Y 2020 Earnings Call

Company Participants

- George Quinn, Group Chief Financial Officer, Member of the Executive Board
- Mario Greco, Group Chief Executive Officer and Member of the Executive Committee
- Richard Burden, Head of Investor Relations

Other Participants

- Andrew Ritchie, Analyst
- Ashik Musaddi, Analyst
- Farooq Hanif, Analyst
- James Shuck, Analyst
- Jon Hocking, Analyst
- Michael Haid, Analyst
- Michael Huttner, Analyst
- Nick Holmes, Analyst
- Paris Hadjiantonis, Analyst
- Peter Eliot, Analyst
- Vinit Malhotra, Analyst
- William Hawkins, Analyst

Presentation

Operator

Ladies and gentlemen. Welcome to the Zurich Insurance Group Annual Results 2020 Conference Call. I'm Myra the Chorus Call operator. I would like to remind that the 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 Agency Management.

Please go ahead sir.

Richard Burden {BIO 1809244 <GO>}

Good morning, good afternoon everybody. Welcome to Zurich Insurance Group's Full Year 2020 Results Q&A Call. On the call today is our group CEO, Mario Greco; and our

Group CFO, George Quinn. Before I hand over to Mario and George for some introductory remarks, just a reminder for the Q&A. We kindly ask you to keep to a maximum of two questions and if we have time, we'll circle back around again.

So, with that, I'd like to pass it over to Mario.

Mario Greco {BIO 1754408 <GO>}

Thank you Richard, and good afternoon ladies and gentlemen, and thank you very much for joining us today. I'd like to give you a few remarks before handing over to George. 2020 has been an unprecedented year with unforeseeable events of ranging from global pandemic and recession to civil unrest in the United States and the high level of natural catastrophes. Throughout this challenges, we have supported our customers and local communities while ensuring the safety and the well-being of our colleagues. The performance over 2020 confirms the strength of the business, the agility of our people and the effectiveness of our digital strategy with our business remaining fully operational throughout. On the back of this, we have increased customer satisfaction and employee engagement. This is already leading to growth in our customer base and will be supportive of further growth in the next months and years.

Our results demonstrate strong underlying performance with the decline in business operating profit for the full year, explained entirely by COVID-19 and by the above normal levels of the natural catastrophes. Even with these effects, our combined ratio remain at the level that when we started this journey would have been considered as a challenge to achieve.

The underlying performance of our property and casualty business was particularly pleasing. Not only did we experience a strong growth in gross written premiums, but we also saw strong improvement in the underlying combined ratio of 2.6 points. Claims related to COVID-19, net of reinsurance and associated frequency benefits have remained in line with the $450 million we reported at half year. A level which stands favorably against the peers of similar size in the industry.

This performance reflects the work then in recent years to improve the portfolio as well as the benefit of the recent price increases, combined with the current price trends which are expected to continue through this year, I'm really confident that our property and casualty business is well positioned to deliver further strong profitable growth. Our life business also showed the strong performance over the year with the growth of 7% excluding the effect of COVID and despite falls in investment yields and in Latin American currencies. The Group has focused on life protection business and capital-light savings products for over a decade -- a decision that serves us well as global investments remain at historical lows.

Farmers Management Services saw an improved second half performance and together with the acquisition of the MetLife, property and casualty business, I'm confident in the future prospects for the Farmers Business. During the year, we paid our 2019 dividend on time and in full. Our confidence in our plans and continued strong balance sheet means that we are proposing a stable dividend in Swiss francs in regards to 2020. As I look at the business today, we have adapted our plans to the changed reality, and I'm confident that the strong deliver in 2020 and the work done in recent years to improve the business position us well to deliver on the commitments we made in 2019 for the end of 2022.

I will now hand over to George to make some additional remarks.

Thank you.

George Quinn {BIO 15159240 <GO>}

Thanks Mario and good afternoon, good morning to everyone. I'd like to add some additional points on capital and the switch to the Swiss Solvency Test from Z-ECM. Today, we've reported an SST capital level, this is obviously not the one you were expecting, the principal drivers are an update of the Q3 estimate that we reported back in November, increased capital consumption related to additional growth that we expect to see in 2021 and some operating variances. It's obviously not good when the most significant item in the analysis have changed has nothing to do with the business. I'm sorry for this, and we've made changes to our processes so the best can happen again.

Although, we may not be happy with it, we go to this point, we are very comfortable with where we are. The updates of the Q3 SST number, it doesn't impact the other measures of capital on the old Z-ECM basis were in the upper half of the target range and we have a very significant excess from a rating agency perspective. In the past, we've also indicated that for -- if you compare our European Union business as a Solvency II ratio would be around 90 points higher than the SST ratio and this remains the case today. Although, we don't have a Solvency II ratio for the group, we remain comfortable that our SST capitalization would translate into Solvency II ratio at the upper end of those published by our peers.

As mentioned at the time of the third quarter, we've also provided a new capital target based on the Swiss Solvency Test with our target for the future being to maintain an SST ratio at or in excess of 160% which is equivalent to the previous 100% level on the Z-ECM. This underlines our commitment to a strong balance sheet and the maintenance of at least AA standards across all capital metrics. And perhaps, just away from the capital topic for a second, I just want to reiterate Mario's earlier comments regarding the strength of the performance of the business over 2020 and the confidence that, that gives us on the outlook for 2021 across all of our businesses.

With that, I think we're now ready for Q&A.

