S&P Capital IQ

CONTENTS

Zurich Insurance Group AG SWX:ZURN

FY 2016 Earnings Call Transcripts

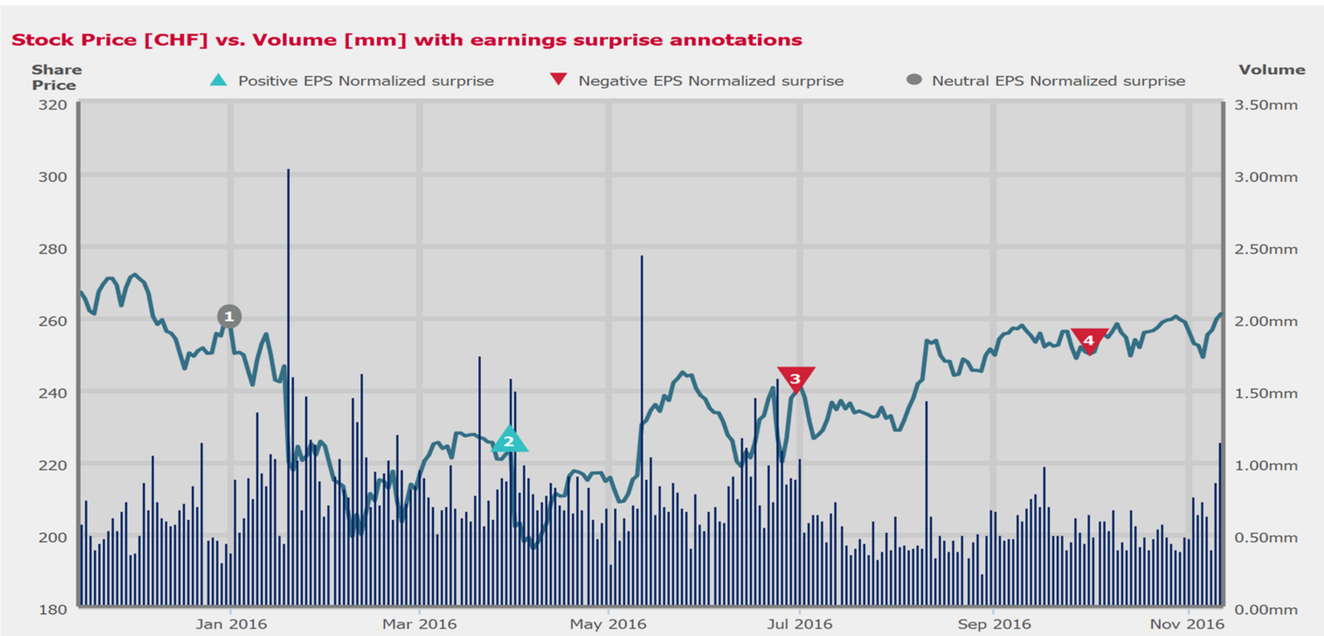
Thursday, February 09, 2017 12:00 PM GMT

S&P Capital IQ Estimates

	-FQ4 2016-			-FQ1 2017-		
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	SURPRISE	CONSENSUS
EPS Normalized	5.81	4.55	(21.69 %)	6.37	(26.23 %)	22.23
Revenue (mm)	11260.33	11928.34	5.93	-	-	50264.84

Currency: CHF

Consensus as of Feb-09-2017 10:57 AM GMT



Call Participants

EXECUTIVES

George Quinn
Chief Financial Officer and Regional Chairman of Europe, Middle East & Africa

Mario Greco
Chief Executive Officer

Richard Burden

ANALYSTS

Andrew Hughes
Macquarie Research

Andrew James Ritchie
Autonomous Research LLP

Dhruv Gahlaut
HSBC, Research Division

Farooq Hanif
Crédit Suisse AG, Research Division

Michael Igor Huttner
JP Morgan Chase & Co, Research Division

Nadine Adrienne Marion van der Meulen
Morgan Stanley, Research Division

Nick Holmes
Societe Generale Cross Asset Research

Paul De'Ath
RBC Capital Markets, LLC, Research Division

Ralph Hebgen
Keefe, Bruyette & Woods Limited, Research Division

Thomas Seidl
Sanford C. Bernstein & Co., LLC., Research Division

Vinit Malhotra

Presentation

Operator

Ladies and gentlemen, good morning or good afternoon. Welcome to Zurich Insurance Group Annual Results 2016 Conference Call. I am Maria, the Chorus Call operator. [Operator Instructions] And the conference is being recorded. [Operator Instructions] The conference must not be recorded for publication or broadcast.

At this time, it's my pleasure to hand over to Mr. Richard Burden, Head of Investor Relations and Rating Agency Management. Please go ahead, sir.

Richard Burden

Thank you. Good morning, good afternoon, and welcome to the Zurich Insurance Group's Full Year '16 Results Q&A Call. On the call this afternoon, we have our CEO, Mario Greco; and Group CFO, George Quinn. [Operator Instructions] But before we start with the Q&A, I would like to hand it over to our CEO, Mario Greco, who will make a few introductory remarks.

Mario Greco
Chief Executive Officer

Thank you, Richard. Good afternoon, everybody. So let me quickly assess what has been done in '16 and what these numbers have and what they don't.

So I think '16 was a year of profound changes at Zurich. We changed the organizational structure, but more importantly, the management team has been changed in composition and roles. We went down into the country's [ph] organization. In the second half of the year, we also merged the commercial and the Global Corporate organization in Europe, in U.S. and in the rest of the world.

