Q1 2018 Earnings Call

Company Participants

- JÃ¶rg Schneider, Gesellschaft Aktiengesellschaft

Presentation

JÃ¶rg Schneider

Ladies and gentlemen, welcome to our audio cast about the main messages, facts and figures in Munich Re's Q1 result. As usual, the conference call this afternoon will focus on Q&As. As we announced 2 weeks ago, Munich Re had a strong start to the year with EUR 827 million net earnings in Q1. This was driven by: a good operational performance across almost all business segments; a quite resilient investment result against a bumpy capital market backdrop; and above all, by low major losses in reinsurance.

In primary insurance, we continue to be on track with ERGO's strategy program. Overall, we are well underway to achieving our financial targets for 2018. The FX result in Q1 was negative by EUR 68 million due to the continued appreciation of the euro against other currencies. The tax ratio of 20.4% was in line with expectations. The annualized return on risk-adjusted capital amounted to 13.2%. And the return on equity totaled 11.9%.

Let me start my review of financial development with the investment result. In Q1, we observed a rise in interest rates, particularly in the U.S., accompanied by volatile stock markets and widening credit spreads. Overall, the investment result was pleasing. And with an annualized return of 3.1%, meets our expectation for the full year. Despite share prices declining across the world, our equity investments made a positive contribution to the group's investment result as write-downs were more than offset by disposal gains and the typical positive impact from hedging derivatives. We also recorded gains from disposal in our fixed income portfolio, mainly because ERGO started to fund ZZR, although at a much slower pace than in Q1 2017. But due to policyholder sharing, this had limited impact on net profit.

Interest rate derivatives had an adverse impact, mainly on the P&C reinsurance segment, which posted a rather moderate ROI of 2.7%. This is also due to a quite low running yield of 2.5%, which can be partially explained by the usual dividend seasonality and lower income from associated companies. Including an average reinvestment yield of 1.9%, the running yield for the entire group amounted to 2.6% in Q1. For the full year, we still expect that the running yield will bottom out at last year's level. But due to rounding differences and currency effects, we will probably fall slightly short of the ambition for 2018 of 2.8%.

Let me now give you the highlights by business segments. In Life and Health Reinsurance, we are very satisfied with our Q1 technical result of EUR 140 million. This reflects claims experience that was better-than-expected on aggregate, mainly in North America and the

U.K.. But once again, partly offset by negative developments in Australia. Moreover, the result was positively affected by the recapture of a portfolio in Europe that has been in runoff for many years. Fees from deposit accounting of transactions with limited risk transfer increased slightly as against Q1 2017. We are optimistic that we can meet our annual target of at least EUR 475 million for the technical result plus fee income.

In P&C reinsurance, the Q1 combined ratio was 88.6% of net earned premiums. We recorded an extremely low major loss burden of only 1.4%. This was driven by reserve releases made necessary by positive runoffs, (nat cat) claims in prior years. They more than compensated for the benign loss experience in Q1 and led to a negative nat cat loss of minus 1.1% in the combined ratio. Large man-made claims of 2.6% also remained below our average expectation.

We continue to set provisions for newly emerging claims at the top end of the estimation range and expect corresponding profits from their runoff over time. Notifications for basic losses from prior years again remained clearly below the expected level. Reserve releases amounted to 4.1%, in line with our guidance for this year. On a normalized basis, the combined ratio amounted to 99.3%, which is consistent with the original outlook of around 99% for 2018.

In April, EUR 1.4 billion of premiums were up for renewal or roughly 8% of the total volume of the P&C reinsurance segment. These mainly relate to single clients and treaties rather than to the larger portfolios. The renewals were dominated by markets and contracts which were not affected by the 2017 hurricane losses.

Across the whole portfolio, we achieved a price increase of 0.8%, including interest rate effects of 1.8%. The market environment was comparable with what we observed in the January renewals, i.e., stronger rate increases were only achievable in loss-affected programs. For others, broadly flat pricing environment prevailed. Furthermore, we are pleased with the premium increase of 8.1%. We were able to seize attractive opportunities in select lines and markets.

So much for reinsurance. I now turn to ERGO. The gratifying net profit of EUR 77 million, which fell short of last year's exceptionally strong Q1 result, is absolutely in line with the earnings guidance for 2018 as a whole. The Q1 result was driven by a good financial development. In German Life and Health business, higher earnings in health were offset by significantly lower disposal gains in life compared to Q1 2017. Also, earnings increased in international operations, mainly due to further strong improvements in Poland.

The combined ratio of ERGO's German P&C segment amounted to 101.7% and was heavily affected by a winter storm. Adjusted for the corresponding above average nat cat burden and for seasonal fluctuations in claims and premiums, the underlying combined ratio supports the 2018 guidance. Also in light of our strong claims reserving position, we are sticking to our 96% target for the full year. Thanks to a positive one-off tax effect, this segment posted a break-even result in Q1.

In ERGO International, we recorded good technical results in P&C operations, thanks to the ongoing strong performance of Ergo Hestia in Poland on the back of a further improvement in motor business. We are pleased with the results of the international health business, mainly due to a positive development in Spain. This translated into a strong combined ratio in Q1 of 95.3%, which is well below our guidance of 97%.

IFRS equity decreased by 3.6% in Q1. Besides the negative impact from FX and our share buybacks, the contribution of the strong Q1 profit was offset by a significant decrease in unrealized gains in both our fixed income and equity holdings. This came on the back of rising interest rates and falling stock markets. However, unrealized on and off balance sheet reserves in our investment portfolio still amount to EUR 22.9 billion, of which almost EUR 7 billion belongs to shareholders.

The Solvency II numbers provide an even better reflection of economic realities. At 245%, the Solvency ratio in Q1 remained almost the same as at the end of 2017. Strong operating earnings, supported by a positive effect of very low major losses, compensated for an aggregate unfavorable developments in capital market parameters, resulting in largely stable eligible own funds. There was also hardly any change in the SCR as various insignificant effects offset each other.

As mentioned in March, all capital management activities in 2018 were already reflected in the Solvency II ratio at the end of 2017, including the repayment of the GBP 300 million hybrid bond. The capitalization of Munich Reinsurance Company under German GAAP continues to provide headroom for distributions. In a few weeks, we will begin the next share buyback round of another EUR 1 billion, which should be completed by the AGM in 2019.

Let me quickly turn to the outlook for the remainder of the year. With the exception of the reinsurance combined ratio, which was lowered to 97% due to the favorable large loss experience in Q1, expectations for 2018 have not changed in comparison with the figures stated in the 2017 annual report. We are aiming for a group net profit in the range of EUR 2.1 billion to EUR 2.5 billion, which we are all the more confident of achieving after the good First Quarter.

Thank you very much for listening. I look forward to our Q&A session at 2:30 p.m., Munich time.