Swiss Re Ltd SWX:SREN

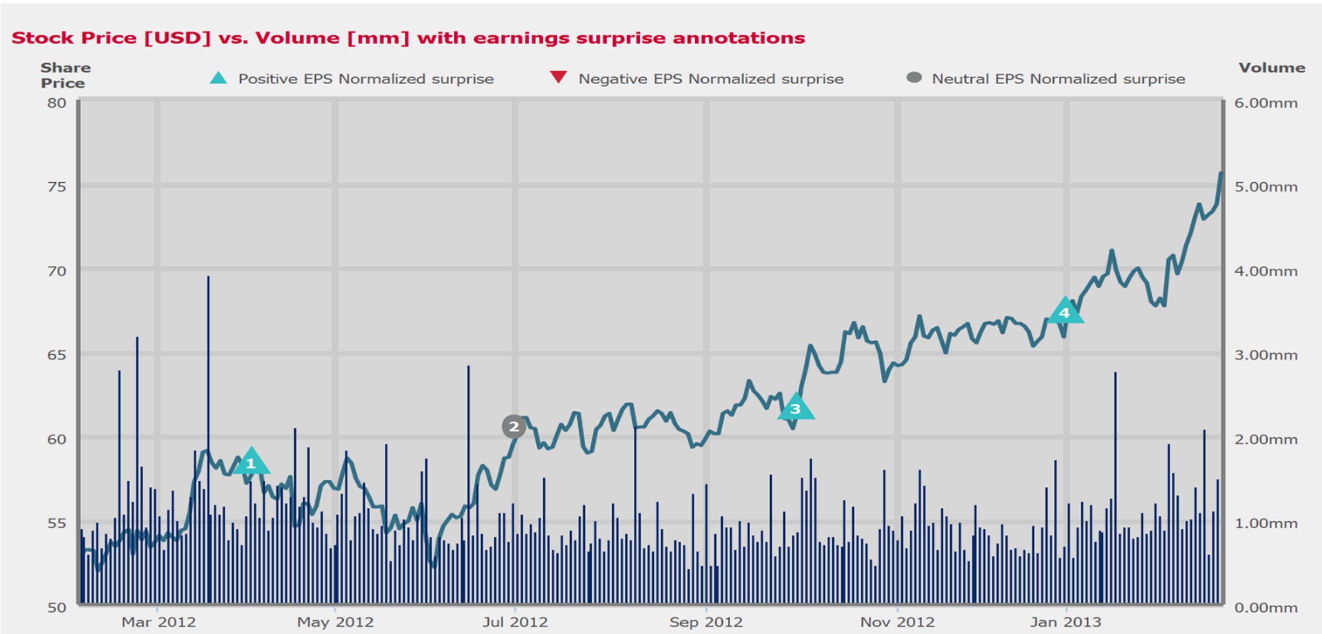
FQ2 2013 Earnings Call Transcripts

Thursday, August 08, 2013 12:00 PM GMT

S&P Global Market Intelligence Estimates

	-FQ1 2013-	-FQ2 2013-		-FY 2013-	-FY 2014-
	CONSENSUS	CONSENSUS	SURPRISE	CONSENSUS	CONSENSUS
EPS Normalized	2.88	2.29	1.75	9.60	8.53
Revenue (mm)	7487.60	6979.04	10.49	33824.61	34856.63

Currency: USD
Consensus as of Aug-08-2013 10:56 AM GMT



- EPS NORMALIZED -

	CONSENSUS	ACTUAL	SURPRISE
FQ1 2012	1.94	3.33	71.65 %
FQ2 2012	0.02	(0.12)	NM
FQ3 2012	3.23	6.30	95.05 %
FQ4 2012	0.50	1.53	206.00 %

Table of Contents

Call Participants	....	3
Presentation	....	4
Question and Answer	....	11

Call Participants

EXECUTIVES

Eric Schuh
Former Head of Investor Relations

George Quinn
Group Chief Financial Officer

Matthias Weber
Former Group Chief Underwriting Officer

Michel M. Liès
Former Group Chief Executive Officer

ANALYSTS

Andrew Broadfield
Barclays Bank PLC, Research Division

Andrew James Ritchie
Autonomous Research LLP

Fabrizio Croce
Kepler Capital Markets, Research Division

Frank Kopfinger
CA Cheuvreux, Research Division

Jason Kalamboussis
Societe Generale Cross Asset Research

Kamran Hossain
RBC Capital Markets, LLC, Research Division

Maciej Wasilewicz
Morgan Stanley, Research Division

Michael Igor Huttner
JP Morgan Chase & Co, Research Division

Stefan Schürmann
Bank Vontobel AG, Research Division

Thomas Dorner
Citigroup Inc, Research Division

Thomas Fossard
HSBC, Research Division

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

Vinit Malhotra
Goldman Sachs Group Inc., Research Division

William Hawkins
Keefe, Bruyette, & Woods, Inc., Research Division

Presentation

Michel M. Liès
Former Group Chief Executive Officer

Good morning or good afternoon. Thank you for watching this presentation on Swiss Re's Second Quarter 2013 Results. My name Michel Liès, and I'm Swiss Re's Chief Executive Officer. As you have become used to for full and half year results, you will see 2 presenters and with me is George Quinn, our Chief Financial Officer.

In the first of the presentation, I will remind you on my priorities and provide an overview on where we stand with regard to our P&C businesses, moving on from the focus on Life and Health Insurance and Capital Management at our Investors Day. These of course wouldn't complete without our views on the July renewals in reinsurance, but it also contains an update on where Corporate Solutions is on its growth journey.

I will then hand over to George who, in the second part of the presentation, will be setting out the key drivers of our financial performance in Q2 2013. I'll be back at the end for summary and outlook, as well as our financial targets.

So, let's get started straightaway. Slide 4 states the near to mid-term priorities that I have set for Swiss Re. This slide is unchanged from June 24, our Investors Day, when I showed it to you last. All points remain valid and the message is the same. Our aim is to both perform and grow profitable business and sustainable earnings.

At Investors Day, we focused on the first 3 sections of this slide, as they corresponded to the sessions on the day. I said back then that we won't talk about the 4 section, Property and Casualty reinsurance and Corporate Solutions at Investors Day as we will do so with our second quarter results, well, now, the time has come. We expect to continue to outperform our peers in P&C, starting with a good performance of our P&C Reinsurance business at the July treaty renewals.

On Slide 5, you can see that our reinsurance treaty business continue to grow in July and in the right way. Private deals and tailored solutions allowed us to expand our portfolio into July renewal by 12% even in challenging overall market conditions.

Overall, the economic or risk adjusted price adequacy reduced by 5% compared to business up for renewal. However, it remains at an attractive level. Year-to-date, we achieved 11% growth in our P&C treaty portfolio with overall economic or risk adjusted price adequacy marginally decreasing by 1%.

We consider this as a very successful outcome and I'm also pleased we continued to show good progress in target high growth markets. As you can see from the 25% growth rate year-to-date achieved in these markets, excluding China, which itself saw reduction.

What is more? As you can see on Slide 6, our portfolio composition is shifting as a result of rate developments. For example, we have seen a shift from China to the U.S. as we wrote some lower volume in certain solvency related quota shares in China, which consists to large extent of Casualty business. This is also the reason for the reduction I mentioned a minute ago. This Chinese quota shares have been replaced by U.S. Casualty business where margins are improving.

We continue to write the substantial amounts of nat. cat business. Risk adjusted price adequacy remains at attractive levels, even after the rate reduction in July. In the broader U.S. nat. cat market rate reductions were around 15% and even 20% for Florida in June. Again, we are not a market follower and we expect our market leading position and our superior ability to select risks and clear capacity to lead to better outcomes.

We are positive on the outlook for our P&C Reinsurance business also we expect competitive pressures to persist. As you've become accustomed to, there will be more details available on these subjects in our Monte Carlo Investor and Media presentation on 9 of September.

Let’s now move to Slide 7 and talk a bit about our direct P&C business Corporate Solutions. In fact, I’m not sure there is much more to say than they are fully on track for their profitable growth program. The Direct Commercial business is seeing slightly different pricing trends. For Corporate Solutions one could summarize these as overall stable at this point in time.

Corporate Solutions keeps growing profitably and overall we are well on track towards executing the strategy to achieve the gross premium volume of US 4 billion to US 5 billion by 2015 at return equity level of 10% to 15%.

Turning to Slide 8, you should not come as a surprise that the underwriting performance of the Group's P&C business. P&C Reinsurance and Corporate Solutions combine keeps looking very good.

This slide clearly demonstrates the continued success of our underwriting approach as witnessed by falling combined ratio in what is still a low interest rate environment, despite the upward move in yields during Q2. I reemphasize that disciplined underwriting and cycle management remain a key priority for Swiss Re.

With that, I hand over to George for the second quarter 2013 financial results. George?

George Quinn
Group Chief Financial Officer

Thank you, Michel, and good morning or good afternoon. I’ll start with the financial highlights for the quarter on Slide 10. I think you probably accustomed to the fact that our quarter results can many moving parts and this one is no different. There are number of one-offs or less frequent items and I’ll try to highlight these as I goes through the presentation.