In the meantime, we launched important portfolio restructuring actions. We underwrote a number of books. Through the year we kept improving our results quarter-by-quarter, so what you'll find in the year-end numbers, I think, it is a good achievement of the first year of the journey, which is going to take us for the next 3 years. Also what you find is a very consistent contribution by life, by retail business where Farmers has been especially strong, and also by the commercial and corporate business, which has been improving over the previous results.

I'm also pleased to report on the $300 million reduction in nominal amounts of the cost basis, which is something that we indicated to you that will be the target for '16, and it was achieved and give us good traction and confidence for continuing in '17 and in the next years.

So the way I would look at this result is, we're getting traction, we're getting confidence on what we can do. The movements are all indicating the right direction. The re-underwriting skills are clearly there in the results, also clearly there. More will come in '17 and in the next years, and the targets are exactly as reachable as we've thought they will be.

Before I hand it back for questions, let me also anticipate something that likely you will ask, which is on the M&A scenario and the market situation. There have been a lot of rumors and a lot of chats on M&A. Our position is, again, unchanged with respect to November. We have a strategy which is not based on extraordinary transaction, it's not based on M&A. However, we have been doing in '16 some transactions which all share a common theme. They're focused transactions on given markets or given customer segments and they strengthen our strengths. So they keep building on where we're already strong and keep creating further opportunities for us to maintain, acquire, develop our leadership position in market or in customer segments.

That is to say that we will continue looking at the market in the same way we have been doing, but we don't participate to the last rumors in the market, and we don't see anything that makes us changing our views.

With that, I will open the line now to questions. And George, myself and Richard will be happy to handle your questions.

Question and Answer

Operator

[Operator Instructions] The first question comes from Farooq Hanif, Crédit Suisse.

Farooq Hanif
Crédit Suisse AG, Research Division

Firstly, on Global Corporate. It remained disappointing in Q4 and for the year, although, obviously, it's improving. Can you talk about the things that you think will disappear through re-underwriting in 2017? So for example, perhaps, financial risks or things that have been a problem in Q4? And what impact do you think, continued impact it will have on top line in Global Corporate? And my second question, moving to the WCM. Clearly, very strong. I presume this does not include the impact of investment portfolio derisking. So if you could comment on that. But also, how do you think about your service capital position and what your priorities are for using that budget?

Mario Greco
Chief Executive Officer

Can I start, Farooq? And then I'll pass it to George for further comments and especially on the capital sides. I mean on Global Corporate, what matters to me is that business is improving and results are improving. One thing you should be mindful of is that through the year we changed many responsibilities in Global Corporate, which also meant that we reassessed customers' position, customer interest, and we took different decisions on a number of them. That was important to be made, and so this gives me optimism for now the continuation of the journey in the next years. I will pass it now to George for his part.

George Quinn
Chief Financial Officer and Regional Chairman of Europe, Middle East & Africa

So first of all, on Global Corporate, you're absolutely right. The performance that we've achieved in Q4 is not the one we've targeted and it's clearly the area of most significant opportunity for us looking forward to '17. I mean, after James Shea's arrival, he's done a review of the portfolio. We've discussed now with him as part of the planning process and he does have further plans to adjust the portfolio, but that will also mean -- it's a combination of -- in some areas we'll reduce capital allocation because returns are low, and other areas we may increase capital allocation along the lines that we outlined at the Investor Day. So I mean we do have a detailed plan that's country-specific, that this line of business targeted to further improve Global Corporate and to bring it to the level of return that we require. We -- I think it is a tough market, though. Difficult conditions, it's probably the most competitive market that's out there, but for us we have a required level of return for that business, and we'll keep making the changes required until we get there. From a top line perspective, I mean, we're not as -- we don't expect to see as dramatic a change as we saw during this year. And if I -- some of the things that we've done this year should start to feature into earnings as we move through '17. So I mean, in contrast to the red double-digit impact if I'd up premiums this year, I mean, something in the low single-digit range is what we anticipate for Global Corporate in '17.

Farooq Hanif
Crédit Suisse AG, Research Division

And just following up on expense ratio, which has got -- has had some focus today. I mean, are you worried that some of your bottom line through absolute expense reductions are going to get swallowed up in the ratio that you show? Or is that really not a concern?

Mario Greco
Chief Executive Officer

So I think this came up -- probably discussed the same topic a year ago and I guess, it was a concern there that, I mean, something that we do in the top line it might be offset by what we do on the expense side. I mean, we said then and it's still true today that we'll tackle the nominal expense first. And if we need further adjustments to achieve the target rate that we have, we'll do that afterwards. But I mean, the key focus for the time being, achieve expense goals that we have and achieve the required technical hurdle rates on today's businesses that we've got. At Z-ECM, there'll be some impact of the derisking that's taking place already through the last quarter of last year. The main impact in Q4 is interest rates. So in particular, the steepening of the curve reverses some of what we saw in Q1. From a budget perspective, I guess, we don't think of it in terms of a budget per se around $100 [ph] to $120 [ph]. It's really about capital allocation. We will share a regular review of where our current capital is deployed and whether there are alternatives that would give us more attractive returns to investors. And that's what led -- some of the things we did last year in the countries we've exited and, of course, we've redeployed that capital in other markets where we believe we can achieve an overall improvement. We'll go through the same process this year. I mean, that's true for countries, true for the regions and certainly true for the group. But from a budget perspective, I mean, we're obviously adequately capitalized. We're in position today where if we had opportunities to expand in the market, offered attractive rates of return, we could do it. Although, as we discussed before, it is now obvious that we have significant growth ahead of us in the short term.

Operator

The next question comes from Dhruv Gahlaut, HSBC.

Dhruv Gahlaut
HSBC, Research Division

Two questions. Firstly, could you talk about the legacy portfolio, what you have in U.K. as well as Europe in terms of the size of liability? And what is the capital attached to it given the RSA transaction which you've done yesterday? Would that be something as in you would look for your liabilities as well? Secondly, Slide 11, you've given a blended rate in terms of change of still around 2%. How would you say claim inflations stacks up with this on a blend basis.

