Q1 2016 Earnings Call

Company Participants

- David Cole, Group Chief Financial Officer
- Matthias Weber, Group Chief Underwriting Officer
- Patrick Raaflaub, Group Chief Risk Officer
- Philippe Brahin, Head-Investor Relations

Other Participants

- Anasuya Iyer, Analyst
- Andrew J. Ritchie, Analyst
- Andrius Budnikas, Analyst
- Daniel Bischof, Analyst
- Frank Kopfinger, Analyst
- In-Yong Hwang, Analyst
- Kamran Hossain, Analyst
- Sami Taipalus, Analyst
- Thomas Fossard, Analyst
- Vinit Malhotra, Analyst
- William Hawkins, Analyst
- Xinmei Wang, Analyst

MANAGEMENT DISCUSSION SECTION

Operator

Ladies and gentlemen, good morning or good afternoon. Welcome to the Swiss Re's First Quarter 2016 Results Conference Call. Please note that today's conference call is being recorded.

At this time, I would like to turn the conference over to David Cole, Group CFO. Please go ahead, sir.

David Cole {BIO 7251632 <GO>}

So, thank you very much. Good morning or good afternoon, everyone and welcome to our first quarter results conference call. I'm here today with Matt Weber, our Group Chief Underwriting Officer; Patrick Raaflaub, our Group Chief Risk Officer; and Philippe Brahin, our Head of Investor Relations.

Swiss Re started the year with a strong first quarter in what remains a challenging environment. Our business units contributed positively to a group net income of $1.2 billion. The first quarter reflects the benefits of our strategy and systematic capital allocation to diversify our access to risk and attractive segments.

P&C Reinsurance reported a strong ROE of 19.1% supported by large and tailored transactions and benign nat cat experience. Life & Health Reinsurance reported an ROE of 16.1% also driven by large transactions and reflecting continued attractive growth in all regions.

Corporate Solutions delivered good results in the first quarter with an ROE of 13.5%. The acquisition of IHC in the U.S. provided attractive growth. Life Capital delivered a very strong ROE of 21.2% benefiting from the net realized gains from the derivative portfolio of Guardian.

It's the first time that we reported under the newly created business unit structure reflecting Admin Re, the Guardian acquisition as well as open life and health books. Our asset management team produced a strong ROI of 3.7% despite the low interest rate environment. And finally, we also reported today our latest group SST ratio, estimated earlier this month to our Swiss regulator, FINMA. This remains very strong at 223%. As we promised earlier, we conducted comparisons and analysis (02:08) of our group SST ratio with an equivalent group Solvency II ratio. You may've seen the video of our group CRO, which explains that our Solvency II comparable ratio is estimated to be 312%

So with that I'll hand over to our Head of Investor Relations; Philippe Brahin, who'll introduce the Q&A session.

Philippe Brahin {BIO 19081619 <GO>}

Many thanks, David, and good day also to all of you from my side. Just before we turn to the Q&A, I would like to remind you to please restrict yourself to two questions each and re-register for follow-up questions. So with that operator, could we please have the first question?

Q&A

Operator

The first question comes from Daniel Bischof, Baader-Helvea. Please go ahead.

Q - Daniel Bischof {BIO 17407166 <GO>}

Yes. Good afternoon, two questions please. Firstly, could you provide some more details on the reserve strengthening on the liability motor side, for instance on motor I would be interested to know which accident years these movements relate to. And on that, I mean last quarter was the first one, for quite some time with an overall negative development. I mean, I appreciate there are always some movements but it will be helpful to get your view on the reserve for the equity.

And then the second one is on the demand side, I mean you benefited from the two transactions with AIG and Citi Holdings fully in line with the focus on tailored transactions, which we see does not provide any top line guidance, but maybe you could, just provide some comments on the pipeline or the demand side in general, both in P&C and Life & Health specifically and further large transactions.

A - David Cole {BIO 7251632 <GO>}

Okay. Thanks, Daniel. I'll let Matt take the first question.

A - Matthias Weber {BIO 16674983 <GO>}

Okay. So we have indeed a little bit of prior year loss development on the motor side especially coming from Germany where we make an adjustment to our longevity pattern that is relevant to assess the amount of the research. We also had some prior year development related to our umbrella business and I'm mentioning this because umbrella also includes the motor portion and we made some adjustments there related to the last two to three accident years and that's the majority of where our motor adverse development came from. With respect to the large transaction pipeline, we never go into details related to our pipeline, but in the long text comparison, our pipeline right now looks rather full.

A - David Cole {BIO 7251632 <GO>}

All right. Thanks, Matt. You actually picked up both questions. So, thanks. And, let's go to the next question.

Operator

The next question is from Xinmei Wang, Morgan Stanley. Please go ahead.

Q - Xinmei Wang {BIO 17860767 <GO>}

Hi, hi. Thanks for taking my questions. So firstly I wanted to ask on capital. In the past, the message has been that a 200% SST related to $3 billion to $5 billion above S&P AA. Has that binding constraint changed under the new SST methodology and how should we view that in relation to excess capital in terms of the buyback. I mean, does your previous commentary on the buyback still stand? And my second question is on the nat cat normalization. I appreciate you change that in terms of how you do the normalization this year with some of the budget going into next year with late reporting? And I am just wondering if you could give some color on why you decided to make the change this year as opposed to previous years on that? Thank you.