Our second quarter result was robust and our storyline is unchanged. All business units have contributed positively and good net income came in at $786 million, which translates into earnings per share of $2.28 and an annualized return on equity of 10%.

The Group combined ratio of 100.1% reflects a significant number of large losses in the quarter which I’ll describe later. Our investments it almost 3.8% which is partly due to gains realized in government bonds as a result of a rebalancing into corporate bonds and equities, and reinsurance net income was $609 million in the quarter, as we recorded above average nat. cat and man-made claims.

Life and Health Reinsurance suffers some negative effects from the recaptures that we announced earlier in the year and also from reserve strengthening on disability business in Australia in the quarter which I'll outline in a few moments.

As already mentioned by Michel, Corporate Solutions continues to demonstrate progress towards it growth plans and capital generation has been stronger than expected. This is resulted in capital levels that exceed that needed for the growth plan, so Corporate Solutions has paid a dividend of $489 million to the Group in the second quarter.

Admin Re had a good quarter exceeding our expectations both in terms of net income and gross cash generation. I’d highlight the dividend of $357 million paid to the Group in Q2. And finally, something has been anticipated for some time and seems to have started, interest rates have been rising with about 60 basis point increase in the U.S. 10-year rates in the quarter.

This has led to a sharp reduction in unrealized gains on fixed income assets. And this together with the regular and special dividends of 7.50 francs per share that were paid in the second quarter led to reduction and shows equity and book value per share to $84.03 or 79.50 francs. There is no major impact from an interest rate rise on economic capital and if I given a short duration position it’s even a very slight positive.

On Slide 11 let me draw your attention to the unrealized gains by business unit and for the Group in the bond table. For the Group the after-tax amount contained and shows equity stands at $1.65 billion. By the end of the first quarter this number was $3.93 billion.

This is significant change but is broadly in line with the sensitivities that we included with the full year results disclosure. We updated these sensitivities as of the end of the second quarter and they are included in the appendix to this presentation.

Let's take a closer look at the P&C Reinsurance business now on Slide 12. Net premiums earned continue to grow as you'd expect following the expiry of the 20% P&C quota share at the end of last year.

As the growth contribution from the non-renewal of the quarter share increases over the course of the year we expect a higher premium growth rate for the full year. Growth in gross written premiums is slowing down with a marginal increase in the quarter.

As I mentioned earlier we’ve seen above average large losses for the quarter and the combined ratio of 100.7% reflects this. Large nat. catastrophes contributed 13.4 percentage points to the combined ratio, which is about 6.3 percentage points more than expected. The large nat. cats include the floods in Europe where we’ve estimated claims at $300 million and the floods in Alberta, Canada where are our initial estimate is $177 million.

Reserve releases contributed 3.5% percentage point benefit and overall, taken together with nat. cats this adds up to the underlying combined ratio of 97.9%. This number is over obviously higher than our guidance of 92% for the year for P&C Reinsurance.

We expect the second quarter to have a higher combined ratio than 12-month view because of nat. cat seasonality, 94% to 95% will be normal given the lower exposure to nat. cat in the second quarter.

The difference beyond is due to significant level of man-made losses experienced this quarter, including a substantial market revision to the Costa Concordia loss, losses from our mining facility in Utah and losses from our fertilizer plant explosion in Texas. Some volatility we expected and there is nothing in the quarter that changes our view about the fundamentals as you can see from the year-to-date view.

Return on investments was 2.9% partly due to lower yields. The business unit was also the beneficiary of one-off release of tax reserves adding to net income of $468 million. The tax benefits are mainly due to favorable decisions relate to corporate restructuring or to favorable order outcomes.

There is no reason to believe this would change or would lead to lower long-term tax rates for the Group and our longer-term expected tax rate has not changed, we still expect 24% to 26%.

All this together results another strong 17.8% annualized return on equity for the quarter. I’d also like to note that we’ve today published the annual work book on our P&C reserves as per the end of 2012. You can find that at the usual place on our website.

Life and Health Re on Slide 13. This business unit continues to be challenged for the reasons that we outlined at the recent Investors Day. I’m pleased to see that the business keeps growing in the areas that we have a positive effect on future, for example Health business and the high growth markets, and you see this in a growth rate of 13.4% in operating revenues and 15.7% in premiums and fee income.

As you saw at the recent Investors Day, this is part of the management action plan. The running yield is also improving as we are rebalancing our asset portfolio reaching 3.5%, which compares to 3.2% in the quarter a year ago and in the first quarter of this year.

Despite this, our pre-2004 U.S. business continues to underperform. The performance of the recaptured YRT businesses has been more negative than we expected. In the current quarter, the pre-tax loss from this block was just over $100 million.

I don’t expect to see similar impacts every quarter, by now we expect a net loss for this block to be around $100 million for the year, compared to the breakeven performance that we expected when the recapture was announced.

This only reinforces the importance of the plan that we said at the Investor Day. The experience this quarter does not change our view on the estimated $500 million negative GAAP impact that we expect to encourage we fix this business mostly the in 2014.

Our overall Health Reinsurance business produced strong result in the quarter and this is despite adding $82 million to reserves for Disability business in Australia. This is a risen on total permanent disability and disability income coverage we've provided to insurance some of the states superannuation schemes in Australia.

There been substantial delays in reporting and become aware that we've underestimated the claims as the schemes have provided data as part of recent tender or renewal processes. The positive is that favorable morbidity experience elsewhere has offset this.

Lower realized gains compared to the prior quarter continues the reduction in net income to $141 million, a tax benefit with the same underlying drivers as P&C Reinsurance in support of the results.

The effects that I mentioned just now it can be seen in operation income more for Life and Health Re business Slide 14. The additional reserving of this giant business is included in the mortality morbidity part of the chart, the effects of the pre-2004 business including the recaptured YRT business come in the next block, which we now show consistent with the way that we shown this at the recent Investors Day in June.

The pre-2004 post-level term business is actually improved somewhat over the previous year's quarter as was expected and the resulting operating income levels though are not acceptable. We've outlined how we are tackling these issues at the Investors Day and we reiterated our stated goals, management actions and targets, highlighting in particular a targeted return on equity of 10% to 12% by 2015.

Moving on to Corporate Solutions, I mentioned already the strong growth in our Corporate Solutions business with net premiums earned up by 28% to $686 million for the quarter. We can see how the business is on track to achieve its ambitions. There is a relatively high accumulation of nat. cat losses in the quarter, while this is above expectations in terms of dollar losses, as well as normal expectations of volatility.

Gross premiums raised are up by more than 11% if we are levy for some of the one-off effects in the prior period, resulting from harmonization of pre-estimate across business unit and the combined ratio 96.9% included 4.8 percentage points more nat. cat losses than expected, slightly more than the positive effect of prior year reserve releases of 3.7 percentage points. The underlying combined ratio adjusting for these 2 effects is 95.8% for Q2, about 1% better than our guidance of 97% for the year.

Net income after-tax was $55 million for the quarter. I know that while our reinsurance businesses enjoyed a tax benefit in the second quarter Corporate Solutions actually faced a slightly higher than expected tax rate as more of the earnings were generated in higher tax jurisdictions.

Admin Re has surprised us positively this quarter, the efforts of the management team is bearing fruit as higher than expected gross cash generation of $107 million and a dividend of $357 million paid to the Group demonstrates. The asset rebalancing is showing also an Admin Re's return on investments on running yield which have reach levels of 5.6% and 4.2%, respectively.

Altogether these results contribute to an annualized return on equity of 7.2% for the quarter. We don't expect these levels of profitability to continue as a significant element of the performance results from realized gains triggered by the asset rebalancing. Our prior guidance of low single-digit returns continues for the time being.

You've probably all seen a recent press release on Admin Re in the speculation of letter, understandably we received many questions on our U.K. business as a result. We've had a slide on Admin Re to the appendix and it was a regional balance sheet split both on U.S. GAAP and EVM basis, and I hope that you find these numbers to be useful.

We've been talking about investment performance as part of the BU I'm now on Slide 17, the Group investment results to summarize. You can see our average invested assets have decreased year-over-year, which is mainly the results of mark-to-market effects from rising interest rates and the sales of government bonds in the quarter. These sales were partly prompted by the decision to implement a short duration possession and we exclude cash proceeds from the invested assets total.

We sold government bonds to start to build up our strategic short duration possession of $7 million of DV01 and at the end of the second quarter the Group established $4.4 million of the $7 million target.

DV01 measures the sensitivity of the Group's interest rates and our $1 million short DV01 possession means that the Group will generate $1 million of economic profit for every one basis point rise in interest rates.

The Group ROI decreased from 4.5% in Q2 2012 to 3.8%. Compared to the first quarter this year, however, the Group ROI increased by 0.4 percentage points. This improvement is driven by both higher regular investment income as a result of the asset rebalancing and realized gains on the fixed income and equity portfolio of $309 million. Finally, the lower asset volume I highlighted earlier supported the increase.