George Quinn
Chief Financial Officer and Regional Chairman of Europe, Middle East & Africa

So let me start with the first question on legacy. So within our European -- the European side of our legacy portfolio, the largest piece by far is a U.K. employees' liability exposure. We've got about possibly $2 billion of reserves in that portfolio. From a capital perspective, it's a relatively small part of the overall reserve position of the group. So I mean, if the group has, say, $50 billion, $55 billion of reserves, I mean, we look at something certainly less than 5% of the total. From a capital perspective, I mean, it tends to diversify away in the economic systems, so the economic impact of disposing of it is not particularly significant. Has a larger impact for S&P, so I mean we're talking about a few hundreds of millions of dollars of S&P capital. I mean, everything that we have in legacy is not something that we intend to dust and look after for the rest of its natural life. We are looking to try and find exits, attractive economics. So I mean that's something that we have been exploring. We continue to explore the capital side of it. I mean, it's not unimportant, but to be honest, it's just to remove the risk factor, be a more important motivation for us. Beyond that, within Europe, I mean, what we typically have is small amounts of relatively long-tail lines in some of the continent European countries, but they are very small in comparison to the U.K., EU bloc. Your second question was about the loss cost inflation compared to the...

Dhruv Gahlaut
HSBC, Research Division

The 2%, yes.

George Quinn
Chief Financial Officer and Regional Chairman of Europe, Middle East & Africa

Yes, I mean, we estimate Q4 around 1%, so we're still seeing positive margin improvement.

Operator

The next question comes from Andrew Ritchie, Autonomous.

Andrew James Ritchie
Autonomous Research LLP

Just reading the commentary and results, I'm still a bit confused on the accident year, ex-cat loss ratio in Q4, is that still containing an above normal level of large losses? I'm talking ex-cat. So I think the implication is it's still slightly inflated versus what you described as normal. And in relation to that, when you talk about the outlook for the combined ratio, what's the assumption on a normalized level of cap? Is this going to feature in as reinsurance and exposure? It used to be around 3.5%. Is that still the case? And second question is just on expenses. I'm still confused to what the bottom line impact of the cost savings was in 2016? I appreciate you achieved $300 million run rate, but what was the bottom line impact? Because there's some confusing commentary. Clearly, under the IFRS expense measure which is used by more, but some of that is subaccounting effect. Now to just clarify, bottom line impact in '16 and the expected bottom line impact in '17?

Mario Greco
Chief Executive Officer

So on the first question, on the large loss component. Compared to what we had planned for, it was still slightly above, and so that's part what drives the outcomes for Q4. I mean, we've been really cautious both in the commentary and in other comments we've made to not make comments that this is volatility. I mean, we've taken a view that it is what it is. We have an expected return, and that's what we expect people to achieve. But I mean, it's sounding [indiscernible]

Andrew James Ritchie
Autonomous Research LLP

Just to be clear towards is that one of the reasons why the combined in Q4 didn't hit what you talked about at the end of Q3?

George Quinn
Chief Financial Officer and Regional Chairman of Europe, Middle East & Africa

It's one of the reasons. But you can see if you look at the numbers, I mean overall for the group, the loss ratio is actually in a pretty decent place, notwithstanding what we discussed earlier on Global Corporate. The expense rate charge in Q4.

Andrew James Ritchie
Autonomous Research LLP

So it's still slightly above what you planned for the -- on...

George Quinn
Chief Financial Officer and Regional Chairman of Europe, Middle East & Africa

In that quarter.

Andrew James Ritchie
Autonomous Research LLP

And on the cat?

George Quinn
Chief Financial Officer and Regional Chairman of Europe, Middle East & Africa

On the cat, so cat -- given the covers that we now in place both for last year, and in fact, we've increased the amount of cat cover we have in place for '17. We expect, again, long-term expectation, around 3% compared to the prior 3.5%. On the bottom line impact of expenses, Richard and I were talking about it earlier. I think at times we try and do too much to explain what's taking place, and I think that had the unintended consequence of confusing people. I mean the simple way to think of this is that we have a $300 million bottom line impact after you allow it for currency. If you look at the financial end, you'll see a larger number, but we don't give ourselves credit for the currency impact, that $300 million.

Andrew James Ritchie
Autonomous Research LLP

So is it incremental $400 million in '17 then?

George Quinn
Chief Financial Officer and Regional Chairman of Europe, Middle East & Africa

I mean, but the currencies will move around over time.

Andrew James Ritchie
Autonomous Research LLP

Sure. At constant effects, I mean?

George Quinn
Chief Financial Officer and Regional Chairman of Europe, Middle East & Africa

So yes. Correct.

Operator

The next question comes from Nadine van der Meulen, Morgan Stanley.

Nadine Adrienne Marion van der Meulen
Morgan Stanley, Research Division

The first question is on -- yes, your comments around claims inflation that you just made, that they're around 1% for the group. Could you give more details on the regions with regard to the claims inflation and the rate increases that you're putting through? And the second question is on the cash remittance. The guidance of over $9.5 billion for '17 to '19, if I, sort of, simply compare that to the $2.8 billion in 2016, that means on an annual basis, it's about 12% higher each year in the next 3 years. Can you explain where that uplift is coming from? Is that all from the operational earnings improvements? Or are there other sources as well, for example, reduction in service capital in certain units? And then, I shall ask quickly on the ultimate loss ratio for 2016. It looks a little bit low relative to previous years. Would this have by any means an impact potentially on future reserve for leases? Can you comment on that?

