S&P Capital IQ

CONTENTS



# Swiss Re Ltd SWX:SREN

## *FQ2 2016 Earnings Call Transcripts*

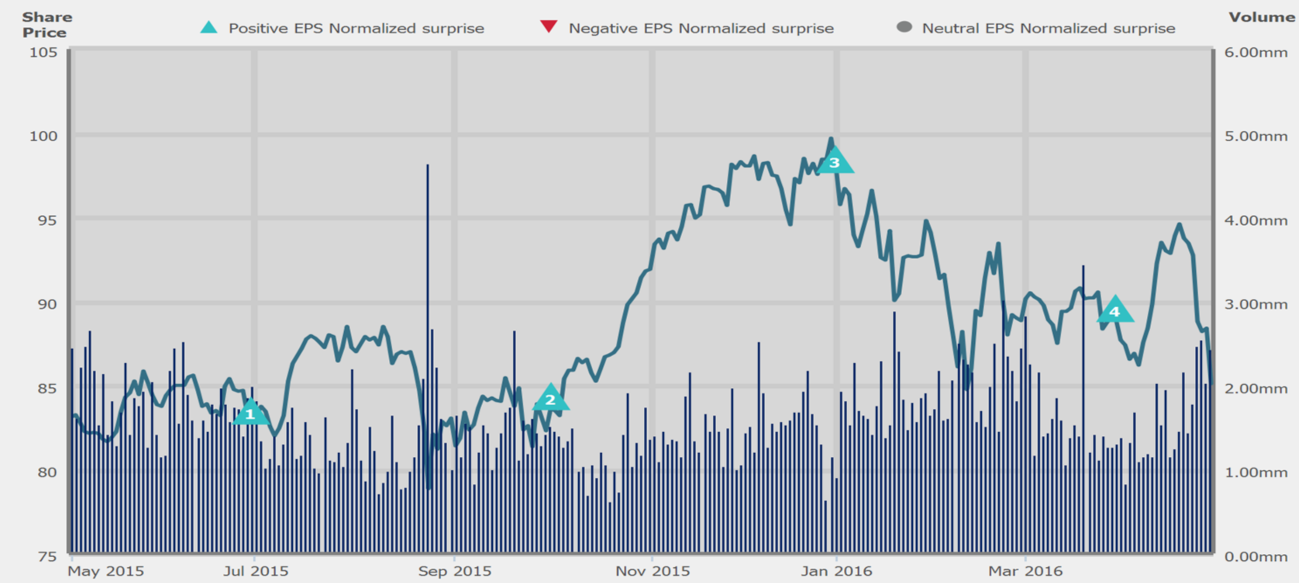
Friday, July 29, 2016 12:00 PM GMT

## S&P Capital IQ Estimates

| | -FQ2 2016- | | | -FQ3 2016- | -FY 2016- | -FY 2017- |
|---|---|---|---|---|---|---|
| | CONSENSUS | ACTUAL | SURPRISE | CONSENSUS | CONSENSUS | CONSENSUS |
| **EPS Normalized** | 1.74 | 1.77 | ▲1.72 | 1.98 | 9.70 | 9.05 |
| **Revenue (mm)** | 7504.10 | 8037.00 | ▲7.10 | 8371.83 | 32593.70 | 33742.26 |

Currency: USD
Consensus as of Jul-29-2016 12:54 PM GMT

**Stock Price [USD] vs. Volume [mm] with earnings surprise annotations**




**- EPS NORMALIZED -**

| | CONSENSUS | ACTUAL | SURPRISE |
|---|---|---|---|
| **FQ2 2015** | 2.17 | 2.20 | ▲1 1.38 % |
| **FQ3 2015** | 2.14 | 3.73 | ▲2 74.30 % |
| **FQ4 2015** | 2.44 | 2.52 | ▲3 3.28 % |
| **FQ1 2016** | 2.66 | 3.48 | ▲4 30.83 % |

# Call Participants

## EXECUTIVES

**Christian Mumenthaler**
*Group Chief Executive Officer*

**David A. Cole**
*Group Chief Financial Officer*

**Philippe Brahin**

## ANALYSTS

**Andrew James Ritchie**
*Autonomous Research LLP*

**Frank Kopfinger**
*Deutsche Bank AG, Research Division*

**In-Yong Hwang**
*Goldman Sachs Group Inc., Research Division*

**Kamran Hossain**
*RBC Capital Markets, LLC, Research Division*

**Olivia Sylvia Brindle**
*BofA Merrill Lynch, Research Division*

**Philip Martin Richard Kett**
*Macquarie Research*

**Sami Taipalus**
*Berenberg, Research Division*

**Thomas Fossard**
*HSBC, Research Division*

**Vikram Gandhi**
*Societe Generale Cross Asset Research*

**Vinit Malhotra**
*Mediobanca - Banca di credito finanziario S.p.A., Research Division*

**William Hawkins**
*Keefe, Bruyette & Woods Limited, Research Division*

**Xinmei Wang**
*Morgan Stanley, Research Division*

# Presentation

**Operator**

Good morning, or good afternoon. Welcome to Swiss Re's Second 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 Christian Mumenthaler, group CEO. Please go ahead.

**Christian Mumenthaler**
*Group Chief Executive Officer*

Thank you very much. Good morning, or good afternoon, everybody, and welcome to our Q2 results conference call. I'm here with David Cole, our group CFO; as well as Philippe Brahin, our Head of Investor Relations.

