S1 2011 Earnings Call

Company Participants

- German Egloff, Group CFO
- Martin Strobel, Group CEO
- Martin Wenk, Chief Investment Officer

Other Participants

- Fabrizio Croce, Analyst
- Farquhar Murray, Analyst
- Jochen Schmitt, Analyst
- Michael Huttner, Analyst
- Michael Klien, Analyst
- Ralph Hebgen, Analyst
- Rene Locher, Analyst
- Stefan Schuermann, Analyst

Presentation

Operator

Good morning. I'm Dino, the Chorus Call operator for this conference. Welcome to the Baloise Group half-year results 2011 presentation. (Operator Instructions) At this time, I would like to turn the conference over to Mr. Martin Strobel, Group CEO. Please go ahead, sir.

Martin Strobel {BIO 5296838 <GO>}

Thank you, very much. Ladies and gentlemen, it is my great pleasure to welcome you to our analyst meeting. German Egloff and I will present our semi-annual results to you. Both of us and Martin Wenk, our Chief Investment Officer, will be available for your questions in the question-and-answer round.

We intend to concentrate solely on the essential facts in our presentation. This will give us more time for a detailed question-and-answer session. After the short introduction, I would now like to go to slide number 3.

First of all I would like to present to you the highlights of the half-year results 2011. After that, German Egloff will take you through the key financial figures. Building on that, I would like to illustrate the course of the business from a market and customer perspective. To finish off, I would then like to present to you where we stand in terms of our strategic program, Baloise 2012. And end with our financial outlook.

Let us start with the most important performance indicators relating to our semi-annual results. They are illustrated on slide number 5.

Ladies and gentlemen. Baloise has realized a solid result in the first half of 2011. This result is based on our efforts to improve the operational excellence. Our profits were stable, despite a continuing low interest rate and an all-time low euro.

Our strategic program, Baloise 2012, is fully on track. It delivers a significant contribution to our profitability, as well as to our growth.

Our strong growth in premiums shows that we are successfully putting the opportunities offered by the market to good use. And we are able to build on our market positioning. Our Sound Safety World brand positioning creates higher customer demand in our target segments.

Once again our Nonlife business proved to be a strong pillar of Baloise. The combined ratio stands at a very good 93%. This high margin of our Nonlife operation grants reliable and high cash flows.

Our Life earnings recovered strongly. Here the stable, albeit low, interest rate level helped, as well as the effects from Baloise 2012. The positive development of our Life business can also be clearly seen in our strongly improved new business margin.

In a challenging financial environment we can build on a resilient investment income, demonstrating the strength and the quality of our asset management.

At the end of June, Solvency amounted to a strong 227%, one of the highest figures in the industry.

We are proud of our remarkable footprint in Belgium. The integration of Avero was completed and we expect the closing of the acquisition of Nateus in the near future.

After this brief outline, I would now like to hand over to German Egloff who will take you through the main financial points of the semi-annual report.

German Egloff {BIO 4782831 <GO>}

Thank you, Martin. Good morning, from my side as well. I am pleased to walk you through the results of the first half of 2011.

I can present a half year with solid figures. Once again, we were able to rely on our good operating performance and achieved sound results. Headwinds came up through external factors, in particular the euro development versus Swiss franc. The depreciation of the euro compared to the Swiss franc impacted both the balance sheet as well as the income statement.

The closing date exchange rate, which is decisive for the balance sheet and the impairments, closed over 2% down compared to the beginning of the year. The average exchange rate relevant for the profit contributions of the foreign units fell by a further 8% compared to the beginning of the year. The loss is nearly 12% compared to the first half of 2010. As we have seen, this negative development has, unfortunately, continued since June 30.

Premium growth of 3.2% was very pleasing. Here, I refer to the figures in local currencies relevant for the evaluation. We were able to achieve above average growth in many markets. Growth drivers were the Nonlife segment and the Group Life business in Switzerland. Business volume was lower, as expected.

The previous year still profited significantly from the Italian tax amnesty and the expected EU directive, which brought Lichtenstein and Luxembourg an extra volume of unit-linked business.

I would now like to explain the main aspects of the results, starting with the Nonlife business on slide 8.

The Nonlife business recorded very good growth of 7.5% in local currency. This increase in volume was positively impacted by the consolidation of the Avero in Belgium.

Building on the measures to strengthen our operational excellence and the strategic program, Baloise 2012, we could again achieve an excellent operating result with a gross combined ratio of 90.3%.

Profit before interest and taxes declined, due to the lower financial result. Nevertheless, on the whole, the Nonlife business proved itself to be a sustainable and reliable earnings power[ph] and contributed the largest share to the Group results.

Let me now explain the development of the combined ratio in detail on slide 9.

The biggest impact on the development of the combined ratio is stemming from the slightly higher claims burden and the lower impact of prior-year loss development. The underlying loss ratio was about on the same level as last year.

Large claims above CHF4 million have a negative impact of 1.5 points on the combined ratio. Again, we recorded some large claims between CHF3 million and CHF4 million, adding a further 0.9percentage points.

The unwinding of the German units. And the integration effect in Luxembourg and Belgium, weigh on the combined ratio. The positive effects from the efficiency enhancement measures of Baloise 2012 couldn't fully compensate this effect.

Slide 10 illustrates how the combined ratio developed in the individual countries. With the exception of Croatia, we were again able to achieve high margins in our major markets, guaranteeing stable cash flows. An excellent value of 84.3% was achieved in Switzerland.

Please note that the impact on the combined ratio due to the July storms will be reflected in the second half year. According to what we know at present, we expect these storms to impact the Group net combined ratio by towards 2percentage points, taken over the year as a whole.

We observed a strong improvement of the combined ratio in Germany. This is mainly due to a lower claims burden of major claims, in particular.

Due to the first time consolidation of Avero. And positive one-off effects in the previous year, therefore the development of the combined ratio in Belgium should not be compared to the previous year. Nevertheless it's at a very pleasing level.

Luxembourg, which again proved very profitable, delivered an encouraging result.

The combined ratio in Austria is the best the unit has ever achieved. Even if the result benefits from the absence of large claims, it still shows that the growth in target customer strategy, now in place for a number of years, is making a positive difference.