Mario Greco
Chief Executive Officer

Thank you, Nadine. So on the claims inflation topic, it's hard to do just a claims inflation when looked on about pricing region by region. I mean, overall, you've seen the figures for rate, you've heard my comment on lost cost. If you break it down, the positive end of the spectrum, and generally, Europe is in pretty good shape. I mean, Italy is the only area where we see more pressure on the margins and other things but I mean, U.K., Germany, Switzerland, Spain, all looking in very good shape and above the average for the group. In North America, a more challenged mid-market commercial, also the corporate end of America, I mean things are probably closer to flat than improved in that particular market. I mean, much more competitive dynamic and much harder to get rate that's significantly ahead of lost cause. And in Global Corporate, generally falls on that same trend, so stronger in Europe, slightly weaker in North America. And I would say, of the 2 key regions -- I mean, Lat Am is in decent shape. Maybe slightly below overall Asia PAC because of the changes that we've made in the portfolio. So for example, we've been reducing our exposure in Australia, which is one of the weaker markets but maybe slightly above the average overall impact. On the cash remains topic -- so, just to repeat something that I said at the Investor Day just to make sure that the frame of reference is correct, so we've had a target for the last 3 years of 9 -- you've seen what we've announced today, so we've significantly exceeded that. We've set 9.5 as a target for the next 3 years and that includes absorption of the restructuring cost that we've talked about before. So I mean, gross of restructuring, the cash target would be significantly higher than the one we've published today for the last 3 years. The vast majority of that comes from operational improvement. I mean, as you'd expect, we always have some plans around capital movements or extraordinary dividends that we've taken -- I mean, most of that over the course of the last 2 years around -- particularly around Farmers. So we've taken care about that capital of Farmers Re because it's wasn't required to support the business there. And I mean, we don't have an equivalent impact plan for the next 3 years. We do have an expectation that some of the things we talked about before around some of the excess capital in North America, on the commercial side coming back to us. But the uplift is to the vast majority is driven by the improvements in operational performance and higher dividends that, that permits. On the ultimate loss ratio between '16 compared to previous years, I mean, it depends what you look at in terms of previous years. Obviously, if you compare it to '15, it's significantly lower. But I guess, we'd all expect that, I mean, given that what we know happens. '15, you then got a mix of years going back. I think if I look at where we end the year at an ultimate loss ratio perspective, I look at the triangles, I look at the paids [ph], I mean, we're in a good place compared to what I've seen from the group starting prior years. And as far as reserving goes, I mean, we feel comfortable with where we are reserved overall. We've talked already about the PYD and our intention to keep it in a reasonably narrowband and try and maintain some consistency. And if I look at what we've done over the course of the year, I mean, my view, and I appreciate that it's subjective, is that -- I mean, even with the PYD delivered in the range that we've talked about, I mean, our view would be that we've actually strengthened the overall reserve position. So today, we'd be -- I mean, if anything, slightly more confident than we were a year ago.

Operator

The next question comes from Paul De'Ath, RBC.

Paul De'Ath
RBC Capital Markets, LLC, Research Division

A couple of questions, please. Firstly, just a point of clarification already on the dividend. You made a comment that you paid us or you're going to pay the dividend part in reduction of cat contribution reserve and part from retained earnings, and it'd just be interesting to know what's kind of driving that? Is that markedly different to what you've done in the past? And that's question one. And then secondly, just looking at the Q4, you've sort of alluded to the fact that part of the reason why you missed on the guidance in terms of combined ratio was -- and due to large losses and partly due to expense ratio and -- but I mean, what -- I guess, what was the surprise on the expense ratio side? Was it that you couldn't cut the cost that you thought you're going to? Or was it due to top line being lower than you thought or what -- I guess, what was the surprise for you there?

George Quinn
Chief Financial Officer and Regional Chairman of Europe, Middle East & Africa

So on the first one, on the dividend, you've probably seen in prior years that, I mean, we talked to a dividend, but technically it's been a distribution from reserves. And because of Swiss law, I mean, we already got to make those distributions, selling to retail shareholders in a form that's free of withholding. There's a given amount that we have defined by prior capital issuance that would permit us to do that. As we pay the dividend this year which is over CHF 17 per share, as we partway go through that number, we exhaust our ability to make distributions from those reserves. So we technically make the CHF 17 payment in 2 pieces: one is the distribution and one is a more traditional, ordinary dividend. And with that, we will have exhausted our capacity to distribute capital than that more technical way. In the future it should be ordinary dividend. On the expense ratio side of things, the -- I mean, I think if you look at the number for the quarter, I mean, we anticipate that we'll see a step up in Q4. We have a seasonal pattern to expenses that, I mean, we've had over several years. So we would expect to see around a 1% move up. I mean, we still have, I mean, beyond that another 1.5 points of there to explain. I mean if you dive into it more deeply, I mean, there's a combination of effects that drive that up, but I mean, premiums are probably the thing that drive it most. And of course, maybe the thing that we haven't anticipated as well as we may have done was the way that GWP would feed into the earned premium. If you look at the GWP numbers for Q4, moves are not as significant if you allow for RCIS and the impact of disposals that we would've seen earlier in the year. And given that we have an expectation that next year premium volumes will be fairly flat, and that will be a temporary impact. But what it does do is, of course, it will cause a rebasis [ph] -- the expense ratio that we start from. But I mean as we go through the course of 2017, you'll see the expense ratio start to move down again as we get the benefit of the expense and efficiency program that we're still pushing through the organization come through with a relatively stable top line.

Operator

The next question comes from Thomas Seidl, Bernstein.