A - David Cole {BIO 7251632 <GO>}

Okay. Thanks for both questions. I will pick up the first and then hand over to Matt for the second. So, first, the overall economic regime, SST hasn't really changed a whole lot. We did get some clarifications from FINMA regarding the treatment of certain types of equity-related assets, hedge funds, PEs and those kind of things, which contributed a little bit I think to the positive – more positive outcome for SST 2016 and we had ourselves originally included our estimate.

In terms of any potential impact on the S&P frankly, there is none. As per our earlier communications, I think we continue to maintain a very strong capital position. The different binding constraints changed a little bit over time, depending on primarily what happens with interest rates, to be frank. But there is no real change in overall communication from earlier this year, nor from earlier discussions about how S&P and SST more or less relate to one another.

Also related to the buyback, there is no change in our previous communication regarding that as well. So we maintained a strong capital position. I think we're in a position to be able to respond to opportunities that may arise. We'll look to see how our capital position develops over the course of the year, which maybe a combination of profits that emerge, losses that may occur, opportunities to invest may occur. And later in the year, we'll determine whether or not it would be appropriate to actually launch the new buyback program that was recently authorized by our shareholders.

So, the broad message on capital management is no change from earlier communications. Let me then turn over to Matt for our discussion about nat cat normalization.

A - Matthias Weber {BIO 16674983 <GO>}

Okay. Related to your question if it's okay, I'd like to take the opportunity to over deliver a little bit and give – explain the changes we made and why we made the changes in the broad context, I will not forget about your specific question and add it at the very end.

The story does not include every individual detail and I believe knowing all the details though probably not adds to understanding our numbers and understanding Swiss Re, but could make sure that I would use more than five minutes to maximum 10 minutes to talk about this.

And, in my opinion, that should be the cap. So, I would like to explain to you how we adjusted the combined ratio in reinsurance in the past and how we will do it going forward including what we did already in Q1 of 2016.

Let's go back to February last time we met. At that time, I explained or we explained the 2015 results to you and when we did it, we highlighted the absence of reinstatement premium, higher than expected profit commissions and sliding scale commissions, as a result of the incredibly low experienced nat cat loss burden in 2015. In order to explain the difference between our expected combined ratio, which last year was 97% for Reinsurance and our actual combined ratio, which when adjusted for nat cat and prior year development was 99.8%. We used this opportunity to fundamentally review our nat cat normalization process related to our combined ratio including seasonality of losses and adjustment to premiums and commission figures.

On a quarterly basis, when we release a portion of our total expected nat cat loss burden from our accounts and replace them with actual reported losses, and we replace only a portion of our total expected nat cat loss burden. The reason why we release only a portion is to reflect late cedent reporting related to the actual losses. This approach leads to the correct U.S. GAAP combined ratio, which we publish.

In the past, when we adjusted the combined ratio to normalize for nat cat, we adjusted for the difference between total expected and reported nat cat losses. This led to a too conservative estimate of the adjusted combined ratio.

We therefore adjusted the methodology for 2016 as follows. The $1.5 billion total expected nat cat loss is still a good estimate for the full year and remains the basis for our 99% expected combined ratio for the full year, so no change there at all. However, to determine the adjusted combined ratio we now adjust for the difference between released and reported nat cat losses, which leads to a more realistic adjusted combined ratio than in the past.

We now also use a seasonality pattern that reflects the portion of the nat cat loss to be released rather than the total expected nat cat loss.

The new pattern looks as follows; 19% in Q1, 13% in Q2, 41% in Q3 due to U.S. hurricane, and 27% in Q4. And in addition we now also take into account adjustments due to reinstatement premiums, profit commissions, and sliding scale commissions.

For 2016, the amount to be used to normalize the combined ratio is therefore approximately $1.2 billion. Together with the portion of the total nat cat loss that will not be released in 2016, that however will be released in 2017, due to late reporting this will still add up to the total expected nat cat loss of $1.5 billion for the full year.

Applying this methodology, the nat cat normalization impact for Q1 is $232 million. Maybe a remark at the end, please note that while the new methodology is more precise than the old one, which was too conservative. The adjustment to the combined ratio will continue to be an approximation and subject to change.

That's the explanation I would like to give. And now related to your specific question, why did we do now? The reason is, we realized in February when we explained the 2015 combined ratio, how important the reinstatement premium and the profit commission and the sliding scale adjustments can be in a year with a very unusually low nat cat loss ratio. That was the trigger for looking deeper into our methodology and since we did this, we felt now is the right time to review it in full and to adjust it to bring it to the best of our knowledge.

A - David Cole {BIO 7251632 <GO>}

Thanks, Matt. I appreciate that. Also, I just like to remind this, as Matt indicated, there always will be some approximations here, and at the end of the today we are referring to estimates. These estimates are based on a number of assumptions about the future events including future renewals, pricing levels and business mix. So, at the end of the day, it's important to recognize that we do our best, but an estimate is an estimate. So I'd just like to leave the question on that. Now we'll go to the next questioner, please?

