Speech on the 2016 Half-Year Financial Results

Ladies and gentlemen, I'm delighted to present to you the highlights of the first half of 2016.

Slide 5: Highlights

We are very satisfied with our operating performance during the first six months of this year. Our underlying profit rose significantly, the combined ratio was below the target range of 93–96 per cent and equity is higher than it was a year ago. This financial stability means that we can actively manage our business. We are equipping Baloise for future challenges by strengthening reserves in the German non-life business and adding a substantial amount of over CHF 250 million to technical reserves in the life business.

Overall, the Baloise Group generated a profit for shareholders of CHF 223.6 million for the first half of this year, which constituted a year-on-year reduction of 10.1 per cent. This drop was due to the addition of CHF 54.8 million to reserves in the German non-life business. If it had not strengthened its reserves, Baloise would have generated an operating profit of CHF 261.5 million, which would have equated to an increase of 4.8 per cent. However, by taking this one-off action we are putting the German business on a sound footing.

In addition to this measure, the business mix in Germany is undergoing a significant shift away from industry and towards SME and retail business. Finally, new approaches to promoting sales are helping to boost growth in profitable target segments. We expect these to stabilise the financial performance of our German business. German Egloff will go into more detail on the strengthening of reserves.

Baloise's net combined ratio was a healthy 92.5 per cent and only just above the prior-year level. If reserves had not been strengthened in Germany, the ratio would have been 88.7 per cent. EBIT in non-life business went down, but would have been up by 0.5 per cent year on year if the effect of the steps taken in Germany and the ongoing portfolio optimisation are excluded. Overall, the volume of non-life business expanded by 3.1 per cent.

In our life business, we were able to continue with the planned switch to capital-efficient risk and unit-linked products. As a result, our investment-type premiums increased by 18.5 per cent, whereas traditional business declined.

Turning to our investments, we can see that Asset Management has been very successful in adapting to the environment of low interest rates and the uncertainties surrounding currencies. The net return of 1.8 per cent was 0.2 percentage points higher than in the prior-year period. We also used the prevailing conditions to end the share buy-back programme earlier than planned.

I'll now hand over to our CFO, German Egloff, who will talk about the individual operating segments in more detail.

Slide 7: Non-life Earnings

Many thanks, Gert.
I'd now like to review our operating performance in the first half of 2016 with you.
I'll start with slide 7 and our non-life business.

Later on, I'll go into more detail about the strengthening of reserves in Germany that Gert mentioned just now. What I'm about to say ignores this effect for now.
Overall, the results for the non-life segment were very encouraging.
The volume of business grew to over CHF 2.1 billion in the first six months, which was a rise of 3.1 per cent. In Switzerland, there was a slight slowdown in growth due to ongoing review and restructuring work and to a selective underwriting policy in accident insurance and daily sickness allowance business. All other national subsidiaries

generated a positive level of growth. The business mix also improved because growth was particularly strong in our highly lucrative target segments.
The investment income was up by 13.6 per cent year on year. This is proof positive of how well we have responded to the difficult investing environment by reallocating investments.
Both claims and costs were slightly higher than in the first half of last year, which I will now explain on slide 8.

Slide 8: Non-life Net Combined Ratio

At 92.5 per cent, the net combined ratio was just about on a par with the excellent ratio reported for the first half of 2015. If reserves had not been strengthened in Germany, the ratio would have been an outstanding 88.7 per cent. Whichever way you look at it, we were below our target range of 93–96 per cent for the first six months.
There was a small increase in the expense ratio, which amounted to 31.9 per cent in the half-year period. This can mainly be attributed to DAC write-downs in Belgium and to project costs in Switzerland – in other words, not due to structural reasons.
Continuing the trend seen in recent years, the prior-year claims development was positive, reducing the claims ratio by 2.6 percentage points. The adverse impact of large claims increased slightly compared with the first six months of last year, amounting to 3.6 percentage points in the reporting period. This was the result of natural disasters and individual large claims. Adjusted for large claims incurred and profit on claims reserves, the underlying claims ratio was a very good 59.6 per cent. This figure underlines the high quality of our non-life portfolio.

Slide 9: Non-life Net Combined Ratio by Country

On slide 9, we can see the changes in the combined ratios of the individual countries. The combined ratios for Switzerland and Luxembourg were excellent, with both countries improving on what had already been outstanding ratios in the prior-year period.
Switzerland reported a ratio of 78.4 per cent, which constitutes a reduction of 6.5 percentage points. The reason for this is the relatively favourable claims environment in

all sectors and the improved business mix. What's more, the profit on claims reserves benefited the claims ratio.

Our international markets of Belgium and Luxembourg also exhibited a very high level of operational profitability. As in Switzerland, we have a strong market position in these countries. In Belgium, the combined ratio was a very good 94.1 per cent, even though the claims ratio was adversely affected by two major events.

Slide 10: Reserve Strengthening in Germany

By contrast, there is potential for improving the technical profitability of the German non-life business. I'd like to look at this briefly on slide 10.

In Germany, we have repeatedly been confronted with losses on claims reserves over the past few years. Furthermore, the low interest rates mean that it will become necessary to strengthen reserves for annuities in the liability insurance business. That is why – and because we want our resources in Germany to be focused on the future – we strengthened reserves in the German non-life business by around CHF 55 million. Specifically, we have lowered the discount rate for annuity reserves by 0.75 per cent. In addition, the claims reserves were strengthened by an amount that means that future profits in Germany will no longer be impaired by legacy issues.