Thomas Seidl
Sanford C. Bernstein & Co., LLC., Research Division

First question is on your guidance for the year, 12% ROE. I think the underlying ROE last year was 11%, so you would probably need to achieve some 9%, 10% improvement in operating profit from the guidance you put out today for P&C. I only get to $300 million. So I wonder, what are the other missing parts to get to the at least $400 million operating profit improvement. And the other question is on Page 11, again on your rate change. About 40% of your U.S. portfolio is long-term liability, and with the steepening of the curve, should we not expect basically rates to come down as you and others start to price in the better interest rate environment?

George Quinn
Chief Financial Officer and Regional Chairman of Europe, Middle East & Africa

Thanks, Thomas. So, I guess, on the first one, I mean obviously, we need to sit down together and could throw you a more detailed model, but, I guess, what I'd point to maybe above everything else, is if you look at what we intend to do on the expense side, that's a very big step towards that gap that you have referred to on the ROE. And beyond expenses, we do expect to see some improvement on the technical side. I mean, I appreciate -- it becomes more difficult to get as we go on, but given the portfolio action that we have taken and it's like some of the portfolio steps that we'll take next year, we anticipate further improvement [indiscernible] and doing those things in combination will be what drives the improvement to more than 12%.

Thomas Seidl
Sanford C. Bernstein & Co., LLC., Research Division

Can I follow up, please? So on the expense side, I would assume that this is already part of your 1.5% lower combined ratio guidance and on the live side, you basically guide for flat operating profits. So, I guess, the expense part is already captured in that.

George Quinn
Chief Financial Officer and Regional Chairman of Europe, Middle East & Africa

So again, I mean, we have an expectation that through the course of next year, we'll achieve that $400 million pretax cost reduction. If, not only in one area. On the rate change and the risk that that causes, and I mean the market to react and, essentially, halter reductions, I mean, I think if you look at things from a longer-term perspective, I agree with you that, I mean, ordinarily when some of the pricing factors or the cost production factors change, the market eventually competes them away. I think, though, typically, there's a lag around interest rates. I mean, hard to say precisely how long it would be, but I think if we did see rates move up, I'm not convinced that you'd lose that benefit immediately. I agree that, over time, it'd be very, very hard to retain it.

Thomas Seidl
Sanford C. Bernstein & Co., LLC., Research Division

So year-to-date, you don't see that type of activity from competition?

George Quinn
Chief Financial Officer and Regional Chairman of Europe, Middle East & Africa

I'm not aware of it at this stage.

Operator

Next question comes from Vinit Malhotra, Mediobanca.

Vinit Malhotra

I just wanted to understand, George, this -- the divergence sort of between NAC and GC in terms of the loss ratio of the underlying loss ratio. Is it that NAC's doing more effective tiering because of the investments in the data mining tools or is there something that explains that in this quarter again, from [indiscernible] previous quarters, but just trying to understand a bit more. And the second question is or just, sorry, to come back on the expense ratio. But there is also a comment on commissions going up because of business mix. If you could just elaborate a bit. Is it that you have to pay more commission so that people can justify all you've cut or what's the story there?

George Quinn
Chief Financial Officer and Regional Chairman of Europe, Middle East & Africa

Yes, okay. Thanks, Vinit. So on NAC versus Global Corporate, I mean, there are, obviously, quite different markets and they have -- I mean even from an end [indiscernible] perspective, completely different starting points. I mean, NAC, I mean, has some exposure at the top end of its business to things that are similar to the things that Global Corporate has at the bottom end, but I mean the nature of what they do is quite different. I focus on things like workers' comp, on the construction side, we have the right markets, we've got F&I. Obviously, we have to crop in a big way after the acquisition. I mean, Global Corporate, I mean, the entire programs for the company you'd expect. I think -- I mean, I think if we look at what NAC's done, we're very happy with the execution from the team at NAC. They do invest a lot on data analytics using new technologies to try and create product to help us recite our price more effectively. And they've done a number of things during the course of '16 that in fact, Kristof spoke about at the Investor Day. Global Corporate, I think -- I mean the issue is partly where we start from it and partly the market. So it's a very, very competitive market. It's, obviously, the one that's most impacted by, for example, cat pro and risks, and we all know what's happened from a pricing perspective there. But again, within that, I mean, if you look at the portfolio, again Mario talked about this at the Investor Day. I mean, we could look to try and shift probably a mix in a way that we think would deliver a more attractive return. We have been a bit too concentrated in areas where I think we've seen more margin erosion over the last few years. So a more balanced portfolio around Global Corporate would certainly help us. I know that's high on Jim Shea's list of priorities. The challenge is the extent to which the market will allow us or support that shift over time.

Vinit Malhotra

And George, just in 3Q, there's, obviously, the European lines, which are true-ups in Global Corporate. Was it a similar effect in 4Q? Or was it only losses that led to this worsening [indiscernible]?

George Quinn
Chief Financial Officer and Regional Chairman of Europe, Middle East & Africa

Well, I appreciate the question. I always have this temptation to analyze things to death, and I think the problem with it is that you can find excuses for almost everything if you do that. Maybe in the end, our conclusion is it's just not where we wanted to be. This is clearly where we see the biggest opportunity for improvement. On the expense ratio commissions, a mixed topic. So, I mean, the one thing we have seen, but it means, it's future licenses. It's slightly positive for the combined ratios. It may explain a shift in the expense ratio driven through the commissions side. I mean, again we've got a bit more consumer masking [ph] in the business in the book. We know we have more coming on stream in Latin America over the course of the next 12 months. And, of course, the acquisition that we'd like to complete, that we currently have under way will also be something that drives potentially the mix or rather the mix within the combined ratio in a different way. So I think on this topic, I mean, we'll try and do more as we come up to Q1 and help people understand how it might develop as we go forward because it will be a key topic for us, but it's that mass consumer element of the portfolio that tends to drive up the commission component.

