Q3 2014 Earnings Call

Company Participants

- George Quinn
- James Quin

Other Participants

- Andrew J. Ritchie
- Andy D. Broadfield
- Atanasio Pantarrotas
- Farooq Hanif
- Marcus P. Rivaldi
- Michael I. Huttner
- Niccolo C. Dalla Palma
- Nick Holmes
- Paul C. De'Ath
- Stefan Schürmann
- Thomas Seidl
- Vinit Malhotra

MANAGEMENT DISCUSSION SECTION

Operator

Ladies and gentlemen, good morning or good afternoon. Welcome to the results for the nine-months September 30, 2014 Conference Call. I'm Stephanie, 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. Please go ahead, sir.

James Quin {BIO 18345789 <GO>}

Thank you and welcome to Zurich's results presentation for the third quarter of 2014. I'm joined by our CFO, George Quinn, who will make a few short comments before we open the Q&A. As usual, please keep to two questions.

I'll now hand it over to George.

George Quinn {BIO 15159240 <GO>}

Thank you, James. Good afternoon or good morning, everyone. As James said, I'll make a few and short introductory remarks. So first, in General Insurance, we've reported a combined ratio of 97.7% for Q3. And within that, we have good progress on our accident year ex-cat combined ratio which is 1.4% better than in the prior year and that's due to continued improvement in our underlying loss ratio.

Cat losses are well within expectations for Q3, but perhaps a bit higher than you may have expected, given a generally quiet quarter. And this is mainly because of Hurricane Odile which cost us $90 million. On PYD, we have a positive contribution to the combined ratio of 0.6% for the quarter and the nine months. And that's again a bit less than the expected range of 1% to 2% that I indicated at the time of our Q1 results.

About the (01:35) Q2, this is due to some specific identifiable issues with some volatility to be expected. But it doesn't change what we expect from this in the future.

The Life results are in line with expectation and we continue to progress on our strategy to reposition the business. And some of the costs associated with these initiatives are included in the results.

And in Farmers, we have some good news. We're back on a growth track in terms of gross premiums. We are pretty much flat in terms of policies in force.

Overall, we characterize this as a solid set of results. But as you would have seen from the presentation this morning, we may start to see some headwinds in the next year or so, given the market environment that we face.

This doesn't require any change in strategy on our part, but it does mean that we'll need to push harder on some of the levers that we have around optimizing the capital allocation, around expenses, amongst other factors, to make sure that we hit our targets.

And with that, I now look forward to answering your questions.

Q&A

Operator

First question from Vinit Malhotra, Goldman Sachs. Please go ahead, sir.

Q - Vinit Malhotra {BIO 16184491 <GO>}

Hi. Good afternoon. Just – so my two questions, first is, George, in the comments in the presentation in the morning, there is a mention that part of the 150 basis points underlying loss ratio improvement comes from NAC and Europe. Could you please comment a bit more if NAC driven by the analytics and if Europe, more the result of this retail focus and equivalent? (03:20) And also, I'm curious why not Global Corporate, given that pricing that it's all been a little better at least in NAC. So do you have any comments on that?

And just secondly just on the – you also said that you did not assume tailwinds, but probably you had assumed a neutral position when they invested their targets or set both on markets, on pricing markets, intersets (03:52) et cetera? So how much is the concern around the headwinds that we see? Thank you.

A - George Quinn {BIO 15159240 <GO>}

Thank you, Vinit. Good afternoon. So on the improvement that we see across GI, I mean, you're absolutely right, we did attribute in the commentary, improvement to NAC and in Europe. I mean we see significant improvement in Global Corporate, I mean, it's at least about 3 points, but the challenge on Global Corporate is that the – I mean, the sector (04:23) is just generally more volatile because of the impact of large losses. So it's a bit harder in a given quarter to isolate the specific improvement in Global Corporate, but we do believe that that also contributes to the underlying 150-basis-point improvement.

In terms of driver for NAC and for Europe, I mean, NAC – I mean it's been – we're investing a lot on the predictive analytics side of it, but I think it's, I mean, it's a little bit rash to claim at this stage. It's already a major driver of the improvement. I mean, NAC has a market-leading position in the U.S. in a number of particular industry sectors. I think they're using the competitive strengths that's benefiting also from market improvement in those areas. It's combination of both.

In Europe, I think it's mainly general rate improvement has been driving the improvement we're seeing there.