Let me start with a brief overview of the results we published this morning. As you've seen, we reported solid results, even though the quarter was impacted by large losses and persisting challenging market conditions. Q2 2016 group net income was $637 million, bringing us to a total net income of $1.9 billion, and an ROE of 10.9% for the first half.

P&C Reinsurance reports an ROE of 9.4% this year, impacted by a series of large losses, such as wildfires in Canada, the earthquakes in Japan, and floods in Europe.

In the July renewals, we continued to reduce in capacity to our flow business, and growing our portfolio of large and tailored transactions. These transactions are placed with us on a private basis, and offer differentiated economics.

In this context, we managed to maintain our risk-adjusted price quality at 102% year-to-date. Life & Health Reinsurance maintains its solid performance, with an ROE of 10.1%. Corporate Solutions results are impacted by 2 large 2015-related casualty losses and the business units reports a negative ROE of 4.2%. Because Corporate Solutions currently mainly operates in the excess layer business, it is exposed to a relatively high degree of volatility.

Life Capital delivers another quarter of strong performance, with an ROE of 13.4%, once again benefiting from net realized gains from the derivative portfolio of Guardian. We continued to reduce the exposure of this portfolio to this volatility during the quarter.

Finally, our Asset Management team produced a strong ROI of 3.7%, despite the low interest rate environments. Overall, our invested asset base increased, driven by the Guardian acquisition.

All business units have now paid dividends to the group and the capital position of the group remains very strong.

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

**Philippe Brahin**
Many thanks, Christian, and good day also to all of you from my side. [Operator Instructions] So with that, operator, could we please have -- could we please take the first question.

# Question and Answer

**Operator**

[Operator Instructions] The first question is from Xinmei Wang, Morgan Stanley.

**Xinmei Wang**
*Morgan Stanley, Research Division*

There are two questions please. My first question is on the losses in the pricing environment. Given that we've seen quite unusual large losses in this quarter, I was wondering how unusual do you think the losses are? And would you say that given there's an opportunity now to deploy capital in this market? And then my second question is on the combined ratio guidance for 2016, in P&C Re. Do you think the 99% underlying guidance is still achievable given the results? And I think Matt also mentioned on the 1Q conference call that we should expect more growth in casualty and may be some more pricing impacts to come through?

**Christian Mumenthaler**
*Group Chief Executive Officer*

Okay. I'll take the first one. So in terms of the net cat losses, Q2, I think overall the sum was $351 million, the biggest chunk of it comes from Canada. That is higher than expected for Q2, but I have to put it in context, right? In Q1, we had no nat cat losses. And so together, actually, Q1 plus Q2, the overall cat losses are slightly below our expected. So taking that into account, I doubt that this, in itself, will lead to higher prices in the next renewal rounds. I think what will eventually move prices apart from a potential large loss is a whole series of other factors, pressures coming from all different angles, one of which being obviously the low interest rate environment, which hurts people. One could be on the reserving side, if reserve releases start to be less abundant. And then yes, if loss ratios, overall, just approached the average expected loss and you take some of the other factors, we could get into a situation that even in the absence of a very large loss, prices start to stabilize again and maybe go slightly up. But I would say Q2 in itself is really nothing particularly in terms of the cat loss.

**David A. Cole**
*Group Chief Financial Officer*

Let me then come back to the second question, thanks for that. You need to recall, the discussion with Matt, at the time of our Q1 results, you recall the Q1 we had adjusted combined ratio for P&C Re of a little bit below 96% at 95.7%, now with Q2 reporting 101.9%. So for the first half, 98.8%, which is just slightly underneath the guidance that we've given for the entire year of 99%.

There's nothing at this point that would lead us to conclude that we should adjust that. And what Matt was talking about is just the inherent uncertainty of these estimates, if you will, given the uncertain exact mix of our business, what happens if pricing over the various subsequent periods, so there's nothing now in our Q2 results or developments off the back of the July renewals that would suggest to us that the 99% guidance is still not the appropriate figure.

**Operator**

Our next question is from Olivia Brindle, Bank of America Merrill Lynch.

**Olivia Sylvia Brindle**
*BofA Merrill Lynch, Research Division*

My first two questions. The first one just thinking about your updated combined ratio and methodology. When you talked about that in 1Q, you mentioned this $300 million of cat losses, which effectively comes through as prior-year development, the following year. And so I was wondering if you could update us on how much of this is in the year-to-date numbers? So effectively relating to 2015, how do we think about that $300 million? And then secondly, on the reserving position and thinking about your buffers, the longer tail lines of business, I'm just trying to quickly look through the triangles that you published and compare them to where we were previously. And so it sort of looks like on your general liability lines, you're slightly healthier, but the motor is maybe slightly weaker, I'm just wondering if that seems like a fair assessment? And in particular, in light of some of the reserve additions you've made on the motor side, year-to-date, has that sort of restored your buffers to previous levels? That will be helpful to hear.

**David A. Cole**
*Group Chief Financial Officer*

Thank you. So let me actually start with the second, I'll come back to the first. So thanks for mentioning the reserve book that we also publish, as you know, every year at this time. Couple of general comments, we haven't changed our reserving philosophy. We continue to be a prudently reserved best estimate across the entire book, which we go through the process of 4x a year. All these individual adjustments on various lines across the different geographies. But overall, I would say we've maintained our comfort in terms of where we are within the best estimate range. We tend to be north of 50 actually, generally positioned somewhere between 60 and 80, and that continues to be the case. As always, the individual lines are a little bit above that, and the lines are a little bit below that, but overall I think we continue to feel that we have a very appropriate prudent level of reserves, and nothing has changed now, related to developments in Q2 that alters that position. As to the adjusted combined ratio, actually I'm going to say, Olivia, no, not a whole lot more to give you on that. We published our numbers for Q1, and for Q2. We're going to come back, of course, at least on an annual basis, and give you folks some updates on that. But I think sometimes there's a little bit of a move toward a most overly defined, overly experience type of granularity and accuracy in some of these things. So we're going to keep with the numbers that we've produced. There's nothing that's changed, we still have the overall expected loss budget of $1.5 billion. The recognition that not all of it comes through the form of actual claims during the course of the year, that some part of it will holdover from previous years. So no update there.