In Croatia, the above market growth, which was nominal, still weak given the recessive[ph] in economic climates, resulted in a combined ratio of above 100%, despite great efforts to cut costs.

All in all, based on the country results represented here, the gross combined ratio for the Group equates to an excellent 90.3%.

I'd now like to address the Life business on slide 11. Last year the business volume. And here, especially, the single premium investment type business, was strongly influenced by the Italian tax amnesty and the expected EU directives, as I mentioned earlier.

Gross premiums in local currency remain stable, despite the extremely difficult interest rate environment.

Profit improved significantly. The measures of Baloise 2012 are taking effect, which is also reflected in the lower costs. Additionally, the previous year was negatively influenced by falling interest rates, whereas these remain stable in the first half of 2011. The value of new business developed very encouragingly.

The increase of over 50% mainly stems from Switzerland, which benefited from the interest rate development within the last 12 months and the operational improvement, such as cost reductions or the changed business mix. This is also reflected in the new business margin that has improved by over 10percentage points.

I would now like to move on to the investment side on slide 12. Our asset management achieved a pleasing result in the face of the development of the markets. However, the high volatility remained challenging. In particular, our full attention is demanded by the development of the euro that has been going still downhill since June 30. And was, meanwhile, almost on par with the Swiss franc. Although we see a different trend in the last few days, we are still below the level of the half-year closing.

But also the negative development of the dollar, interest rates and the stock markets, which have all lost a lot of ground compared to their status at the end of June, are placing a strain on our business.

The most recent developments have caused us to increase the foreign currency hedge on the Swiss unit bonds further. And also reduce the share quota compared to the balance sheet (inaudible) through the derivatives. As you can see on slide 13, this was still 6.7% on June 30.

In these volatile market conditions it's good to be able to rely on a high quality investment portfolio. Our broadly diversified portfolio generates stable recurring earnings on a broad base. Our investment property, which has delivered consistently high revenue, stands out as a very reliable component.

The quality of the bond portfolio, which makes up for about 50% of the asset allocation, is presently often these costs[ph]. The quality of our bond portfolio, which was excellent already in the past, has even improved compared to the end of the year. Approximately 60% of the bond portfolio has a rating of AAA. And over 93% are rated above A. It was not necessary to perform any impairments on the total bond portfolio.

You will find a detailed list of the Government bonds of the so-called GIIPS countries that have come under scrutiny on slide 14. We have a total GIIPS exposure of about 4% of the bond portfolio, respectively 2% of the total insurance assets. We actively monitor the situation of these countries and will react on possible changes. As already mentioned, there are no impairments on these bonds. Furthermore, based on current information and understanding, we have no intention to participate in the EU financing program for Greece.

Let me now move on to the components of the investment yield on slide 15. The recurring income is robust, despite negative effects of the euro and the interest rates. The negative currency effect is, again, visible on the fixed income securities. This effect is partly compensated by the currency hedges under the balance sheet item Others. This equates to a net currency loss of CHF44 million.

The lower investment income is due to reduced realizations. This results in a non-annualized investment yield for the first half year of 1.3% in Nonlife and 1.7% in Life.

Finally I'd like to explain the change in equity on slide 16. Equity remains stable at around CHF4 billion and the negative development of the currencies is also reflected in the change in equity under the position annualized gains and losses. This effect is, however, over compensated by the half-year profit.

The available funds are resulting in a solid Solvency I ratio of 227%. Standard & Poor's recently positively acknowledged this strong capitalization in their rating report; you can find this information on our home page.

I'd like to thank you for your attention and hand back to Martin.

Martin Strobel {BIO 5296838 <GO>}

Thank you, German. I would like to elaborate on our business from a market and customer perspective. Let's start with a look at growth, which is illustrated on slide 18.

In the first half of 2011, the accelerated growth in our major markets, Switzerland, Germany and Belgium, successfully increased their growth and gained market share in most segments. Their growth is based on a sound positioning with our Safety World and innovative solutions that met the demands of our target customers. The growth in Belgium is also supported by the integration of Avero.

Our operations in Luxembourg and Liechtenstein -- you'll find Liechtenstein under other units on the left table -- are both confronted with a decline of business volume. We expected this decline since the previous half year was supported by the extraordinary effects in freedom of services business, the Scudo Fiscale in Italy and the effects of the then expected introduction of the European savings directive. Take out this baseline effect. And you see a stable premium development in Luxembourg and a further acceleration of the growth of our innovative variable annuities business in Liechtenstein.

It feels good to see the growth we achieved in a large number of countries and segments in the first half of 2011. I would like to especially highlight our growth of 7.5% in the Nonlife segment. This growth is clearly above market and shows that we systematically develop this core business of Baloise.

Having taken a look at growth, I would now like to provide you with some explanatory notes on the income side. These are illustrated on slide 19.

Looking at the EBIT of Baloise, we are proud of the development in Switzerland. Although being confronted with a continuing very low interest environment and an all time low euro in the first half of 2011, the EBIT increased by 68%. This remarkable increase is due to a solid Nonlife result, a strongly improved Life result and a further improved Banking result.

Our non-domestic operations are all affected by the currency translation; the weak euro takes its toll. On top of that, Germany now invests in the unwinding and the integration efforts. These investments. And the missing positive unwinding effects from the first half of 2010, explain the development of the EBIT.

In Belgium, integration effects of Avero, as well as acquisition efforts of Nateus, mirror themselves on EBIT level. Furthermore, we see a more normal Nonlife result without extraordinary prior-year loss experiences this year.

From the divisional perspective it is clear that our Nonlife business remains the most important earnings pillar of Baloise. The strong operational performance was affected by currency effects in the investment result in Switzerland, as well as on the Nonlife earnings from our non-domestic business.

Our Life earnings recovered strongly. A more stable financial environment and the positive effects of Baloise 2012 are the main reasons for this positive development.

Our Banking division was able to improve earning power; not a given in such eventful times.

And now to our Swiss operations, which are illustrated on slide 20. Once again, our Swiss business demonstrates its excellent operational profitability.

Nonlife, our management of target customers, combined with our Safety World positioning, leads to an above-market growth of 2%. Our Swiss operations achieved an outstanding operational performance with a combined ratio of 84.3%. Our investment in effective processes is paying off. The EBIT in the Nonlife business was affected by negative currency effects on the investment results.