On the rate environment, I mean you've seen the comments I've made today on the market outlook, which, I mean, just to be clear, it impacts everyone. I wasn't trying to be specific about Zurich and so on. And hopefully, I'm not seeing much, it's very different from Q2 but come back to planning, when we put the targets together for the discussions in December last year. I mean, we haven't seen tailwinds, but absolutely (05:47) – we didn't see any significant headwinds either. And I think we will see some rate pressure over the course of the next 24 months. And I guess the commentary this morning was designed to acknowledge (05:59) that the company sees, well, I think almost everyone else sees.

So, I mean, hopefully, it's not really new. It's really a signal that we're awake and aware. And also more importantly, to signal that, I mean, we completely understand it, that means we can't stand still. And therefore, more effort is required to make sure that we get to where we have to be.

And as I pointed out in the press release this morning, I mean, I think we're fortunate in the position that we have a number of different levers at our fingertips which range from the continued application of the very solid (06:39) underwriting practices that we have already that have been part of the driver of that 150-basis-point improvement. And we have an expense opportunity, I think we can be far more efficient than we are.

Fairly, I mean, we're blessed with – because of high quality problem on the capital side, we have a significant excess against our key target metrics, and I mean, that positions us well both for the organic opportunities and the inorganic. I mean, you're absolutely right, no headwinds, no tailwinds assumes; we'll work harder and get to where we need to be anyway.

Q - Vinit Malhotra {BIO 16184491 <GO>}

Thanks very much.

Operator

Next question from Michael Huttner, JPMorgan. Please go ahead, sir.

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

Just a couple of things. On the reserve or prior-year (07:29) development, can you say how much was the UK and whether it's a kind of three-year or two-year recurring pattern? and what – how we should understand the 1% to 2% going forward as being sustainable given that there are – some of your competitors are seeing the opposite?

And then on the tax side, I was interested to see that, yes, you're guiding to slightly higher, and I wonder if you could give me more insight into that. Is this is a mix effect because you have more profits out of the U.S., which is a high-tax country, or is it generally a rise in taxation from all countries? Thank you.

A - George Quinn {BIO 15159240 <GO>}

Thanks, Michael. Sorry. We're muting the phone in between.

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

I beg your pardon. Sorry.

A - George Quinn {BIO 15159240 <GO>}

I'm going to press the hang up button which should be no good (08:56)

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

Don't worry. That's all good.

A - George Quinn {BIO 15159240 <GO>}

Good afternoon. So first of all, on the reserve releases, UK APH, there's a charge in the quarter of $70 million. I mean, it's not an overall book. I mean, APH in total is about $2.7 billion of reserves. I mean, it's paper things (08:48) that you don't do every year. Yes, (08:49) we did do it on a periodic frequency. I don't know if it's two years or three years. I mean, it's typically three years. And so, I mean, it does come around from time to time.

And I think as – I mean, as you're well aware, I mean it's pretty rare that someone has an APH review and then it answers a reserve release. So, it's a risk factor, for sure. From an overall perspective, I mean, – and I said this at Q2, so I'm obviously aware of repeating it again.

But I mean, again, if I look through it, I can easily see that we're within the expected range. So, I mean, I have no reason to expect anything different from 1% to 2% in a longer-term perspective, and we're not changing the game. But things like UK APH will come along from time to time. But I mean I hope that's not everything is like APH. We will have reserve reviews occasionally that do actually (09:43) But we expect 1% to 2%.

On the tax rate, so – I mean, (09:52) but the tax rate comment today, I mean, isn't really the result of the rate you see for the quarter. It's not really connected to that. I mean, the rate we've seen, we have 33% for the quarter. We anticipate 29.4% for the full year. I mean that's a mixture of impacts which range from, I mean, things you've heard of before like Russia, changes in tax rates in Chile, the impact of things like Hurricane Odile and they have to have a (10:23) low tax jurisdictions for us.

But I mean, structurally, I don't foresee the change. But we're looking through planning, so we're obviously forecasting or estimating what we expect to be projecting for the next two years to three years. And given the mix that we see, I certainly see a tendency for the rate to rise. And again, just a note of caution around the fact that even if tax rates, I mean, more generally falling than rising, I guess the tax base in most jurisdictions has been broadened.