The running yield on fixed income portfolio increased to 3.2%, up from 3% a quarter earlier. Compared to last quarter we've seen an improvement in the running yield. For the first time in quite awhile we've added investments at high yields than the assets sold. Of the 20 basis point improvement, half is from higher yields and the half is due to the change in valuation as a result of interest rates.

Acquisitions were made of book yield of just under 2.5% while the book yield in disposal was just under 2.4%. Going forward, we expect the running yield to improve further by approximately by 5 basis points per quarter as we continue to rebalance.

The 1 point to note is that this does not consider the negative impact of the short duration position as the cash positions are not in the running yield. If you look for this, you will see a marginal reduction in company's investment income, maybe of the order of about $30 million, mainly affecting the 2 P&C business. We can, as you know, choose to reverse this at anytime.

Our portfolio continues to show very low levels of impairments and a minimal exposure to peripheral European government bonds. I highlighted the drop in common shareholder's equity early on, here you can see the components. We paid the regular and special dividends in April and in here you can see the effects of unrealized gains or the effect on unrealized gains from the rise in interest rates in the quarter.

This effect has no economic and does not have any significant impact on our capital adequacy. One important topic of the Investors Day in June was an optimal capital structure. As we highlighted on Investors Day, we're aiming to reduce leverage by $4 billion by 2016. The first step has already been taken via tender offer, which resulted in the repurchase of more than $0.5 billion of senior debt in July.

I'll provide you with an update of the capital structure including their current net worth as of the end of June with the Q3 results. And we will continue to update you regularly in future as and when we provide capital, economic capital updates.

With that, back to Michel.

Michel M. Liès
Former Group Chief Executive Officer

Thank you, George. Let me summarize George's and my key points. All business units contributed to these quarters result, which has proven very robust in light of substantial large and smaller nat. cat and man-made losses and several other one-off effects, many of them negative.

The P&C businesses have continued to deliver profits in this environment and reinsurance has achieved a very successful July renewal at somewhat lower economic rates but with the portfolio mix that adjusted well to the market opportunities and proved the value of our client-centric business model.

Corporate Solutions keeps growing profitably and has paid a dividend to group far sooner than we had anticipated. Life & Health Re has absorbed several, mainly negative, one-off effects in this quarter but has remained on track regarding new business, where we've seen growth in health and the high growth markets.

Admin Re has delivered above expectation both in terms of earnings and gross cash generation and it has paid an attractive dividend. Also you can see from our investment results both for the group and the business unit that asset rebalancing is on track and producing the desired results, namely higher running yields and ROIs.

The implementation of our optimal capital structure which will be EPS and ROE accretive has also started and we will keep you posted on this. Finally, I would like to state again that we are positive regarding Swiss Re's renewal outlook into 2014.

We strongly believe that knowing our unique underwriting and capital strengths, we can continue to deliver very good results in all P&C businesses, also next year and the years thereafter. That includes doing this selectively in the high growth market.

You know I would, and I indeed will, talk about the financial targets, 2011 to 2015, to conclude this presentation. We are looking beyond this date in steering the group but delivering the targets is our top priority.

You know the targets are 5 years targets and not quarterly ones, but we like to keep track as to where we stand. I also want to point out that with this quarter, half of the journey towards 2015 is behind us.

With both ROE and EPS again being above the watermarks that we've set ourselves, I think it's fair to say that it was successful journey so far and that we are indeed well on track. I strongly believe that our targets help us focus on the things that matter most and that it's no coincidence that I could report to you both successful renewals and the group results that ensures we continue to stay on track towards delivering our ambitions.

You'll see an update on our economic net worth target with our Q3 results. With that, I would like to thank you for watching this video on Swiss Re second quarter 2013 results.

[Break]

Michel M. Liès
Former Group Chief Executive Officer

Good afternoon or good morning, everybody. And welcome indeed to our second quarter 2013 results conference call. I'm here with our Group Chief Financial Officer, George Quinn and Matthias Weber, our Group Chief Underwriting Officer. Before jumping into the Q&A, I will hand over to George for some opening remarks.

George Quinn
Group Chief Financial Officer

Thanks Michel. And let me add my welcome to all of you on the telephones. I will very briefly summarize the key points as we see them from today's results. All the business units have contributed to this quarter's results, which has proven very robust in the light of substantial large and smaller nat. cat and man-made losses and several other one-off effects, many of which are actually negative.

The P&C businesses continued to deliver profits in this environment and reinsurance has achieved a very successful July renewal. Life & Health reinsurance has absorbed several mainly negative one-off effects in the quarter but has remained on track regarding new business but we're seeing growth in health and in the high growth markets.

Admin Re has delivered above expectations both in terms of earnings and gross cash generation and has paid an attractive dividend. Also you can see from our investment results, both for the group and the business units, that the asset rebalancing is on track and producing the desired results namely higher running yields and return on investment.

Finally, we are positive regarding Swiss Re's renewals outlook into 2014. We strongly believe that knowing our unique underwriting and capital strengths that we can continue to deliver very good results in our P&C businesses, also next year and the years thereafter.

With that, I'll hand over to Eric who will host the Q&A session. Eric.

Eric Schuh
Former Head of Investor Relations
Thank you very much, Michel and George. So operator, we'd like to turn to the Q&A and in the usual way, could people restrict themselves to 2 questions each and ask follow-up questions in a new cycle. Could you please also indicate whether your question is directed to Michel, George or Matt. So operator, could we please take the first question.

Question and Answer

Operator

The first question comes from Jason Kalamboussis from Societe Generale.

Jason Kalamboussis
Societe Generale Cross Asset Research

I just had 2 questions. The first one is, the remittance from CorSo was surprising in the way that we knew that you had excess capital in it. But we thought it was going -- I thought that it was going to stay there for bolt-on acquisitions. So is it something that we should read as you deciding that there are no immediate opportunities? So you had that upstreaming of around $500 million but that of course you know that you don't have immediate opportunities in the next 1 year to 18 months. You do have certainly as much that is left within it and that it can come back when you need it. So it was the first question.

And the second one is around your attritional ratio. It looks quite high and I was trying to understand. Of course, it could have been a difficult quarter, but there is also a lot of volatility when we look at all the quarters since 2011. I think the last time we saw something as high as that was fourth quarter of 2011. How should we look at your attrition ratio because in other reinsurers you see it just going -- reflecting a lot more of the impact of the pricing, as opposed to have big swings? And especially going to the second half, how should we look at that? Thank you very much.

George Quinn
Group Chief Financial Officer

So I'll start with the CorSo question, Jason. So the reason for the dividend paid in the second quarter wasn't an absence of opportunity. The plan remains the plan for CorSo. I think you've seen that make a good progress through, not only the second quarter, but the first half of this year when they have -- I'm sure they will have opportunities for inorganic growth over the course of the next 1 year or 2 years. But that's really about the fact that they had generated more capital, both than we expected and then they need to accommodate their growth plan. So this is true excess that's come back to the group. The second question, so your question was about attrition, is that right?

Jason Kalamboussis
Societe Generale Cross Asset Research

Attritional ratio. So if I exclude from the combined ratio, expense ratio, look at your claims ratio, take out nat. cats and take our reserves releases, so looking at the claims loss ratio exclude -- on an accident year excluding nat. cats, it does look that it is -- there is a bit of -- a lot of volatility and also it's on the higher end. Now, of course, you have the smaller claims that can impact it. But normally you should have the benefit of pricing -- or better pricing that you had last year that we should be still be finding in the second quarter or how should we look at it?

George Quinn
Group Chief Financial Officer

So Matt's volunteered to answer that.

Matthias Weber
Former Group Chief Underwriting Officer

Okay. Hi Jason. Thank you. This Matt Weber speaking. If you take out nat. cat, we still have volatility left in the loss ratio coming from man-made losses. And the volatility on the man-made side is actually driven by the property line of business and also by specialty lines. We are in a position and we do write risks that have a size of $100 million or bigger, we can do that. And we take the majority of these risks net on our balance sheet and if you now think if we have one loss on $100 million risk, a total loss, that accounts already to approximately 3% combined ratio points on a quarterly basis. And in the specific case of the

Q2, if you look on page 29, there, we list basically 2 losses we incurred, 2 large losses we incurred on the man-made side. One is Rio Tinto loss in Utah and the other 1, the West Fertilizer company loss which is a fertilizer plant in Texas which exploded. And these 2 losses together already accounted to more than $100 million. So we said it already last quarter then we have to explain why our actual loss ratio was lower than expected that it’s due to the volatility on the man-made side and now it’s the other way around. Due to the same volatility, we have a little bit higher losses. But we checked nothing unusual, it’s within normal amount of volatility and we are absolutely not worried about this.

Operator

The next question comes from Vinit Malhotra from Goldman Sachs.

Vinit Malhotra
Goldman Sachs Group Inc., Research Division

So I'll keep to 2 questions for now. Just staying back on the Slide 29, for Matt, the nat. cat hedging effect from retro-cessions or loss warranties or cat bonds of minus $0.3 billion was a much bigger number last year of around $0.8 billion. And given the whole environment of favorable ILS market, I was wondering what could be causing this transfer of risk to be reduced from Swiss Re out to the market or to other providers? So that's the first question. The second question is just on the CorSo. I just want to clarify, I think heard Michel say that the pricing trends in CorSo were stable or flat versus what we are generally seeing is that in commercial insurance market pricing is up. So I just want to clarify whether I heard that correct or not. Thank you.