**Olivia Sylvia Brindle**
*BofA Merrill Lynch, Research Division*

If I could just follow up on the reserving side for motor quickly, are you comfortable now having made, I guess, 2 quarters of additions on the U.S. side? And that, that's reflective of market conditions? Or should we expect anything further there?

**David A. Cole**
*Group Chief Financial Officer*

No. Absolutely. I mean, of course, I don't know what will happen going forward. But based on all the information that we know, the information we see from our cedents, we've gone through our portfolios, we've topped them up as you mentioned earlier this year, a second time now in Q2, but we believe that the level of reserving that we have for that business is also there prudent.

**Operator**

Our next question is from Kamran Hossain, RBC Capital Markets.

**Kamran Hossain**
*RBC Capital Markets, LLC, Research Division*

I've got two questions, one for Christian. I guess 4 weeks into the job as CEO, can you just maybe run through what the biggest concerns, I guess, that you're looking to address at Swiss Re in the coming years? So kind of what are the things that are on your desk, top priority? And the second question, I guess, one for David. In terms of the realization of gains, obviously, second quarter saw quite a bit of that again. In Life Capital specifically, will these continue throughout the year? Or are you pretty much done now?

**Christian Mumenthaler**
*Group Chief Executive Officer*

Thanks, Kamran, for a tricky question, very smart way to asking. So anyway, to me, there's, obviously, no big surprises, because I've been part of the executive committee for 10 years now. So my life hasn't completely changed in these last 4 weeks, nor I have discovered anything I didn't know before. So it's very much everything in a continuous mood. What is very clear and obvious is that we're in a cycle, we enter a period that is more difficult, so that's the whole industry, and they have started a while ago. And I think all the new CEOs in Europe, in particular, in the insurance industry, will say some of that. One -- obvious one is the low interest rate environment, which now, off this quarter, is probably going to stay even longer, low, which particularly impacts Life & Health, primarily Life & Health, to some of our clients, but also some of us, because the investment side is really important. So that must be a concern of every CEO in the insurance industry. And the other one is the obvious pricing cycle in P&C, which is nothing new, it always happens. And we certainly keep very calm, but we know it's concerning and it's not pleasant when you're on the way down. So we see some slowing down of that, but it's not yet at the bottom it seems. And so I'm mentally prepared for 1 or 2 difficult years before the cycle inevitably turns, because I still believe in cycles. Obviously, I see nothing that would prevent cycles to continue in the future. So -- I have no big news for you, I think it's pretty simple, we have the asset side, we have the liability side. And liability side is the P&C, CorSo area, which is a higher concern. Other than that, there is nothing particularly on my mind.

**Kamran Hossain**
*RBC Capital Markets, LLC, Research Division*

I'm sure we'll hear more in December.

**David A. Cole**
*Group Chief Financial Officer*

Let me pick up the second question, thanks for that. Let me be very short, there's no way that we would expect the level of profits that Life Capital has delivered in the first half would be repeated in the second half. As you know, we acquired Guardian, we're in the process, and in fact, by and large done what we want to do, to bring that portfolio under our governance, positioning it also for Solvency II, moving a little bit out of the derivatives market more into the cash market. Also looking at the underlying investments and determining do they meet our quality expectations as well. So we've been transitioning that investment portfolio, over the course of the last 6 months. And we've frankly, benefited, sometimes it's good to be lucky as we frankly benefited from. During that period of time interest rates have been reducing, while we were still sitting on that derivatives portfolio. But that is now, as I mentioned, by and large done. There's still maybe a still of trimming and managing the portfolio that we would expect to do subsequent to the Part VII transfer, which is, as you know, we anticipate during the course of 2017. Offsetting the P&L benefit that we've seen, it has had a little bit of a drag on the level of cash generation that we report, as a result of the same lower interest rates driving a higher solvency requirement under Solvency II. We experienced an impact of that a little bit more significantly in Q1 than in Q2. Actually very happy to see that the underlying business is very much performing in line with our expectations. The integration of Guardian, very much going in line with our expectation. And also, on that basis, we've reconfirmed our target of $1.4 billion to $1.7 billion of cash coming off of that business during the period 2016, 2018.

**Operator**

The next question is from William Hawkins, KBW.

**William Hawkins**
*Keefe, Bruyette & Woods Limited, Research Division*

Can you tell us what lessons you're learning from these 2 losses you've taken in the Corporate Solutions division? I'm not sure I understand the facts completely, but on the one hand, they seem to be 2 completely discreet loss events, but there seems to be a great coincidence in location, size, timing and nature of loss.

So is there something on the underwriting side that you need to learn from that? Or what's going on with those losses? And then very brief on the point of detail, did you get your exposure there, as a follow up in a syndicate or were you the leaders of that exposure [indiscernible]? And then secondly, a capital management question. This looks like we're heading towards the first year in about 4 years when you're going to have a normal P&C result. If that happens, it looks like your P&C Re earnings is going to be at least $1 billion lower than they've been for the past few years, which may imply that the dividend from P&C to the center could be lower than for the past few years, which then makes it look like the buyback coverage into the future carries significantly greater risk. You've never kind of committed medium term on that point, but how concerned should we be about the sustainability of the buyback if you do end up getting a few more normal years of P&C results?