Questions And Answers

Operator

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

Q - Jon Hocking {BIO 2163183 <GO>}

Hi, good afternoon everybody. I've got two questions please. The first one on, so where you are in terms of rate increases versus claims inflation. One of your US peers they have a very similar price increase as yourselves in the fourth quarter was talking about 4% claims inflation. I wonder whether you could comment on that and also comment on EMEA would also be helpful, please. And then the second question, on slide 41 where you've got the SST bridge for 2020 in the market movements piece of 16 points for market volatilities, is that main interest rate volatility and I wonder whether you could come up with any of those reversed already in 2021. Thank you very much.

A - George Quinn {BIO 15159240 <GO>}

So Jon, it's George. So maybe on the pricing point first, can you hear me, okay?

Q - Jon Hocking {BIO 2163183 <GO>}

Yes, loud and clear, George.

A - George Quinn {BIO 15159240 <GO>}

Yes. Excellent. Good. So on pricing so you, so you've seen what we've reported today in terms of price trend in the business, continues to be very strong through the fourth quarter. If you look at the various geographies, US still stands out, so we are -- I mean, we're just about the same level that we saw in Q2, Q3 were about 17% for the year and we're above that in Q4. So, there is no obvious saying at this point that things are slowing down in any significant way.

Distribution across the lines of business is similar to what you've heard from me before at the Q3 call, so in the 20s across the two main classes of property and liability and lower on the others was motor just in double digits, workers' comp has actually come up quite a bit in Q4, so maybe responding a bit to the yield pressure, but specialty including credit is still pretty -- I mean, it's close to 1% currently.

From a loss cost inflation perspective, these are similar to what we saw in the year so we've held a view. So if you look at -- I mean, all in, we are seeing a bit more than 5% if you adjust for exposure because it's (indiscernible). I think the challenge of going to the market is that the pandemic has slowed things down in the system during 2020 and I guess at some point that will start to unwind. I mean, we've taken a very cautious approach around my liability and so for example, when you look at activity -- activity is down -- there might be a tendency to perceive those frequency and we've ignored that, then there is having process. So, we've assumed that even with the absence there's no change in underlying trends for the time being.

In other markets, so if we look at Europe, I mean Europe from a headline perspective and it's not as strong as the US, so the overall rate, we would see around 5% essentially has been coming up through the year stronger than the fourth quarter and the market that stands out is the UK, so UK is in double digits. It's obviously driven by commercial and again, stronger in the second half of the year again, Q4 well above the average for the year. From a loss cost perspective and the trends in Europe a bit different to those we see in the US -- you don't see quite the same issues that exist around social cost inflation, if you look at pain points in Europe in the portfolio, they tend to be pretty similar to what you see elsewhere, so it tends to be casualty lines, it tends to be professional indemnity, some financial lines like D&O for example. But, I guess kind of sum total of all of this is the significant margin expansion, both in the results, in the second half of the year and we expect that to continue into 2021 and in fact, given what we're starting 2021 most likely that will mostly spillover in 2022 in terms of outcome.

On the slides and then the volatilities, so I mean it will be volatility across a wide range of the asset classes. I mean, you're seeing quite a bit of move on interest rates, I'll be part of the driver. I don't have the precise breakdown and I can't give that to you immediately. The challenge with a bit, is that because of the look back period that we have in the volatility model, will take quite a while to work its way through the system. So, I think the elevated volatility I assume, I mean the markets come down, it will average down but we'll have that type of impact in the reported number -- I would expect for most of 2021 if not into early 2022.

Q - Jon Hocking {BIO 2163183 <GO>}

Okay. It's very clear. Thank you.

Operator

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

Q - Peter Eliot {BIO 7556214 <GO>}

Thank you very much. Sorry, the first one is on solvency George. But, I mean I guess you always set the quarterly Z-ECM ratio estimates were accurate within 5 percentage points. It sounds like this was a more of a sort of one-off event. I mean, should we sort of think going forward, is the sort of quarterly SST estimates as being sort of pretty accurate or should we expect it to move around, yes, I guess that sort of goes for the full year number as well. So, I guess you haven't sort of fully filed that yet with the first one.

Second one on P&C investment income, looking about it, I guess it fell by 155 in H2 alone, given that trend and given the big gap to the reinvestment yield, I was quite positively surprised that you were guiding to sort of only a drop of 50 to 100 for the whole year in 2021. So, I'm just -- I wonder if you can, I mean is that just explained by the maturity profile of the assets or is this sort of something else that I'm missing there. Thank you very much.

A - George Quinn {BIO 15159240 <GO>}

Yes, thanks Peter and no need to apologize for the first question. So, I mean I think all of you would expect the numbers to be pretty accurate, so that's what you can expect from us going forward. I mean, we made changes in Q4, which was to automate quite a bit of the quarterly production that's of course what's triggered the revision that we've reported today, and I expect which is the level of quality that you're familiar from across the other capital metrics that we disclose on a regular basis, so you can expect it to be accurate.

On the P&C investment income, I think the reason why you see this impact is there's really two things taking place this, if you look at last year, as you point out, you see a full that's larger than you'd expect and that's because you have a combination of yields also what we think is probably -- but not probably, we can see that dividend receipts are quite a bit lower than they've been in the prior year and if you look at the numbers, it's about $50 million in the P&C number for 2020.

So, as we look at the yield change next year -- I mean, we've got about 100 basis point gap booked to the new business, so that still equates to about $100 million but we're expecting to see some of the absence of dividends in 2020 start to recover in 2021. So, I think it's those two things that offset to some degree, which is why you're hitting that $50 million to $100 gains.

Q - Peter Eliot {BIO 7556214 <GO>}

Yes, that's great. I guess I was thinking of the dividends more sort of H1 phenomenon whereas I was sort of looking at the running yield on H2. But I appreciate, there's a lots of moving parts. Thanks a lot.

A - George Quinn {BIO 15159240 <GO>}

Thank you.