Matthias Weber
Former Group Chief Underwriting Officer

Okay. So the answer to your first question is last year, we did have Berkshire Hathaway quota share in place which already provided a hedge of 20% of all the business, all the nat. cat exposed to business we wrote. And this year, this Berkshire Hathaway quota share is no longer in place. We still do have some run-off benefit from this quota share but compared to the hedging provided by the quota share last year, this run-off benefit is comparably small. Related to your second question, on the CorSo side, our CEO’s remark was an average of our observation on the global basis where we can say right levels have stayed flat. And important market is the United States and in the United States, price levels have increased over the last several quarters and the strength is still ongoing in the specific case of the U.S.. It’s especially strong for casualty business.

Operator

The next question comes from Tom Dorner from Citigroup.

Thomas Dorner
Citigroup Inc, Research Division

Two questions, please. The first is a general one on your outlook for P&C renewals going into 2014.
I mean, like your peers, you sound relatively optimistic. I just wondered is that driven mainly by the advantage that you get form your scale and being able to do private transactions or do you feel that the -- there is a sort of floor on the impact of alternative capital going into next year in terms of the pricing? And then the second question is on the reserve strengthening that you saw in Australia and indeed, many of your peers have seen to some extent. Can you just give a sense is that sort of a worst-case scenario? Could that get worse, do you think? How comfortable are you with that number? Thanks.

George Quinn
Group Chief Financial Officer

Matt, shall I do the first one?

Matthias Weber
Former Group Chief Underwriting Officer

Okay. With respect to the outlook we are indeed positive and you perfectly well summarized some of the main reasons already why we are positive and scale private transactions, tailored deals where were tailored solutions, where we do have a competitive advantage. I believe you have also driven a good track record that we are able and good at selecting risks and managing the cycle and we will of course continue to do that. Second observation, indeed if we look at the price level changes that are happening in the capital markets from the influx of additional capital that has happened over the course of the next -- of the last 6 to 8 months. We have indeed observed a stabilization at price levels in the capital market right now are stable. They are not decreasing. And that is the current situation. Maybe one thing which you did not mention but which I would like to add is the following. Relative price changes is one thing to look at the but the other thing is also where is the average price quality of our book of business. And there I'm very pleased to say that the average price quality of the business we have on our balance sheet and our book is clearly above our technical requirement, our hurdle rate and that is maybe an additional reason why we continue to be very positive about the P&C outlook. George?

George Quinn
Group Chief Financial Officer

Thanks, Matt. So Tom, on the second one on the Australian DI issue, I cannot promise its worst case. We've -- I guess, probably to explain how we discovered the issue in the first place. So this relates to a number of schemes that we are involved within Australia that have recently come out for renewal and as part of the renewal process, the clients have provided significant data. And in fact, in some cases the first data that we received and this revealed the problem. So we've had this for about 4 weeks. We tried to be prudent in arriving at estimates that we've put and on top for reserve strengthening on the DI business in Australia. I mean, at this stage, we don't believe that anything material that we'll have to add. I mean, I don't see it as worse case.

Operator

The next question comes from William Hawkins from KBW.

William Hawkins
Keefe, Bruyette, & Woods, Inc., Research Division

First of all, George, the outlook that you gave for the YRT portfolio, you reassured us that you are still looking at $500 million for next year. But you have also just told us that the actual versus expected in the second quarter seems to have spiked an awful lot more than you originally anticipated. And that's led to your more negative guidance for the experience for this year. To the extent that actual has been significantly higher than expected in a very short period of time, can you just comment on how you can be so comfortable that $500 million is still the right figure for next year or whenever? And then secondly, with regards to the reserve development, I know that can be volatile and there's a lot of moving parts, but it's the first time we've seen a relatively low single-digit figure for quite some time. And I'd like to know if you can give us a bit more color on what's going on there. Is it that the actual versus estimated in the casualty book that you've referred to frequently has come down and, if so, why? Are you seeing more claims inflation or something or is that in that particular area the experience is the same but there's maybe an offsetting negative elsewhere? So just a little bit of color on that dip in what is obviously still healthy, positive development. Thank you.

George Quinn
Group Chief Financial Officer

So in the first one, I mean what we've seen in the quarter, I mean a large chunk of the, I guess, the excess claims that we've seen in the YRT book are related to high-value face amounts. So we can isolate, for example, claims above $5 million. And we have significantly more than, for example, Q2 than we saw in Q1. Now Q1 it was someone else's, we recaptured it. If you look at the 6 months, it does look like volatility. Therefore the conclusion we reached for the time being is there is no reason to change our longer-term view of how this book performs. And I guess, we're cautious given the history of this book but again when we saw better experience in Q1, when we had a gross and we seeded it, but the experience was worse in Q2. It's one quarter but we'll watch it carefully. I mean, we have no reason to believe that the figure that we gave at Investor Day, would now be insufficient. On the reserve developments, I think the history can be volatile. I think it was a year ago Q1 2012, we actually had negative development on the reserves; I think a bit more than $100 million. I think, if you look at this quarter, I mean with all the normal caveats so, what I don't want to do is to be giving the impression we now count on reserve development for future earnings. Our normal comments would apply; but just to drill into what happening this quarter. I mean there are probably 2 or 3 discrete items that’s worth highlight. So I mean, Costa Concordia, you've seen already. So that’s a $64 million increase because of the market loss estimate increase. And on top of that, we have adjusted our view of workers comps reserves which is something that those of you that have followed us for long enough will be familiar with. We’ve added gross of about $160 million to workers' comp, as we changed the methodology this quarter.

I don't expect to change the methodology next quarter, but workers' comp has a history of providing us with negative surprises. I mean, those are the 2 bigger items. So just over $60 million on Costa Concordia negative and $150 million negative on workers' comp. If you are prepared to isolate those 2, everything else looks then pretty much in line with what we’ve seen before.

William Hawkins
Keefe, Bruyette, & Woods, Inc., Research Division

And the workers' comp years of origin, George, is that still the really old legacy stuff, or is that more recent stuff?

George Quinn
Group Chief Financial Officer

No. I mean, if you look at our history, I mean, up to 2001 we recently launched a book of worker’s comp. We acquired GE, GIS is worker’s comp book in 2006 with that deal and is typically both of those books and if I -- the acquired piece has been more problematic than our own.

Operator

The next question comes from Thomas Seidl from Sanford Bernstein.

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

Two questions, please, 1 on cycle management. It appears to me that you seem even to accelerate growth now at the July 1 renewal even though rates are weakening. I hear, of course, Matt saying that in relative terms price is still above target. But is it the right moment to grow? And are you applying those weaker run rates than the others in the market that allows you to gain market share, in particular on the nat. cat side, where you almost held the expected volume? And the second question is on Life Reinsurance, where you showed us a higher running yield, 3.5% versus 3.2% last year. When I look at the asset mix of this business, of course, it's slightly higher risk, as you anticipated. But nothing is really striking where I would see how you could achieve this higher running yield. Can you provide me more color how you achieved this quite constituted result?

George Quinn
Group Chief Financial Officer

I’ll take that the first one and Matt can complement. I think when we speak about decreasing price and gross we should has Matt said, the few minutes ago also take into account what is the level we are starting from and that’s reason why you have seen combination of growth with some decrease making some case sense. And definitely from an absolute standpoint, if you grow 12% and you have a decrease of 5% from a level, which is definitively, quite above our benchmark, we do see an absolute contribution to the result of the company and that’s reason why we definitively do not see any kind of contradiction in these behavior.

Matthias Weber
Former Group Chief Underwriting Officer

I think, that was nicely said. You asked me to complement. So I'm doing this. In addition to that I might add, right, our goal is to maximize economic profits and shareholder value in a sustainable way in the long term and in this specific case given that the price levels are still clearly above our hurdle rate which are derived from the 11% ROE target.

It absolutely did make sense for us to take advantage of our global reach and our global distribution network which we have and write additional business, even if these additional business incurred. A little bit of rate changes relative to long year ago. Of course always on the condition that the price levels are still about our hurdle rate which I can certain to you that this was the case.

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

And this includes -- sorry, this includes U.S. nat. cat?

Michel M. Liès
Former Group Chief Executive Officer

This includes U.S. nat cat, yes.

George Quinn
Group Chief Financial Officer

So Thomas, I'll touch on the Life and Health Re topic, the announcement that remitted at Investors Day is really it is the continuation showing this started earlier, I think we indicated already with the full-year results that we were shifting asset allocations across the group, again primarily focused on Life and Health Re. Remember, there's been a reasonably sizable shift towards credit. That the announcement on the Investor's Day simply added to that. I mean, we've moved to I think in the course of about first 6 months of the year something like $5 billion from cash which yields not very much at all and government bonds, which doesn't yield much more, towards credit was about another $5 billion in total to go. And so you'll see further improvements through the remainder of year.