Operator

The next question comes from Michael Huttner, JPMorgan.

Michael Igor Huttner
JP Morgan Chase & Co, Research Division

I have 2 questions. One, which is a pure speculative question. You have this German life business where $400 million will be used in the ZZR in next 5 years. Have you thought of selling it, and what numbers are you looking at? The reason I ask is that -- heard that somebody wrote that in December, there would be demand from UNIX portfolio and he put a price on it on $1 billion. So clearly, there's a market for this kind of stuff, which is a profit market that buyers are not expecting to be paid to take the business. And then, the second question is Jim Shea he's the new guy at Global Corporate, right? And what's his -- how's his incentive structured? Because of the one hand, I don't get it. Why would I want to start in a business with effectively kind of being wound down and merged into countries, and it does appear from reporting, I get 0 visibility, very difficult to argue I should get paid much. But, on the other hand, he might get the benefit that all these claims, which I imagine you're very large claims decided yes, your banding them against claim -- let's just get their money back early. And you even might say no, it's not like that. I'm thinking, maybe it is a bit like that, but these claims will naturally dry up over the next couple months or maybe 6 months and then your -- the business might actually look even better than you were hoping. How is the incentive structured relative to these 2 potential trends because, our guess is, I don't really know.

George Quinn
Chief Financial Officer and Regional Chairman of Europe, Middle East & Africa

Excellent, so 2 traditional Michael Huttner questions. You'll appreciate -- I'm going to ask Mario to answer the second one in a moment. On the first one, you'll appreciate I'm not going to answer that one. I mean, I think the thing I would point you to, though, is again one of the comments that Mario made back in November when we had the Investor Day, I mean, we take a decision many, many years ago, about what our priority would be when it came to the products, what we thought we could serve clients best, and that's reflected in the product mix today. And it's certainly been one of the things that's helped our German business from being a much bigger challenge than it would be otherwise. So I mean, we don't have a burning problem in the German life business. We have some capital that's not earning quite what we'd like it to do, but I think our team there with the challenges that they have, is actually doing a very, very good job. Mario, do you want to comment on Jim's incentive?

Mario Greco
Chief Executive Officer

What can I say to you, Michael? The transformation that Jim is bringing is -- to start with, it's a different approach. Jim has been an underwriter for a number of years. So he is bringing straight underwriting culture to the organization. And so we are refocusing everyone to work client by client, account by account, portfolio by portfolio. The other thing that still needs to be appreciated is -- skills are not infinite and it's definitely not infinite for us. Between corporate and commercial, we were replicating skills. That cannot work or cannot work infinite. So by bundling together under Jim all these people, we have a unification and a better use of the skills. Also, I think it's much more clear now the way in which he's operating compared with before because the people belong to the countries and Jim is responsible for setting targets for giving them underwriting priorities guidelines and even directly some global businesses, which clarifies a lot of accountability issues that we had before, but it's a huge change for us and it's something that has caught us busy for a number of months last year.

Michael Igor Huttner
JP Morgan Chase & Co, Research Division

Absolutely. Just a question, how much capital is in German life?

George Quinn
Chief Financial Officer and Regional Chairman of Europe, Middle East & Africa

If you go back to our presentation, and you'll probably remember very well from 3 years ago. I mean, within that, we've given -- we have an underperforming capital element. Germany makes up -- it's not quite half, but it's not far away from the $10 billion that we identified then.

Operator

The next question comes from Andy Hughes, Macquarie Group.

Andrew Hughes
Macquarie Research

A couple of questions if I could. First one -- sorry to overanalyze it, but Global Corporate. So I'm just a bit confused because when we went through the kind of tiering exercise, I noticed you're not updating on the tiering on the slides today, and so are you basically saying that the tiering exercise didn't really work in the way you anticipated? Because I remember when we talked about kind of Q4 last year. We talked about how on the new underwriting strategy their loss would've been lower. And clearly, you've got large claims now. How -- are these large claims from tier 4? Or are they large claims from a different tier that was previously categorized? And the second question is on NAC, and it's a pretty simple one. What would the combined ratio being x the crop business in Q4, x, I guess that earns over Q3 and Q4 and therefore, when we get to Q1, obviously, it will revert back to close to where it normally is?

George Quinn
Chief Financial Officer and Regional Chairman of Europe, Middle East & Africa

So on the Global Corporate topic, I'm going to refer to an answer that I gave a few moments ago. I mean, you can certainly pick out things that I could claim if it wasn't for this, it would be better, but I mean, in the end, it is what it is. I mean, we have an expectation of a higher return from this business, we've taken steps through the course of last year. We continue to tier, and we haven't shown the tiering. I mean not because it shows a different picture, it shows exactly the same picture. But in the end, it's the outcomes that matter rather than the inputs here. I think we're still confident that the steps that we've undertaken through the course of '16, we'll have a positive impact. But I said, we're not yet to the level that we'd like to see. And that will be part of what we address again through the course of '17. As I mentioned earlier, Jim has been through the portfolio. He's identified from his perspective the changes that he would like to make, as of maybe taking capital away from some areas and moving them to others. I don't expect the same significant top line change that we saw in '16, but we clearly, have more work to do on Global Corporate.

Andrew Hughes
Macquarie Research

Can I ask what happened on the 1st of January renewal selects? Obviously it's a very big -- big thing for Global Corporate.

George Quinn
Chief Financial Officer and Regional Chairman of Europe, Middle East & Africa

Global Corporate, I mean, with the exception of a couple of the European markets, it's a continuous business throughout the year. So I mean, it's not like reinsurance, where it has a big Jan 1. It's a pretty continuous profile.

