

VONTOBEL

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SAA – AFIR

**Investor expectations from
actuaries – a listed
insurance company's view**

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Performance creates trust

Content

Sell-side analyst – what is this?

Insurance company valuation insight

Investor expectations

The stockbroker image...



"We're expecting stocks to rally, but we don't know which ones and when."














...what we really do - Vontobel Brokerage

Integriertes Geschäftsmodell



Life Sciences	<ul style="list-style-type: none"> ▪ Grosse Pharmaunternehmen ▪ Biotechnologie ▪ Medtech und Dienstleistungen ▪ Spezialitäten-Chemie
Finanzdienstleistung	<ul style="list-style-type: none"> ▪ Banken ▪ Versicherungen
Konsum	<ul style="list-style-type: none"> ▪ Nahrungsmittel & Getränke ▪ Luxusgüter ▪ Detailhandel ▪ Medien
Industrie	<ul style="list-style-type: none"> ▪ Maschinenbau ▪ Technologie ▪ Bauzulieferer ▪ Energie ▪ Immobilien
Bonität	<ul style="list-style-type: none"> ▪ Unternehmensbonität ▪ Wandelanleihen ▪ Cross-Asset

Vontobel Research Products

	Products	Time and effort	
Daily	<ul style="list-style-type: none"> ▪ Morning Focus 		
Periodic	<ul style="list-style-type: none"> ▪ The Week Ahead 		
	<ul style="list-style-type: none"> ▪ Buyback Monitor 		
	<ul style="list-style-type: none"> ▪ Swiss Stock Guide 		
	<ul style="list-style-type: none"> ▪ Value Investments 		
	<ul style="list-style-type: none"> ▪ Emission's report 		
Ad hoc	<ul style="list-style-type: none"> ▪ Alpha List 		
	<ul style="list-style-type: none"> ▪ Company Review Report 		
	<ul style="list-style-type: none"> ▪ Company Fundamental Report 		
	<ul style="list-style-type: none"> ▪ Sector Report 		
	<ul style="list-style-type: none"> ▪ Flash Notes 		
	<ul style="list-style-type: none"> ▪ Individual request 		

Content

Sell-side analyst – what is this?

Insurance company valuation insight

Investor's expectations

Information sources for valuation analysis

Base/Tool

- Annual reports (IFRS, US GAAP, Swiss GAP)
- Embedded value reporting
- Regulatory statutory filings (often at a time lag)
- Management meetings/discussions
- Industry reports/consultants/media, etc.

Usefulness

main source

supplementary

“back-testing”

important

market research

Valuation matrix – some key ratios

VALUATION MATRIX INSURANCE COMPANIES		Reporting base	
Key Ratio	Basis/details	IFRS/ US, local GAAP	Embedded value
Price/earnings	Reported earnings per share	X	
	Normalised or adjusted earnings	X, adj	
	Operating profits	X	
Price/book value	Reported book value	X	
	Normalised or adjusted book value	X	
	Tangible/net asset value	X	
Price/embedded value	Reported embedded value		X
	Adjusted embedded value		X
	New business multiple (life)		X
SOTP	Sum-of-the-parts valuation, ROE based	X	
	Sum-of-the-parts valuation, NAV & inforce based		

Separate issue in valuation process : solvency assessment (Solvency I transparent, SST not really)

P/E: some accounting issues to consider

Issue

- Asset classification
- Real estate treatment
- Asset impairment
- Write-up assets
- FX movements
- Goodwill

Comment

P&L impact from trading book

Fair value through P&L

Different strategies (20%,50% - 6m or 12m)

Fixed income in P&L after recovery,
equities only on disposal

Mostly reflected in P&L (impact of hedging)

No annual/linear goodwill write-down
(earnings more volatile and overstated?)