In the Life business, gross premiums remained stable. In Group Life we grew strongly with annual premiums up by 7.7%. As an established full service insurer we enjoy our customers' trust and are able to grow with them.

With the aid of our innovative life insurance products, we were able to add new pension insurance business to a substantial degree. Our innovative variable annuities, as well as our newly launched unit linked structured insurance product, were well accepted by our target customers. These successes supported the strong increase in investment-type premiums. They increased by 66%.

The Life earnings recovered strongly. The more stable interest rate environment in the first half of 2011 and the positive effects of Baloise 2012 are the main reasons for the strong increase of the EBIT.

The effects of Baloise 2012 can also be clearly seen at Baloise Bank SoBa. Due to the growth and lower costs the operating result, as well as the net income, increased. The cost income ratio declined by 3.6percentage points.

Baloise Bank SoBa grew substantially. As a bank with regional roots we benefited from our trust-based positioning. At the same time, our Switzerland-wide business model, together with the insurance agent, gathered pace. You can find more information on Baloise Bank SoBa on the Internet, or in the appendix to this presentation.

On slide 21 I would like to give you a brief summary of our international operations. In Germany, the realignment is progressing well. The development of the premium income and the claims developments are favorable.

Our Belgian business is characterized by strong growth at a growth rate of almost 38% in Nonlife and almost 33% in Life business volume; we gained substantial market share. This strong growth is due to the acquisition of Avero. But also, without the acquisition of Avero, our Belgian business grew strongly with 6.2% % in Nonlife, demonstrating the good positioning of our Company. Our acquisition of Nateus is not yet included in the figures. We expect the closing in the near future.

In Luxemburg, our local operation made substantial progress. The integration of Fortis IARD is successfully completed.

In Austria we are continuing to expand our insurance sales force and are now substantially outperforming the market in terms of growth. In Nonlife, premiums grew by more than 10% and in Life, almost 6%.

In Croatia, optimization measures are making an impact. Nonlife premiums and costs overall are improving, even in a declining market environment.

Baloise Life in Liechtenstein, as already pointed out, we see a decline in the freedom of services business. Our variable annuities business gathered pace. In Switzerland, for instance, VA premiums grew by 20%. In addition to Switzerland, we now sell this product in Germany and Austria, thus further broadening the growth base for our innovative Life business.

I would now like to work you through the actual status of our strategy. Let's start with slide 23.

Our goal is to become one of Europe's most profitable and fastest growing insurers by 2012. In actual and quantifiable terms, this objective is aimed at increasing Baloise's sustainable earning power by CHF200 million per annum up until 2012.

In order to reach this target we have initiated the Baloise 2012 program in 2009. We are right in the middle of implementation and are fully on target.

Where do we stand in terms of implementation? Meanwhile many optimization initiatives are well advanced or completed. We further improved claims management in Switzerland, for instance. The efficiency programs in Belgium, Switzerland and Croatia yielded substantial cost-reduction effect in the first half of 2011. Also measures on Group level are having an impact; for instance, our newly established Group procurement.

Growth initiatives are making good progress. Detailed here are the expansion of the insurance sales forces in Austria and Croatia as well as the pricing initiatives in Switzerland and the development of the Life business in Belgium. Our good growth figures can also be attributed to the success of these initiatives.

The development of new growth segments is also making good progress. We have already spoken about the development of our investment type Life insurance.

In terms of implementing Baloise 2012, we are right on target. In 2011 we anticipate this program to generate a positive effect of between CHF100 million and CHF120 million. In 2012 we will feel the full benefit of this program. Baloise's sustainable earning power will increase by CHF200 million per annum up to that point.

Following this overview, I would now like to take a more detailed look at three initiatives on slide 24.

In the optimize category, the bundling of forces in German initiative of Deutscher Ring and Basler Germany has successfully passed critical milestones. Nearly all employees have been assigned to their future work place. Two-thirds of the departments are already organizationally separated. The workers' councils support these process constructively.

Our business case to realize annual synergies of EUR20 million to EUR25 million net after tax and policyholder is fully on track. At this point, our German operations are in the investment phase to reap the full benefits in the coming years. We're happy to see that our newly integrated German operations gained traction in the marketplace. We see a stable premium development in Germany in line with the market development.

The second example, a growth example, is provided by Belgium. We systematically advance our Life business. In three years, from half year '08 to half year '11, the Life business grew by an astonishing 64% in Belgium. There are many factors supporting this extraordinary growth. Let me mention just two of them.

First of all, we developed innovative products for private and corporate customers that were very well received. Second, we systematically invested in the development of sales channels. We strengthened the cooperation with brokers and financial advisors. These sales figures are very promising. With the integration of Avero, Mercator now serves the entire Belgium market, including Wallonia and Brussels. These new regions offer substantial new growth opportunities for our operation in Belgium.

The final example is taken from Baloise Switzerland. Here Safety World, our unique positioning to make our customers safer, has an impact on growth and profitability. Our household product in Switzerland comes with a safety package offering unique safety services to our target customers. One example, after a theft at your house or apartment, we not only cover the claim but offer psychological assistance for you and your family to help coping with the side effects of this unpleasant event.

The effect of this innovation is impressive. 25% of the customers that buy or renew the household product buy this additional safety package. The customers are impressed with these new prevention services and like our added-value approach. And we generate value for Baloise. The increased cross-selling ratio at our target customers helps to further deepen the relationship. At the same time, the products sold within the safety package offer attractive margins for Baloise.

These were three examples out of 100 initiatives in our Baloise 2012 program. I hope I could demonstrate that Baloise 2012 is a very dynamic and successful program.

To conclude, I would like to take you through out outlook on the future on slide 25. Our ambitions remain unchanged. Over the cycle we are aiming for 15% return on equity. We are looking to steadily increase earnings per share and maintain our combined ratio well below 100%.

I would like to summarize the most important key issues once more. First, we achieved a solid profit backed by operational excellent. With the continuing implementation of Baloise 2012 we will further strengthen the growth and profitability of Baloise. Second, based on our proven operation excellence we generate a cash flow, which leads to a high level of stability. Third, our solvency is strong.