Operator

The next question is from Anasuya Iyer from Jefferies. Please go ahead.

Q - Anasuya Iyer {BIO 18981555 <GO>}

Oh, hi. My two questions, the first one just on the negative prior-year developments again, I just wondered if you had any commentary about whether within that there's any offsetting impacts and therefore, what that looks like on the positive side? And my second question was on casualty. So I can see that the casualty in the year-to-date premium has gone up to 51%, obviously as you reduce your flow business, and I'm just wondering as you see more negative prior developments in casualty, are you worried about this? Are you worried that this reach for casualty growth brings more unexpected reserve developments in that area? Thanks.

A - David Cole {BIO 7251632 <GO>}

Excellent. Thanks for both questions. I'm going to, I think, ask Matt to respond to both.

A - Matthias Weber {BIO 16674983 <GO>}

Okay. So, also, here I would like to tell you a little bit more than you asked for to get, I hope this is okay. We had in Reinsurance adverse development of $141 million in total, more than half of this adverse development actually does not come from loss site or from the loss reserve site, it comes from update to premium estimates and commission estimates. Please note that when we close a quarter some of the premium figures and some of the commission figures are not reported or not yet reported by clients and they have to be estimated and then subsequently they're or will be replaced by actually reported figures. Some times when we make these estimates we're a little bit too low. Sometimes we're a little bit too high and this or the last time we made these estimate last year, it looks like we were a little bit too high, which means too optimistic and now as a result of this we had prior year development related to the premium and related to the commission, which actually is bigger than the total prior year loss development related to losses. To be more specific in Property for instance, we had to make an adjustment of $42 million coming from the premium and the commission side. In Casualty, we had to make an adjustment of $17 million again coming from the premium and the commission site.

Coming now to the losses, which I believe is what you're asking for. The remaining $67 million of loss reserve development alone could be more than explained by development coming from the New Zealand earthquake. That alone explains all the negative development.

In the rest of our book, we had some favorable developments and we had some buckets of adverse developments. I mentioned already, Motor (20:08) for instance, there we had a little bit - by the way it's not dramatic at all, but we had a little bit of adverse loss development. In the specialty lines area, we had a good amount of favorable development. We needed to add some strengthening to our U.S. specialty (20:30) reserves, for instance. So you win some, you lose some, but if we take out the New Zealand earthquake loss development, the rest is plus/minus awash on the loss reserve site.

A - David Cole {BIO 7251632 <GO>}

And if I may, (20:49) if I go to the question about casualty, I'd just like to remind everyone our philosophy approach to reserving remains unchanged. Best estimates, I think we continue to have what we consider to be a prudent overall reserving level. If you look at our portfolios throughout the year, every quarter, we have adjustments. We try to keep this up-to-date as possible with underlying development. There's nothing in the Q1 figures that leads us to conclude that we have somehow reached an inflection point and there's something different about the way we would like to talk about our reserves vis-à-vis the way we talked about in last quarter or the quarter before that.

Let me just turn back to Matt now for the question on the casualty.

A - Matthias Weber {BIO 16674983 <GO>}

Okay. So you asked me whether I am concerned with the fact that we have 51% of our renewed 20 (21:39) business in the area of casualty. The answer is, look, as an underwriter I always am concerned about everything. That's my job. I have to be a little bit paranoid. However, I am not more concerned with respect to our casualty book knowing that the reason for the increase of the casualty portion to 51%, right now it could change as we progress through the year, but right now it's 51%, is entirely driven by a very small number of large transactions, which I have seen and which a good number of specialists have looked at and thoroughly whetted and we were when we wrote (22:36) these deals and also now we continue to be confident that these deals will continue as expected, meaning they will be profitable.

A - David Cole {BIO 7251632 <GO>}

Thanks, Matt. May we go to the next questioner now?

Operator

The next question is from Andrius Budnikas from Citi. Please go ahead.

Q - Andrius Budnikas {BIO 18952195 <GO>}

Hello. This is Andrius Budnikas from Citigroup. Two questions please. The first one is on Life & Health Re [Life & Health Reinsurance]. Could you give us more information regarding the underlying performance of this business unit? How much of this strong performance is sustainable going forward? In other words, could you tell us the normalized ROE for this business in this quarter?

The second one is on Life Capital. Could you explain us what gives you confidence that the gross cash generation over the next three years will be in the region of $1.4 billion to $1.7 billion, given that this quarter the run rate was well below expectations? Thank you.

A - David Cole {BIO 7251632 <GO>}

Yeah, thanks. I'll actually pick up both of those. So first on Life & Health Re. Now we've had this quarter of, I think, very good result. Always we're going to be on the life portfolio, we think about the notional value or the policies we have over the period of times, they are in force there's (23:51) going to be some noise and volatility.

In 2013, we announced we wanted to address a number of very important performance issues. We said that we wanted to express our view about the sustainable earnings, potential of this (24:06) business by saying, we thought we could bring it to a 10% to 12% ROE on the equity base of about $5.5 billion (24:11). And during the course of the 2015, we could normalize each time back to that.

