Fresh perspectives

The issues before us require fresh perspectives, open minds and courageous solutions.

"Our business has never been in a better position to deliver on the promise of supporting progress."

Dear shareholders,
Even before 2014 was over, it was clear that the year would be remembered as one of 'war, terror and epidemic.' Unfortunately there's some justification for that. Still, I wonder if this misses some of the bigger forces at work. Extremists and extreme cases are simply that — extreme. However, I've been with Swiss Re for 24 years and on its Board of Directors for the last 17. And looking at 2014 from that perspective, I can say that the overall outlook is mixed but not all bad. Indeed there are some tough problems to solve, but there are also many bright spots. The key in my view is to always stay focused and not lose sight of the overall picture. See the challenges as well as the opportunities — opportunities which Group CEO Michel Liès and the Executive Committee are in good position to seize.

The new normal is getting old
After the financial crisis, central banks did a commendable job of contributing to the stabilisation of financial markets and restoring confidence. Yet seven years later, the crisis response has almost become the norm. Interest rates remain at historically low levels, as does inflation. I am convinced that this still remains the single biggest threat to our industry.

Low interest rates are, however, not only an issue for the financial services industry. Low rates represent a de facto tax on all savers and result in low government funding costs which, coincidentally, make it easier to delay hard public policy decisions. Low interest rates also threaten to distort financial markets in important ways, such as by affecting the supply of capital for investments. Leaders in both the public and private sector need to address the problem underlying historically low interest rates, which is clearly low economic growth.

What is Swiss Re's ongoing strategic response?

The longer the low interest rate environment lasts, the more it erodes the running investment income from our very large asset base and depresses gross margins, in particular in the Life & Health Reinsurance segment, but also in Property & Casualty. Swiss Re's response has been to maintain historically high margins from underwriting also for 2014. This combined with exceptionally low losses from natural disasters has allowed Reinsurance CEO Christian Mumenthaler and his team at P&C Re to produce another outstanding year in 2014.

We all have read a lot about alternative capital forcing its way into reinsurance and trying to substitute for traditional reinsurance. I do not think that Swiss Re is particularly vulnerable to such market forces and that the market available to us remains as large as it ever was. It is our strategy to maintain a global footprint and to do business virtually in all countries open to us, to maintain long-standing relationships with our thousands of clients, to diversify the distribution channels and not be dependent on a small number of intermediaries. We want to differentiate our offering to clients by adding value through sharing expert knowledge and our high credit quality.

In addition, we also experience once again a time where large insurance companies retain larger shares of their business and reduce cessions to the reinsurance market. With our Business Unit Corporate Solutions we underwrite risks of large non-insurance corporates and their captive insurance companies directly. For our globally diversified book of large risks we need access to such risks on a continuous basis and cannot depend entirely on the short-term reinsurance programmes of a small number of global insurers. Agostino Galvagni, our CEO in Corporate Solutions, has achieved a lot with his team: he has grown the business significantly over the past few years, has maintained strong underwriting standards at the same time, and has expanded the Unit's global footprint, staff and business infrastructure. Corporate Solution's contribution is growing and gives us strategic flexibility.

But back to Life & Health Reinsurance

As mentioned, Life & Health Reinsurance is suffering most from the low interest environment: some of this pain is due to accounting effects as the ever-lower rates produce significant unrealised capital gains in the equity of the segment which in turn make it very difficult to achieve a high ROE.

In the case of Swiss Re we also had some homemade problems in our very large in-force life books from contracts going back 10 years or more. In 2013 we committed to our shareholders that we would fix the issues with these long-running contracts in cooperation with our clients. Together with her team, that is what Alison Martin, the Head of Business Management in this segment, has achieved. This largely explains the partial revaluation of contracts in our in-force life book that burdened the 2014 results, which in turn, however, eliminates a drag on our future results in the segment. We are optimistic about future returns in Life & Health.

Where is the growth?

Several years ago we pointed out to you that the company will experience a shift of business gravity towards emerging markets, in particular Asia. This process is well underway and those in charge of all segments are continuously refocusing their efforts. By the end of this year, we expect 25% of our premiums to be generated in High Growth Markets but only less than 20% of our present resources are deployed there. This will require ongoing attention by both Reinsurance and Corporate Solutions — less so for Admin Re® which is focused now on Europe — and will help to further diversify our sources of revenue. This is good for Swiss Re as we have built relationships in the new markets for many years.

Well diversified asset allocation

Guido Fürer, our Group Chief Investment Officer, is in charge of managing our portfolio investments along with his team. In addition, our Treasury Department manages our considerable cash position and the team under John Dacey, our Group Chief Strategy Officer and Chairman of Admin Re®, is managing our book of private equity and Principal Investments. I am very proud that the contribution to profits from our asset base remains significant despite the difficult investment environment. We are convinced that a well-diversified asset allocation is the safest way to achieve a good risk/return profile even in those circumstances.