Peer group valuation: P/E and P/B multiples

Swiss peer group valuation															
Company	Curr.	Rat.	Price as of 3-09-14	Perf. YTD	ROE		EPS			P/E		Price/ NAV 2014E	Div. yield 2014E	P/B 2014E	Market cap. in CHF mns
					2013	2014E	2013	2014E	2015E	2014E	2015E				
Vontobel Universe Switzerland															
- weighted average				10.9	11.9	13.9				10.3	9.7	1.2	5.3	1.12	
- average				12.7	11.0	11.7				10.8	10.4	1.2	4.1	1.11	
Bâloise	CHF	o	122.0	7.4	9.9	10.3	9.6	13.6	11.2	8.9	10.9	1.10	4.5	1.02	6,100
Nationale Suisse	CHF	o	82.5	28.4	11.4	11.3	4.7	4.7	5.3	17.6	15.5	1.84	3.0	1.84	1,819
Helvetia	CHF	n.r.	461.3	3.1	9.6	9.7	42.0	42.9	43.6	10.8	10.6	1.09	4.0	1.01	3,991
Swiss Life	CHF	+	231.8	25.2	8.1	9.0	24.6	24.7	26.3	9.4	8.8	0.88	2.6	0.77	7,436
Swiss Re	CHF	+	75.7	2.9	13.7	14.9	11.9	7.9	8.9	9.6	8.6	1.06	5.6	0.94	25,750
Vaudoise	CHF	+	412.0	7.9	12.2	11.7	42.1	46.8	48.2	8.8	8.5	0.91	2.9	0.91	1,236
Zurich Ins. Group	CHF	o	279.0	14.2	12.0	15.3	24.9	26.0	27.7	10.7	10.1	1.38	6.1	1.31	38,258

Zurich peers Europe															
Company	Curr.	Rat.	Price as of 3-09-14	Perf. YTD	ROE		EPS			P/E		Price/ NAV 2014E	Div. yield 2014E	P/B 2014E	Market cap. in CHF mns
					2013	2014E	2013	2014E	2015E	2014E	2015E				
- average				1.9						10.3	9.6	n.a.	3.9	1.21	
Allianz	EUR	0	131.9	1.2	11.7	11.6	13.2	13.9	14.1	9.5	9.4	NA	4.5	1.10	72,664
AXA	EUR	0	19.2	-5.2	9.4	9.8	2.1	2.1	2.2	9.2	8.7	NA	4.6	0.88	56,014
Generali (Group)	EUR	0	16.1	-6.0	11.4	10.4	1.4	1.4	1.6	11.5	10.1	NA	3.5	1.14	30,193
Aviva	GBP	0	529.0	17.6	14.1	14.2	0.4	0.5	0.5	11.1	10.2	NA	3.1	1.72	23,554
Zurich Ins. Group	CHF	o	279.0	14.2	12.0	15.3	24.9	26.0	27.7	10.7	10.1	1.4	6.1	1.31	38,258

For insurance company valuation, price to book value makes more sense than price to earnings

ROE target overview of Swiss insurers

Financial targets	Mid/Long-Term Guidance	Comment
BALOISE mid term targets	8-12% ROE ; combined ratio target 93-96%; grow in key target market segments	15% ROE was cut back to 8-12% (wide range due to volatile "E")
HELVETIA 2015+	Financial objective 2013: organic growth > market; 94-96% combined ratio; 1.2%-1.5% life NB margin; 10-12% ROE ; 30-50% payout ratio; "A"-Rating	Currently guiding towards the lower end of the 10-12% ROE target (low interest rate environment)
NATIONALE SUISSE 2015	Top line growth >4%; Specialty lines growth >10% p.a. to ~40% of top line; Net combined ratio >95%; Net profit CHF >110mn by 2016;	No ROE target
SWISS LIFE : Mid-term Guidance	8-10% ROE 2015, Div payout 20-40%, CHF350-400mn cost cutting	8-10% ROE on equity ex-revaluation gains on bonds
SWISS RE : mid/long-term guidance 2011-15	ROE 700bp > US 5-year risk free bond yield; 10% EPS growth over 5-years, 10% economic net worth & dividend growth over next 5 years	Segment ROEs (Non-life Re and CoSo 10-15%; L&H Re 10-12%; Admin Re new business 11%)
ZURN mid/long-term guidance - across-the-cycle	12-14% BOP after tax ROE on equity ex-revaluations	New targets announced in 2014 (old was 16% over-the-cycle BOP ROE)
VAUDOISE Mid-term	10-12% ROE target	Achieved more than 12% in most of last few years

ROE target a challenge: volatility of return and equity

“Soft” factors in company assessment

Issue

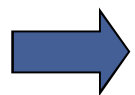
- **Management meetings/road shows**
- **“Networking”** (insurance industry/consultants...)
- **Investor discussions/market sentiment**

Impact

“gut feeling”

“bottom-up mirror”

“trend mapping”,
“liquidity flows”



The challenge is to include „soft“ findings into the valuation model and earnings forecasts (we usually have a 12-months view)