**Christian Mumenthaler**
*Group Chief Executive Officer*

So I can take the first one. Even though CorSo is obviously not yet my speciality, but I'm working a lot to get into it. So as you can imagine, we studied that in quite some detail, right, this 2 losses. And I think there's really I can't see any commonality between the two, except that may be they're in California and they have a tort system there that gives very generous rewards to claimants. But I would say, taking a step back, right, if you think about the whole strategy of Corporate Solutions, to me it still makes complete sense to have that strategy as we're a risk knowledge company and it gives us access to risks we wouldn't have otherwise. I think the philosophy of it is also quite clear, that is we write risks to the balance sheet, the full balance sheet of Swiss Re, so we don't try to optimize, this little subpart of the business, which means they don't buy tons of reinsurance to isolate themselves from returns. As a result of that, I would expect a higher overall return on average from Corporate Solutions compared to some peers. But also some higher volatility where sometimes they have larger losses. And the team hasn't changed over the years, and if I look at their track record, I think they're definitely completely fulfilled that expectation. So the general performance has been higher than average in the industry, but this quarter we don't see our competitors yet, but this quarter has been hit by 2 losses, which is disappointing, but has to be expected. I think another fact plays a role, which is that the book isn't that large yet, so that adds, I guess, to the volatility we have to expect from that book of business, and that's something that should take care of itself over time. I mean this said, it's clear that in this part of the business, everywhere that the margins are going down, as they do in P&C Re. And the only right thing to do for the team is to be very careful on their underwriting side, having strong discipline. And I think there's a lot of evidence of that, that I could find. In particular they have stopped growing, basically now 2015, they haven't grow, this year, they grow a bit, but that's through acquisitions. If you take everything out, they are actually quite disciplined. So I have full trust in the business, and at this stage, I don't think we need to change anything drastically just because of these 2 losses.

**William Hawkins**
*Keefe, Bruyette & Woods Limited, Research Division*

To summarize that it does sound like you're thinking it's more bad luck, than anything you need to address.

**Christian Mumenthaler**
*Group Chief Executive Officer*

Yes.

**David A. Cole**
*Group Chief Financial Officer*

Well, let me pick up the second question about capital management. The first thing is just to reiterate that the way that we've expressed this in the past continues to apply today. I say that really just underline what we hope will, over time, really be seen as a consistency. There is no commitment indeed to future share buybacks, even the possibility for 2016 is subject to how our capital position will develop during the course of the year, as well as the opportunities that we would see to invest it back into the business side at acceptable returns, and that's also in line with what we've said in the past. There's no doubt that if you did look back over the last several years, you're absolutely correct, we've, I think, printed some extraordinary profits off of our P&C Re business. Even in the first half of this year, notwithstanding the fact that pricing has been under pressure, given the loss and burdens so far in the first half, ROE for the business is still a very respectable 13.7%. But in terms of forward-looking comments, let me just reiterate our approach, which is, of course, to maintain the financial strength, to maintain the regular dividend. We are able to increase the regular dividend whenever we are successful in investing into attractive opportunities in the business. That takes precedence over additional share, capital repatriations, but still when we find ourselves sitting on this excess capital, that we don't really believe we'll be able to reasonably deploy within a fairly short period of time, then we look to give it back. And that takes place in the first instance, of course, through the dividend. But then as an additional tool, we have the authorization, which needs to be renewed in principal every year. We have an authorization from our shareholders. So I would caution about penciling in these things. We said that before, there's no difference today than what I've said about that in the past. We'll continue to watch how the business develops, our capital position develops, the opportunities to invest develop. And later in the year, if we come to the conclusion that, it looks like we're going to be sitting on this excess capital, then we'll come back to the market with some further communication around the buyback.

**Operator**

The next question is from Andrew Ritchie, Autonomous Research.

**Andrew James Ritchie**
*Autonomous Research LLP*

Actually just following up on William's question, just on capital deployment. The first question, David, year-to-date, you've seen very strong growth in the business, the bespoke transactions, is that still sort of diversifying growth, because obviously, it's been in casualty lines such that the economic capital -- the incremental economic capital required or SST capital required hasn't been that significant? Or are we at the point where it's no longer diversifying because casualty sort of reached 50% of the book? So maybe just comment on the capital intensity of the 18% growth year-to-date? And the second question, linked to capital deployment, you're very confident that Guardian is going well, that's now integrated. Are we at a point now where you'd be comfortable looking for further deals in the U.K? Is the business ready to do more deals? We obviously saw some press commentary about third-party capital, which I think you commented on in the press. Maybe for Christian, if you just remind us again what your attitude is to the third party capital in Admin Re and the appetite for further deals?

**David A. Cole**
*Group Chief Financial Officer*

So let me pick up the first one, Andrew. Yes. And you're right, up until now, the additional casualty business that we've been writing has been more diversifying than anything else. That of course, would not continue forever, particularly if we continue to on the one hand grow that line of business while we are taking a little bit of capital off the table and the windstorm property nat cat area. But so far, it actually has been growth that hasn't really overall across the group required a lot of additional capital. Our capital position remained strong. You've seen, of course, all the dividends that come out of the group, but also on economic basis, obviously, we had some volatility in the marketplace, but our capital position allows us, I think, to carry that volatility quite nicely. So far, that additional business mix or development hasn't really taken a whole lot of additional capital? Christian for the second.