Operator

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

Q - Andrew Ritchie {BIO 18731996 <GO>}

Hi there. First question is on your outlook for NEP growth in P&C, I guess if I have been writing the press release I would have been tempted to say mid to high single digit, I'm just trying to unpack kind of your guidance of mid-single digit, which I assume is 5, because the stock of unearned premium reserve is the highest has been I think for five years you, I think imply you're not renewing some of your reinsurance. And then on retail, I guess retail is COVID impacted, but again, retail and SME seem to bounce back in the second half. So could you just unpack I guess my angle is why only mid single-digit NEP growth for 2021 and the second question on reserves I guess, just an update, I think the implication is you that added a little bit to US liability ex-work comp in the first half. Did you do that again in the second half and on reserves I noticed Australia or Asia-Pacific is the gift to keep giving what is it, was there another sort of round of looking at some of the long tail business there. There appears to be looking at the PYD by division. Thanks.

A - George Quinn {BIO 15159240 <GO>}

Thanks Andrew. So on outlook, I think I'd probably start by saying that we wouldn't necessarily conclude that mid single digits, could only encompass 5 and so we might be slightly more generous than that. I agree with you that it's only compared to -- there are some factors driving the results and you've commented on some of them. You would anticipate something at the higher and in fact, of course if foreign exchange stays where it is, the loan will drive it quite a bit higher than the mid single digits.

I mean the -- I think we'd like to be a bit cautious on the growth outlook. I mean we want to leave room as necessary to make sure that we can continue to manage the portfolio, we did some of that last year. So for example, MedNow [ph] and some of the credit lines were targets for reduction. I mean I don't know today that there are a significant parts of the portfolio that we'd look to shrink, but we have tried to be a bit cautious just to reflect the fact that I mean we do at times, as we review the portfolio identify parts where perhaps we're not quite as enthusiastic about growth, but certainly like-for-like, and you'd probably see something a bit higher than mid single digit growth even allowing for something that's not 5 if everything continues as those. On reserving, I mean no great done major changes in the second half of the year around US liability. I think there is a -- as I address but it's quite small compared to what we see before workers comp, workers comp in the US and European retail continued to be the biggest drivers of the positive vote on NPS. You're correct Australia continues to be the gift that keeps on giving and in this particular case it's PI and the particular design and construct. So, it's a cladding topic in Australia that is driving that experience, but I mean, overall as you can see from the outlook, I mean, we can easily manage PYD target.

And if I look at reserve strength into future, arguably, if you were to -- if you were to take a slightly more short-term view of workers comp, so we take a fairly long look back on the like factors for workers' comp. If you can move to a five-year rather than the 10-year or longer perspective and there would be a very substantial surplus in the current reserve position.

Q - Andrew Ritchie {BIO 18731996 <GO>}

So, is it fair to say not all of that -- I think you said this earlier on, I just wanted to clarify, not all of the frequency benefit was allowed to drop through, some of that has been trapped in reserves, is that fair?

A - George Quinn {BIO 15159240 <GO>}

Yes, that's fair. So, just given the uncertainties that are still out there, we've decided it's appropriate to hold some of that back for them.

Q - Andrew Ritchie {BIO 18731996 <GO>}

Okay, thanks very much.

Operator

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

Q - Farooq Hanif {BIO 4780978 <GO>}

Hi everybody. First question on expense ratio, so you've very kindly shown what the ratio would have been without the premium refund effect. Can we just take that as a base for 2021 and can you talk a little bit about how, given the commission ratio seems to be flattening out, how some of your expenses could actually work into that ratio over the next few years. And then secondly on cash remittances, so you've obviously had a higher payout ratio because of surplus capital you say in the P&C business. I mean, is your aim going forward to try and manage that number to be quite smooth and avoid discontinued continuity or do you think we could see more kind of the surplus capital upstream to support that number going forward. Thanks a lot.

A - George Quinn {BIO 15159240 <GO>}

Thanks Farooq. So on the first one on the expense ratio, so, I think I need to be a little bit careful what I say, I think, I mean as a CFO, I'd love to just tell you that, yes, absolutely we're going to maintain expenses exactly where they are. There's clearly an expense change that is driven by the circumstances of last year that's definitely going to continue into the early part of next year and some of the structural changes that will happen in the way that we operate means that some of that -- most of that maybe never comes back into the organization, but I think to make the assumption that there is no prospect of any of it flowing back is too aggressive.

Having said that, I mean, you know that from the Investor Day that we had in November 2019 there's ambition to bring the expense ratio for the group claims around 12 so there's a number of other initiatives that are currently ongoing. I'm trying to push efficiency, we're looking to try and again reduce and adjust the resource allocations in the group, so that we're -- just some of the back-end within the corporate center and allow the business to expand slightly while still achieving the overall goals for the group.

So, I think it would be in the very short term assuming that we start to see, for example, travel come back to normal, you would expect to see some of that come back into the picture, but not as much as we have in the past. On the commission ratio, so I mean, you've seen that flow, I know we've talked in the past of it. I mean we do have level of appetite for that and I think we're not that far off of it. I mean, we do continue to evaluate transactions with distributors that we think would be a good use of our capital. I mean, they tend to be the -- because the mass consumer type things that do still come with elevated commissions.

I don't know that we'll do that in 2021, but I want to leave open the possibility, but I mean there is a limit to how far we would be able to see the commission ratio rise. On the cash remittance topic. I mean I don't want to say I'm a bit greedy and I think it just makes sense from a group perspective, if we can move capital into the center, it is better off doing that because it gives us far more flexibility to deal with any challenge that kind of occur, in any particular part of the group. I think the reality of it is though, as we approach regulators, particularly to deal with excess capital position stresses target, I mean regulators don't tend to react to, well to sudden shift in the capital base of a subsidiary. So, we'll normally try and agree a step-wise process over say, two years, three years to bring us back down to target and we've been doing that pretty consistently over the course of the last four or five years. I mean, the challenge or even maybe the good news behind as we address existing excess capital is what we tend to find is that by the time we finish that process the business has now generated new excess capital level and we then go back and agree a plan to take that.

