmes {BIO 3387435 <GO>}

Oh, hi there. Thank you very much. Couple of questions. The first is, there's been quite a wide range of experience with social inflation among your US peers and I wondered what your take on that is, means, how should we read across to Zurich. And then secondly, Z-

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ECM sensitivity to interest rates is still high, I see. And I just wondered, are you doing anything to reduce that? Thank you.

A - George Quinn {BIO 15159240 <GO>}

Yeah, thanks, Nick. So on the social inflation topic, and that's partly reflected in the comments I made earlier around this topic of the loss picks for next year. It's a bit hard for me to make any relative comments on Zurich versus the rest of the market. But I think you guys know that we have done a number of things already, so the -- I mean from a mitigation perspective number one is, the price change that we talked about earlier. We've obviously shifted the mix of business significantly. If you look at liability in our portfolio, I think we're down by something like 5 points, 6 points compared to we were four years ago. If you look at -- I mean something that the US firms sense to, or US firms sense to us which is around excess, which is not the only place that has the issue, but it seems to have a bit more of it, maybe in some other areas.

If you compare what's happening on limits, the attachment points, and I'm looking at the graph as I speak, I can see the limits coming down year-on-year from 2015, and I can see the attachment points rising year-on-year from 2017. So, I mean obviously, as that gap closes -- it can't close entirely, otherwise, there is no business to be done, but obviously that combination means that you're a bit less exposed to that topic, and I think some of the things that we did earlier in the strategic cycle positions us well for that.

So I mean, we do see that social inflation issue, I think maybe not quite as much to some others for the combination of reasons I've just given you.

On the interest rate topic. So -- and I think I referred to, briefly earlier, I think in response to James' question. So I mean as a very long end, which is not entirely but mainly a German topic, I mean there are some issuers out there who are now issuing some very long-dated bonds, we were discussing it earlier this week. I mean -- ALM is the focus for us.

But when we're buying bonds that are going to mature in the year '21, '20, I think we need to be a wee bit careful about, I mean just going two kind of way with the yield topic. So we are looking for ways to reduce interest rate sensitivity. Again, there'll be a limit to how far we can go just because our model has none of those features that softened the impact, but I think we would like to bring it down, trying to -- in a relatively pragmatic way.

Q - Nick Holmes {BIO 3387435 <GO>}

Great, and thank you. That's very interesting. Can I just come back very briefly on social inflation. So without sounding too arrogant on, you kind of -- things that you anticipated, this trend perhaps earlier than some others. So you are pretty comfortable with the position?

A - George Quinn {BIO 15159240 <GO>}

I got my boss and he's kind of shaking his head. So I mean, I would love to tell you that we knew this was going to happen and we did all of this with this particular scenario in mind.

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But that would be a lie. I mean we were trying to fix issues that when you refaced the positive side effect of that by doing the hard work at that time, it means that we're in a reasonable place today. But I can't claim that we had foreseen this particular eventuality.

A - Mario Greco {BIO 1754408 <GO>}

(Multiple Speakers) I think we told all of you in '16 that we will do this and we ended up by following the strategical choice, we ended up in the right part of the market. It's not because we saw it but just because we wanted to change the nature of our books and the timing was lucky.

Q - Nick Holmes {BIO 3387435 <GO>}

Makes sense. Thank you very much.

Operator

(Operator Instructions) The next question is from the line of Vinit Malhotra, Mediobanca. Please go ahead.

Q - Vinit Malhotra {BIO 16184491 <GO>}

Yes, good afternoon. Thank you very much. So my question, I have one question only please on the retail and other segment, where obviously crop has confused the picture a bit on the underlying combined ratios, and somewhere in the notes or the comments, there is a statement that even excluding crop, the underlying would be better.

Could you help us understand that a bit more. Could you provide some more color on how much or what's happening between mid-market or other retail segment for something to help us more. Thank you very much.

A - George Quinn {BIO 15159240 <GO>}

Thanks Vinit. So I mean if you put in context, I'll pick a retail other, so we are, so nearly 3.6 [ph] for the entire year, which is, I will give it my highest accolade of not bad. Now, or so the second half is a bit weaker than the first, so we are nearly 4.6 [ph] in the second half. Crop makes up a reasonably significant slug of the premium in the second half of the year.

And retail, we got about $1.5 billion of earned premium for the year for crop and the bulk of that appears in the second half. I mean, crop has an adverse impact on the Group overall of 0.6 and retail is a bit more than half the bit, but to keep it nice and simple, I'm going to assume it's half. So you can double it for retail, and you can double that again for the second half of the year. So I think that's why you get this comment, that if you adjust nay 4.6 [ph] down for something like four times crop impact, you still see an improvement.

Q - Vinit Malhotra {BIO 16184491 <GO>}

Alright. Thanks, George.

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Operator

Next question comes from the line of Niccolo Dalla Palma, Exane BNP Paribas. Please go ahead.