So, I mean, that is why I've increased the guidance today. I guess the most important point to make though is this does not change our expectation of achievement of the target. So, I mean, (11:13) part of it is mix, part of it is Latin American. And generally, they have higher tax rates, but I need more profits before I pay more tax.

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

I see. So I should understand the tax comment as not as negative, but effectively you're saying the U.S. is going to deliver a lot more earnings.

A - George Quinn {BIO 15159240 <GO>}

Not quite the U.S.

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

Sorry. Sorry.

A - George Quinn {BIO 15159240 <GO>}

Yeah. So, I mean, if you look at the places with a higher tax, I mean, Latin America is the place that stands out. So, mix means slightly more of expectation of profit from Latin America.

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

Excellent. Thank you

A - George Quinn {BIO 15159240 <GO>}

Thank you.

Operator

Next question from Andrew Ritchie, Autonomous. Please go ahead, sir.

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

Hello. Hi there. Two quick questions, George, sorry to go back to your transcript this morning, the problem of getting the transcript out, we can look at every word. The implication is that there's slightly more headwinds than maybe you felt from the operating environment.

But is there – at least from what you've said, particularly the expression you used is meaningfully improved efficiency. It seems that – have you discovered a new opportunity in terms of, be it cost saves, re-underwriting? You said there's more headwinds in the environment, but from a bottom-up perspective, is the growth more confident as you found new opportunities to improve things bottom-up? That's what I'm reading from that, but maybe that's reading too much, just clarify that.

Secondly, Farmers, I mean, is the beginning of a growth phase it too early to call that? Is there any more confidence? You had quite a lot of confidence at Q2 and we've seen that come through. What is the sort of new business indications or customer feedback indications running at now in terms of future momentum? Thanks.

A - George Quinn {BIO 15159240 <GO>}

Thanks, Andrew. So on the first one, on the efficiency point. I mean, I'm expecting at some point at the course of the call, someone's going to ask me about, say, 1% expense ratio in GI. I mean, that's a logical well-thought through reason behind the expense level and it's not that it just happened to be that number. So we are deliberately investing to try and create the best platforms to make us more competitive in a number of markets. But, I mean, that's not a sustainable level for the expense ratio.

I mean, we're certainly setting a hard target for a year. I know that when Mike Kerner looks at it, I mean, he looks at the peer group. I mean, he certainly has the ambition to be at least as good if not better than the peer group. And you know what type of number peer group expense ratio start with. (14:05) So, I mean, we're not – I don't see a restructuring or some brand efficiency plan today. But I think there are a number of areas where we have an opportunity to be more efficient and it's more important that we take them, given some of the commentary that you have from me, I mean, not only me but from other markets observers on rates.

So I think I wouldn't characterize it as a group who's just discovered them because we've had a number of things pointed out just over some time. But I mean, we're going to do the logical and obvious things to make sure that we can maintain the commitments that we've made, and expenses will play its part in that process.

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

And just a quick (14:44) one, when you talk about commitments, you're talking both the ROE and the bulk growth commitments, is that – or do you put more emphasis on one than the other?

A - George Quinn {BIO 15159240 <GO>}

So we have two sets of targets, one financial and one strategic. And they're all equally important.

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

Okay.

A - George Quinn {BIO 15159240 <GO>}

On the Farmers growth side, so I mean with the benefit of hindsight, it seems obvious, I mean if you look at the chart, it would be hard to believe that you couldn't have reached this point, I mean, given what we see around retention, new business and agents, et cetera. I mean, we remain optimistic, I mean, I want to avoid – I know that you say something that target for Farmers today, obviously, we're looking for them to sustain what we've achieved, but we'll have Jeff Dailey at the investor update in December, and he'll go into this in more detail there.

But obviously, we're very pleased with the fact that back in growth, I mean, financially, it's not immediately significant impact there is, but I hope that from a sentiment perspective, it gives people more confidence that, I mean, we actually have a very effective model here on the exchanges.

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

Okay. Thanks.

Operator

Next question from Andy Broadfield, Barclays. Please go ahead, sir.

Q - Andy D. Broadfield {BIO 7273415 <GO>}

Hi. Good afternoon. Two questions, please, one on capital and one just to expenses, to be original. On the expenses, you have – the outlook across your business. It's hard to see any major (16:28) momentum that won't be driven by self-help frankly, so your momentum has to be driven by actions that you take.