We now, going forward have said, we're going to drop that caveat about the equity base of $5.5 billion (24:22). So we believe through the cycle we can deliver sustainable earnings between 10% to 12% ROE. Q1, we actually delivered something above that. There are always going to be some pluses and minuses, but there's nothing that I actually think I should point out specifically as being some form of fashion or one-off.

We're not going to be normalizing the ROE on the life business going forward. I do feel quite comfortable that we're in a strong position. We've addressed some of the underperforming portfolios that we previously identified. We've put the right capital mix in place. We've put the right asset mix in place to reflect the duration of the other liabilities. So we continue to drive attractive business. So that actually feels quite good.

As to your second question about the gross cash generation of Life Capital, so as of the January 1 for the largest part of that business to the Admin Re part, which falls under the Solvency II rules, we of course moved from Solvency I to Solvency II assessment the level of capital required. So there's just some transition related aspects associated with that. Perhaps more importantly, we had brought on board the Guardian portfolio in Q1.

We've not optimized the portfolio. We are on our way to having done so. We've already taken some very important steps now and anticipate we'll be able to by and large around those steps out during the course of the next several months. So certainly Q2, Q3, we should have finalized that to bring it into what we think will be down to more sustainable going forward position from a Swiss Re perspective.

Now, while we've been doing that, we also of course, experienced in Q1, very significant financial market moves on the (26:04) credit spread, perhaps even more importantly interest rate. Now, that impacted our Q1 results in a number of different ways. You've all seen, of course, the positive impact on the realized gains coming off of the derivatives portfolio. Offsetting that, of course, we had an increase in the level of liabilities on the basis of the lower market value discounting rates.

So there were a number of transitional elements in there. The minus $25 million (26:29), I think, should be put in that context. Going forward, if we look at the business, if we look at where those liabilities and assets are expected to perform, how we intend to continue the integration of Guardian, including the Part VII towards the end of this year, beginning of next year. Also, we'll be moving from the standard formula to an internal model based formula over time.

We still remain confident that the business in the UK will throw off actually a little bit more than $1.4 billion in cash, part of which we will invest in our open life business outside of Admin Re. So that is what leads to the overall $1.4 billion to $1.7 billion, which is confirmation of our earlier communication.

Q - Andrius Budnikas {BIO 18952195 <GO>}

Thank you.

A - David Cole {BIO 7251632 <GO>}

Go to the next questioner please?

Operator

The next question is from Kamran Hossain, RBC. Please go ahead.

Q - Kamran Hossain {BIO 17666412 <GO>}

Hi, I'm Hossain. Three questions. First on, I mean, sorry it's (27:29) coming back to the prior year development, and I don't know Matt is more paranoid (27:33) on that, but I could only just ask. There's, I guess, the prior-year development and the unfavorable development, was that season related or was that Swiss Re driven? And then, I guess the second part to that one is, have you recalibrated your forward-looking liability models to kind of reflect these kind of movements that you've seen? That's first question.

The second question, just on the large loss budget, does this make any impact on the kind of how you think about the buyback going forward? So do you need large losses to be a little bit lower to execute the buyback? Do they have any impact still? Just interested in any thoughts from that. Thank you.

A - David Cole {BIO 7251632 <GO>}

Okay. I'll ask Matt to address the first and I'll comeback around the second question.

A - Matthias Weber {BIO 16674983 <GO>}

Okay. I assume when you distinguish between cedent related and Swiss Re related, what you mean is, is it due to higher than expected reported losses coming from the cedent to Swiss Re or is it due to a massive volatile change on the Swiss Re side. And the answer is, and again on the loss side, the total amount of adverse development is less than 50% of the total adverse development we have seen. Both factors are included.

For instance, New Zealand is cedent related, motor is cedent related in the U.S. However, motor in Germany, there we slightly adjusted our methodology to take into account the increased longevity of people who encountered a motor accident. So both elements matter. However, again, both elements are less than 50% of our total research development. More than 50% comes from the premium and the commission side.

A - David Cole {BIO 7251632 <GO>}

Thanks, Matt. As to the second question, let me just reiterate a couple of things. First, no adjustments that we made now to the way we talk about normalizing our combined ratio, the way we look at the emergence of losses. We'll change the way we have start about or (30:03) communicated around capital management and more specifically about the buyback.

We think about what may happen during the course of 2016, obviously, the occurrence of large loss and/or perhaps smaller losses in unexpected places, can have an impact on the way that the market respond. We could have opportunities come to us throughout the course of the year to invest. Overall, profits, developments of the other non-P&C related segments can also influence our overall capital generation during the course of 2016.

So I think we'll just reiterate that we assume a certain level of losses in any given year. We know that frankly speaking – and most years, historically, we show little bit lower losses than what we would reflect on an average basis. If you just go back last 10 years or 12 years, you want to go back to deal (30:59) before Katrina in 2005. You'll see that between 2004, 2015, we basically had two years where we were above our expected loss budget and the other years were actually below it, sometimes even very low below it. So I think you need to understand that we assume a certain level of loss. We'll look to see how those losses develop during the year. It's not just the individual number that would be important to us. It would be what type of loss emergence, where. Matt, you want to add?