This had an adverse impact on the combined ratio in Germany of around 15 percentage points, taking it to 116.3 per cent. Without this one-off negative effect, the ratio would have improved year on year.

On a positive note, the expense ratio in Germany went down. The initiatives to reduce headcount are proceeding to plan. We are confident that, by taking these steps, we have laid the foundations for holding the net combined ratio below the 100 per cent mark in the coming years.

Slide 11: Life Earnings

Let's now move on to slide 11 and the life business.

The slight contraction in the volume of business was a consequence of deliberately scaling back new business – particularly in traditional single-premium business – in view of the interest-rate situation.

As a result, the business mix shifted further towards innovative, capital-efficient insurance solutions. This is highlighted by the strong growth of more than 160 per cent by our semi-autonomous pension solution, Perspectiva, and by the marked rise of almost 20 per cent in investment-type premiums. Moreover, this very encouraging improvement in portfolio composition is reflected in the Group’s new business margin, which was actually slightly higher than in the first half of 2015 despite a further decline in interest rates.

At CHF 46 million, profits in our life business were lower than in the prior-year period. This is explained by the substantial addition of over CHF 250 million to strengthen technical reserves in view of the interest rate situation. By the reserve strengthening we make the balance sheet more robust and further reduce the average return required to meet guarantee obligations. Overall, earnings in our life business have thus proven pleasingly resilient despite significant headwinds from the level of interest rates, which have fallen sharply again in both Switzerland and the EU following the Brexit vote.

Slide 12: Change in Equity

I’d like to finish on slide 12 by taking a look at equity.

With equity of CHF 5.4 billion and a carrying amount per share of CHF 116.5, Baloise remains strongly capitalised. This can also be seen from the confirmation from Standard & Poor’s of our credit rating of ‘A with a stable outlook’. The rating agency thereby acknowledged Baloise’s very healthy ‘AAA’-level capitalisation, high operational profitability and robust competitive position in its profitable core markets. Standard & Poor’s also rated our risk management as strong.

The share buy-back programme that we had started in 2015 with the aim of acquiring 2 per cent of the registered share capital was ended earlier than planned on 29 July 2016. As a result of this programme, more than CHF 100 million was returned to shareholders in total.

Having given you a summary of our excellent set of key figures for the first half of this year, I would now like to hand you over to Martin Wenk, who will talk in more detail about the good gains that we made on our investments.

Slide 14: Asset Allocation: Insurance

Thank you, German. It is my pleasure to present the investment result.
Our asset allocation stayed largely the same. The minimal changes are the result of changing market values. Higher bond prices increased this position and decreased most of the others, for example the equity position by 0.2 percentage points. Nevertheless it is difficult to maintain the exposure in certain asset classes, namely real estate and mortgages. We therefore hired some more professionals for our real estate department, while for mortgages our tried-and-tested collaboration with Baloise Bank SoBa is protecting our excellent position in this market.

Slide 15: Details Investment Result Life

Let's have a look at the investment result. My comments pertain to both the life and non-life slides.
The markets started 2016 turbulently and ended the half year in the same way due to the unexpected result of the Brexit referendum. This led to even lower interest rates in developed markets. Despite that effect we were able to maintain our current income at the levels of the prior-year period. We achieved that by switching bonds in all bond portfolios and carefully expanding our US dollar segment, which generates higher yields – even when fully hedged – than the Swiss franc and euro segments. We always decide on the basis of risk-capital-adjusted returns and maintain our high quality standards. However, we worry about the ever diminishing liquidity of the interest rate markets – both the underlying bond market and the derivative market. Banks losing their trading appetite and central banks monopolising certain bond markets make it difficult to invest. 80 per cent of bonds issued in Swiss francs are trading at negative yields! It is a real challenge to find the golden opportunity in the remaining 20 per cent! So it is even more important that rental income and mortgage payments provide a stable base for current returns.
The bond switches mentioned before generated gains on fixed-income investments, and our long-standing portfolio of swaptions returned additional revaluation gains that can be used to strengthen our technical reserves and will lower the necessary yield for future reinvestments.

Some small impairments were necessary on equities but were offset by gains realised on our hedging programme. We carefully revaluated our real estate portfolio and adjusted only modestly.

The equally erratic currency markets left no trace on our income statement. This was due to the absence of any position in pound sterling and our extensive hedging programme. The effects you see in the tables are purely hedging costs.

All in all the investment result in the life segment reached CHF 779 million, an increase of 9.4 per cent compared to last year's result for the first six months and a net return of 1.7 per cent, up from 1.5 per cent.

The corresponding figures for non-life were CHF 150 million – an increase of 13.5 per cent – and a yield of 1.6 per cent, up from 1.4 per cent.

I'll now hand back to Gert De Winter.

Slide 18: Conclusion / Outlook

Many thanks, Martin.

Ladies and gentlemen, Baloise demonstrated its financial stability once again in the first six months of this year. It is therefore underpinned by very strong foundations and is fully prepared for the next strategic phase. For our customers, we plan to simplify our structures and be more than an insurance company, with our future focus on the ever-changing demands in the digital age. For our employees, we want to create an environment that encourages entrepreneurship while, for investors, our aim is to maintain a consistent, attractive dividend policy. Our current objectives therefore remain unchanged.

At the Strategy Day on 26 October 2016, we will present the core aspects of our long-term strategic direction.

Thank you for watching.