Thank you for being so attentive. After this reporting section I would like to give you further insight into two more general topics -- Baloise positioning to make our customers safer and an update on the political agenda. Let's start at slide 26.

You are all familiar with our Safety World positioning. Our promise is, making you safer. To this end we offer intelligent prevention products and services to our customers, like, for instance, the safety services in our household product as described earlier, our safety-orientated HR services and our Group health programs.

But we are doing more. As a responsible corporate citizen we, as Baloise, have established our safety day. Each Friday 13, which normally is associated with bad luck, is turned into a safety day by the employees of Baloise. To be more specific, on the last Friday 13, which was May 13, we made young children safer by offering customized bicycle training. I attended this training session in Austria myself and was impressed to see how eager these 14-year-old youths[ph] were to learn about the safe handling of their bikes.

Or take Switzerland. In cooperation with a large corporation partner of ours we made car drivers in Switzerland safer. Our employees took care of the right pressure in tires at filling stations and cleaned the windshield glass with a special protection, based on nanotechnology.

More than 500 employees in our seven European countries were active as brand ambassadors to make the world a little safer. The success of these safety days strengthens our commitment to further develop Baloise positioning Safety World. It is great fun and, at the same time, we can do some good.

Also Swiss politics should do some good to improve the market framework of the insurance industry, especially in the current economic environment. We asked the Government to improve; the regulations reached today are not satisfactory. You will find details on the next slide.

Each year in autumn the Swiss Bundesrat, the Swiss Federal Council, decides on the minimum interest rate guarantee for the compulsory part of the Swiss Group Life business. From our point of view, it is crucial to take the current development of key financial parameters into account. We were confronted with extraordinary developments in the recent weeks and months. The 10-year Swiss Government Bond stands around 1% right now, for example. Short interest rates are even negative in Switzerland.

Taking these developments into account, the minimum insurance rate guarantee has to be lowered substantially from its current level of 2% to 1% for the coming year. Only with an adequate management of the guarantee level, the long-term stability of the second pillar in Switzerland can be sustained.

Also the pension conversion rate in the mandatory part of the Group Life business has to be adapted to the demographic reality. Right now, the conversion rate stands at 6.9% and will be lowered to 6.8% by 2014. These parameters are too high, which means that the active working generation subsidizes the entire population substantially. The adequate conversion rate has to stand below 6%. We ask the political bodies to adapt their parameters accordingly. This all to ensure the long-term stability of the second pillar in Switzerland.

The third. And last, political topic I would like to comment is the unisex decision taken by the European Court. Basically, the decision says that, although it is absolutely clear that life expectancy between man and woman is different, this fact of life is not allowed to be taken into account when calculating risk-adjusted premiums in life insurance.

We believe that this is a wrong decision based on too populist understanding of being equal. It is crucial for the insurance industry to take objective risk criteria into account when determining risk prices. This adequate pricing leads to an overall increase of efficiency, thus lower insurance premiums and the right signals to improve risk exposure. We therefore are very content that in Switzerland correct pricing is in line with the regulation and that it will remain so in the future.

And now we would be pleased to answer your questions. Thank you, very much.

Questions And Answers

Operator

We will now begin the question-and-answer session. (Operator Instructions) Fabrizio Croce, Kepler.

Q - Fabrizio Croce {BIO 15005585 <GO>}

Now in terms of -- I have only a couple of questions. The first one is in terms of large claims. What was impressive to me was not the large claim above CHF4 million. But rather the one above CHF3 million. It's really -- that is a huge amount. So here I suppose that there is -- so frequency went up pretty sharply and I was looking to have some more flavor on what kind of claims were actually occurring and even if we have to expect this to materialize going forward or these are really more some sort of one-off effects due to some particular methodological, even -- simply to have a little bit more flavor about if it is a recurring item or a fixed one?

And the second one is about acquisition. You seem still to have a very nice buffer in terms of excess capital and the euro fall totally apart. So now I know that you just acquire in Belgium. So potentially you are -- you seem to be down for the time. But still the chance seems to good just to do further more acquisitions. And the question is if you are already also targeting some market or geographies?

A - Martin Strobel {BIO 5296838 <GO>}

Thank you, Mr. Croce for your two questions. I will answer them directly and maybe afterwards German Egloff can support.

First of all, combined ratio development. Actually we are very pleased with the very good combined ratio. To our understanding this is a very good combined ratio and net performance of 93%, given that we didn't have any extraordinary prior-loss development and given the weight that is coming from the integration efforts in Germany, as well as the acquisition efforts in Belgium.

We regard this combined ratio, in this sense, of a very high quality since in the last half year we have seen a major difference between the first half year and second half year. And I think we can expect a more stable development now for this year.

Talking about frequency overall, frequency in most segments is actually going down. Actually we are very happy with that showing. But this is the quality of our business. So this is overall a very good development. There are exceptions to the rule. One, for instance, is Group health business in Switzerland, where we see an increase of frequency due to the economic development in Switzerland. Overall, frequencies are more or less stable or even going down in some segments.

I think also the claims in this CHF3 million to CHF4 million bracket don't hint at a higher frequency in this area. This is a very selected number of different claims from different countries; so no pattern behind this. And, again, overall, 93%, I think, is a very good combined ratio performance.

Q - Fabrizio Croce {BIO 15005585 <GO>}

Coming back on this one. But this means that this 2.4percentage points are recurring actually. So it's structural -- they are structural?

A - German Egloff {BIO 4782831 <GO>}

Well, I think the special thing is that they are purely accidental. So there is no specific portfolio behind it. I think the special thing is just that in a previous year, within that layer, CHF3 million to CHF4 million we had almost nothing, which is accidental as well.

So I would say, yes, in terms of large claims the year was -- this year, you know I have normally the expectation of CHF45 million for the whole year and I always say we will never meet that; either we are below it or we are above it. This year we will certainly be above it, just because of the hailstones in the second half.

But in the first half we were pretty within expectations. So I think it's fair to say that you have to consider a certain amount of large claims and they were pretty normal coming out of the current year. Just in relation to the previous year, it was different.