A - Matthias Weber {BIO 16674983 <GO>}

I would like to add that on the nat cat side, due to the asymmetric loss distribution typically in one year out of five years, we have an actual loss burden that is bigger than the mean expected loss burden. And in four years out of five years, it is smaller.

Q - Kamran Hossain {BIO 17666412 <GO>}

Okay. Thanks. (31:56).

A - David Cole {BIO 7251632 <GO>}

All right. Thank you. Let's go to the next question.

Operator

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

Q - Vinit Malhotra {BIO 16184491 <GO>}

Hi. Good afternoon. Sorry to ask again on the budget change on nat cat. I just want a quick clarification, please, if you don't mind. The $300 million that has been moved forward because of reinstatement or timing differences, is it then fair to assume that this $300 million is going to show up in next year's budget, and then that should be $1.8 million, because otherwise we can't just make the $300 million disappear somewhere? So that's my first question. Is it timing difference or not, just to clarify that. Sorry.

Secondly, we have seen very high level of gains on the credit side, probably from the narrowing of spread. How was the decision taken, because you said just an opportunistic decision? How do you think this affects future investment income potential? And you also mentioned just now the Guardian portfolio not yet fully optimized. Should we expect more of these kind of realization gains in this coming year? Thank you.

A - David Cole {BIO 7251632 <GO>}

Okay. Thanks. I'll ask Matt to pick up the first follow-up and I'll get the second.

A - Matthias Weber {BIO 16674983 <GO>}

So with respect to the $300 million, which you're referring to, you're absolutely right. The majority of this will actually be released next year. However, it will be offset by late cedent reporting nat cap losses. So to the extent that the late reported losses match the amount to be released, it will not lead to any prior year development at all. If one number is bigger than the other, then of course that will lead to either adverse or favorable development.

However, next year if our portfolio stayed stable, which, of course, will never be the case, we would have to add the $300 million to be released next year, again, with $1.2 billion of losses that will be released as a normal course of matter and this will, of course, then still add up to the $1.5 billion.

Q - Vinit Malhotra {BIO 16184491 <GO>}

Sorry. It should add up to $1.8 billion. Shouldn't it, Matt? Because otherwise we are literally taking away $300 million out of the system and not counting it anywhere.

A - Matthias Weber {BIO 16674983 <GO>}

Now because also next year, they will have again $300 million that will not be released next year, but the year after next year, so in 2018. So in fact, if we didn't grow, it will be a very stable situation.

A - David Cole {BIO 7251632 <GO>}

Key thing is just recognizing we've been too conservative in the past in the way that we've calculated this normalized expected contribution to combined ratio. When I think of (35:36) second question...

Q - Vinit Malhotra {BIO 16184491 <GO>}

Thank you.

A - David Cole {BIO 7251632 <GO>}

Listen, we're not opportunistically realizing gains due to lower interest rates. We haven't been doing that. As you know, we came off the back of financial crisis with a very significant de-risked portfolio. Over the course of 2012, 2014, we rebalanced fully in line with what we had indicated we wanted to do over the medium-term in terms of our strategic asset allocation, included, but wasn't exclusively related to putting the right asset mix in place for Life & Health Re amongst others.

In Q1 2016, if you take a step back from the gains associated with the Guardian derivative portfolio, we actually had a lower level of realized gains overall than what we had in 2016. There are (36:23) different reasons for that. The asset management team, of course, is fully aware of the fact that at current interest rate levels, now turning to somehow harvest unrealized gain is not a very sustainable strategy. So I can assure you that's not our policy, not our practice at all.

In terms of the sustainability of the gains that we saw on Life Capital also associated with the Guardian portfolio, look I don't know what will happen with financial market. So certainly I'm going to tell you one way or the other interest rates will be up or down over the course of the next couple of months and quarters, but I will tell you is that we are transitioning that portfolio. Part of that is to reduce this overall derivatives position. I reduce somewhat the long position that we brought on board when we acquired the portfolio.

We are also going through the portfolio that we've acquired to ensure the quality is what we would like for it to be. So there are a couple of higher-yielding investments that we're in the process of disclosing. All of that will continue. Although, I have to say we're probably already well into that right now. So our intent is that by and large, by the middle point of this year and giving a little bit of room around is that before June 30 or after June 30, middle of the year, we hope to have more or less completed the transitionary work that we'd like to. In the mean time, we remain subject to a little bit more volatility than we otherwise would want to carry going forward. We want to clearly work out to our advantage. We're (38:03) always very transparent about that. And in Q2, we'll see how that plays out.

Q - Vinit Malhotra {BIO 16184491 <GO>}

Okay. Thank you.

A - David Cole {BIO 7251632 <GO>}

Next question?

Operator

The next question is from Frank Kopfinger, Deutsche Bank. Please go ahead.

Q - Frank Kopfinger {BIO 16342277 <GO>}

Yes. Good afternoon, everybody. I have to apologize. I would like to come back again to this nat cat budget and to the normalized combined ratio of 95.7%. I understand that there's some sort of timing effect and you shift forward (38:36) $300 billion of budget. However, I think what we all need to get is an understanding, how the underlying developed from last year, Q1 to this Q1. The last year you disclosed a normalized figure of 95.8%, which included, obviously, to a high (38:56), 9.8% nat cat budget by that point in time. Do you have some sort of comparable figure that we could take now to put it against the current 95.7%? This is my first question.