So, the reason that you see this pretty strong number for last year, which of course is quite a bit ahead of what you'd expect given the performance of the business just what we've done with, I mean, one of our largest businesses. So they've talked to their regulator about how they come back to target and the plan is that, that's not just a single year topic, that will be a, say, two year, three-year exercise and that's helped balance some of the shortfall that'd you'd otherwise expect because of COVID in 2020.

Q - Farooq Hanif {BIO 4780978 <GO>}

So, just on that, it's possible but obviously not a guarantee that you could see the payout ratio being above 85% in some of the future years, as you put this into place?

A - George Quinn {BIO 15159240 <GO>}

It's possible.

Q - Farooq Hanif {BIO 4780978 <GO>}

Okay. Thank you very much.

A - George Quinn {BIO 15159240 <GO>}

Thanks Farooq.

Operator

The next question is from Michael Haid from Commerzbank. Please go ahead.

Q - Michael Haid {BIO 1971310 <GO>}

Thank you very much. Good afternoon. Two questions, first on the net realized capital gains you had in the fourth quarter, which were significantly above my expectations, can you tell us what were the motivations of this high disposals of equities and real estate. I saw that you left the equity ratio within your portfolio unchanged. And second question, with respect to expectations for the top-line growth in P&C and 2021, I saw you expect a mid single-digit -- possibly above 5% growth in P&C on net earned premiums, also the SST was burdened by some higher growth assumptions presumably in P&C, I would have expected some pressure actually on commercial premiums not coming from price, of course but from volumes -- premiums are tied to client revenues. So, can you tell us your view on how this affects the growth and maybe you can provide a breakdown of how much of the premium growth is price driven and how much is volume?

A - George Quinn {BIO 15159240 <GO>}

Michael, thanks very much. So, on the first topic of net realized capital gains. So, you've got variety of drivers, so property is straightforward -- within property I think we've talked in the past about the fact that we've got one of our largest business units, that is probably slightly over exposed to property from a capital structure perspective as well the overall allocation that we have the property I think is perfectly reasonable. The way that we've actually financed that from a capital perspective, is inefficient and we've been correcting that over the course of, I mean, probably the last two years. I think there's still a bit more to do, but Urban and the team has made great strides in this topic, in fact some of what you see at the end of last year again as I was addressing that overweight position in one of our businesses. On the equity side, I mean it just varies depending on what the managers are deciding to do. I'd say that probably also the realized gains are a bit higher than I expected towards the end of last year, it obviously has a slightly negative impact that it puts a bit of pressure on the ROE, but we tend to leave the team to say what they think they need to do when they need to do it.

And on the growth topic on P&C, I mean I think the point is absolutely valid. So the you've only got a bit of a competition between rate also activity and I think I add a third thing to the mix and that's just the budgets. Some of our clients so I mean I've talked cycling 4% numbers some of their clients over the course of the last six or seven months I know that this point is struggling to some degree. Was, I mean what's happening in the market, but I think we seek to price of selling one issue. I think capacity is this point at least as big an issue for some companies there was an absence. In some lines of business and of course that's plus driving quite a bit of the rate picture.

And so I think there is a, I mean, whether it's activity driven, whether it's just the fact that maybe someone retains a bit more risk either because they still make price or because they have lack of capacity. I mean there is some offsets in the top-line growth, but having said that, when you look at the rate that we're seeing in commercial at the moment, that's going to overwhelm any volume or other impact and we have a load for that and the estimates that we've given today, so in the comments I made to Andrew earlier as we think about 2021, we've said mid-single digits maybe that's a bit north of the midpoint to that range. And certainly, we are also allowing for the fact we may continue to manage the portfolio. So, like I think the opportunity in 2021 is played by stronger and then again foreign exchange if we continue to be throughout the year where we are today that we're also boost growth and the remainder of the year.

Q - Michael Haid {BIO 1971310 <GO>}

Okay, thank you very much.

A - George Quinn {BIO 15159240 <GO>}

Thank you.

Operator

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

Q - James Shuck {BIO 3680082 <GO>}

Hi, good morning, good afternoon everybody. George, my first question is on the reinsurance recoverables, if I look at that number over the last 18 months or so, it's increased by close to $3 billion I think the reserves have grown over that time but even in relation to the reserves that number has gone up, I'm just wondering how much of that actually relates to COVID type issues, and if you could elaborate on any potential friction points with the reinsurers with that amount, please. And then secondly on the SST I think calibration is interesting particularly any compared with the Z-ECM so the market risk is

68% now, that was 52% under Z-ECM from the SST interest rate sensitivity is doubled to about 19.350 bps [ph] the credit spread sensitivities to come down. Can you elaborate a little bit on how you're seeing that market risk and how you going to manage the SST volatility going forward, please?

A - George Quinn {BIO 15159240 <GO>}

Okay thank you. So, on the reinsurance recoverable topic, it's tricky to look at the headline numbers because there is a bunch of stuff in there that's with either captive relationship so I mean things that simply flow straight through our balance sheet on the way back to commercial clients in many cases so it can be a bit misleading to look at the rise and it should be that solely to a rise in gross claims that translate into higher expected to cover now having said that, I mean the point you make about COVID is clear so if you compare. I mean, where we are today to where we were say, at the half year so, since then we've had the FCA decision in the UK and well, as you know our own wording was upheld the industry has lost on the resilience smoothing so that's triggered there is no losses the that topic and has also triggered some additional losses.