Should we expect in the Investor Day that we get a little bit more specific guidance on those actions being taken, because that still feels to me a little bit – that we've got turnaround businesses but not totally clear beyond transaction, what you'll do there? Is there any intention to set targets, you seem to be downplaying a little the degree to which you can do this. It feels a little bit like you're talking about bits and pieces that you can do rather than the great, grand plan. So just some guidance or thoughts around when we're making some guidance from there

And on capital, you stress it frequently in the commentary this morning and you said it again today about the flexibility. I wouldn't expect you to be making any great announcements to my question. But is that, for you, a key lever in starting to ease some of your – some of the areas where there is a little bit pressure on the business? And if you can give us any color on that, that'd be useful.

A - George Quinn {BIO 15159240 <GO>}

I mean it's amazing how two questions can seem to be a lot more than two questions. So first of all in the expenses, I completely agree with you. I mean I think this is – it needs to be self-help. But I think the good news is it's not purely self-help around expenses and that's why the comment on levers, many more than one.

So, I expect it – I mean I don't have much to add to what I said to Andrew a second ago. I mean, I don't expect to take part of the team and to send or to cover expenses. I mean, we'll have two of the business leaders there. I mean, the expenses may come up in the context with the presentations they make. But I don't anticipate that we'll have a session dedicated to expense management in the December update.

And as far as targets go, I mean – and I know it's clear if I set targets, but I mean I think the group actually has enough targets already and I think our focus needs to be on achieving them. And within achieving them, expenses plays its part. I mean it will get clearer as we go. I mean, I'd like to deliver some improvements rather necessarily set out new numbers. But I mean it's clearly an area where we have the potential to improve.

Maybe just to add a couple of other points and the other things so it's not just purely an expense discussion. I mean, even though I'm not that confident on margin expansion being offered by the market environment, I don't believe that the growth completely (19:23) to a whole either. I mean I think that we have an opportunity, for example, in Global Corporate, there are a number of things that we can do to increase the number of products that we sell to the clients. I mean, there's a number of things across the entire client universe, I think, that will still lead to growth. And that would expand the absolute economics even if rates don't help us.

On the capital side, I mean, I don't really have much to add to what I said at Q2 around priorities. I mean, I think you're aware, I mean, only dividends and growth, organic and inorganic, and then if we have excess, the possibility of capital reclassification.

I think, generally, though, I mean, I'm firmly at the belief that, I mean, dynamic capital management is a key part of the management than the insurance company. So I mean there are still things that we need to do to improve the allocation of capital over the course of the next some 24 months. So I do see that as part of the answer to some of the questions. It's not just an R issue; it's also an E issue.

Q - Andy D. Broadfield {BIO 7273415 <GO>}

And S&P still the main constraint on the capital side of the P because there were good news on that earlier in the month, wasn't it, or last month?

A - George Quinn {BIO 15159240 <GO>}

Yeah, it was. So I mean, as you cited, we've been moved to positive outlook and the S&P is still the main constraint.

Q - Andy D. Broadfield {BIO 7273415 <GO>}

Thanks. Okay. Thanks for that.

Operator

Next question from Farooq Hanif, Citigroup. Please go ahead, sir.

Q - Farooq Hanif {BIO 4780978 <GO>}

Hi there. Thanks very much. I wanted to just change direction a little bit. So in the Life business, you've also taken some costs in the other line to do partly with in-force management. And I'm just wondering, obviously, how long is this going to continue, what's the scope of it, and what are you trying to achieve with this particular thing that you're doing right now? So is that sort of expense reduction, capital release? If you give some more information, that'd be quite useful.

And then, on large losses and just the point you make about it in terms of normalizing, if we went back to the old language of the large loss ratio, where would we be right now? Thanks.

A - George Quinn {BIO 15159240 <GO>}

So on the second one, you had me at a distinct disadvantage because I'm not that familiar what the old language, to be honest. Maybe the IR team could help you afterwards, Farooq, if that's okay.

Q - Farooq Hanif {BIO 4780978 <GO>}

Okay.

A - George Quinn {BIO 15159240 <GO>}

Yeah. Sorry about that. So on the other course, on the Life side, so the – unfortunately, I'm not going to give you much more satisfying answer to this question either. So, it's relatively hard to talk about all the things that we're doing because if I do, it wouldn't necessarily help us because (22:11) to the market ahead of time.