Qualitative company assessment: adjusting cost-of-capital

illustrative

Qualitative Assessment (1 strong to 5 weak)	Strategy	Management	Diversification	Market position	Capital Strength	Risk Management (ALM)	"Marketability"	Speculative Attraction	Note for relative risk	Adjusted Cost of Capital %
Weighting	2	3	2	2	2	2	2	2	2.82	
Aegon			2	2	4	3	4	3	3.00	12.5%
Allianz			2	1	3	2	2	5	2.53	10.8%
AXA			2	3	4	2	1	5	2.59	11.2%
Baloise			3	3	3	3	2	4	3.18	11.5%
Generali			2	2	3	4	2	4	2.76	11.6%
Hannover Re			2	3	4	3	3	5	2.94	11.4%
Helvetia			3	3	2	3	3	4	2.88	11.7%
ING			2	3	4	4	2	4	3.00	11.4%
Munich Re			2	1	2	2	3	5	2.35	10.5%
Nationale Su			3	5	3	3	4	3	3.06	11.6%
SCOR			3	3	3	2	3	2	2.59	10.4%
Swiss Life			4	3	4	3	2	4	3.24	11.8%
Swiss Re			2	1	3	2	3	5	2.76	10.8%
ZFS			2	2	3	2	2	5	2.65	11.1%
AVERAGE	2.36	2.71	2.43	2.50	3.21	2.71	2.57	4.14		11.31%

➔ Strategy, management, market position, etc.. We include this in our cost-of-capital assumption as a "soft factor adjustment".

Sum-of-the-parts valuation as base for our price target

Zurich SOTP	Comment	FY13-15E RoC	Cost of capital	P/B multiple	Valuation	Value ps
Non-life insurance	17,000	15.3%	10.5%	1.5	24,810	167
Life insurance	8,800	13.9%	10.5%	1.3	11,621	78
Farmers	3,000	35.6%	10.5%	3.4	10,169	68
Non-core businesses	1,600	0.0%	12.0%	0.0	0	0
	30,399			1.5	46,601	313
Corporate cost/HQ					-5,161	-35
Excess capital above "AA"	4,849				4,849	33
Total group USD	35,249				46,289	311
Total group CHF	31,724					280

➔ Example based on return on estimated allocated capital, adjusted by assumed cost of capital

A word of caution - not a fundamentally driven market!



2009 – 2013:

- Swiss Life
- Adecco

Bloomberg 18.03.14	Adecco	Swiss Life
Market cap CHF mn	14'062	7'086
P/E ratio	19.7	9.0
Price to book ratio	3.6	0.78
Dividend yield		
ROE	15.4	8.1
Applied Beta (2y)	1.257	1.196
Correlation	0.882	

- Example of Swiss Life and Adecco – a stunning share price correlation!
- Makes no fundamental sense: different product, different markets

Content

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8/2014 investor survey – use of ratios and information

Survey summary

Questionnaire	Sent to 30 investors - 11 answers
Geographic reach	CH (5), US (2), UK (2) Europe ex-UK (2)
AM company profile	Big global bank/AM (7), private bank AM arm (2), HF (2)
Investor's profile	Insurance/Financials specialist (8), general PM (3)

What is your level of actuarial know-how?

	Answers	%	Comment
Very good	0	0%	
Good	2	18%	Trained as actuary, but not up to date to today's new developments
Could be better	9	82%	

- Survey not statistically relevant, just providing some insight on investor thinking

8/2014 survey – use of claims triangles in non-life

Claims triangles - do you use claims triangles for your investment decisions?

	Answers	%	Comment
Yes	10	91%	
No	1	9%	Use sell-side for this

Why do you use triangles?


	Answers	%	Single statements/comment
To assess potential future reserve releases	3	27%	Also ask management if reserving at best estimate or above
Used as a criteria of risk selection	1	9%	
Looking for consistency from accident year to accident year	1	9%	
Important for the relative level of reserves assessment/prudency in reserving	2	18%	US yellow books very helpful as standardised
Helpful accident year view to judge on underlying loss trends	1	9%	

Claims triangles - what can be improved?


	Answers	%	Single statements/comment
Split IBNR's/case reserves would be helpful	7	64%	IBNR split is paramount to understand inherent level of risk// More information always appreciated
Geographical/regional breakdown would help	3	27%	It would be helpful to get loss triangles with paid, case and IBNR info split by main lines of business/geographies
(Sub-)segment insight would be appreciated	6	55%	Europe is rather useless, as aggregated and with disturbing FX impact - in the US we appreciate sub-segment and IBNR insight - UK is quite
Net of reinsurance disclosure is a must	1	9%	
Information quite adequate with our needs	2	18%	

8/2014 survey – is embedded value useful to you?