Mario Greco
Chief Executive Officer

Can I also make a comment? So I think in reality, what we appreciate in life is the fact that the trend physical to Global Corporate. You can't really linearize this trend by quarters. It doesn't work that way. I mean, I'm sorry to say so, but the improvements for us are there. Improvements will continue to come. You have lots of dissociative impact in one quarter or the other. The trend is there, and the trend would continue to generate the improvement over time. I have a sense that you're kind of reading a little bit too much in one quarter only.

Andrew Hughes
Macquarie Research

I was looking more at the half year, actually. I was just thinking about 3Q and 4Q this year versus 3Q and 4Q last year. I mean it's basically higher than it was last year in terms of the loss ratio.

George Quinn
Chief Financial Officer and Regional Chairman of Europe, Middle East & Africa

I mean, if you look at the year-to-date [indiscernible] you asked me and I agree. I think we've had better performance on the attrition in the first half. I think we actually had some luck on the large loss side. Second half has been weaker, but there's not much I can add to what I said earlier. I mean, we are aware, we are focused on it and Jim and the team have a plan in place where they expect to drive significant improvements through the course of '17. On the crop topic, I think there's actually a slide in the deck, Andy. So if you have the deck, Andy on Slide 36, you can see there the impacts on NAC of RCIS.

Operator

[Operator Instructions] The next question comes from Nick Holmes, Societe Generale.

Nick Holmes
Societe Generale Cross Asset Research

I wanted to revisit the expense control question and the real question is why is the $300 million not visible in the expense ratio? And can you tell us what are the factors that offset it basically? And can you explain how should we really think about the $1.5 billion? I mean, it isn't, I guess, giving us great confidence that we can't see the $300 million in the actual ratio. And then, second question is just quickly on U.S. commercial, wondered if you could give us, say, flavor of where you think rates will end up this year for yourself. I mean, the market is soft, but you've done rather well in 2016. Do you think you can continue that performance?

George Quinn
Chief Financial Officer and Regional Chairman of Europe, Middle East & Africa

Thank you, Nick. So on the first one, apologies for this, but I'm going to try and take us back to what we had said earlier in the year. We'd indicated that we anticipated the expense ratio would be fairly flat. Having said that, we had a goal to reduce absolute expense levels. If you look at the full year, we've done both of those things during the course of the year, and the reason we thought the expense ratio would be flat is because we anticipated that to improve profitability, which we've done, that would require us to give up some volume. And so I mean, where we -- I mean, I did don't see any expense control issue. If I look inside the group, we have a much tighter expense regime than we've had for some time. There's a focus on further efficiencies that we need to drive out over the course of the next 2 to 3 years to achieve the goals that we had, but in the offset -- put it in inverted commas, is what happens on top line? And that's what drives this difference, but we have achieved the goal that we set on expenses, and I'd refer you to the answer I gave to Andrew Ritchie earlier on the call. On the U.S. commercial market, I think, the team have done pretty well. I mean, as we look forward, when we look at planning, we would expect in the U.S. market a bit along the lines of the -- you asked even from earlier that rate and loss cost in the U.S. market in '17 will be fairly in balance so -- of all the markets, that's one of the most competitive ones out there currently.

Nick Holmes
Societe Generale Cross Asset Research

Just coming back on the expense ratio. What sort of expense ratio in P&C should we expect for 2017?

George Quinn
Chief Financial Officer and Regional Chairman of Europe, Middle East & Africa

So I'm really tempted to give you the plan in great detail, but I mean, we have a goal for our return on capital, so both our ROE goal is the primary one that we have. We all appreciate that we cannot get there without improving the overall combined ratio. I mean, our expectation is that we will see us move from what's around in 99 down by that 1.5 points and we'll see contributions from both expense and from loss improvement.

Operator

The last question comes from Ralph Hebgen, KBW.

Ralph Hebgen
Keefe, Bruyette & Woods Limited, Research Division

Ralph Hebgen from KBW. Three things, if I may. The first one goes back to Global Corporate, I'm afraid. Just one point. In the fourth quarter, I noticed that there was a reserve increase again in Global Corporate. And I thought that was a little bit disappointing because it came after 3 quarters where we had a net release run rate in the region of 4 percentage points. So it would be interesting to just hear some commentary on what generated the need to have a reserve increase in the fourth quarter. Was there were a little bit of true-up at the year-end involved? And where are we're going to go from here? That's question #1. Question #2 is relating to cash, specifically in the life segment. I noticed there, you reported $0.4 billion. That's like $100 million or so below the run rate, which we've seen in the recent years, and I think looking at the numbers that might have been generated by Spain, which had a higher acquisitions strain. So perhaps, on that one also some commentary what generated that lower run rate in the life segment. And are you happy to confirm your guidance going forward, that cash generation in the life segment is going to be increased from here onwards? And the final one is just the factual check on the excess of loss attachment point in the large loss reinsurance treaty. What are your plans going forward into 2017? Are you going to lower the attachment point there? And that's it. That's question #3.