A - Martin Strobel {BIO 5296838 <GO>}

And now, Mr. Croce, coming back to your second question, excess capital and acquisition. First of all, it's very important to understand for Baloise that we focus on an organic strategy. Our main efforts and focus is on the organic development, in terms of Baloise 2012, in terms of growth, efficiency improvement and coming up with innovations of Safety World to really increase market share in this.

So we only do M&A if a really good opportunity arise. And we have seen very interesting opportunities in Luxemburg and in Belgium recently; you have quoted them. Each M&A case has to fulfill three criteria -- it has to fit the strategy, it has to fit the culture of the Company, it has to have an accretive business case. All these three criteria have been fulfilled by these three acquisitions. We regard them as being bolt on.

And going forward. And that was your question, you can expect the same from Baloise. First, you can expect focus on the organic development of the Group. Second, if there are bolt-on acquisitions in our existing core markets that fulfill these three criteria, we will have a close look on them. So no change in M&A policy going forward.

Q - Fabrizio Croce {BIO 15005585 <GO>}

Now that we are speaking, another one pops just in mind in terms of questions. Very -- in terms of the 2percentage points additional claim that you said comes out of the hail, if I analyze, actually this. So if I look only to the second half, this means that the combined ratio in the second half should go up some 4percentage points. And so my question is, how -- did the reinsurance coverage not grip[ph] or was the claim really such gigantic?

A - German Egloff {BIO 4782831 <GO>}

Well, it's a bit early to be too specific there. But I can tell you the total amount was about CHF50 million. And since it comes out of different lines of business. And part of it goes to the Swiss elementary pool. But since we expect that we were pretty within our market share, all this comes back on a net basis as well.

So that's the current -- it's early to be more specific there, that might change. But our current estimate is about CHF50 million net, which is on different lines of business and that's the reason that the reinsurance recovery is relatively small.

Q - Fabrizio Croce {BIO 15005585 <GO>}

Which means that the 2percentage point -- the guidance is actually --

A - German Egloff {BIO 4782831 <GO>}

2% -- I mean CHF50 million, CHF2.5 billion premiums, or CHF3 billion premiums. So that's just a rough calculation.

Q - Fabrizio Croce {BIO 15005585 <GO>}

It's a fairly conservative estimate.

A - German Egloff {BIO 4782831 <GO>}

It might be a bit less. But up to.

Q - Fabrizio Croce {BIO 15005585 <GO>}

Okay. Wonderful.

A - German Egloff {BIO 4782831 <GO>}

Just one remark about the acquisitions, I wouldn't add to the acquisitions. But in your question, you just said it seems that you have a lot of excess capital. I would be very, very careful with the excess capital at the moment, because since markets are so volatile at the moment and since you know that we have market consistent solvency models, I'm really careful about how to handle the capital. So we are very careful there, just to add this.

Q - Fabrizio Croce {BIO 15005585 <GO>}

Yes, okay. Wonderful. Thank you.

Operator

Michael Klien, Nomura.

Q - Michael Klien {BIO 4262408 <GO>}

I have two questions, if I may. Firstly, on your FX exposure and your hedges, you mentioned that you increased the hedging of the euro exposure of the Swiss portfolio.

Could you maybe give us some indication in terms of the net notional exposure that you currently have?

Also, considering that you have lost close to CHF200 million from the FX exposure that you have unhedged, are you taking any further consequences, apart from the hedging? In other words, it seems like shareholders have been losing money for quite some time. It's quite significant. So maybe it might be a good idea to take some other consequences as well.

Secondly, on duration, I seem to remember that your duration gap had been around two to three years. Now that interest rates seem set to remain low for some time, also in connection, obviously, with where the Swiss franc is trading with these other currencies, are you looking to reduce this gap further or are you happy with the current gap? And maybe if you could just provide us an update where the actual gap is currently.

A - Martin Strobel {BIO 5296838 <GO>}

I will hand you over to Martin Wenk who will answer.

A - Martin Wenk {BIO 4193573 <GO>}

Okay, I can give you precise information regarding the hedge ratio. We increased that from 85% to 95%. The reason is that we have a sound hedging practice in place that we follow. And we followed that in the first half and we followed that in the second half. And due to the high volatility we had in July and August, we increased that to this 95%.

But the fact is that the hedge ratio, basically, is determined by the risk capacity of every single unit we have. So if I give you that average, that means that it can be very different from one unit to another. But, as I said, the risk capacity is really the determining factor of the hedge ratio.

Then you can say that --

Q - Michael Klien {BIO 4262408 <GO>}

Let me come back on that. So currently you have got a hedge that is still not complete. So you're, in essence, allocating risk capital to FX moves. And I guess underlying, since you have not completely hedged it, this means you expect the Swiss franc to weaken versus the euro. Is that right?

A - Martin Wenk {BIO 4193573 <GO>}

I certainly will not take the lowest levels to determine the ForEx strategy we have. We are going for a long-term view and, in this view, it will have to come back, to a certain extent, from the all-time lows in July. That's one thing.

On the other hand, don't forget what we are talking about now is purely this FX exposure of the Swiss companies regarding the investments. We do have FX exposure also from translation effects, from commissions that are lower and so on. And there a hedge is almost impossible because you just pay for it with the interest rate differential.

So we have those two legs[ph]. And for the Swiss investments in foreign currency bonds, we do have this fixed hedge program in place. While as for the coupon payments and for the dividend payments from our subsidiaries, we do not have a hedge in place because, on the long term, that takes you much more from your strengths if you always have to pay the interest rate differential.

And regarding the figures, the gross impact on our result in the first half was CHF60 million. That's for total --

Q - Michael Klien {BIO 4262408 <GO>}

(multiple speakers) the comprehensive income that you have a further, I think, CHF140 million and the P&L impact was CHF60 million. So total of roughly about CHF200 million, which I thought is quite costly to have this mismatch.

A - Martin Wenk {BIO 4193573 <GO>}

Yes. On the other hand, I don't think it's really fair to add the two together because if you take the translation effects of, let's say, the income we have out of foreign currency bonds that are dedicated to our foreign exposure. So if you have a German Life insurance, you have the exposure in euro, you have investments in euro and just by the translation at a certain point in time, namely June 30, this is less; but we still have the liabilities against that that you don't see in that figure. So you have to think about that as well.