Q - Farooq Hanif {BIO 4780978 <GO>}

Yeah, okay. So, on the Life side, so is this going to be potentially, I mean, something that we should bear in mind and hope it'll (22:26) happen again and recurring? So, when we think about little one-offs versus recurring items?

A - George Quinn {BIO 15159240 <GO>}

So, I think, I mean, what you see this quarter – well, I wouldn't immediately call it as one-off. I wouldn't expect it to go at the same level in all of the following quarters. I mean, also, we're preparing for – I mean, what you heard from Kristof during Q2 in the targets – not the targets but the planned improvement that he has on board. And so we'd take some of this, I guess the proprietary steps necessary to work on the operational improvement that he's talked about and also work on the capital sort of things for Life.

So, I mean, you'll see more of that in due course, and you'll definitely see more of that in May next year, where Life will be one of the key focal topics.

Q - Farooq Hanif {BIO 4780978 <GO>}

Okay. Thank you so much.

Operator

Next question from Atanasio Pantarrotas, Kepler. Please go ahead, sir.

Q - Atanasio Pantarrotas {BIO 5933123 <GO>}

Yes. Thank you for taking my question. Good afternoon. I have two questions. One is regarding your statement about the softening market in GI. I wonder if we have to consider the current level of accident year loss ratio at around 64% as the bottom. So we can expect to see some deterioration ahead and what could be the strategy of Zurich in the case of a softening market? I mean, we have expected to see reduction in volumes to defend the profitability as we saw in 2009 and 2010?

Second question is on realized gain, I saw that you realized, this year particularly, high level of gains both in below operating line and also in the Life business. And I wonder if you, without this realized gain in the Life business, your net investment income is still pretty much good or you need that to realize some gains in order to give credit enough to your policyholder? Thank you.

A - George Quinn {BIO 15159240 <GO>}

So at least a softening market in GI, first. So, and obviously these comment today, I really like to (24:44) highlight that particular risk that you referred to. And if we do see a softening market, what do we do? And I think many of the things I referred to earlier in the call. So a focus on continued discipline in underwriting. I think you've seen the company's track record here. We are not driven by volumes. We are absolutely focused on profit. Obviously, we have the same positions that we've created over time, but I mean we have a focus on margin before anything else. I mentioned earlier the potential for efficiency and then, of course, we also have the capital flexibility that I highlighted earlier. So I think all three of these things would play into our routine (25:30) to make sure that any softening that we see in the market doesn't endanger the overall targets that we have.

On the Life side, you're right, there's a particularly high level of gains. If we focus first on the bulk component, I mean, that's really a policyholder piece of the equation and it's not been driven by our shareholder need or expectation. So, I mean, I don't see it as a particular issue for sustainability of the Life performance.

Both sides of BOP and in NIAS, I mean, you've seen – probably a reasonable level of gains but I guess I'd highlight particularly in Q3 that, I mean, that's somewhat automatic. It's more an outcome of the accounting than a decision that the company has made because it's mainly the revaluation of property. So, unfortunately, we don't entirely control that. But those are the drivers of the gains that you've seen.

Q - Atanasio Pantarrotas {BIO 5933123 <GO>}

Okay. Thank you very much.

Operator

Next question from Paul De'Ath, Royal Bank of Canada. Please go ahead, sir.

Q - Paul C. De'Ath

Hi there. And just a couple of quick questions, hopefully. Firstly, on Farmers, just looking at the margin, the 7% margin on there, you mentioned in the speaker notes that this is kind of in line with long-term guidance. I guess in the more short term, is this kind of the level that we should be expecting that margin to be at?

That's question one. And then question two was just very quick thing on the non-core result, which obviously was one of the kind of swing factors in the numbers for this quarter. Just if you could sort of elaborate slightly on that and where that number might be going in the next few quarters, that would help a lot. Thanks.

A - George Quinn {BIO 15159240 <GO>}

Okay. Thanks, Paul. So first of all, in Farmers, I mean, yes, I would guide you to expect the margin to be around that level. I mean, I think we've seen it around here in the past. Our guidance was at 7%. It was sustainable and that's where we've ended up this quarter. So, I mean, I would suggest that you use that as the forward-looking. (27:47)

On the non-core side of things, I mean, non-core is slightly different. As you point out, we've gone from, I think, it was kind of $24 million or $25 million profit in the same quarter last year to almost the same number the opposite same this quarter.