And the second question is also on the Guardian portfolio and the impact from the derivatives. If you exclude all these noise from the derivatives, could you shed some light on how you see the underlying development and contribution of the Guardian portfolio and ideally you have some number for this?

A - Matthias Weber {BIO 16674983 <GO>}

Thanks. Okay. So regarding your first question, I take this. We did not readjust the adjusted combined ratios of the past to reflect what would they have been had we applied also the current methodology. So all I can repeat, it was too conservative and you have an order of magnitude by how much approximately, and that's how much I can explain.

A - David Cole {BIO 7251632 <GO>}

Okay. As to the second question, so if you take away a couple hundred million so (40:19) rough order of magnitude of the gains associated with the derivatives portfolio, then I think you end up with still a very acceptable underlying result, certainly in line with our overall expectation, in line with our overall target of achieving ROE of between 6% to 8% for this business in the medium-term. So I think the underlying result was very much in line with our expectation. Obviously, there was a significant impact from the derivatives book.

Q - Frank Kopfinger {BIO 16342277 <GO>}

Okay. Thanks.

A - David Cole {BIO 7251632 <GO>}

Thank you. Can we go to next question, please?

Operator

The next question is from Sami Taipalus from Berenberg Bank. Please go ahead.

Q - Sami Taipalus {BIO 17452234 <GO>}

Hi. Good afternoon, everyone. Thanks for taking my question. The first is one on these large transactions that you've been doing quite a lot recently. And I'm just wondering how those impact concentration risk within the Group and how you've managed this concentration risk? I suppose I'm particularly thinking about this because you've talked about Perry Braithwaite insurance (41:23) a little bit in the past.

Then my second question is on the comparison you made between the Swiss Solvency Test ratio and the Solvency II ratio. Now, I appreciate, I'm taking a bit of artistic license here, but if I scale the Swiss Solvency Test numbers and apply them to your Solvency II ratio, you get to a minimum requirement on the Solvency II basis of 260%, which is quite a bit above what your peers have. So I'm just wondering if you're having any discussions internally about maybe reducing the minimum requirement that you have on the SST ratio given how conservative it seems that this ratio is. Thank you.

A - David Cole {BIO 7251632 <GO>}

Thanks very much for both questions. So, Matt, why don't you take the first, then I'll ask Patrick to pick up the second?

A - Matthias Weber {BIO 16674983 <GO>}

So with respect to concentration risk, I must admit it's not totally clear to me what exactly you mean by concentration risk. However, as we increase and continue to increase the portion of large transaction in our book and reduce the flow business, as long as price levels deteriorate and continue to deteriorate, we of course, increase a little bit the volatility coming from to a possibility that once single risk or the book of one single client could develop one way or the other way from what we expected it to develop.

However, please also understand that our biggest exposures coming from the underwriting side are in the area of pandemic risks and nat cat. And with respect to these risks, large transactions are treated exactly the same way as smaller transactions are treated. We're looking at the contribution from each and every one of these transactions, independent on how small or how large they are and we control the total and make sure that the total exposure with respect to these correlating perils stays within the allocated capacity limits.

A - David Cole {BIO 7251632 <GO>}

Thanks, Matt. Patrick, do you want to pick up the question about Solvency II?

A - Patrick Raaflaub {BIO 16381419 <GO>}

Yes. So, Sami, I'm not sure whether your scaling up from SST to Solvency II is really helping us a lot. I mean, we have a group risk policy, which states on the capital side what our target capital level is. It depends on a multitude of parameters. It has a respectability component of the clients expect us to have in terms of capital. It also has a concept behind it, which says that we expect to be able to weather a shortfall event, shortfall type event and still be in business, hopefully to benefit from what we expect then to be excellent market conditions.

And then there are also other considerations such as S&P Capital and statutory capital constraints. So all in all, this leads to this expression of an SST based capital target or capital tolerance, a buffer that we want to hold above the minimum. The minimum on the SST is 100% and SST is really the metric that we look at in terms of economic capital model. What we have provided here is really just the translation to help understand what a comparable Solvency II ratio would look like. But I don't see this translation effect result in any revision of our capital risk tolerance. Obviously, we are constantly thinking about the capital risk tolerance. And any element of our group risk policy is permanently also challenged and can be potentially revised.

A - David Cole {BIO 7251632 <GO>}

Thanks, Pat. Indeed (46:00) just walk to Solvency II is really just for facilitation purposes, but it doesn't change the regime under which we operate. Of course, on a Group-wide basis, this was Solvency test and breach of our underlying operating subsidiaries carrier would (46:13) be the local relevant regime and the various jurisdictions where they operate, some of which are operating in Europe under Solvency II, others operate in the U.S. under the safe (46:23) regime, some operate in Asia under the respective regimes there. So the overarching capital regime for Swiss Re remains the SST.

Q - Sami Taipalus {BIO 17452234 <GO>}

Right. Thank you.

A - David Cole {BIO 7251632 <GO>}

Thanks.