Q - Niccolo Dalla Palma {BIO 16052945 <GO>}

Just a couple of last questions from me. The -- on the central cost, you still guide to $750 million to $800 million. You did much better in 2019. What would explain the -- a deterioration from there. I think you pointed out, the lower headquarter cost.

And the second question is on the reinsurance protections that you have today, nothing changed in the excess protection. Is there any significant change worth flagging on the quota shares. Thank you.

A - George Quinn {BIO 15159240 <GO>}

Great. So, thanks, Niccolo. So the first question. So you're absolutely right, I mean, we saw a very, a further significant reductions in the central costs last year. We haven't yet been able to pass all of that onto the businesses for various reasons, as my intention to do so in 2020, which is why we've guided you back up to that slightly higher level of -- at $750 million, or maybe slightly higher.

So we'll pass on the benefits, but with a wee bit of a lag. That's why you see that combination of topics. On the reinsurance protection, you're absolutely right. So we haven't changed the attachment point on the cat aggregate. Not really looking to make any significant changes across the programs.

We've had a number of renewals on Gen-1. Some of the larger cat program actually renewed last year for -- it's a multi-year contract. So it won't come up for renewal this year. So you won't see obviously for that reason, any significant change there. So not much to add on regions actually.

Q - Niccolo Dalla Palma {BIO 16052945 <GO>}

Thanks.

Operator

The last question is a follow-up from James Shuck from Citi. Please go ahead.

Q - James Shuck {BIO 3680082 <GO>}

Thanks. A couple of follow-ups, please. So just on Farmers. So GWP growth is around 3%. The policy in-force will keep declining. We're down 2% continuing just since H1. The net promoter scores keep going up though, Mario, and I know that you've been a big proponent of the link between net promoter scores and increased retention. It doesn't seem to be working at Farmers, at least in terms of the policies in-force, and also given

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the rollout to East Coast. So could you just comment a little bit about what[s not -- what isn't working at Farmers, at least on the P&C side.

Secondly, on the expense base. So the other underwriting expenditure ratio improved to 13.5 points at full year. I think you've intimated that the goal is to get to better than 13 points, in time. I'm not really sure what you mean by in time, what kind of time frame you've got for that, and are you expecting the absolute level of expenses, $9.2 billion on the controllable cost base, are you expecting those to decline in absolute terms, please?

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A - George Quinn {BIO 15159240 <GO>}

So I'll do the first one, and second one first. (Multiple Speakers) So, on the expense base topic, I guess it probably depends on what you ask me and the CEO, or you ask someone else. I mean at the Investor Day, I mean what we indicated -- a both is what we're looking for. So we still believe we have pockets of inefficiency in the group and together with the support of the Chief Operating Officer, we're going after that currently.

So you will see reduction there. We're also anticipating that because we expect to see continued growth in retail, and for the reasons I gave earlier around the commercial book, actually stronger growth in commercial this year which would be rate driven, we expect that also to contribute to expense, efficiency. Where would that leave us overall?

I mean, I think you might see the expenses are roughly the same level, maybe slightly reduced compared to prior periods. I mean, they won't be what you've seen in the course of the last three years. Maybe, we're looking for something in the kind of the $400 million range, around in the $1.5 billion that you saw before, and timeline, over the three-year period.

There's other things I'd say, the three year period don't matter but we're not going to talk about them until we start doing that. So this expense commitment is for this three-year period.

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A - Mario Greco {BIO 1754408 <GO>}

Yeah. On Farmers, two things have been happening and they were absolutely planned, and in any sense expected. One is that we are restructuring the agency force. I think we have been showing the characteristic of the new agents that we are hiring, but we also closing or merging a number of old agencies and when you do that, there is, of course, an attrition. The reason we're doing this it is by having bigger agencies more structured, we can much better used the power of the data and the capacity to sell products through the forces of these agencies. And then the second factor is that it's not only for the reason of the wildfires, but following the catastrophes, prices have been -- have been still growing. And when you growth prices, it's difficult to go and gain more individual customers and that's a lot of the market that not even retention or net promoter score growing can overcome, and if we increase the prices, and you will acquire few new customers.

So no new customers, and the game becomes the one of maintaining your existing customers. We think that especially in the second half of the year, the numbers will turn into positive customer growth, and we're looking forward to see that happening.

A - Richard Burden {BIO 1809244 <GO>}

I think that concludes (multiple speakers) sorry, James, do you have a problem? (multiple speakers)

Q - James Shuck {BIO 3680082 <GO>}

No problem. So, thank you. That's fine. Thanks.

A - Mario Greco {BIO 1754408 <GO>}

Okay. Thank you, James.

A - Richard Burden {BIO 1809244 <GO>}

Okay, well thank you very much everybody for dialing in today. If you do obviously have further questions, then the IR team is available for your calls or questions. And with that, we'll close the call.

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.

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