I mean we still have a number of portfolios in there. I mean the priority is to get rid of them and ideally release the capital as quickly as we can. So you will still see a bit of volatility in non-core, I mean, the decisions there will be driven by what we perceive to be shareholder value.

But that doesn't mean it's relatively difficult to predict the absolute impact in a given quarter. I mean, having said that though, the maybe amounts that we have left are not huge. It's unlikely, I think, that you'd see large – very large swings in profits or losses on a given quarter that I mean you might see a bit disturbance from time-to-time. So my apologies that I can't really give you a clear steel (28:54) on the likely level for non-core business.

Q - Paul C. De'Ath

Okay. Thanks.

Operator

Next question from Thomas Seidl, Sanford Bernstein. Please go ahead, sir.

Q - Thomas Seidl {BIO 17755912 <GO>}

Yes. Thank you, good afternoon. Two questions. One on the General Insurance side, we note that the main area growing right now is international market, 9% in local currency, however, this is the weakest margin market. And I wonder whether we should expect, hence, a deteriorating business mix and if this is sort of the right direction Zurich wants to go.

And secondly on Farmers at 0.6% growth according to what we know, this means Zurich – Farmers is still losing substantial market share in the U.S. And I remember from the Investor Day last year that one of the actions management wanted to take was cost-cutting as Farmers to be more competitive. And I wonder if you could give us an update where Farmers is on this cost-cutting journey?

A - George Quinn {BIO 15159240 <GO>}

Thanks, Thomas. On the first one, I mean for obvious reasons, it's not (30:04) to achieve a deteriorating business mix. I mean, we're looking to allocate capital to areas that generate rate returns. If we see growth whether it's in Global Corporate, NAC, international markets, Europe or anywhere else, that we believe offers attractive returns then we have the capital to support it. But obviously, we're not looking to chase this turn (30:26) by allocating capital to business that doesn't return the required level of return.

Q - Thomas Seidl {BIO 17755912 <GO>}

I think – so, it's fair to say that IM or international market is the lowest RE segment and also looking just to the plain number like combined ratio net of nat cat is 102% which is markedly above the rest of the group?

A - George Quinn {BIO 15159240 <GO>}

Yeah. I mean it's coming back to gross. I mean it's 9% from a low base but 2% adjusted in Global Corporate and you can guess which one has the far more significant contribution in profitability.

On the second question on Farmers, I mean I think if you still put the point sets, I think you're right. But I mean I think we would go further than simply to look at the point sets. (31:15) If we look at the core of what Farmers reached – have attained (31:18) over time. So, therefore, we excludes the 21st Century brand which, of course, is not supported any more. And we also exclude the business insurance ran through independent agents. We see a number more like 2.6%. I mean we'd always be happy with a number that's higher, but given where Farmers is coming from, I think we're very happy with the progress that we've made. I mean we hope to see more. We hope to see it sustain what they've done. But, I mean, for me, this is a relatively important watershed for Farmers.

On the cost control side of things, I think things are broadly flat. And Jeff and the team has certainly been looking at trying to optimize things in Farmers management services, but I don't have a particular update for you. And of course, we'll Jeff, again, with the investor update in December, and we'll see if we can give you a bit more insight there. Thank you.

Q - Thomas Seidl {BIO 17755912 <GO>}

All right. Thanks, George.

Operator

Next question from Nick Holmes, Société Générale. Please go ahead, sir.

Q - Nick Holmes {BIO 21515144 <GO>}

Hi. Thank you very much. I just wanted to come back on the GI expenses. A lot of your peers seem to be focusing on direct insurance. And really, you don't seem to be doing this nearly as much as some of the other major European insurers. I just wondered if you could tell us a bit more about the rationale for this. Because, I mean, it does seem to be a very obvious way of managing expenses down. Thank you.

A - George Quinn {BIO 15159240 <GO>}

Thanks for the question, Nick. So the – I mean, it's not as though it doesn't have the right insurance businesses. It does. It has one in Italy. It has one in Germany. I mean, but our focus is typically on a different segment of the market. I mean, Zurich is a – in terms of a Zurich proposition, we normally offer more than simply the (33:22) lowest-touch possible product. And therefore, I mean, you don't normally find us compete at the bottom-end of the market, on lowest-priced, lowest-cost product. It just doesn't fit with us.