Is Market Consistent Embedded Value useful to you?

	Answers	%	Comment
Yes	4	36%	Yes, complementary to IFRS reporting// MCEV is the only rational long-term metric to assess and calibrate the real level of economic capital // If a company does not provide MCEV we get cautious
 Yes, but	5	45%	Yes, however not as a valuation metric//Useful for sensitivities in times of market stress // Yes but not a priority - MCEV appears somewhat impaired as a valuation tool.
No	2	18%	No, not really: MCEV is useful of what value is likely to be achieved with old EEV numbers giving a view of what value can realistically be achieved// I would prefer to see a maturity profile of the in-force value using realistic assumptions which give a better picture of cash flow emergence together with sensitivities (investment/spread, lapse, biometric assumptions)

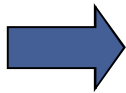
MCEV - what could be improved?

	Answers	%	Single statements/comment
 No clear standard allowing to compare one company to the other - need consistent assumptions	6	55%	More consistency between companies would be very useful// Lack of comparability and standardisation//It would be nice to have a level playing field of definitions//There should be the same assumption for a local market, e.g. Allianz, Axa and Zurich using same assumptions for Switzerland
More insight into segments would help	1		
The delta in reserves of local GAAP to MCEV	1	9%	
Less is better than more	1	9%	

8/2014 survey – is profit by source a key focus?

Is profit by source a key focus?

	Answers	%	Comment
Yes	11	100%	Fee, spread and risk margin disclosure brings a better understanding of what drives profit// It is important for our valuation matrix//Useful to judge for direction of profit growth in life insurance//A key focus as we have a strong preference for insurers making money with technical rather than investment margin// Important to assess quality of earnings - market gives higher multiple to higher earnings quality// I like to understand how the insurer makes money - I like the Australian disclosure of sources of margin// We recently declined to invest in IPO which did not provide profit by source insight!
No	0	0%	

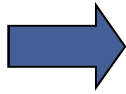


Profit by source is a key focus for investors when looking at a life insurance company!

8/2014 survey – IFRS phase II?

Will IFRS Phase II help the insurance sector understanding?


	Answers	%	Comment
Yes	1	9%	Yes, but these more sophisticated metrics do not lead to straightforward interpretations
Do not (want to) answer the question	6	55%	Not informed enough on current developments//Not aware of details but waht we understand, this might be too far away from cash and real earnings//
No	4	36%	Not sure, if it is very volatile, then it will not have much usefulness//Non-life is fairly well understood today, not sure if new IFRS view will help understanding of industry - see no need to change NL side//Reporting is potentially getting more complicated and more



The industry does not seem to care about IFRS really, at this stage. This might be because of 10 year on-going IASB discussions on this future new insurance accounting standard.


8/2014 survey – information on cash?

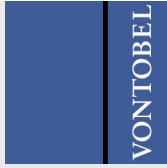
How important is information on cash for your investment decision?

	Answers	%	Comment
 Very important	8	73%	Helpful for appreciation of dividend paying capacity//What is cash - is it the change in surplus capital or is it the cash to the Holding Co?//Very important - it is an audit number, not an actuarial number, actuaries will not like it...//
Rather important	2	18%	
Not important	1	9%	

The future of information on cash/capital?

	Answers	%	Single statements/comment
Will be more important	5	45%	Will be more important, certainly in the UK - however, we need a comparable definition/standard of what "cash" is//Will be important, also in regard to IFRS Phase II//Yes, e.g. Allianz recent disclosure/effort on this issue was very much welcome//There is increasing momentum here and it will become standard for the industry!
Equally important	2	18%	It is the only way to get a generalist comfortable having exposure to the insurance sector - pressure on the industry comes from the UK//
Not important	1	9%	
No answer	3	27%	
A state-of-the-art example for cash reporting?			No great example, maybe L&G talking their share price up or Aviva bringing their share price down// No good example, maybe Zurich//A state-of-the-art insurance company is an oxymoron...

 **Key survey findings:** MCEV still in use but needs fixing, claims triangles are important but even more so profit by source on the life insurance side. IFRS Phase II appears still far away... and information on cash (dividend...) is very important for investment decisions into the insurance sector!



Thank you!

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