I mean in general, both of those have been absorbed by reinsurance currently so it has increased the recovery and, in fact, I mean through a combination of COVID and the other cat losses through the year like more sally the civil unrest topics we're relatively deep into the aggregate at this point. So there is a more substantial recovery expected that now in terms of risk from that, and I mean, obviously, we are in regular contact with a reinsurance partners we updated and prior to renewals aggregate. I mean, not just about the drivers of using potential ranges on for the couple of they're backing, and, of course. Well, no one said yes absolutely will just waiver through. I mean we're not anticipating significant issues here. I think the, we've tried to structure. I mean what we expect in a relatively conservative manner and not trying to be aggressive, although we attach this to the reinsurance protection.

I think that puts us in a good place in terms of risk around expected recovery. So, I don't think those it is an indicator in that higher number, that means as a higher risk.On the second point on Z-ECM versus SST and volatility I mean it is I mean, apart from the thing I talked about in terms of is a tricky year. I mean we've seen market risk consumption passively increased by pretty huge amounts mainly driven by the two things it came up at the top of the call. So obviously, interest rates, as you mentioned also market volatility.

I mean, from a risk perspective and have manage going forwards. I mean I think everyone is aware that I mean SST is going to bring it will bring more stability and Z-ECM and if I mean that's partly reflected in the what's happened in Q4 in terms of the difference in the movement of the two numbers. I think in terms of risks and how we approach the management over, I think that's the philosophy actually should be the same. I mean the, if you look at it fundamentally Z-ECM typically doesn't have. I mean any dampening measure. We do get some benefits under SST that we pick up some of the US from the Solvency II entities.

Although we get no benefit of that on the required capital side. So, I think the existing mechanisms that we have in place to manage our interest rate risk will certainly help us, but I think also as we think about capital allocation going forward. And some of the things that we're going to do anyway to reduce some of that sensitivity, even under the old model equally filers under this. So I think as we look at some of the portfolio action in some of the portfolio simplification that we intend to take over the next year or two. You know it's a close correlation between those portfolios and the contribution to this particular risk.

Q - James Shuck {BIO 3680082 <GO>}

Okay, thank you very much George.

A - George Quinn {BIO 15159240 <GO>}

Thank you.

Operator

The next question is from William Hawkins from KBW. Please go ahead.

Q - William Hawkins {BIO 1822411 <GO>}

Hello, thank you very much. George, I wonder if I could come back to the answer you gave Farooq about the cash remittance. Could you help me maybe by being a bit more explicit on what the excess capital was within the $3.4 billion, again you've guided qualitatively to neutralizing the impact of COVID, but obviously it depends on how much of that growth for that is in America or anywhere else. So if you could be helpful on that will be kind.

And then again, just to be clear, in your final part of the answer, given that you've got more excess capital to come up this year and possibly the year after and given that the moment your budget still look all right rather than saying it's possible you're going to be higher than $3.4 billion or whatever in 2021, is it not almost inevitable or is there some other moving parts of the downside, I wouldn't just thoughts off and then secondly, please could you maybe give a bit more color on your thought process behind some of the changing assumptions on the ROE waterfall on slide 7, I mean familiar, I guess, the investment income and portfolio quality changes directionally seem quite obvious, but I'm a little bit surprised that you've reasonably visibly count the business growth impact and also the productivity again, I would have thought given the hard market and given the opportunities you're taking. I appreciate the growth is capital intensive, but I still would have thought that your growth should actually be accretive to ROE rather than incrementally dilutive and again activity that rate is lower, but both, everything we've heard from Zurich over the past 18 months is about better productivity rather than tighter so why of those two numbers taken a bit of a hit.

A - George Quinn {BIO 15159240 <GO>}

Yeah okay, so on the first one on the US special is a excess of what we reported today, so hopefully that answered that question.

Q - William Hawkins {BIO 1822411 <GO>}

I'm sorry. Say again?

A - George Quinn {BIO 15159240 <GO>}

This special is a benefit 20%, can you hear me well?

Q - William Hawkins {BIO 1822411 <GO>}

Yes. I can George sorry. Thank you.

A - George Quinn {BIO 15159240 <GO>}

Sorry, I lost you for a sec and so it's just to be relatively per se. So the second part of that question, so is the fact the create some expectation that some of that will continue I mean does that mean that we are anticipating something address no, I just mentioned a bit conservative I mean, I think if you look at the cash remittance numbers that we've generated so in the last cycle we were quite a bit ahead of what we expect it to be. And of course that was to a significant extent we're not entirely but to a significant extent driven by us, making sure that we were efficiently managing the placement of capital around the Group, and there is no change in that process for us today.

On the second topic on the COVID, let me just turn to the page so I think on the concerns of the productivity, it's not, we've lowered the target is simply a reflection of where we've now got into in the current number and so, I mean the ambition is still was saying, but we actually delivered a part of it and I think for the reasons that I gave an answer to the earlier question from Farooq around the expense ratio.

I mean we've maybe we've accelerated but we maybe we've had some help in the course of 2020 has given the change in activity, but the overall goal is certainly unchanged, it's just a reflection of a change in the starting point is a way to, I thank you in terms of growth. I think what's happened there is, if you go back to the Investor Day conversation that we had back in 2019. They were selling more of an expectation of retail growth and the modeling that we've done.

And of course some of what we had geared up to do is completely targeted to see that as a more significant driver of the plan over the course of the period seen from today. We just don't have that perspective. So it's not that we don't like that, so we wouldn't take advantage of that, if that was to offer it. But we just think that the market conditions around that topic and not as conducive then we'll see far more driven by rate on the commercial side. So, I think that's really why you see some of the change, yes.