So we're looking to – I mean, we've been doing a lot of work over the last two years to segment the portfolio. We look for the customers that we think the value proposition fits best and then particularly, (33:47). And it does mean that in some markets, we run a high-expense ratio. But of course, we look for customers to pay for that, and we look to provide the customers with the service that that would imply. And I think given the way that we operate an expansion – a wholesale expansion of the business into what's really a low-margin business on the direct side, I'm not sure it would make much sense for us.

Q - Nick Holmes {BIO 21515144 <GO>}

Okay. So you don't think that in personal lines, direct is sort of some – the big question mark in Continental Europe that could change personal lines quite dramatically?

A - George Quinn {BIO 15159240 <GO>}

I guess that's a much broader and bigger question. It's a question, I think, that we would see the model that we've seen elsewhere, for example, in the UK or maybe in these essential things like GEICO or Progressive in the U.S., importantly. (34:44) I'm sure, to some degree, you will.

But do I believe that's the only segment in the market that would be open to a company like us? No, I don't. Do I believe that we can find attractive returns in the segments that we have the proposition to satisfy? I absolutely do. So it's not that I ignore it. It's not that I think it's unimportant. But it's a segment of the market where I don't think we are particularly well-equipped to compete and we don't target that particular area. So we're looking at a different sector.

Q - Nick Holmes {BIO 21515144 <GO>}

That's great. Thank you very much. Very interesting.

Operator

Next question from Stefan Schürmann, Bank Vontobel. Please go ahead, sir.

Q - Stefan Schürmann

Yes. Good afternoon. I have two questions. The first one is on basically the survival ratio of your asbestos book. Can you maybe update on that now after having added to reserves and the – sort of the three-year survival ratio?

The second question is on basically claims inflation. I mean, you clearly state that the claims inflation is running below your average rate increases, but I mean, do you see any maybe increasing signs on the claims inflation side which is part of your statement that you see basically more headwind from the market environment?

A - George Quinn {BIO 15159240 <GO>}

So, on the first one, I don't know the answer to the question. And in fact, just before we started, I've realized that we have not yet answered the question. We'll have to get back, Stefan, on that one.

Q - Stefan Schürmann

Yes, sir.

A - George Quinn {BIO 15159240 <GO>}

Apology. On the claims inflation side, I mean, I guess the break spot for the time being is that, I mean, claims inflation still doesn't seem to be a major issue with the rate and loss costs still seem to be in reasonable balance in Q3. And there's – I mean, if we look around the portfolio, we don't see signs that claims inflation is eminent.

But having said that, I think we have to be cautious and we have to be cautious in some particular areas, I mean especially, obviously, the long tail ones that we're particularly exposed to. But I guess part of the current environment is that the, I mean, the trends are really driven by competition rather than claim inflection.

Q - Stefan Schürmann

Okay.

A - George Quinn {BIO 15159240 <GO>}

That's my perception.

Q - Stefan Schürmann

Yeah. Thank you.

Operator

Next question is from Niccolo Dalla Palma, Exane BNP. Please, go ahead.

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

Good afternoon, everyone. I have two questions. The first one on Global Corporate, earlier in the year – actually, Mike Kerner showed an interesting slide on where you are in terms of the international programs around $3.8 billion and how it had been growing for the last few years. I wonder whether you could give us an update on how that is growing now. And any comment you can make on the competition from the reinsurance sector in today's business or from new players? Or whether it's still something you feel only a very few players can offer? Hence, the growth is quite sustainable at those, close to double-digit levels.

And the second question on the APH reserves strengthening whether you could tell us which of the three letters it was. The reason I asked is there is some discussions on industrial deafness claims in the UK. Is that the reason or is it the asbestos part? I can follow up with the IR team later if necessary. Thank you.

A - George Quinn {BIO 15159240 <GO>}

No. No need to follow up, because that one I know. On the first one on the Global Corporate side, let's come back for an update on the $3.8 billion, I don't have that at my fingertips. On the competitive environment and whether this is a difficult sector to charge, I mean there are very, very few people who can do what our Global Corporate business does. It's an incredibly high-touch business that requires an immense global network.

I mean, our risk engineers and in some cases, almost looking at integrated part of the risk management with some of our clients, so I think it's a very difficult business to replicate that requires – it's a heavy administrative burden not only from policy issuance through claim settlement. It's clear to me that there are a number of people who'd like to be in this, but I don't think it's easy at all. I think the barriers to entry to this particular group are extremely high indeed.