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

Okay. But it's mainly a reinvest and not that you achieved the higher running yield?

George Quinn
Group Chief Financial Officer

I think if we look at the prior quarters, typically we're reinvesting at lower yields, typically because of the mix, because of the, I guess, I will call acceleration of the effort to rebalance the portfolio, I mean, we've seen the first quarter in sometime where we actually have invested a higher rates than the rates –than the assets we sold. We have about 20 bps differential on the running yields and it's half due to reinvestment rate and half of it is simply the revaluation of the assets. So the former is, I guess, the value driver.

Operator

The next question comes from Kamran Hossain from RBC Capital Markets.

Kamran Hossain
RBC Capital Markets, LLC, Research Division

I've got 2 questions. First one, on the dividends back to Group from Corporate Solutions and Admin Re, just on these. Do you think you are in a better capital position now than you'd assumed at the Investor Day? Were these dividends back to Group already planned? So that's question one. Secondly, I guess it's just coming back to pricing and price adequacy. Very helpfully explained that you plan to shift into casualty over the remainder of the year. Could you just talk about the relative price adequacy of the casualty business that you are picking up versus the cat business that all the headlines have suggested is coming down? Thanks.

George Quinn
Group Chief Financial Officer

So, on the first one on the dividends, both of these dividends we received this part of the normal year end process. So we maybe reach conclusions, once we statuary financial statement have been finalized. I mean, in the case of Admin Re, it was always planned. It would be a dividend given the gross cash generation targets that they have. We ended up with a higher dividend capacity probably because of the asset rebalancing. So that's change the valuation interest rate in the U.K. so we get benefit from that. On the CorSo side, I mean, it was referred to earlier, I mean, we had capitalize the business to commodity all the growth that we had planned, But, again, probably away the similar to P&C reversing the business generate more capital than we had anticipated. Again we took that dividends about the event process so by the Investor Day, we actually received both of the cash payment. So I knew of both of those when we had the Investor Day.

Kamran Hossain
RBC Capital Markets, LLC, Research Division

Okay. So, just to summarize, I guess slightly higher expectation at Admin Re but CorSo completely expected?

George Quinn
Group Chief Financial Officer

Correct. CorSo, I think, is a positive surprise.

George Quinn
Group Chief Financial Officer

Matt.

Matthias Weber
Former Group Chief Underwriting Officer

Okay. So on the relativity between casualty, price quality and nat. cat related price quality, of course, it depends on the market and the price qualities are different in different markets. In the U.S. market which on the global basis accounts to 70% and with respect to primary that we have seen increases in rate level, there I would say on the economic basis taking into account and discounting and the investment returns or that are possible taking into account the fact that interest rates are still very low. I think there is more to go, more that needs to happen on the Casualty side before we can really open our champagnes and fill the glasses and start drinking. We are clearly not yet there. I think we are seeing encouraging first steps and we believe in momentum in the market what has started is likely to continue for awhile but we are not yet where we believe the market should be.

Kamran Hossain
RBC Capital Markets, LLC, Research Division

So U.S. Cat business is probably still better across the U.S. Casualty?

Matthias Weber
Former Group Chief Underwriting Officer

I would not heavily disagree with the statement.

Operator

The next question comes from Michael Huttner from JPMorgan.

Michael Igor Huttner
JP Morgan Chase & Co, Research Division

And on the dividend, so you've received from subsidiaries $1.9 billion in Q1 and about $800 million and a bit in Q2, so $2.7 billion. Is this money which had effectively already been used to pay the 2012 dividend or is this money which is ready to pay available should you choose to, of course, to pay the 2013 dividend? That would be my first question.

And then going back to, I think, Jason's question on the attrition, you actually give a figure of, I think, 97.9 in P&C Re, adjusting for expected nat. cat and prior year development. The previous quarter the figure was 86.8, so that's an 11 point different, quarter before that 81.9, before 92, before 95, before 92? Now, I know there's, what is in Q2 which we are not aware of, I know you mentioned the large claims, but only 3 points, they are not 10 points. I'm missing something and I'm wondering what it is or what it isn't, maybe you can help me out on that?

George Quinn
Group Chief Financial Officer

So on the first question first Michael, just to direct your attention to Slide 11, if you have it near you in the Investor pack, you'll see a column that's highlight is Group items, within that we have common shareholder equity and essentially the assets of that business are made up of 2 reasonably launch blocks, one is a block of private equity assets that we dividend at the reinsurance company in the early part of this year, it's about $1.5 billion and the remainder is typically, not exclusively, but almost all generally highly liquid forms of investments.

I mean, that's a capital part that the Group continues to use and the way, I think, is in the best interest of its investors. So clearly this is where we would pay the future dividend from and if we had opportunities to invest that and try to raise the return then potentially we'll also use that same capital base for that.

Michael Igor Huttner
JP Morgan Chase & Co, Research Division

Okay. And you would sell the private equity stuff or you could potentially, or should I exclude that?

George Quinn
Group Chief Financial Officer

I think, I mean, you can always do a secondary sale of private equity. I mean in my experience the prices offered in the secondary market are typically eye-watering and it's best not to.

Michael Igor Huttner
JP Morgan Chase & Co, Research Division

Not to -- okay. So just a difference. Okay.

Matthias Weber
Former Group Chief Underwriting Officer

I assume that the 7.1% which you mentioned, if I heard you correctly so that refers to the expected nat. cat loss ratio in the quarter. And with respect to nat. cat, especially related to flood and wind and hurricane, there is a relatively strongly expressed seasonality. Typically of the total pool of expected nat. cat losses we incur by writing the book which we currently have. Our expectation based on our models is that 20% of this is earned during the first quarter, 15% of it is earned during the second quarter, 40% is earned during the third quarter, this is driven by the hurricane activity on the northern hemisphere, which concentrates in the third quarter and the remaining 25% belongs to Q4. And this is the reason why if you just look at the ratio between expected nat. cat loss and net earned premium that there is a relatively large variation from quarter-to-quarter.

Michel M. Liès
Former Group Chief Executive Officer

Maybe I just add one thing to Matt's comment. As we were preparing the quarter with the business units, we saw in particular in reinsurance a fairly large number of, I call them large claims that didn't meet our large threshold. So I mean we had a large discussion whether we would change the definition or present some additional views on the claims expenses; we've chosen to follow we've ordinarily done. What we are saying is, a fairly lengthy list of smaller rate in both nat. cat and man-made fall beneath the threshold that typically puts on that slide in the appendix.

Michael Igor Huttner
JP Morgan Chase & Co, Research Division

In terms of the, I know, I missed little bit, is this something you would normally expect to see in an economic recovery? So, factories are doing nothing, start the machines, suddenly find and repaired them, they can keep breaking and I put that in insurance claim, is it -- is that what you'd normally expect at the start of an economic recovery?

Matthias Weber
Former Group Chief Underwriting Officer

Personally, it's, let me say, I -- we know there is correlations between the economy and the loss activity and typically what you described, I would expect to see these interface where the economy is really booming and this is not yet the case in many of the mature markets. So the loss activity we have seen on the man-made side, I really would attribute this to just normal volatility, which we have in our book and what happens the nat. cat side has anyway little or nothing to do with how the economy is doing. Now there is a correlation, for instance on the property side, when the economy picks up, business interruption losses tend to be bigger because loss of income is covered and when the economy is hot, loss of income is bigger, so there is absolutely a correlation there. But I believe you're not yet at the face in the economic cycle where we can basically plan the economy for these additional losses.

Operator

The next question comes from the Andrew Ritchie from Autonomous.

Andrew James Ritchie
Autonomous Research LLP

Two areas, I think for George and Matt. Also the first 1 is certainly for George and Matt. Looking at Slide 30 again on your P&L probable maximum loss scenarios, I appreciate the ending of the quota share, I mean, they are gone up albeit, I thought the plan was to buy more hedging to limit the increase of that and if I look at particularly North Atlantic hurricane? Is that where you want to end up or is there a plan to purchase more hedging for that, maybe just to clarify that? And in relation to that, does it matter -- did you ever look whether that number is relative to your GAAP equity, because it looks very high versus history or is it purely versus economic and SST capital and therefore, even the last SST indication took account of these levels of P&L? And the second question, Admin Re, thanks for providing the split between U.K. and other. Could you give us any flavor of an update on the excess capital at Admin Re and where it would be U.K. versus other? Thank you.

George Quinn
Group Chief Financial Officer

So, Matt's going to deal with number one, I will deal #2.