Regarding the duration, we are still continuing our efforts to close that gap. We have done that to a certain extent in the first half of this year by 0.2 years. But we don't do that at any cost and certainly at those levels we are seeing now, I don't deem it really a good time to continue that. And we have the strength and the risk capacity to wait for better times. And we will do that and we will profit if interest rates will come back to a normal level, which is low, which will remain low.

That's our view. I don't say they go up fast. But I mean the 90 basis points in Switzerland have been driven by really extraordinary facts and, to a certain extent, we see now coming back and probably we will see some more.

Q - Michael Klien {BIO 4262408 <GO>}

Okay. Thank you.

Operator

Stefan Schuermann, Bank Vontobel.

Q - Stefan Schuermann {BIO 3235442 <GO>}

I have two questions, also. First of all, on the exposure to Southern Europe, or the GIIPS states, could you give us the split in Nonlife and Life as well?

And then the second question on the new business margin, the 19.2%, could you give us some flavor how much the improvement came from underlying efficiency improvement, how much came from the change in business mix and how much from basically improved market conditions?

A - Martin Strobel {BIO 5296838 <GO>}

I will hand over the first question -- or the both questions to German Egloff.

A - German Egloff {BIO 4782831 <GO>}

Well, for the split on Life and Nonlife, you'll find some information on page 31 in the financial statement; that's about what would be (inaudible).

And the question about the Life margins, I would say it's about 50/50 between efficiency improvements and economic environment.

Q - Stefan Schuermann {BIO 3235442 <GO>}

Okay. Thank you.

Operator

Michael Huttner, JPMorgan.

Q - Michael Huttner {BIO 1556863 <GO>}

Just wanted to run through the one offs in the first half, because I just want to make sure that I don't repeat them in the second half. Could you maybe explain the level of EBIT? What was in there for integration costs maybe as a figure? Also, how much was the FX impact in terms of EBIT? I know there's a gross amount of CHF60 million. But I'm never quite sure how much belongs to policyholders. And then anything else which came in. So I can have a rough idea of what I can roll forward.

And then the second thing, on Solvency. And I suppose that's asking Fabrizio Croce's question maybe another way round, can you give us a feel for what's happening on the Swiss Solvency test front? You alluded to it, saying MCEV-based models are not brilliant when interest rates are falling. But I've -- I didn't look it up. So I've forgotten your sensitivity to this stuff. But maybe you can give us a little bit of a feel. That would be really helpful.

And then the final point is, if you were to impair Greece. And I know haven't and you've got good reasons. So that's fine. But if you were, I estimate a number of CHF14 million at the EBIT level. Is that about right? Thanks a lot.

A - Martin Strobel {BIO 5296838 <GO>}

Thank you, Mr. Huttner for your three questions. I will hand you over to German Egloff.

A - German Egloff {BIO 4782831 <GO>}

For the integration cost, that is not quite easy to differentiate all that. I would say you could consider it's about 1 combined ratio point in Nonlife; that's about the figure. But part of it is really in costs. And part of it might be -- or integration effect, part of it might be in claims as well, because you have claims handling reserves in a first consolidation. And they come in the claims' loads.

So it's quite -- because we did the first consolidation and the merger of the two companies at the same time, it's not quite easy to differentiate that. But that would -- I would say about 1 combined ratio point is a fair assumption.

Now for the sensitivity of the SST, the situation there is that we have sent in our model at the end of April. And we are in close contact with the regulator in Switzerland. There are questions and answers and further requests and further answers. We think we will have a feedback at the end of September; so therefore, it's probably too early to say something there.

You're right, it is MCEV based, the internal model. But, of course, there is a Nonlife model as well, for the whole Group model. So therefore -- and that's probably -- wouldn't be fair to give sensitivities on that as long as we don't really know what will be accepted and what not.

Now, for the Greece impairment, you see there in the -- if you valuate the whole Company, most of it is really already in the balance sheet. It's just the difference between the available-for-sale bonds and the hold-to-maturity bonds that is not reflected yet. And that are about CHF4 million. And if you then again look at the finance report, you see on page 30 that we have about roughly CHF75 million unrealized losses on AFS bonds.

So the question is just really whether we bring them from the balance sheet through P&L. So it's not changing the value of the Company. You -- your -- I'm not quite sure whether I understood you right, your calculation ended up with CHF14 million, was that right?

Q - Michael Huttner {BIO 1556863 <GO>}

Yes, after taking policyholders.

A - German Egloff {BIO 4782831 <GO>}

Well, that's probably a bit too optimistic because, again, on page 31, you see that 41% is in Nonlife and 59% is in Life. And from the 59%, it's about -- 20% is legal quote[ph] business. And the rest is non-legal quote business. So if you start with CHF75 million, you're certainly ending up with a higher figure than CHF14 million.

Q - Michael Huttner {BIO 1556863 <GO>}

And just on FX, what was the FX impact in EBIT in the first half?

A - German Egloff {BIO 4782831 <GO>}

On a gross basis, CHF60 million.

Q - Michael Huttner {BIO 1556863 <GO>}

But this is before policyholders, right?

A - German Egloff {BIO 4782831 <GO>}

That's before policyholders, yes.

Q - Michael Huttner {BIO 1556863 <GO>}

And after policyholders?

A - German Egloff {BIO 4782831 <GO>}

Well, then you have to refer in the presentation. On page 15, you see the Nonlife/Life split; there you have to make a fair assumption.

Q - Michael Huttner {BIO 1556863 <GO>}

Right. But that -- I don't see CHF60 million on this slide, I see CHF21 million plus CHF78 million, which is CHF99 million.

A - German Egloff {BIO 4782831 <GO>}

No, you see the CHF44 million. You see the CHF44 million. And the additional difference comes from impairments on shares, which were created by euro movements and from translation effects. So I would say the difference between CHF44 million and the CHF60 million is probably net -- you can assume to have them net before taxes and after policyholders.

Q - Michael Huttner {BIO 1556863 <GO>}

Okay, lovely. Thank you, very much.

Operator

Farquhar Murray, Autonomous Research.

Q - Farquhar Murray {BIO 15345435 <GO>}

Just two questions, if I may. Firstly, could you give an update on Nonlife pricing and claims' inflation in the core geographies, in particular Switzerland?