On the APH side of things, I mentioned earlier that we've added just under $70 million to APH in the UK and there's a bet on the A, so about $30 million is from the asbestos side, and the remainder comes from health-related topics.

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

Thanks very much.

Operator

Next question from Marcus Rivaldi, Morgan Stanley. Please go ahead, sir.

Q - Marcus P. Rivaldi {BIO 5739374 <GO>}

Good afternoon, everybody. So just coming back to the comments you made about achieving strategy, I mean only a few months ago now, I think in London, the sense I got was that there's a very high confidence within the group of exceeding the bottom of your target range and the sense I felt was you already have, at your disposal, lots of levers to drive the R element of that to a point where you can be achieving that? The terms today (40:10) clearly is a lot more, I think, cautious and I think I'm just confuse about the reasons you're giving out for that. It seems to be very apparent and have been there for quite some time. So I was wondering if you're going to comment about that.

Secondly, you also – I think, the half of your questions lots and lots about capital management and you gave a sort of structure of how you think about capital management. How's the managing the E moved up the agenda in terms of the priority list there? And then finally, just a question on the numbers, on Global Life, of the Europe was a major contributor to improvement in the Q. Is there any way you can give some sort of guidance, soft guidance with regards to your new sources of earnings, disclosure about what was driving that, please. Thank you.

A - George Quinn {BIO 15159240 <GO>}

So on the – so first one, achieving strategies. So apologies that I have caused confusion, I think – I mean, this probably might be enough (41:06) for communication. I guess what we're trying to do today to actually do in the (41:13) communication, something that I think we've been doing in the one-on-ones already. I mean, it wasn't really an attempt to change tone but it really was an attempt to make it clear to the market in general that we recognize what I think everyone else recognizes that I mean it won't get easier from here.

But I mean, it was actually aimed to be a slightly positive message around a negative one and that I mean, as you pointed out, around Q2, that was – and I clearly told and I think everyone I met that we have the levers out on disposal, that we believe will be sufficient to get us where we need to be.

So I mean this wasn't an attempt to change direction or somehow signal some fear that the targets are not achievable. I mean, actually it was the opposite. It was trying to signal that we're realistic about what's taking place and we believe that in addition to the realism, we actually have the tools at disposal to address the issues that that realism brings; so apologies for the confusion.

On the capital management, has the E moved up the agenda, absolutely not. I mean, E is always really high on the agenda. And net – I think that, I mean, it's typically very difficult in an insurance company context, particularly in Life, to make significant changes in the capital allocation and the current environment is going to be relatively painful. It's going to cause volatility in the reported earnings that would not be welcome.

But having said that, I mean, because very few people do it, I think if you can do it, I think there's a benefit to be had so I mean I'm a firm believer that managing the E is actually more important than anything else for the business. So, if we look at the capitals allocated, it has a return that generated, but E is just really high on my list of priorities all the time.

Sorry. The last one was Global Life, but I didn't catch the question, Marcus. Could you repeat it for me?

Q - Marcus P. Rivaldi {BIO 5739374 <GO>}

Yes, certainly. So you just off the – Europe was a major driver for the improvement during Q3 this year. And I was just wondering if you could give maybe some color around the new sources of earnings disclosure. What may have been driving that particularly?

A - George Quinn {BIO 15159240 <GO>}

So I apologize. I can't connect it back to the source of earnings for you. We are always – we're focused on a number of areas trying to improve profitability. That obviously benefits us. But I mean, there is more going on into Global Life than simply Europe and some of the improvements that we see in other parts of the business is somewhat massed.

So for example, I mean, we've had very substantial growth in the contribution from the Zurich Santander business. But it's not so visible because of the impact of currency. And of course, currencies are risk that we take right in that business. I mean from a longer-term perspective, I would expect to see Latin America be a disproportionate contributor to what we see in Global Life.

But on top of that, I expect Europe to continue. I mean, the large part of what Kristof and the team are trying to do on the in-force management side is focused around Germany and the UK. We believe we can be a bit more efficient. We can tackle some issue around asset allocation and we can look at capital. So I mean I expect to see some of that continue.

But I mean, apologies, I can't connect it back to the source of earnings for you.

Q - Marcus P. Rivaldi {BIO 5739374 <GO>}

Okay. Thank you very much.

Operator

Ladies and gentlemen the conference is now over. Thank you for choosing Chorus Call and thank you for participating in the conference. You can now disconnect your lines. Good-bye.