Q - William Hawkins {BIO 1822411 <GO>}

And at the risk of stating the obvious, the retail comment you just made is COVID related, right?

A - George Quinn {BIO 15159240 <GO>}

Sorry, say that again?

Q - William Hawkins {BIO 1822411 <GO>}

At the risk of stating the obvious the cautionary comment you made about retail is all COVID related?

A - George Quinn {BIO 15159240 <GO>}

I mean it depends, the, so I think in my mind the way I see here is the certainly is a issue that's obviously knocked some parts of the business, it will take longer to recover. And I guess the part of our portfolio is always there is the travel topic. So you see it overall in the Cover-More number and in particular in the APAC number, but there is a secondary issue, which is that the -- I think the frequency have driven a more competitive retail environment I think that will persist for a while and it just makes I think the environment bit trickier so, for us it is makes a bit more sense to allocate bit more of the capital towards commercial because that's what we see the stronger opportunity economy.

Q - William Hawkins {BIO 1822411 <GO>}

That's great George, thank you.

A - George Quinn {BIO 15159240 <GO>}

Thank you.

Operator

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

Q - Michael Huttner {BIO 21454754 <GO>}

Good enough, and you must be -- in your words quite pleased I expect the numbers here quite cautious, but I had questions, because my peers are so good on questions, but I couldn't think amazingly clever. One is on Farmers and the other one is on business for sale from the farmers would be a bit contentious here and say, well you can say the business model is to lose market share actually had capital and by businesses with the 2009 or something so in first century now in you're buying MetLife, and I just wondered how you would react to something which is a little bit aggressive policies and linked to that, why isn't the farmers in that roughly waterfall chart through 2022 and then the other broad question kind of fishing a little bit is, when you talk about allocating capital are the business is the sale or can you can you say something about, there are some businesses with you like in the kind of mentioning retail, not so that's it. Thank you.

A - George Quinn {BIO 15159240 <GO>}

Thanks Michael, I think I'm pleased with almost everything apart from maybe one number, the I think on Farmers. I mean, I remember the questions that you posed to Jeff at the Investor Day back in 2017. When we were all together in London. I understand why you put it that way but that's debt I know the way we think of it. I mean we don't. I mean that's

a. I mean from a longer-term perspective, I don't think you need to operate at farmers operate that way I mean if you see the business and the business model today we know that I know you guys are all very familiar with I mean, the very positive nature there's obviously fairly consistent concerned the growth is hard to come by, because of the expense levels that you end up with a structure we've talked in the past, but I mean that's at least partly compensated by the way that people think about the return on capital within that structure, I think it's just is too easy.

So, the one of the things we've been doing with Jeff and the team is working really hard to working how can we support the business more what do you have to do to make sure it's competitive and to try and get away from that so that well this thing is a highly priced premium product and therefore plays in a completely different market and I think maybe the customer segmentation is a bit different, but I mean, Jeff and the team. No, when we look at the pricing, I mean the competitive and we just need to try and make sure that we can support the exchange the client to same ways to make the distribution system more effective because I mean, when Jeff talked to me and Mario it we can see that when we look at benchmarks against some of the obvious peers in the US and we've got again that needs to be closed that so things that we want to focus on and we think that will drive some growth that will drive higher production would drive higher fee returns for us

And we're also hoping that the acquisition of the MetLife business and the addition of a new distribution China will actually help accelerate some of those things. So I understand why you made the point but perspective on, it would be completely different, farmers isn't the ROE will is hidden in that business growth number, so apologies -- for not with me did you have a second part to your question?

Q - Michael Huttner {BIO 21454754 <GO>}

Yes, it's the fishing question what businesses are you thinking. So given that you just sound a little bit less a bit more lukewarm and retail. And then we would like to digital agency businesses or my favorite know determine life whatever.

A - George Quinn {BIO 15159240 <GO>}

So, I think. So you can appreciate the lots of reasons why I'm talking to list group of businesses that we may. I mean on sale in the future. I think I just one thing to be careful of to the comment I made to well on retail, I mean that's no, it's not a long-term perspective, that will be something we don't like retail and only love commercial is simply a capital management topic, I mean we're looking for the stronger returns and to the extent that we can move sort of capital around on a way that things that we will always do what we can to maximize that.

So there's nothing wrong with retail. The challenges enrollment season orphan quite the same return. So, if you look at the portfolio and I won't get into an yes, that precisely what and where, but I mean, you guys can see how we allocate capital today, you can see we had a risks don't fit with the model. Overall, you're well aware of what solutions, the outside world offers. I mean hopefully we can use the market to help us again further improve the capital allocation over the course of next couple of years. It's actually more than that.

Q - Michael Huttner {BIO 21454754 <GO>}

Thank you.

Operator

The next question is from Nick Holmes from Societe Generale. Please go ahead.

Q - Nick Holmes {BIO 3387435 <GO>}

Hi, there. Thank you very much. Two questions please. The first is, can you tell us more about what's causing the 90 percentage point difference between SST and Solvency II sort of which parts of the business which risk areas. And then secondly, would it just make sense to publish a Solvency II estimate for the Group or is that simply a waste of time, do you think. Thank you.

A - George Quinn {BIO 15159240 <GO>}

Thanks, Nick. I was just, I'm reflecting on the second part of your question, thinking that I probably have a few too many capital measures rather than a few to view. I mean I understand why the terms of the immediate comparability with others rather than this fairly soft summary that we gave of how you end up with something that optically look to lower but Troy in the end ends up being substantially higher.