Matthias Weber
Former Group Chief Underwriting Officer

Okay. Related to your questions on hedging, if it's okay with you I would like to spend just 1 minute to just repeat how we determined the amount of hedging. We have temporary evolution, of course, of capital of U.S. GAAP capital, of economic net worth, also S&P capital. And we look at this on periodic basis and depending how big these capital figures are, we adjust our net risk appetite for nat. cat and other lines upwards or downward. So related to your first question we absolutely look at all these capital amounts. However, the most important for us to answer the question, how much risk are we willing to take on our balance sheet is the economic net worth because it's really an economic capital that is available. We are absolutely within our net risk appetite for all periods including tropical cyclones in the Atlantic and the question whether or not we will increase our hedging or decrease it in the future will depend on the price level on the incoming sites or basically on the business we write, it will depend on the price level on the hedging site. And if one is higher than the other, we might even write more and hedge more or write less and reduce our hedging depending on the sign of the difference and of course, in addition to that we will also continue to look how our economic net worth and other capital measures, evolve over time. So, right now we are good and we are updating our views on a frequent and periodic basis.

Andrew James Ritchie
Autonomous Research LLP

And just to confirm, I guess, this is for George, the last thing is SST number because it's based on projection effectively allowed for these levels of P&L, is that correct interpretation?

George Quinn
Group Chief Financial Officer

Correct.

George Quinn
Group Chief Financial Officer

So, Andrew, on the second question on Admin Re, and so, I mean, if you cast the main back to the investor presentation that we did last year, we gave some disclosure of the end distribution of S&P capital across the business units. And given the way that the capital requirements within the business units to determine which is typically statutory capital requirements and I couldn't give you a firm number but the majority of the excess capital in Admin Re would then have been in the U.K. business and is still likely to be that way today. I think the one thing to be cautious of is that, I mean, obviously, from an SST or economic perspective things look a bit different. The actual capital requirements are attracted by the peak risks and mortality and asset risks are the peak risks for the Group so Admin Re, sorry…

Andrew James Ritchie
Autonomous Research LLP

Because that's when Admin Re is within your capital system.

George Quinn
Group Chief Financial Officer

Correct.

Andrew James Ritchie
Autonomous Research LLP

Okay. But you're saying on local statutory basis most of your excess would be in the U.K.?

George Quinn
Group Chief Financial Officer

From an S&P perspective, I tried to translate the actual physical capital held in comparison to the S&P excess that you saw before.

Operator

The next question comes from Andy Broadfield from Barclays.

Andrew Broadfield
Barclays Bank PLC, Research Division

Two questions, please. One, just on the July renewals, just to understand a little bit better the nature of the growth and you've talked a little bit about private or privately placed contracts. I was wondering out of the 12% growth you report on premium level and whether you can give us a flavor for the -- is this a large number of contracts or is this a few number of very large contracts? My sense is that you've potentially placed quite a few large and a number of large contracts rather than just lots and lots of smaller ones. And, if so, if they're new privately placed contracts, what were those contracts for, is it higher session rates, is it just taking it out of the broker market into a yield, or where has that come from? That's the first question. And the second question relates to the capital surplus in the business and refers a little bit back to the Investor Day. I think out of that Investor Day certainly I came away with the view that you've got really a very large level of surplus capital. And -- but your ability to distribute it is going to be, if that was what you chose to do would be, you couldn't distribute that full theoretical surplus? Therefore, I guess the question is do you feel compelled to take the re-risking on the investment side and to write lots of business, because otherwise, the alternative is really to be forced to hold surplus capital earning nothing which you can't distribute either?

Michel M. Liès
Former Group Chief Executive Officer

Okay. So Matt will take the first one.

Matthias Weber
Former Group Chief Underwriting Officer

Okay. And you are right with your expectation and this tailored transactions and tailored deals typically we are talking of relatively small list of larger deals and this is also true if you look at Q2. It has to be this way because typically these deals are quite work intensive because we tailor them and once they fall below certain size, it’s just not worth pursuing them. So it’s very typical that we are just talking of a relatively small number of deals that’s also the reason why this business typically is a little bit lumpy sometimes. We are lucky and write a little bit more than what we expect and sometimes a little bit less and in the second quarter we have been a little bit on the successful side as well. George?

George Quinn
Group Chief Financial Officer

On the capital surplus point, Andy, I mean, so you’re right, I mean, just to restate the numbers so that people remember from the Investor Day, we estimated a 245% SST, our target is 185% SST and that would imply a very substantial surplus. But just to connect it back to the answer that I gave Michael earlier on the Q&A. In the group item figure is a good sense of the real immediate flexibility the firm has. And so as I pointed out there, we have about bit more than $5 billion in the Group as of the end of Q2 with $1.5 billion of that in the form of private equity which of course is not liquid and that’s before the dividends that we anticipate for the full year that we’ll receive in the early part of next year.

So I mean I still expect the group to have significant flexibility. I think we’re in a relatively luxurious position. But it's clear that even if today the group determined that it wanted to pay out all the excess it would not be feasible and in fact one of the ambitions and aims has to be to get the structure of the group right so that we can achieve those target levels and that’s both for the group and for the business units.

On the asset risk, so did we feel compelled to do this because of some aspects of the capital structure. I mean, yes, that’s absolutely no, I mean, we do look at the smart ways to utilize pockets of capital that’s difficult to get, I mean any company would, but that didn’t play a role and the re-risking discussion. I mean we said mid-term asset allocation back again in April of 2012 and really what you’re seeing was announced back in June is the further steps to get it there, but it wasn't related to a particular fundability issue. I mean I think compared to most we’re actually in a very liquid position.

Andrew Broadfield
Barclays Bank PLC, Research Division

Perhaps just to ask, maybe turn the question round a little bit? If you weren't -- if you can't find a way to utilize that capital, which and through growth or whatever other alternative method, what do you do with it? Do you just have to sit and swallow it and accept that you're going to have diluted returns? Is there anything else that you believe you can do to try and utilize or free up that locked-in capital that's undistributable?

George Quinn
Group Chief Financial Officer

Well, I think for reasons, obvious, and I'm never going to sit here and except that something we locked-in that we can't do something worse and therefore we should accept any kind of return on the money. I mean you have to make the machine work harder. I mean, we've got lot of smart people here and represented with relatively complex problems, they can find solutions to it. So I mean the answer is we set targets for returns that require capital and that's the returns that are required. If your capital is trapped, you better un-trap it.

Andrew Broadfield
Barclays Bank PLC, Research Division

Okay. And just back to you Matt as well, the other part was these policies you've won, these big contracts, what whether your [indiscernible] doing before that, were they just with the border market or were they just new business to the market in general?

Matthias Weber
Former Group Chief Underwriting Officer

It's a combination of various situations, right? In some cases we are able to take existing tailored deals and increase them that does happens sometimes it is an additional opportunity which just didn't exist before if a client has a new need that ideally can be addressed by a tailored solution and sometimes it's also a conscious decision of a client to transform a piece of business from the open market into something that are more structured and is more tailored, so all of the above can happen.

Andrew Broadfield
Barclays Bank PLC, Research Division

Okay. But no clear trend in this business?

Matthias Weber
Former Group Chief Underwriting Officer

Yes.

Operator

The next question comes from Thomas Fossard from HSBC.

Thomas Fossard
HSBC, Research Division

Two question on my side, one for George, one for Matt. The first question for George will be on the, again, on the Corporation Solution dividend. I fully understand all the reasons behind this dividend probably ahead of what you would have expected initially. Should we now plan such a dividend payment every years even which remain unchanged, that would be the first question. Second question for, Matt, would be could you remind us how we should relate the risk-adjusted return indication you are providing for your reinsurance business? For example minus 1% year-to-date with the guidance of combined ratio for the Reinsurance division i.e. for example, if you on the full-year basis or if next year you risk adjusted your return were to be down 2 or 3 points, or 2%, 3%, would that be 2 or 3 percentage points higher combined ratio we should expect? Thank you.

George Quinn
Group Chief Financial Officer

So on the first one Thomas that's great question. The short answer is no. I mean I think in the near-term I don't expect the CorSo to pay more dividends when they're back to the normal expectation where they'll use their capital base in terms of their growth and so for the time being, this is the CorSo dividend. Matt?

Matthias Weber
Former Group Chief Underwriting Officer

Okay. With respect to the minus 1%, I would like actually to answer the question which you didn’t ask but it’s nevertheless in my opinion important. And this is, sometimes people compare different reported rate change figure from different sources with each other and my comment there is just, there are different definitions of risk and therefore also different definitions of risk adjusted. In our case we don’t take into account loss trends, exposure trends, rate level changes, but we also do take into account changes in the interest rate environment, so it’s really on an economic basis. And I’m not always sure whether this is always the case. How exactly rate changes translates into combined ratio, that depends on a number of factors and so the future combined ratio guidance will depend on a number of factors. Rate level changes are one factor but they are not the only factor that do matter, for instance the total amount of equity that is available is another important factor. How much business will be write, et cetera, et cetera. So at this point it’s too early to in my opinion start thinking about how this could potentially translate into future combined ratio guidance or at least I would not be in a position to do that.

Operator

The next question comes from Stefan Schürmann from Vontobel.

Stefan Schürmann
Bank Vontobel AG, Research Division

And just a question on the assets rebalancing, you said that basically $5 billion was invested into credit and another $5 billion might go and mostly in Life and Health. When I look at your asset mix, you still have quite a big chunk into short-term and cash will be nearly 24% even slightly up from last quarter and a lot of that's sitting in P&C and CorSo. So when should we expect you to put some of that short-term cash into maybe these 2 units at maybe higher rate, can you elaborate on that a bit?