**Christian Mumenthaler**
*Group Chief Executive Officer*

Yes. I mean you saw our reaction, which was basically that we wouldn't comment on the market rumors. So not surprisingly. I think, this said, we said at the Investor Day last year that we would be exploring options to have other capital in that business. And I think the main reason is that it's clearly a very interesting business, with potentially a lot of growth potential, in particular now the environment you see, I think, from all of our segments, that could actually one where there is a level of interest. You see tons of capital who'd love to enter, but doesn't get access, because the regulator here would be worried to give it to them. There's clients who don't want necessarily to give this to a hedge fund or a private equity group, et cetera. And yet with Swiss Re, in the middle, which has all the knowledge, the capabilities and everything, but potentially not all the capital to do significant transactions in the space. So it's all about this puzzle and how to solve it. And I think there could be interesting opportunities. And we're going to continue to explore these opportunities.

**Andrew James Ritchie**
*Autonomous Research LLP*

And Guardian is sufficiently integrated now, that there wouldn't be a lot of risk in buying another block, is that fair?

**Christian Mumenthaler**
*Group Chief Executive Officer*

Sure. Guardian is on track, right? And you have to think about the lead times of anything. Obviously, if we found shareholders for the existing book, that's not distracting anybody from a further acquisition. If it was about further acquisition, it is always a lead time of at least 6 months, if it's not 9 months. And then if it's a separate legal entity, and you do Part VII, you can also park it for 1 or 2 years, or 3 years and then do it. So I don't think we're necessarily limited in doing a transaction in view of all the timelines. But the integration is not finished. But as I think about of all these pieces, I think fundamentally, we can discuss about other transactions at this stage.

**Operator**

Our next question is from In-Yong Hwang, Goldman Sachs.

**In-Yong Hwang**
*Goldman Sachs Group Inc., Research Division*

My first one is on the large transaction that we've been seeing. Just wondering from the demand side what is driving these deals? Are they very much client-specific issues? Or do you see a common theme versus regulatory changes for the large deals that you've done in the last year or so? And my second question is on the Life & Health, there's a comment in the presentation about an adverse experience in the Americas, just a bit more detail on what that is? Because I think one of your life reinsurance competitors in the U.S. has reported quite good U.S. mortality trends. So yes. Thank you.

**Christian Mumenthaler**
*Group Chief Executive Officer*

Yes. So let me take the large transaction bit. There are various motivations, but I think a common pattern is when you have a new CEO, a new CFO taking over, they look at the whole portfolio, they look at what kinds of ROE they get from all bits and pieces, they have new plans to grow in certain areas and they like to free up capital in old areas, sometimes even if it's a loss, sometimes without generating an IFRS or GAAP loss. And then the transactions themselves can be all kinds of things, there could be adverse development coverage for P&C reserves, for example. It could be going forward quota share that takes out business that has a high combined ratio, if that's what's bothers them. It could be a nat cat protection over several years, or an aggregate under their cat programs, and aggregate meaning, a program that adds up all the loss in the year, and if the sum of small loss in the year exceeds a certain amount we pay. So some are structured solutions that are very specific to the needs of a company. But generally, it's for people who want to free up capital or take out volatility. It's not so much driven by Solvency II, let's say or regulatory regimes at this stage. One exception that is the big Life & Health transactions, they are sometimes driven by that.

**David A. Cole**
*Group Chief Financial Officer*

Let me pick up the second question about the experience on the Life & Health side. Listen, one quarter doesn't really say a whole lot. You made reference to some other player who has referenced to some positive experience. So I think if you look back over the last couple of years, more often than not, we've also had relatively speaking positive experience from a mortality, morbidity side. This quarter, we had a little bit less positive experience versus expectation, but there's no real trent here. The underwriting business continues, I think, to perform in a way that gives us comfort regarding through the cycle type of return. We had 10.1% ROE this quarter, notwithstanding a higher equity base, and notwithstanding some periodic adjustments that we do just going through and looking at the valuations and on top of that, the quarterly negative experience versus expectations. So I don't see anything in here that suggests something other than just a random volatility.

**Operator**

The next question is from Vinit Malhotra, Mediobanca

**Vinit Malhotra**
*Mediobanca - Banca di credito finanziario S.p.A., Research Division*

So one on P&C and one on life, please. On P&C, we will be looking at these nat cat pricing and noticing a lot of comments in the industry that pricing is stabilizing a bit. So I was a bit surprised to see that you're saying now that we are reducing nat cat in the U.S., that's from your July renewals. Could you just comment a bit about, is this in your view the right time to reduce the U.S. nat cat, so that's first question. And on the Life & Health, obviously, we've seen the turnaround in Life & Health as a segment, but just going one step lower into the segment, Life & Health separately, I noticed that health has shown some of the adverse effects that In-Yong just discussed with you. And the health EBIT is actually a bit lower than the recent history as well in this quarter. So just if you could comment, once again, in 1Q, we changed -- you changed the ROE target definition from the old 5.5 equity base to current equity base, but equity base has again gone up by $1 billion or so in this quarter. So in the total context of health being a bit weakish, depending on model updates and changes, is the 10 to 12 ROE on a new current ROE still in place?