Then secondly, following on your comments on duration, I think, re Huttner's question on the SST, is it fair to assume that the interest rate sensitivity of your MCEV is broadly unchanged from the start of the year, i.e., year end 2010? Thanks.

A - Martin Strobel {BIO 5296838 <GO>}

I will answer the first question and I will hand you over to German Egloff for the second questions.

You were asking about the pricing environment and the claims' reconciliation[ph] development in Switzerland, if I understood you correctly?

Q - Farquhar Murray {BIO 15345435 <GO>}

Yes.

A - Martin Strobel {BIO 5296838 <GO>}

Here we see quite a stable development. We don't market an extraordinary aggressiveness. And this has changed. This was different three or four years ago when certainly the big groups tried to lower price to gain market share. That has stopped, since especially the big groups now follow very strict the policy profit before growth. And that helps the Swiss market a lot.

And you can see the combined ratio performance of our business and of our competitors. You see that you have a very healthy environment, combined ratio fund-wise, in Switzerland. And I expected this, from a pricing perspective, to remain stable, either -- or to add -- there might be a chance to further improve, since what happens now is that in some areas, we see an increase of frequency.

This is all the businesses that are related to the economic development of the country. For instance, the Group Health products are related to the development of the economy. And here we see -- as expected, we see an increase on frequency. And that offers. And already has offered, the opportunity to increase prices in this business.

So pricing environment, put all this together, remains stable at a very good level in Switzerland.

Maybe now the SST question, German?

A - German Egloff {BIO 4782831 <GO>}

Well, it was actually an MCEV question. The best I can offer is really since the end of the year because we're not -- we have not done a full-fledged MCEV. At least, we don't disclose it for half year. So, therefore, there is no new sensitivity; it's just new business calculated for the half year. So therefore, that's the best I can offer.

Q - Farquhar Murray {BIO 15345435 <GO>}

Okay. Great. Thanks very much.

Operator

Jochen Schmitt, Metzler Equities.

Q - Jochen Schmitt {BIO 4227302 <GO>}

I have two questions, if I may. Firstly, on your real estate portfolio, net rental yield looks relatively high to me. So how does your portfolio valuation compare to recent transaction-based multiples? Or, to ask the question a slightly different way, can we assume that you carry hidden reserves on your real estate holdings, compared to recent transactions?

And secondly, very quickly, it might be a bit early at this stage. But could you provide an update for your dividend policy for fiscal 2011? Thank you.

A - Martin Strobel {BIO 5296838 <GO>}

Thank you, Mr. Schmitt. I will hand you over for the first question to Martin Wenk and the second I will answer.

A - Martin Wenk {BIO 4193573 <GO>}

Our real estate valuation is based on a discounted cash flow model that we apply that is commonly used in the industry. And that one is checked on a regular basis by external estimations of our portfolio.

We do that on a rolling basis. So that after four years, basically, all the holdings are estimated by an outside firm and we do have to submit that also to the authorities. And those comparisons show since a long time that there is no big difference between our DCF model and the valuations from the outside firms.

A - Martin Strobel {BIO 5296838 <GO>}

Okay, now on the dividend policy. Mr. Schmitt, in the past you have seen that Baloise has paid very attractive dividends and we regard this as being at the core of our business model. We want to be regarded as a company that really has an attractive dividend yield for our investors; have done so in the past and will do so in the future.

This is -- our ability to really have attractive dividends and have high payout ratios is very much linked to two facts. First of all, the operational strength of our Company. And you might have seen some key performance indicators; for instance, the very good combined ratio development. You have seen the strength of the Life business, you have seen the strength of the Banking business. So this all supports strong cash flow that's available for dividend payment.

At the same time, we have a very strong balance sheet; you have seen the Solvency I figure of about 227%. Based on this SST model we handed in. And it's not really accepted by FINMA for the time being. But if you just take this model that we use as an internal model, we are in the green, looking at the SST level.

So, going forward, we will offer an attractive dividend yield for our customers. The exact amount, that will be determined when the year has closed. And will then be determined by the supervisory board. So it's too early to give concrete figures. But the attractiveness will remain.

Q - Jochen Schmitt {BIO 4227302 <GO>}

Okay. Thank you, very much.

Operator

Ralph Hebgen, KBW.

Q - Ralph Hebgen {BIO 6297020 <GO>}

One question on the combined ratio; it's a bit detailed. It relates to the large losses. And it's just a question of clarification. If I look at the just reported numbers on slide 9. And they are the numbers relating to the first half 2010, you say that large claims above CHF4 million represented 2% of net premiums earned. In other words, 2percentage points on the combined ratio. And if I look at the same disclosure last year, i.e., as made in 1H '10, there you report on slide nine that large claims over CHF4 million represented 3.5%.

Now, this may appear like a question of detail. And clearly it is. But it affects the underlying loss ratio and I was just wondering whether we are comparing like with like, or whether there was some restatement made in this set of results.

A - German Egloff {BIO 4782831 <GO>}

There was a mistake last year in the chart. And it was quite simple. There were large losses from previous periods and we had a double count in it, in large losses and in premium prior-year loss development. So that was the reason. And we have taken that out now.

Q - Ralph Hebgen {BIO 6297020 <GO>}

So, in other words, what we find here, in 1H '10 --

A - German Egloff {BIO 4782831 <GO>}

Is the proper statement.

Q - Ralph Hebgen {BIO 6297020 <GO>}

That's correct. Cool. But it only affected really large claims and the underlying loss ratio. It didn't affect --

A - German Egloff {BIO 4782831 <GO>}

Exactly. So that's why we didn't really say it's a restatement because the figures, at the end of the day, were the same. But in the chart, it was a double count.

Q - Ralph Hebgen {BIO 6297020 <GO>}

Okay, that's brilliant. That's perfect. That explains that.

And then also, if I look at slide 35, this question now relates to the new business value. And actually I need to find it first before I ask my question. Slide 35, I see the value for new business in Switzerland, in particular, increased very materially indeed. Would you just be able to give us some color what was driving that particular increase?

I see that you initiated the sale of new products in Switzerland. And you mention a new suite of products with guarantees. Perhaps you would be able to explain how much that new product initiative contributed to that material increase. But also how much of that increase is due to macro factors.