So, I mean I can't. I'm not going to commit to us doing Solvency II number. I mean the cost of day that would be -- we'll be pretty substantial. I know that one of our friends did that a couple of years back and I understand why they did it but it is tricky and just given the complexity of our businesses, and just given the other demands are out there want them to daily IFRS 17 for example, which is not a small undertaking it's just be it be hard to not only justify be hard to find the people around to actually do it for us.

So, I mean it's what we typically thing it to be? I mean what we can see clearly in the EU businesses. It comes with lots of caveats because these are typically standards model EU businesses are standard model Solvency II comes and you need to be cautious, when you're comparing them to the internal model outcomes of some of the peers for the entire group, I mean, when you look at, I mean what drives it, I mean there's a variety of different topics.

I mean ranges from things like, I think like the structure treatment of known Solvency II businesses and the way that capital requirement to say we show for interest rates and the capital requirements, some of the run-off capital requirements or additional expenditures have that are required in the Solvency II model. I mean there's a whole wide range of drivers, but then in the best is if you look at the EU businesses, we can see precisely what the differences are versus SST. We have an average about 90% currently it wouldn't be that significant, if you were to, move the entire group to a comparison to an internal model, but we're still talking about many point I understand the reason yes,

Q - Nick Holmes {BIO 3387435 <GO>}

I mean that that's very, very helpful, but just your pointed 10s of percentage points versus internal model. I mean if one was sake not standard model of the EU subsidiaries, but the, if they would be on an internal model and vessel. I mean, I think you've said in the past 7 that it's 40 to 50 percentage points around about that versus peers is that, I mean, I think you said that a few years ago. Is that still a valid comparison?

A - George Quinn {BIO 15159240 <GO>}

I think is a very substantial number and that's been the reason for only hesitation system, the basis for that calculation is quite all at this point today, so I want to be cautious, but as many times. I mean the challenges even if I calculate that number, other than to show you guys what is I can't do anything with it. It doesn't help me in managing the business I need to manage to the things that are relevant for us today and that's Swiss Solvency Test S&P's capital requirements and these are the things that needs to drive what we do.

Q - Nick Holmes {BIO 3387435 <GO>}

Great. Fair enough. Thank you very much.

A - George Quinn {BIO 15159240 <GO>}

Thanks Nick.

Operator

The next question is from Paris Hadjiantonis from Exane BNP Paribas. Please go ahead.

Q - Paris Hadjiantonis {BIO 19703051 <GO>}

Yes, hi, good afternoon from me as well. The first one on SST you've given us a minimum level that you're targeting, but I was wondering if you can give us an idea of what do you consider optimal so where should we be expecting you to operate, let's say and the second one is on the catastrophe ratio, which is going up to 3.5 for 2021. I was just wondering what is driving that, is it business and exchanges higher frequency or something else?

A - George Quinn {BIO 15159240 <GO>}

Great, thanks very much. So, on the SST topic so we've obviously indicated today that target is to be operating or above 160 historically if you look at the numbers we've been closer to the 200 Mark and so, I mean I would expect that you point normally see us operate somewhere between where we are currently in place somewhere at the high and maybe closer to 200 of course that will depend quite a significant degree on the external environment, what's happening in the financial markets and also on in terms of opportunity, because if we can deploy more capital attractive rates in the book as we can today, I mean we will use that capital strength to go do that. On the cat topic, what's driving it. I mean if you look, I mean maybe a couple of things. So we've taken off some of the core share that we had in the property book in the US. So that brings in a bit more cat exposure. I mean we're buying roughly the same protection. The deductible is slightly higher than it was last year. This given the growth in the portfolio overall. And it's really those two things in conjunction is trying to the slightly higher cat loss expectation.

Q - Paris Hadjiantonis {BIO 19703051 <GO>}

Thank you.

Operator

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

Q - Vinit Malhotra {BIO 16184491 <GO>}

Hi, good afternoon, George and Mario. Thank you, just very quickly, first thing is the litigation risk with George. In the past and today. Well, you commented, you remain comfortable with puts more gradual nature regarding wordings that we have seen a particular ruling in the US earlier this for the announcements, and if you still remain comfortable that just what I'm looking. So if you can comment on that please.

Second thing is just on the SST target. The 160. I mean the problem, I face of that see 160 was 182, I get to an excess capital, if you like of close to $5.5 billion because when I see $110 million versus $100 million I get to $3.5 billion. So, I'm just trying to figure out, I mean you've given like today that 100% those value equivalent to 160 of SST, but then just doesn't seem to be heading up on the excess capital calculation and also it's been 160 feeling a little like compared to the peer group. Just can you comments, please.

A - George Quinn {BIO 15159240 <GO>}

Thanks. Yes, thanks Vinit. So I guess short answer to the first question as I remain comfortable. I mean I think the, I mean, is to be expected and it will not be a completely straight line to the outcome. The overall outcome that we expect to the ends, but if you look at what's happened in the US so far across the industry, I mean the vast have gone in favor of the insurance companies. Even at the dismissal stage so before it reaches full trial and I think the, I mean you're going to see in most states and just given the numbers of state you're probably end up with state Supreme Court level for most jurisdictions. So, even with all of this all of these decisions at this stage. This point for everyone at the very end of this process. The key course in each of the states or way on the topic so even if you get a variety of outcomes and you've seen already in Ohio, where the case that we've had attracted some attention, a few weeks ago we signed done I think these things will get tied up at the end and we remain confident in the position that we've adopted and on SST and target ratios the I guess the you make an assumption and there is it's not unreasonable but I'm not sure I'd actually say that so I think and so the assumption or is that somehow the number that we've presented today is say precisely equal to the midpoint of was there Z-ECM is actually higher than the midpoint as you've seen in the disclosure based on the estimates that we've got, I mean there will be some differences between them and if you allow for the fact is edition maybe a bit higher than Bitcoin and if you want to correlate to the number that we published today.