**Christian Mumenthaler**
*Group Chief Executive Officer*

Okay. I'll start with the nat cat while the others think how to answer the health questions. So I mean, when people say price are stabilizing, I think that's a nice description for further decreases. So from a mathematical point of view, I would say the second derivative is turning positive, but not the first one, which means that the decline of the decline is not happening anymore. So instead of whatever minus 10, you now have minus 3, or minus 2, or minus 5. But it's still negative. And as you can see now our long-term price adequacy of 102%, we cannot afford much more, right? We're hitting the target of where we stop creating value for shareholders. And so I absolutely told the team, already in January, but now they are preparing for the renewal if prices go down further, even if it's smaller amounts, that we should scale back on this whole business further. We have already scaled back 7%, which gave back some of the U.S. nat cat and we will scale back further if necessary. And I think that's the only right thing to do. So it's a question really of, if the margin is very thin, even a small decline makes it really uneconomic, and we should be very consequential in that. On health, I don't know...

**David A. Cole**
*Group Chief Financial Officer*

Yes. Life & Health, well, let me just first start with the second part of your question, which is about the equity base. You're absolutely right. whenever we were, let's just say, in the business doing the work that we had identified back in 2013, we said we thought that by 2015 we'd be able to generate a ROE of 10% to 12%, but we completely uncomfortable with what may happen with interest rates over that period of time, so we said let's fix the equity base at that $5.5 billion. Of course, we proceeded to implement those different actions, continued to write good business, put the right asset mix in place, dealt with some of this pre-2004 issue in the U.S. and then also finalized by putting the right capital structure in place for the segment. Now a couple of years beyond that, I think 2015, we were very pleased with the results. Also through 2016, we have an ROE for the quarter for 10.1%, but for the half, still 12.6%, I think off the top of my head. If you look more specifically, indeed the equity base has gone up, but we said that we thought the 10% to 12% would still be an appropriate target. Independent, if you will, somewhat of the equity base, I guess it's not without risk that's taken, but we think we also need to be able to give some sort of sense of comfort, confidence to our investors. The health results in Q2, actually there were some updates on the assumptions and valuations, of course, had a negative impact in health. The actual experience for health in Q2 was positive versus our expectations. So I certainly would not see something there to indicate trouble in terms of performance going forward. Just reiterate that 10% to 12% is a through the cycle target. We're not going to hit it every quarter, there will always be some volatility, also in the Life & Health business. If you just take a second to think about the absolute magnitude, the size of our in-force book as we go in order to just completely, rigorous cost of basis going through our portfolios on the basis of new data, on the basis of review of our model, assumptions we made from time to time need to be adjusted, there's always going to be some volatility. But we feel comfortable that the book, as a whole, is a good quality. And the underlying performance will continue to meet our expectation.

**Operator**

The next question is from Sami Taipalus, Berenberg.

**Sami Taipalus**
*Berenberg, Research Division*

Just first question on your liability business, and some of the stuff that you've got in your reserve disclosures, if you look at the ultimate loss ratios and they tend to be in sort of mid-80s to 90s on Liability Reinsurance. And if you add on the expense ratio on to that, you get to probably around 120 for recent treaty years in terms of ultimate combined ratio. I'm just -- I just wonder how that sort of a combined ratio make sense in the current interest rate environment, because again this is the book you've been growing quite a bit recently. And I appreciate what was said before about it so being relatively capital when you're diversifying, but it seems nevertheless like this pretty low level of [indiscernible] that was the first question. Then the second big thing I wanted to ask about was the reserves and CorSo, this time, even if you strip out those 2 major large claims that you flagged, there still seems to be a little bit of adverse PYD in Q2 and there was a bit of adverse PYD in Q1 as well, which is quite a sharp turnaround from what we were seeing last year and the year before that. Is there any trend there? Or is this just sort of random volatility?

**David A. Cole**
*Group Chief Financial Officer*

So on the second question, yes, there's a small little bit of PYD excluding these losses. These 2 specific losses are a little bit challenging in that regard because they happened in 2015. We only got real information about it this year, and it shows up as a PYD. But in the general context the way we discuss PYD somewhat of a different animal. If I look back over the last couple of years, we've had years where there's been positive, years where it has been negative, PYD I'm talking about, there's a little bit of a quarterly volatility around that. But if you strip out this $100 million, what it was $103 million, coming off of these 2 losses, a meaningless figure for Q2 for Corporate Solutions. So I don't think there's really a story there. I have to say, you puzzled me a little bit with your first question, and I don't exactly recognize some of the figures, but maybe we can take it off-line, to go into a little bit more of about the specific line or specific year that you're referring to. But just in general, listen, we recognize it from time to time, the combined ratio on a reporting year basis, can sometimes even go above 100% and still be an attractive book of business to write. But I don't think it would be appropriate tint that you may have that somehow we're sitting on serious lines of business or reserves, where we're expecting an ultimate loss somewhere in the range of 120%. I think we can follow up if you don't mind, off-line, but I don't recognize that.

**Sami Taipalus**
*Berenberg, Research Division*

Well, it really isn't anything complicated. If you look at the slides in your reserving presentation, I mean, I may have misread this, but the ultimate -- where it says ultimate loss ratio, it's kind of between 85 and 90 roughly, for all experience years except 1, since 2007. And your normal expense ratio is around 30% to 35%. So if you add those 2 together, you get to somewhere around 120. So I mean, I don't -- that seems quite a bit above 110, so I'm just wondering why? And there's not really much.