A - German Egloff {BIO 4782831 <GO>}

Well that was all important. But the most important thing was since this is a 12-month comparison, the most important thing is the interest rate movement, really. That makes a lot of difference. And then, of course, efficiency gains as well. But I would say 50% of it is the macros and the rest is product mix, efficiency and so on.

Q - Ralph Hebgen {BIO 6297020 <GO>}

So you would -- if you were to report this number now, about 50% of that improvement would be eroded by the macro development which we have seen since the reporting date. Or well we don't need to quantify this. But --

A - German Egloff {BIO 4782831 <GO>}

I know what you mean. Yes, 50% is probably too high. We will see at the end of the year.

Q - Ralph Hebgen {BIO 6297020 <GO>}

It would go down if we were to report it now. And then, of course, who knows when interest rates are going to go up.

A - German Egloff {BIO 4782831 <GO>}

That's right.

Q - Ralph Hebgen {BIO 6297020 <GO>}

Okay. Fantastic. Thank you, very much indeed.

Operator

(Operator Instructions) Rene Locher, MainFirst.

Q - Rene Locher {BIO 1921075 <GO>}

So my first question is on integration costs. You reported on slide nine that you have some integration measures in Germany, Luxembourg and Belgium. Now my question is, following the acquisition of Nateus, can we expect further integration costs in H2 or then in 2012?

And my next question is on slide 20. It's the Group Life business, Switzerland. And we have seen from most of your competitors quite a healthy growth in single premiums. Now, I can see that your premium income in Switzerland, it's more or less stable. So I was wondering what was the development of single premium income in Group Life business, Switzerland?

And then just a last question on insurance accounting. If I go to the half-year report 2011 on page 24, in the Life business on the expense, one line says result from financial contracts. And there we have a huge swing there from minus CHF16 million in 2010 to plus CHF141 million in 2011. I was just wondering if you can explain that to me in more detail. Thank you.

A - Martin Strobel {BIO 5296838 <GO>}

Thank you, Mr. Locher. I will answer the first two questions. And then the question on the financial figures will be answered by German Egloff.

First of all, integration costs. On slide 9, we disclosed that around, in the Nonlife part, 1percentage point of the combined ratio is associated to either the unwinding or the integration efforts, be it in Germany or in Belgium.

Going forward, we expect the closing of Nateus in the near future. And, obviously, there will be integration efforts on the costs side by Nateus. It takes some effort to integrate an acquired company into your platform. And you will see this, I think, in the second half of '11 and the first half of '12, as we see it now for Avero and the situation in Germany.

Now, second question was single premiums in Group Life. We have a decline here of about 5%, half year, half year. And the reason is we re-focused a strategy arbit[ph], a strategy a bit in Group Life business where we say, okay, to increase the value of new business, we are more selective taking new business on board. And you see that we have grown strongly in the annual premiums; 7.7%, this is very high. And this is actually what we are aiming for, since we have very, very decent margins here in the annual business that also includes a risk component in the Group Life business.

And for the single premiums, we didn't really go for big growth here, given the margins right now. We could have grown much stronger; you've seen market development, we have seen extraordinary figures. Actually we are quite happy with the level we have right now. It might improve a bit in the second half, since there are many customers of ours who want to increase their technical reserves. But we don't really try to -- we don't try to attract it proactively, given the high level we have here already, the CHF15 million of the single premiums.

And this translates itself. This is one component of the improvement of the new business margin to have a much more selective approach in the Group Life business. This is also true for the kind of companies we win as new customers. So we really increase value of new business in the Group Life arena.

Now I'll hand you over to German --

Q - Rene Locher {BIO 1921075 <GO>}

Mr. Strobel, can I just -- a follow-up question, please. Just on this 1% you see, or your 4% the mandatory part of the Group Life business. So in the non-mandatory part you're at 1.25%. Are you thinking about lowering the guaranteed rate or the rate in the non-mandatory part.

A - Martin Strobel {BIO 5296838 <GO>}

Right now we feel very comfortable with the 1.25%. We expect that the market will move in this direction, given the interest environment. And I don't think that we -- that might not change substantially going forwards.

A - German Egloff {BIO 4782831 <GO>}

I would say that depends on the mandatory part as well, because you certainly have to compensate that and the decision there is not yet taken. If the mandatory part goes to the level we actually think it should be, there is certainly no urge to punish the extra mandatory part.

Q - Rene Locher {BIO 1921075 <GO>}

Thanks.

A - Martin Strobel {BIO 5296838 <GO>}

And now, German, on the --

A - German Egloff {BIO 4782831 <GO>}

That's a technical one. The reason is actually the unit-linked business, because the whole unit-linked business goes through the income statement and leaves the income statement again.

So you have to -- those -- your line items, the result from financial contracts, the minus CHF15 million to CHF141 million is related actually to the realized capital gains and losses on investments. And there you have the compensation.

You can, as well, refer to page 27. And there you see the realized gains and losses on investments at own risk and at the risk of the insurance policyholders. And that makes the swing, actually, because that runs through the income statement. So it has to be compensated for it. That's the reason.

Q - Rene Locher {BIO 1921075 <GO>}

Understood. Okay, thank you very much.

Operator

Michael Huttner, JPMorgan.

Q - Michael Huttner {BIO 1556863 <GO>}

Just a quick question. You referred to one slide and said -- and I understood, probably wrongly, that I would find the figure of CHF44 million there. And I've looked for 20 minutes at this slide and I just wondered if you can help me. It's slide 15. And it's the FX question. Where exactly do I see the figure of CHF44 million there?

A - German Egloff {BIO 4782831 <GO>}

CHF44 million. You can actually -- you see the fixed income securities and other on the Nonlife side and then of which FX impact is. And now if you take the difference between, on the Nonlife part, minus CHF21 million and plus CHF5 million, you are on minus CHF16 million. And you do the same on the Life side and you add it and you end up with CHF44 million.

Q - Michael Huttner {BIO 1556863 <GO>}

I understand. Brilliant. That's very helpful. Thank you. So much.

Operator

Gentlemen, we have no more questions.

A - Martin Strobel {BIO 5296838 <GO>}

Okay. So then we end this meeting. I'd like to thank you very much for your attention and your interest in Baloise and wish you a nice day. Thank you, very much.

Operator

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