Then I think that maybe actually answers the questions that you've asked about whether the excesses at different. I mean, they won't be substantially different today I can't guarantee that, because the two models, or no linear in relation that we will maintain that relationship into the future.

Q - Vinit Malhotra {BIO 16184491 <GO>}

Thank you.

Operator

The ext question is from Ashik Musaddi from JPMorgan. Please go ahead.

Q - Ashik Musaddi {BIO 15847584 <GO>}

Yes, hi. Thank you. Good afternoon. Just a couple of questions I have please. First of all, going back to James question earlier about some SST ratio and stress test, I mean if I look at your hurdle of about 160% so first of all, can you give us some clarity as to what this hurdle means, I mean below this do we think about dividend cut or how do we think about this hurdle rate and if you think about like a combined strengths of say falling rates rising spread and falling equities, which is not a unique stress, which is what typically happen these days. I mean, you can easily 160% because that's a 20 percentage point you have at the moment. So how do you think about the combined stress scenario rather than on an individual basis, so that will be first question.

Secondly you mentioned that you are trying to take a bit more about commercial lines at the moment versus retail lines so how do you, -- how are you thinking about the return differential between the two. I mean clearly price increases are frequency on the commercial lines but is it really translating into a much higher combined -- much better combined ratio so as to make that shift from commercial to retail, because if I remember correctly, I think a couple of years back, you were like pretty much focused on shifting away from commercial into retail and now we are thinking about the worst. So how do you think about over the cycle. Thank you.

A - George Quinn {BIO 15159240 <GO>}

Yes, great. I think on the first one. So the what is 160 main and what were the risk as a combined stress in the number and I think you end up what enhance for, and it's the same actually for both questions. So we're trying to avoid bright line. So, even under the old we approached it -- we had 100 to 120 Z-ECM and it nothing remarkable happened there. I mean the requirement was that there is a formal switch and how we operate internally. So, I am the capital manager. When we are within target the leadership moves to the Chief Risk Officer. When we move outside of tolerance. I mean in practice is nothing actually changes because the two of us we want closer together and whether it's and target or otherwise.

And we look at thanks circumstances about what has to be done. So all the changes is temporary in nature or is there something idiosyncratic. I mean we would apply all the judgment. I think you would expect us to apply, so that we avoid that would become a victim of the capital model and that should not be how this works. So, we have to apply significant judgment. We're required to present a plan. So, but there is nothing it's nothing significant happens as you go from 160 to 159 it really depends on what you think you headed from that will determine what we think the best course of action will be even under that combined strengths.

From a commercial lines versus retail perspective, I think if you look at the results. Okay. Again, I think you I don't want to give the impression, all of a sudden -- you say that mean retail thing is it's not attractive anymore and we suddenly pickup and try and move everything to commercial, given the scale of the organization that given the fact that we need to be a reliable partner I mean you can do, I mean what we are looking trying this where we have the ability to deploy more capital potentially take away in markets that are underperforming. We would look to do that.

The reason for that it's embedded in some of the results today. So for example if you look at, but to ex-cat, just to keep it simple. So retail for us last year would have been lately stronger than commercial so maybe the retail combined this is in the 94s, the accident year combined for commercial will be in the 95, if you look at it again this year. And just given the strength of rate already that's somewhat flipped around, so if you're looking at retail we do ex-cat also to would keep it clean maybe it's improved slightly. So, maybe you're in the 93s and if you're looking at commercial are in 91. And rate trends versus loss cost and commercial is way stronger then you will find that retail. There is a capital penalty that you have to have 9. So the commercial business change to be a bit more capital intensive.

So, it does need to produce a bit more. I mean that kind of differential is meaningful given that we would expect it to broaden rather than narrow the capital allocation choice that we make makes complete estimate.

Q - Ashik Musaddi {BIO 15847584 <GO>}

George (multiple speakers)

A - Mario Greco {BIO 1754408 <GO>}

Can I add a point -- because I don't think we ever said that we want to grow retail against commercial or vice versa. We want to grow both, but the cycle is not aligned into the times at which it's easier and more profitable to grow one with respect to the other. But in general, we don't have a preference. And we try to develop both kind of customers to commission in the retail as well as we can, but again we considered the market opportunity as we are supposed to do and we push harder depending on what is the potential opportunity that we seeing in the market.

Q - Ashik Musaddi {BIO 15847584 <GO>}

That's very clear. Just one more question. Sorry.

A - George Quinn {BIO 15159240 <GO>}

Hang on a second there, I would be conscious of the fact that there's a number of other conference calls. Just for other companies. Richard, are you happy to continue?

A - Richard Burden {BIO 1809244 <GO>}

I think we need to wrap-up in fairness to some of our peers out there. So, we should probably.

A - George Quinn {BIO 15159240 <GO>}

So, Ashik, if you don't mind, would be happy to catch up after the call?

Q - Ashik Musaddi {BIO 15847584 <GO>}

Yes, that's fine. It is not a problem at all.

A - George Quinn {BIO 15159240 <GO>}

...Richard and the team will address it there, but apologies -- too much.

Q - Ashik Musaddi {BIO 15847584 <GO>}

Thank you.

A - George Quinn {BIO 15159240 <GO>}

So, Richard can I hand it back to you?

A - Richard Burden {BIO 1809244 <GO>}

Yes George. Thanks. So, thank you very much to everybody for dialing in this afternoon. We are aware of the outstanding questions on the call, so we will come back to you from the IR team post the call. Have a good afternoon and thank you for your interest.

Operator

Ladies and gentlemen, the conference is now over. Thank you for choosing Chorus Call and thank you for participating in the conference. You may now disconnect your lines. Goodbye.