**David A. Cole**
*Group Chief Financial Officer*

There could be individual. I can pick any one of the different sides you want. I'm happy to go through in detail. There's some years, of course, in soft markets we did have ultimate loss ratios in excess of 100, but if you look at the overall book across the different accident year, treaty years, you'll see I think a very consistent figure below, the ultimate loss level of 100% on the book. So I really -- there may be individual lines, individual years that have experienced of course the ramifications of soft market environments. But one thing I can tell you is that consistently across our book with the exception of recently some updates on the motor side and of course, the ongoing story around asbestos in the United States, particularly, we remain, I think, very comfortable with the way the existing reserves have develop and the overall level of prudent associated with that. As I mentioned, typically, we sit somewhere between 60% and 80% of the best estimate range. Notwithstanding the fact that, over the last couple of years, for different reasons, we've had some prior year positive development. Actually, in the overall positioning within the range, we have not gone down. So we basically stay flat even in some lines of business has moved up a little bit. We're happy to follow up afterwards, if you don't mind.

**Operator**

Our next question is from Thomas Fossard, HSBC.

**Thomas Fossard**
*HSBC, Research Division*

One question left on my side, which will relate to the other rates you've got in mind, regarding any, I would say, big deals or acquisitions or ability to deploy excess capital. I've got you -- in the back of my mind, I've got an 11% other rate, which probably based from a couple of quarters back. Is there any chance in your thinking of how much is other right now? Are you still looking for 11%? Or is that -- has it changed in light of the new interest rate environment? Any update on that?

**David A. Cole**
*Group Chief Financial Officer*

Quick answer, no, no, it hasn't changed. Obviously, that's the kind of thing that from time to time you may have to review. But we continue to believe that for large allocations of capital, I'm not talking about every individual transaction that we do, but certainly for large allocations of capital, that having that type of rule of thumb, if you will, 11% ROE, is on a U.S. GAAP basis, is not a bad thing to have. Of course, we look at transactions using a number of other metrics. And as you correctly indicate with your question, at some point, with low interest rates and overall lower available returns, it may not be the appropriate number to continue to apply. So for the time being, as group CFO, I continue to apply it relatively rigorously.

**Christian Mumenthaler**
*Group Chief Executive Officer*

I think may be one thing to add is, is you're right, that's on a cat basis, but on a PV basis, so you could have a large casualty transactions where in the first year you have to set up reserve relative high, and then you have the interest rates coming through for 7 years. So it meets 11% overall on PV basis, not necessarily the first year.

**David A. Cole**
*Group Chief Financial Officer*

No.

**Christian Mumenthaler**
*Group Chief Executive Officer*

Every large transaction we have a document, and in the document we see the whole EVM view and the whole GAAP view over time year-on-year, and it has to meet this 11% hurdle.

**Thomas Fossard**
*HSBC, Research Division*

Okay. Can I take from your comments the transaction, the large transaction with AIG at the start of the year was based on these type of metrics because I think there were some comments in the market saying that potentially you may have taken this deal on relatively low profitability levels, so typically the size of the transaction with AIG important to this kind of hurdle rates?

**Christian Mumenthaler**
*Group Chief Executive Officer*

I have to say, we're extremely happy with that particular deal. But we look at different metrics. We look at it, we don't look at accounting year or combined ratio being great, every single year. We look at overhaul on the economic basis, right, EVM and also GAAP, right, how will this accumulate. So what is the -- if you want the PV combined ratio, the present value combined ratio and that was attractive for that particular deal. So clients are in the different capital regime, there's different interests and I think that's where you get interesting transactions, win-win transactions is when two companies have different KPIs, they try to optimize, then and they're in different regimes, right, then you have interesting opportunities. And so I'm sure they're very happy with the deal, and we're very happy with the deal, and that's possible.

**Operator**

The next question is from Philip Kett, Macquarie.

**Philip Martin Richard Kett**
*Macquarie Research*

Just one final question for me. On the Life & Health Reinsurance business, there's a comment in the presentation about successful renewals in China and in Australia, and is that now a significant portion of the business?

**Christian Mumenthaler**
*Group Chief Executive Officer*

So, it's not that significant, no. Because you have some renewal business, also in Europe, by the way, but that's at 1 1, it's not a big part of the business, not driving it.

**Operator**

[Operator Instructions] Our next question is from Frank Kopfinger, Deutsche Bank.

**Frank Kopfinger**
*Deutsche Bank AG, Research Division*

I have 2 questions. My first question is on the P&C Re combined ratio, could you elaborate a little bit there on the underlying trends? And I'm thinking especially about on your adjusted way, the way from the 95.6% that we had in Q1 to 102% almost now in Q2, but you could also do if you strip everything out like the reserve releases, nat cat [indiscernible] and so on, do you see the hiccup in Q2? And could you walk us through this increase, what the drivers are here I'm thinking especially on so just by the shift mix, by seasonality and also by the expenses, if you look on the combined ratio. And then my second question is on your buyback, now that you have upstreamed $3.5 billion of dividend to the holding, you've generated $1.9 billion in profits, that's still left over $850 million of nat cat budget, what could be there you really now to do the buyback for next year, or this year?