Operator

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

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

Hi there. First question, on the premium growth in renewable year-to-date, can you just tell me how much of that premium is multi-year deals and are we seeing all of the multi-year premium in the delta? Or another way of putting it is how quickly will the increased volume earn through? And I'm assuming it carries with it probably a normalized combined ratio higher than 99%, given that it's clearly very weighted to casualty. So it's really the speed of earn through and the combined ratio.

The second question, Patrick, in your reported comments, your last comment is intriguing when you talk about looking for convergence or hope for increased on the work (47:36) to help towards increased convergence of economic capital regimes. Is that something you see? Do you see more convergence of SST and Solvency II, or something? I mean, do you think is this possible?

My final – this is just an observation. I think the danger of quite a lot of confusion on this nat cat change on the combined ratio, we keep referring to the fact that previously it was too conservative, your normalized number. Just to be clear. I think you mean it was conservative when you talked about it on a discrete quarterly basis, but it makes no change to the annual basis. Just to clarify that. That's what you mean. Thanks.

A - David Cole {BIO 7251632 <GO>}

Okay. Thanks for the observation. I'll come back to that in just a bit. But let me first go to the question regarding the overall component multi-year and the combined ratio on the cash. Let me ask Matt if he'll address those first?

A - Matthias Weber {BIO 16674983 <GO>}

Okay. So we do have multi-year contracts in the large transactions. We are not disclosing how much of it is multi-year. In case of a multi-year contract, the written premium which we are disclosing here reflects the total amount of premiums across all years if a contract is written on a multi-year basis. However, the earned premium, the earned pattern will be smeared again over a multi-year time period. So when determining the U.S. GAAP earned premium everything is being done as it should be.

And with respect to your question, one B (49:29), the 99% expected combined ratio appropriately reflect the large transactions, which as you rightly pointed out including (49:46) above average amount of casualty business, which almost by definition comes with a higher than average combined ratio. So that is taken into account. It's all good.

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

(50:02) come back on the question regarding the convergence of all (50:05) solvency regimes?

A - Matthias Weber {BIO 16674983 <GO>}

Yeah. So, I guess it depends a little bit on your perspective, but what I was trying to express in the video is really if you take a relatively broad perspective, you can see that there are several countries also outside Europe that are modernizing or modifying their potential capital regimes and they adopt an approach, which is at least logically or conceptually similar to our approach where meaning a total balance sheet risk-based economic or at least partial economic perspective the most relevant examples I would quote here would be China and Mexico. Obviously, there is an exception, a very notorious exception being the U.S. But even in the U.S. you can see at least very partially, a very partial element of internal models being introduced in the NAIC RBC approach with respect to nat cat for example. So, that was really the trend I was referring to and that is certainly a trend that we are encouraging.

A - David Cole {BIO 7251632 <GO>}

Okay. With respect to your question, 2b, so I note in total you've asked in fact four questions. So, with respect to your question, 2b, what I explained applies both on a quarterly basis, as well as on an annual basis. So, in order to do the nat cat normalization, we release $1.2 billion and add-back $1.5 billion, that leads to a too conservative outcome.

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

(51:59).

A - David Cole {BIO 7251632 <GO>}

All right. Next question please.

Operator

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

Q - William Hawkins {BIO 1822411 <GO>}

Hi. Thank you very much. Back on the combined ratio, with no apologies. First of all this is picking up I think on what you were saying Matt to Andrew's question. I'm still confused about what you are doing at the full year stage. You said very clearly in your prepared remarks, that $1.5 billion is the figure within 99%. But when you were talking to Vinit, you were talking about $1.2 billion this year.

So, I don't understand that, and from what I've understood, it sounds like there is a step-change between the nine months and the full year. More relevantly, can you help us understand your underlying combined ratio, because your new underlying combined ratio is 96%. You are still talking about 99% for the full year. So, what I'm trying to get is the message from you guys. If that really is an underlying figure, you are actually telling us that you are doing much better than 99%.

If what you're actually saying is that's not the case and effectively the figure in the next three quarters is going to be north of 100%. On most other things, the whole purpose of this process, which was apparently to create a more smooth quarterly combined ratio, seems to be defeated (53:07), because you've introduced volatility; so, how am I going to (53:10) think about the 96% versus the 99% for full year. I'm sorry if that sounds like many questions, but it was only one. So, secondly, David, could you very briefly just give us an outlook from the actual dividends coming in the rest of the year, such as you can see them, Reinsurance seems to have paid its dividends a quarter early. Are we, given that we haven't seen a dividend from quarter, are we budgeting for a zero this year? And are we still assuming about 300 million from the Life Capital by the end of the year? Thank you.

A - David Cole {BIO 7251632 <GO>}

Thanks, Will. For both of the questions. Now, Matt, you want to pick up the first, and I'll come back to the second.

A - Matthias Weber {BIO 16674983 <GO>}

Yeah. So, look, with respect to the first question, I really don't know what else I could add, or what else I could explain, other than just repeating myself, but I don't believe that makes a lot of sense to do so with respect to the underlying combined ratio and the 99%. So, absolutely, I assume the 96% you are referring to is the one for Reinsurance, where you adjust the 93.3% actual U.S. GAAP combined ratio for nat cat and for prior year development. And the question is why are you guys still sticking with the 99%?