George Quinn
Chief Financial Officer and Regional Chairman of Europe, Middle East & Africa

Thank you, Ralph. So on Global Corporate, I mean you're absolutely right. There is a reserving increase within the book in Q4. I mean, as we talked about before, we're looking to try and manage the overall portfolio and I mean, at all times, we have pockets of strength and there will be some pockets of vulnerability. And we addressed one of those pockets of vulnerability in Global Corporate in Q4. I mean, the overall group outcome was actually I mean, towards the top end of our guidance on PYD. I mean, we've reiterated in the written material, and I'll reiterate it now that for '17, we anticipate, that you'll see PYD continue in the positive 1% to 2% range. On the cash, I think I mean, you're absolutely spot on. So you've picked exactly the thing that drives it. We had a deliberate decision together with one of our partners during the course of the year. I mean, it's actually put a bit more cash than a bit more capital behind a particular product. We saw this from a longer-term perspective. That's in interest of shareholders. It doesn't change our expectations of what life can generate, but I mean, we had an option or something in front of us that we thought was beneficial for the organization overall, and we therefore, made the decision. And on the excessive loss attachment point, I'm going to be slightly more coy than I normally am. I think I was ultra-transparent a year ago on everything around that contract. We just have renewed it at a slightly lower attachment point. So we have tried, together with our reinsurance partners -- I mean given the improved performance that we've seen even on the large loss basis in '16, we've had discussions to try and work with our reinsurers to reflect that and how that contract is structured. So that means the propensity to attach is slightly higher assuming the same level of large losses.

Operator

We have a follow-up question from Mr. Andrew Ritchie.

Andrew James Ritchie
Autonomous Research LLP

Sorry to come back. Just 2 very quick ones. Tax rates, you guide to 29% in '17. I think that's similar to what you said at the Investor Day. When does that tax rate start to drift down because, obviously, the non-life business pays a lower tax rate. I would've thought we'd start to see some benefit of that in '17, but maybe just clarify the strategy there. Second question. You point in the commentary to -- benefits you're getting from in-force management in the life business, at least in IFRS earnings. I guess, what slightly concerns me is when I look at the EV disclosure, there is actually quite a large negative variances to do with poor in-force experience on things like persistency, and I'm not sure what else. So I'm just worried that's a lead indicator that we've kind of exhausted the in-force benefits in IFRS terms because the EV commentary's reflecting there are some in-force issues. Maybe just clarify the disconnect there.

George Quinn
Chief Financial Officer and Regional Chairman of Europe, Middle East & Africa

So on the first one on the tax rate. I mean, the biggest challenge in the tax rate is actually the ongoing restructuring, and a lot of that cost ends up in the -- at home and that's not a very efficient place for us to carry it, but we don't have much choice around that. So I mean, what it really means is that I anticipate the tax rate with will be elevated both this year and next. It will start to trend down, but I'm still expecting for this year that you'll see something in that 28%, 29% range. And something similar maybe slightly lower in the following year. And then, we will start to come back to the longer-term tax rate that you're more familiar with.

Andrew James Ritchie
Autonomous Research LLP

George, what's the tax rate on a BOPAT basis then?

George Quinn
Chief Financial Officer and Regional Chairman of Europe, Middle East & Africa

I don't have that one. So I mean, it's slightly different from NIAS because of course there are elements in NIAS that tax at different rates. But I don't have it in my head with me right now.

Andrew James Ritchie
Autonomous Research LLP

But it would be lower because, obviously, the restructuring is in the [indiscernible] and not a [indiscernible].

George Quinn
Chief Financial Officer and Regional Chairman of Europe, Middle East & Africa

Yes, for restructuring, but it's not always the same answer for realized gains. I mean they can vary depending on which jurisdiction and what the tax law basis is for the realized gain component.

Andrew James Ritchie
Autonomous Research LLP

And the long-term tax rate you think should be what?

George Quinn
Chief Financial Officer and Regional Chairman of Europe, Middle East & Africa

So I think before you've seen from us somewhere around the 25% rate. So I think somewhere in that 25% to 27% range is where we should be targeting given the mix of businesses that we've got. There's one wild card in all of this so, of course, it's quite a large part of our profit is generated in the U.S. and if we saw tax reform there, I mean, that would potentially have a very positive impact on rate for us. On the in-force management versus the EV topic. So, I mean, timing is obviously different and I guess that's what's behind your question and that EV tends to anticipate the entire life of cash flows and extrapolates experience along those -- all those years to expiry. I mean, I don't believe, though, that we've completely exhausted what can be done in in-force management and we know -- I know from the plans that we have that, I mean, some of the things that we intend to do through the course of this year and next, I think, can improve both profitability and the cash signature from the book. But I mean, again, in my head, I couldn't draw that out for you in an EV versus BOPAT comparison. But I mean, let me take it away and think about it a bit more.

Operator

We have a follow-up question from Mr. Thomas Seidl.

Thomas Seidl
Sanford C. Bernstein & Co., LLC., Research Division

Maybe 2 quick questions on Page 17. On the profit, a sort of profit disclosure on life, if I may. I noted a very strong drop into technical margin by 10% and also quite a significant drop in the unit linked fee-based margin. Maybe you could comment on what does it drive? And them what is the outlook on those 2 items, please?

George Quinn
Chief Financial Officer and Regional Chairman of Europe, Middle East & Africa

So first of all, on the technical margin adverse claims experience. So 2 of our regions have had higher claims than were allowed for our pricing. But I mean, that can happen and is driven by some of the incidences -- some of the larger cases that we cover. On the unit length side, I don't recall issues. I need look at it and the team can come back to you, Thomas.

Thomas Seidl
Sanford C. Bernstein & Co., LLC., Research Division

Sure. On the technical margin, is the run rate $1 billion then? Or what is sort of the run rate you would expect here?

George Quinn
Chief Financial Officer and Regional Chairman of Europe, Middle East & Africa

So I think if you look at the drop that we've had this year and you treat most of that as volatility, you would see the run rate.

Mario Greco
Chief Executive Officer

Thanks very much, everybody, for dialing in today. We're aware there's a couple of people still with outstanding questions, and the team will come back to you during the course of the afternoon as we unfortunately don't have any further time today. If you do have any further questions, the whole of our team stands ready to take them. So with that, we wish you a good afternoon.

Operator
Ladies and gentlemen, this concludes today's conference call. Thank you for participating, and wish you a pleasant rest of the day. Goodbye.