George Quinn
Group Chief Financial Officer

Yes. Thanks, Stefan. I mean you’ve got 2 conflicting things going on here, so you’ve seen us take some of the cash and also take some of the proceeds from the sales of government bonds and reinvest that in credit and equity in the quarter. I mean to a certain extent, that will continue in the third quarter. You’ll see us use some of the cash again as we continue the asset rebalancing. The second thing is going on, which is going in the opposite direction is the creation of the short duration possession, so we’re actually selling, I mean something with duration on the government bond side typically and we’re sitting with cash. So you’re got to see us run with a reasonably high cash levels while we maintain the short duration possession. I mean, it’s relatively difficult to provide timeline to that, I mean we have internal targets which if you ask me, I’m not going to give you that would be the trigger for us to change our stance. I mean that’s what’s driving the cash balance and I think you can probably expect to see us maintain a significant cash and short-term position because of that short duration asset probably.

Stefan Schürmann
Bank Vontobel AG, Research Division

So basically, means that you rebalancing Life and Health, and mostly here, we will have the third pickup of maybe the recurring yield if that continuous?

George Quinn
Group Chief Financial Officer

Absolutely, so I mean one of the challenges, I mean, from a group perspective it’s easy. We just say we do this to the overall group asset allocation, but then when we translated for the business units, they have to find the most capital efficient way to take the risk. And typically just because of the nature of the actuarial systems, it makes sense to hold modest demands of risky assets of Life and Health, and if we can reduce local statutory requirements and improve fundability, and short duration very difficult to hold on a Life company. I mean, it’s penal as far as the capital requirements concerned, whereas on a Life -- on a P&C company, again, depends on jurisdiction. It can make more sense and that’s why you’re seeing, one concentrated on Life and Health, and the other is bigger to P&C businesses.

Operator

The next question comes from Frank Kopfinger from Commerzbank (sic) [CA Cheuvreux].

Frank Kopfinger
CA Cheuvreux, Research Division

I have got 2 questions on the duration and your DV01 position. So currently, it's -- DV01 is at minus 4.4 and can you give us an indication where are you on your way there and what is the end target there of your duration set up? And, correlated to this is my question, which role do derivatives play when shortening your duration, are you fully making this by increasing your cash position and if you do, do derivatives, whether we should expect to have P&L impacts there going forward?

George Quinn
Group Chief Financial Officer

Yes. So, on the DV01 the target is to have a $7 million short DV01 position. While I wouldn't stake my life, I would expect that I'll be in a position by the end of Q3. And on the form with which we do this, I mean it's far simpler to simply sell the asset and hold the cash, but I mean we haven't put any restrictions on the asset managers as to the most efficient or effective way for them to do this. But I said that I don't expect P&L volatility caused significant derivative overlays in relation to the duration possession. We'll get P&L volatility potentially from gains as we sell assets to establish the position. But I don't expect derivative volatility from this particular strategy, not significant derivative volatility anyway.

Operator

The next question comes from Maciej Wasilewicz from Morgan Stanley.

Maciej Wasilewicz
Morgan Stanley, Research Division

It's Maciej from Morgan Stanley. I have 2 questions on the economic capital basically. The first one is a comment that you made, George, on the video was that rising yields only have a very mild positive effect on your economic capital position. I'm wondering, because my understanding is that even before the recent deliberate shortening of the duration, you did actually have at least a small duration gap. On top of that, I thought that SST at least looks at forward earnings for capital available as well. I would have thought that for a number of reasons, rising yields would actually be a benefit to economic capital. So I'm wondering if you can flush that out and also whether or not that sensitivity to economic capital is increasing because of the deliberate short? And the second question that related to that is looking at the other side of the equation on the primary P&C market, a few years ago I remember the message out of Swiss Re was that rising yields could be very helpful in reducing the fake capital that exists under, I guess, accounting capital and that could lead to people who currently don't buy -- enough reinsurance, buying more reinsurance to protect themselves from a shorter capital base. I'm wondering do you, are you seeing any of that, do you stand by that as a potential helpful factor for the industry or is that or similar to you, it doesn't really matter?

George Quinn
Group Chief Financial Officer

So, I'll start with number one and may say something on number 2, and the, Matt, can certainly add much more insight. On the economic capital side, I think, my comments are really restricted to the duration play. The model overall is relatively complex but, I mean, for something that's in balance, I would not expect interest rate movements in other direction to have significant impacts. So it's really the increase in duration gap I was referring to in the video. I mean that's been in place at least partly since the beginning of June. It would be a small benefit from it. So that was really what that comment was focused on. Just briefly, I mean, Matt can give you give you more on the -- also the rising yields, you have seen the impact it has on other equity in the quarter. You know that we are not alone in this fact. I mean, I think for the larger clients, they all have economic models which would have similar features to the ones which I just described in answer to the first part of your question. And so, I'd be surprised if many, if any of them were relying on interest rate created GAAP capital. It's not inconceivable that smaller or mid-sized players are potentially more reliant or potentially more exposed to significant value falls and the impact that can have on confidence. So, I think it could be marginally helpful, but I don't think it would be a massive driver. Maybe Matt, you have got a better insight.

Matthias Weber
Former Group Chief Underwriting Officer

I would like to second what George just said. And I think right now the effect we have seen related to U.S. GAAP capital disruption as a result of increasing interest rate is still not large enough to drive to a measurable increase in demand for capacity. So the answer is so far we haven't been able to see this.

Maciej Wasilewicz
Morgan Stanley, Research Division

I guess, just as a slight follow-up on that, I mean the feedback I'm getting from some of the U.S.-based analysts is that the RBC capital ratios for most companies seem to be extremely high, so you'd need -- actually, is unrealized gains even inclusive in RBC? Actually, that's a good question but the point that they're making is that ratios seem extremely high in the primary industry, so you're not really likely to see any benefit even if yields rise quite dramatically. I mean would you -- do you think there would be a benefit if yields rose dramatically, I guess, is another way of asking that?

George Quinn
Group Chief Financial Officer

I mean, in most of the unrealized gains in the RBC in the U.S., I mean, the problem you face there is that you need a very long duration P&C business which has a massive impact. So you need a pure casualty writer or something similar I mean for a P&C -- traditional P&C company you are on a relatively short duration and for the impact of rising yields or falling yields, it should be relatively modest. And I agree, I mean -- if we look at clients from a U.S. statutory perspective in the U.S. and the vast majority are very well capitalized.

Operator

Your next question comes from Fabrizio Croce from Kepler Cheuvreux.

Fabrizio Croce
Kepler Capital Markets, Research Division

I have actually 2 questions, one on the risk transfer and the second on sustainability. So I start with the risk transfer one. I mean if I look to page 30 -- sorry for coming back on this one. It's about the peak exposure, I mean I noticed they go up actually more than 20%, so it's not only Berkshire. You potentially took over some more risk in the renewal. And so my question is, we have now this entire money flowing in from the hedge funds to the pension fund into the ELS market, making actually that activity to deploy business there to transfer risks to the capital market actually very big. So is there an option? Will you accelerate, actually, the risk transfer via these instruments by putting more ELS out, given that you have this risk? Would this be a solution for risk peak? And the second one is about sustainability. I mean even the supporter with a 100% combined ratio looks a little bit shaky. I mean with 86% combined ratio you are still one of the best large reinsurance group. And so the question here is about sustainability into 2013 of this very good combined ratio. If you could give there some sense where we are heading end of the year, and on top, also in terms of growth. I mean you have this 34% emerging market growth, 51% Africa, and Asia and China 25%, so everything looks really great, but is this growth actually as well sustainable, or will we see here some backdrop? If you could give some flavor, some sense also about China, which actually is no longer mentioned as being a growth region?

George Quinn
Group Chief Financial Officer

Why don't we do the following. So Matt, do you mind handling the risk question, I will deal with the combined ratio topic and maybe Michel you can comment on growth? Matt, you want to start?

Matthias Weber
Former Group Chief Underwriting Officer

Okay. So risk transfer, over the course of the last several years we have been able to increase our economic capital in the mid-term average, and with this increase in economic capital increased also our risk appetite. And that's also the reason why you see an increase in our net retained exposure figures related to peak periods compared to last year and the year before. And the reason is very simple, right. And with respect to Hurricane U.S., right now we write more than -- so our gross writings are in fact bigger than our net risk appetite is which means we do buy hedging and we will continue to do it and while its correct the prices for hedging have come down and in some cases have become attractive for us to be used, hedging still means we cede economic profit to somebody else and we cede margin to somebody else. And that's the reason why we do not just increase our hedges if we don't have to based on the comparison of our exposures relative to our capital possession and relative to our net risk appetite because we will like to keep as much of the business as we can based on the balance sheet.