And the answer is, we wrote - as a result of us writing a much bigger amount of larger transactions, more casualty business. This additional casualty business will come with a higher combined ratio; although, over time it will also come with higher reserves and therefore a higher investment income to compensate for this, and this casualty business has just started to earn through and its impact over the quarter, they will become bigger. Secondly, this quarter we were lucky with respect to large manmade losses. And the total amount of large manmade losses, we experienced is clearly below what we experience on average. And therefore, we also believe that the two underlying combined ratio taking into account also large manmade losses is higher than what we experienced in Q1.

And the third reason with respect the renewals, prices are still softening despite the fact that the price softening has decreased, it's still softening and as a result of this we believe that the business in the next few quarters again across almost all lines will come in with a little bit of higher combined ratio relative to the past. So taking into account these three reasons makes us believe that the 99% expected combined ratio continues to be a reasonable number to assume.

A - David Cole {BIO 7251632 <GO>}

I'll come back to your second, I think, your eyes are as always are quite sharp. And, if you look at our Q1 results, you'll see that the Reinsurance unit did pay a dividend of the group of just under $3 billion prior to quarter end. Last year, you may recall that Corporate Solutions did the same a $200 million just prior to quarter end in Life Capital then known as Admin Re paid a dividend during the course of Q2. There's no real specific number that I want to put on the units other than same order of magnitude as previous years would not surprise me. These things are actually just down to a little bit of going through proper corporate process. Our philosophy remains the same. We have a targeted capital level for each of the units and excess capital above that, we like to have the units move up to the group as quickly as they can. So, I would encourage you to look for our Q2 report when I would anticipate that both of the other units will pay dividends up by the end of June. Next question, please?

Operator

The next question is from Thomas Fossard, HSBC. Please go ahead.

Q - Thomas Fossard {BIO 1941215 <GO>}

Good afternoon. I've just got one question left, which is related to SST. It seems to be that a couple of Swiss-based player (58:04), but discretion or potentially FINMA pushed toward I would say going more for the standard formula and scratching internal models. So I just wanted to better understand where - how do you view potentially FINMA evolution in that respect and potentially its implication? Thank you.

A - Matthias Weber {BIO 16674983 <GO>}

So, I guess to get an alternative answer to that question you would have to ask FINMA and as you know, I'm no longer speaking for FINMA. Actually, I've not been for two years now, but what we see is that there is an attempt to develop standard models. So we don't have standard formula and that the SST is a standard model. And to actually encourage smaller – especially smaller insurance firms to use the standard model rather than come up with their own internal model. I don't expect this to apply to Swiss Re or to any of the large groups for that matter, but that's just my personal expectation.

Q - Thomas Fossard {BIO 1941215 <GO>}

Thank you.

A - David Cole {BIO 7251632 <GO>}

Thanks Thomas. Next question please.

Operator

Our last question is from In-Yong Hwang, Goldman Sachs. Please go ahead.

Q - In-Yong Hwang {BIO 18784369 <GO>}

Oh hello. Thank you for taking my question. I'm going to have a last tab (59:33) at the $1.2 billion and the $1.5 billion that we've been talking about. Would it be fair to say that, you can only adjust that number down to $1.2 billion this year, because you had a very benign 2015? Because, if you saw normal losses during the last year, then there will be $300 million late reporting from 2015 that you'd have to be reporting in 2016, so I just want to check that.

And my second question is on the losses that we've seen so far in the second quarter, earthquake in Japan and Ecuador. Is there anything, that's worrying you in terms of the losses in those places? Thank you, very much.

A - David Cole {BIO 7251632 <GO>}

Thanks for both questions. So, Matt, I want you to take the first and either you or I can take the second, if you would prefer?

A - Matthias Weber {BIO 16674983 <GO>}

Okay. And I'll take both if that is okay. So, with respect to your first question, the answer is no, that takes place every year. Because, we have – every year, we have a late reporting loss pattern, coming from our clients. With respect to the losses that happened in Q2, the biggest earthquake, Japan event is right now, under consideration, so we are in the process of estimating our loss and it's too early to talk about it or if any signals with respect to the other nat cat related losses that have happened in Q2 so far. They are not of an order of magnitude that is we're speaking about?

A - David Cole {BIO 7251632 <GO>}

Okay. So just to confirm, these are Q2 events and so there's nothing in our Q1 numbers. We'll look at each of them of course individually to determine what their appropriate level of reserving would be, but as Matt said, this will be little bit too early. I think it's always important for us when we talk about these things, to also just recognize that whether or not the impact is direct (01:01:43), they certainly impact the people and the communities where they've occurred. So, I'd just like to make sure that, that doesn't get forgotten here.

A - Philippe Brahin {BIO 19081619 <GO>}

Okay, David. This is Philippe again. I'd like to come to the end of the Q&A. So, I thank you all very much for joining. Also, big thank you to Matt, to Patrick, and David. If you have any follow-up questions, don't hesitate to call us Investor Relations at Swiss Re. Thank you again everybody for your participation today and operator back to you.

Operator? Now, can we close the call?

Operator

Ladies and gentlemen, thank you for participating in the conference. You may now disconnect your lines.