**David A. Cole**
*Group Chief Financial Officer*

Listen, there are all sorts of different scenarios about what could happen in the remainder of the year that may lead us to conclude that there are better uses of capital than buyback. It could be losses that occur, real losses so independent of what we have in our budget. Windstorm takes place somewhere in the North America, somewhere in Europe, earthquakes somewhere around the world, could be opportunities that arise to invest capital. So I think I'll go back to my earlier comment about the way in which we think about the capital in the hierarchy we think about it but as we get towards the end of the year, if we find ourselves sitting in a situation where the amount of capital we hold is in excess of that, that we think we should reasonably hold to continue to be able to respond to opportunities that arise, then we'll think about the best way to return that excess capital to our shareholders. As for your first question, really not a whole lot more I can add. There's seasonality, of course, every individual quarter is a little bit different. Our business mix continues, of course, to evolve a little bit and also business that we've written in previous periods, previous renewals, now flow their way through our P&L in terms of earned premium and loss expectations. We walked you through earlier a little bit the way that we think about are large nat cat budget and the fact, that it's not exactly linear throughout the year. We've provided with some information about the actual versus expected nat cat and the prior year impact. I don't really have a whole lot more to add to that in terms of granularity or insights, other than, I would caution you that the 99% estimate is an estimate for full year. There are a number of things that can move through the change that over the course of the year. We still believe, after 2 quarters, that it's an appropriate number. I think the actual adjusted CR adjusting for the expected versus actual and prior accident year development, coming in at just under 99%, so just shy of the 99% estimate, is at least some indication that the number may not be too far off, but time will tell.

**Operator**

Our next question is a follow-up by Vinit Malhotra.

**Vinit Malhotra**
*Mediobanca - Banca di credito finanziario S.p.A., Research Division*

I just wanted to just check on these 2 losses in California that we're talking about today. How does Swiss Re normally look at a loss? I mean if the loss occurred in 3Q '15 or 4Q '15, then should it not be the case that it should be reserved to some magnitude back in those quarters? I mean, I just want to understand how this reserving philosophy works, Dave, if you don't mind?

**David A. Cole**
*Group Chief Financial Officer*

No. That's perfectly fair. And the short answer to your question is, yes, the specifics of these 2 losses, however, meant that both the responsibility for the losses, now these are not property losses, these were casualty coming through liability so the determination of responsibility for the loss and also determination of the magnitude of the loss didn't actually take place or wasn't possible until effectively in Q2. So it wasn't possible at the time that the events actually started or occurred. But in principal, you're absolutely right, I mean, this is one of the things that makes us somewhat unusual and the fact we have 2 of these now in the same quarter is even more unusual. But rest assured, we've looked into this quite closely to see as Christian indicated, is there are some sort of trend. And the only think that we can really see is the fact that both of them were in California, but they're completely unrelated to each other. The circumstances just developed in such a way that we didn't have a view of the loss back in the quarter when the event occurred. And it became quite clear to us, specifically also this culpability, the responsibility issue during the course of Q2 of this year.

**Operator**

Our last question is from Vikram Gandhi, [indiscernible]

**Vikram Gandhi**
*Societe Generale Cross Asset Research*

It's Vikram Gandhi from Societe Generale. A couple of questions. One, is on the amount of short-term investments and the cash that you hold. If I look at the total of these 2 elements, the short term and the cash, it's about $17 billion plus, I appreciate it’s come down a bit from the last quarter, but it still looks substantial. So any thoughts around how you intend to deploy this cash? And transmit into some form of running investment income would be helpful. And the second is related to the Life & Health Re business. About 3 years ago you did a cleanup of the book, particularly with regard to the YRTs and the PLTs and so can you give us some comfort around the PLTs. So let's say, a couple of years down the line, the D10s and

D15s move into D15s and 20s, we wouldn't have another cleanup exercise I during -- in a year or 2? So those are my 2 questions.

**David A. Cole**
*Group Chief Financial Officer*

Yes. Thanks. So I'll take the first, and Christian maybe pick up the second. So you're right, you're looking at Slide 29, suppose you see the cash and short-term investments, we still hold a good cash position. Nonetheless, we more or less match in terms of overall asset liability match and we're currently I think minus $2.9 million DDO 1. We have been actually moving some cash into government bonds. As you see, that number has gone up a little bit as well as in the short-term investments, which are typically also just short-term government paper, but you can imagine not government paper with a negative yield, but government paper that still has a positive yield, albeit those papers are also becoming fewer and far between and the yields are becoming a little bit less. It remains a little bit of a quagmire. We have no intent to start putting a lot of cash in vaults or cash in mattresses or anything of the sort. We're looking for good quality credit. We want to maintain the overall asset allocation ranges that we've previously indicated. Actually during the course of Q2, we took a little bit of risk off the table, with equities and alternatives. We continue to look for opportunities to invest in the high-quality assets. But it's hard for me to say exactly where that cash will go. We're not going to go chasing yield that's for sure, continue to hold a good cash position, no doubt, at least for the foreseeable future.

**Christian Mumenthaler**
*Group Chief Executive Officer*

Yes, in terms of PLT, that is post level term issue in the U.S. on our old book of business, I think nothing has changed over the last 2 years. So it continues to be a drag, it will be a drag going forward. The -- we have whole team mitigating it, so that's I think what we talked about at the time on Investor Day and that's going quite well. The team by working together with the client can mitigate it by having basically more people staying off the PLT period with the client, which is better economically for the client and for ourselves, but we can't mitigate it completely away. I think the relevant thing for all of you and our investors is that we have taken that into account into all of our projections, and the 10% to 12% ROE we want to achieve. So it just means we have used the time and continue to use the time to add on more good business and do large transactions where we can, so that we can stay within the 10% to 12%. So if I could -- if I was a magician and could get away with that business, I would immediately get rid of it, but it's not possible and so we just work with it as we do with the whole in-force book.

**Philippe Brahin**

Thank you. This is Philippe Brahin again. So we've come to the end of our Q&A session. Thank you very much all of you for joining. And if you have any follow-up questions, please don't hesitate to contact any member of the Investor Relations team. And Sami, we'll follow up with you on the P&C reserve book as David mentioned. So thank you again, everyone, for participating today.

**Operator**
Thank you for participating, ladies and gentlemen. You may now disconnect.