George Quinn
Group Chief Financial Officer

So, Fabrizio, on the second part of your question, sustainability we see -- you are absolutely right, the combined ratio in the first 6 months has been very strong. I mean - even allowing for the volatility that we saw in the second quarter the year-to-date combined ratio is better than we had anticipated. I mean, we expected 92 for the reinsurance of P&C Reinsurance business, all things being equal. So I mean going into next year, that will be the starting point. And as Matt highlighted, the number of things that overlay. So there would be the very experience so far this year the way in which that then translates into GAAP earnings, the impact of the January renewal in 2013, the impact of interest rates because of course the combined rate is non-economic. Now, I think it is clear that -- if we had some relatively moderate pressure year-to-date I mean 1% rate move, I mean that would translate into a relatively modest impact on the combined ratio, but the January 1, renewal next year will have a big impact too. Michel, do you want to comment on growth?

Michel M. Liès
Former Group Chief Executive Officer

Yes. It would probably, Fabrizio, a little bit (inaudible) and answer, but definitely I just want to reiterate that top-line growth is not an obsession here. But when we speak about growth in emerging market is definitely a long-term trend that we are convinced that it is there to stay. There will be a rebalancing of economic power on this planet but I think we showed also in this quarter precisely the ability that we have even in a country like China to sometimes be more selective. I'm just moving some of the capacity that was in the case of casualty from China to the U.S. So, it's a combination of long term conviction with definitively, the deep cycle management philosophy that the business units you are covering. I do believe that because of the growth of this high gross market there is sustainability, but definitely it would not be linear in any piece of the globe. And we will have probably a situation in which we will have to believe it more moderate growths in the high growth market and come back to some other markets. But I do believe that the long term trend is absolutely clear to everybody.

Matthias Weber
Former Group Chief Underwriting Officer

Maybe, Fabrizio, if I could ask -- if I could add to your second question related to the combined ratio. I think in addition to all the reasons which George and earlier I stated that portfolio composition is a very important one right. And nat. cap in order to be economically profitable require so much lower combined ratio than a long tail business. And our portfolio has been changing over time and will continue to change over time also in reaction to what's happening in the market and what the client needs are. And therefore -- and we will take that into account after the January 1 renewal when we determined the combined ratio guidance and speculating right now is really way too early because we just don't know how our portfolio is going to look like next year.

Eric Schuh

Former Head of Investor Relations

We have 3 more questions in the queue. We will take those. Next question, please.

Operator

The next question is a follow-up question from Andrew Ritchie from Autonomous.

Andrew James Ritchie
Autonomous Research LLP

It's just a detailed question, I think, for Matt. When I look at your triangles that you published for 2012, it stands out that motor classes have seen a deterioration, I think for the last 5 accident years. I appreciate I think that might just be an impact from U.K. PPOs. But maybe just give us a sense as to the outlook for reserve development in that line would be helpful. And second question, sorry -- you might have said this on the video, George, but I just want to clarify, as far as the running yield's concerned the basic guidance is that we should -- is it effectively has bottomed now, because, as far as you're concerned, with the new asset mix being deployed the reinvestment rate is higher than the running yield. Is that what you're trying to say? Thanks.

George Quinn
Group Chief Financial Officer

Yes to #2, and on #1 on the triangles. I mean, it's mainly PPO motor so the periodic payment orders in the U.K.. I mean the, if we conduct a review of PPO motor, like we do for most of the classes, through the course of the year, we'll look at again in the second half. I mean there is no indication today that there was any need for any change there, but it is a volatile class of business and again this is a bit like worker's comp. This is one, because we have a completely nominal basis of reserving, I mean you can see a large shifts and that certainly distorts the triangles given the duration of the business. But it is mainly the U.K. experience that is driving what you are seeing on the triangles.

Andrew James Ritchie
Autonomous Research LLP

So is that a one-off then that you put through last year that you did for …

George Quinn
Group Chief Financial Officer

I think -- from May I think we put 2, at least 2 adjustments really, I mean 1 very large 1 at the very beginning and then 1 subsequent 1, I think maybe 1 or 2 quarters after that. So the -- I mean the -- we look at the stuff we reviewed mortality, morbidity, I mean this stuff looks far more like Life & Health than Motor business when you get into the detail. And we review the experience and the assumptions that we have arrived at once a year. We do that in Q3 for Motor in U.K.

Operator

Your next question is a follow up question from Vinit Malhotra from Goldman Sachs.

Vinit Malhotra
Goldman Sachs Group Inc., Research Division

I actually had a follow up on lack of substitution of the books, it's been addressed. So I'll go to the next point. There have been so many occasions where -- in the last 3 years where there have been these large growth in the renewals side, multi-placed or tailored solutions. And I just wanted to cross check that the higher sort of attrition over the last -- we are recording in these losses in this quarter. Have you seen any link to some of those treaties, some of those more privately placed treaties which grew so rapidly? Have you seen any link? Maybe not, but just wanted to confirm that, please. Thanks.

Matthias Weber
Former Group Chief Underwriting Officer

The answer is no. We haven't seen and extraordinary link between these 2.

Operator

Your next question comes from Michael Huttner from JPMorgan.

Michael Igor Huttner
JP Morgan Chase & Co, Research Division

I have 2 1/2, if I may. The first one -- well, the half is, if I remember -- I kind of maybe that's what you were trying to explain and I kind of missed it. The dividend which you normally get from Reinsurance after the financial year, so current financial year, you get paid in the Q1 and you take that into account when you set your dividend paid out to shareholders? I just wondered if that's the case. In other words, the $3.6 billion isn't the answer for the whole of the year; there's still a bit of money to come, as it were. And the second, at the Investor Day you kind of -- I think Vinit had calculated that your solvency was -- after all these things was about 213% and you said it was a little big higher, so I thought maybe 214%. I didn't do the math myself. I just wondered if after the current renewals, have we shrunk a lot? Are we now down below 200% maybe or something? And the last one is at what level would you say pricing is now no longer meeting your hurdle rate? The impression I have is -- given the risk appetite and the growth and all these things, is that there's still quite a lot of margin before we get there. So it's not this minus 5% we saw at this renewals, but maybe another 5% on top for the whole year, so 1% year-to-date plus. We need 5 years of the same to get there. Is that a fair view? Thank you.

George Quinn
Group Chief Financial Officer

I will do the first 2 and Matt will do the half. On the dividend, Michael -- I mean you are right -- I mean the concept obviously is that we're paying, share was based on the performance of the prior year, and we take into account our expected dividend flows. And received or not yet received actually from the business units, the major subsidiaries. So our cash planning for dividend payments, next year, we take into account that we expect to receive -- I am sorry from reinsurance in the first quarter next year. On the Investor Day on the solvency point, I think the challenge I am trying to what -- I mean there is lots of challenges. It would be a long conversation if I start with the challenges and try to work out how you translate what's happened in the last couple of months into SSSD terms. I mean, I think Vinit's question on Investor Day was mainly arriving the asset allocation shift and the $3 billion figure that we had given. I think the reason I said higher is that, you can treat the $3 billion in 1 or 2 ways. You add straight to target capital or I think you get just about precisely 213% or 214% or you can treat it as an 185% of target capital in which case you get slightly higher SST. So my comment was really the latter, and it would be a bit more than 1 point, but it's a bit higher. And Matt, pricing?

Matthias Weber
Former Group Chief Underwriting Officer

So pricing -- I cannot really answer your question probably the way you expect it to be answered that, that threshold is 11% ROE and that is the same threshold for all markets and lines of business. However, currently the price quality and the price adequacy for the different segments is very different. We really need to differentiate between nat. cat property, man-made specialty, casualty and in addition to that, we would have to differentiate between different markets. And typically what happened, let's now assume prices decreased everywhere 5%. Then it's just a hypothetical scenario. That's not our prediction, I am just saying this in order to explain my point, what then would happen there are -- there in this hypothetical scenario, certain segments which would drop below our hurdle rate and we would stop writing those, which means the piece of business that remains in our book in this case would still be above the hurdle rate on average and we will then also with individual pieces. And therefore your question is a reasonable question on to the assumption that the portfolio stays stable over time and there is no portfolio steering and no risk selection happen, however the reality is that we will do exactly this. We have been doing it in the past. And we will continue to do it. And therefore answering your question would be completely misleading. If prices drop significantly, we will then end up with a smaller book, but the quality of the book would still be very, very good.

Operator

Ladies and gentlemen, there are no more questions at this time.

Eric Schuh
Former Head of Investor Relations

All right. Great. Thank you, Operator. We are -- we are 17 minutes past the hour. It is important to us to answer all the questions, so I hope you don't mind spending another 50 minutes with us. Just 2 points, 20 seconds for me. We will have another event where you can ask and answer more questions in Monte Carlo; September 9, 2 p.m. Zurich Time, will be the presentation, including Q&A. Main topic will of course be P&C Reinsurance there.

And then on the October 4, which is a Friday, this year we will have a joint event -- with together with ABB, Holcim, Nestle and Roche, 4 other leading Swiss companies and us which is going to be on the topic of socially responsible investments. So we will have a SRI conference which is hosted here in Zurich. You will get an invite for that and please also pass it on to the SRI experts in your house. It is open both for buy side and sell side participants. But the topic really is SRI, it's cross sector. Thank you very much for your attention and please give us a ring any time. Good-bye.