We have been advocating one specific change that could mitigate some of the negative impacts while enhancing growth. Infrastructure investment should become a viable asset class for institutional investors like Swiss Re. This would give long-term investors some relief from the low yield environment and at the same time give a boost to the real economy.

Regardless of whether the goal with infrastructure investment can be achieved, ultra-low interest rates can't go on indefinitely. Sooner or later policymakers will have to let go of the support and address the hard business of structural reforms.

As I write this, we are just a few weeks past the Swiss National Bank's decision to end the Franc's minimum exchange rate against the euro. Shortly after that the ECB announced its own multi-billion euro agenda of quantitative easing. While these decisions have little impact on Swiss Re itself given our natural hedge of keeping premium and liabilities in the same currency, it is likely to have an impact on the overall Swiss economy. And the experienced volatility in the markets gives us a bit of a hint how disruptive a shift away from the ultra accommodative monetary policy might be if and when it comes.

Some words about capital, dividend and share buy-back
Our core business is to enable risk-taking. And economic growth depends on exactly that: on risk-taking. We provide confidence and counsel for economic activity to proceed despite uncertainties such as climate change, or new developments like the digital revolution. However, our business has never been in a better position to deliver on the promise of supporting economic progress — despite a softening market environment. Our solid 2014 results confirm just that.

Risk-taking, however, requires a solid base of risk capital exactly for the moment when you have to be able to fund and digest large losses and that moment will come, it always does and it is our business. Our target capital structure is designed to achieve exactly that.

However, over the past few years the frequency and severity of large losses was below expectation, which in turn led to higher profits. For the company it was and still is difficult to find attractive opportunities to reinvest all of this additionally available capital in new insurance risks at returns in excess of our hurdle rates. We extensively used the tool of extraordinary capital repayments, which are tax advantageous particularly for Swiss retail shareholders. And we propose to do this again this year. Then, unfortunately, these reserves are exhausted. As we of course hope that the benign loss trend will continue we propose to establish a share buy-back programme for the next twelve months which we will use to achieve a similar objective: to repatriate capital that we cannot reinvest in the business at our hurdle rates.

There is however another reason that speaks for buying our own shares. Whilst over the past few years the economic value (according to our Economic Value Management (EVM) framework which assesses assets and liabilities on a true economic basis) was close to the market value, we have now seen for some time a trend of economic value significantly exceeding the market value. It makes therefore a lot of sense for the company to invest in its own shares and benefit from the discount. I hope you will support these capital motions at the upcoming AGM.

The year ahead is bound to be at least equally challenging but Swiss Re is very well positioned. The Board of Directors and I would like to thank all our employees for making this possible and giving us the confidence to meet the numerous opportunities and challenges with optimism — as we are committed to continue delivering shareholder value to you.

Thank you for your trust, loyalty and continuous support.

Zurich, 19 February 2015

Walter B. Kielholz
Chairman of the Board of Directors

4.25
Proposed regular dividend in CHF for 2014*
(CHF 3.85 in 2013)

3.00
Proposed special dividend in CHF for 2014*
(CHF 4.15 in 2013)

* Swiss withholding tax exempt distribution out of legal reserves from capital contributions.

Achieving our strategic goals

Now in even stronger position to reach our 2011–2015 financial targets.

"In an increasingly global and interconnected environment, we are well positioned to capture opportunities the market offers."

Dear shareholders,
As we start into the last year of our five-year financial target period, we can look back at 2014 as a successful year. Even though we've had other strong earnings years over this period, 2014 stands out. Why? These results were generated in a much more challenging environment. We maintained our underwriting discipline and could — as shown — actively differentiate ourselves via our services and our knowledge. In addition, we decisively addressed problematic areas in our Life & Health business and took important steps to ensure our future success.

Strong P&C underwriting drives net income
Our Group's full-year net income was USD 3.5 billion. Property & Casualty Reinsurance remains our strongest earnings pillar. Our 2014 results in this segment were strong, with net income of USD 3.6 billion, or 10% above 2013. Successful underwriting, reserve releases and benign natural catastrophe levels drove this strong result.

If you follow the industry closely, you will know that capital in various forms in the reinsurance market is abundant these days. That fact underlines the significance of our strong 2014 performance and demonstrates that we go beyond providing pure capacity. Our success lies in putting Swiss Re's expertise and capital strength to work in solving problems together with our clients. We continue to innovate in traditional areas such as natural catastrophe and liability lines and are active in game-changing, long-term developments such as big data and cyber-risk. This means, looking ahead, that we will stay committed to delivering continued profitability through disciplined underwriting and a systematic allocation of capital to risk portfolios.

An area that we believe has turned a corner in 2014 is Life & Health Reinsurance. The segment delivered a net loss of USD 462 million for 2014. This negative bottom-line result was in large part a clear reflection of the decisive actions we took to enhance profitability going forward. Over the last two years we identified and analysed, in close collaboration with our clients, the problematic pre-2004 life business in the US. The problems had to do with underperforming yearly renewable term business in which the under-performance was expected to continue. This year we actively addressed these issues with the clients concerned. The other action we took was to unwind the asset funding structure supporting a longevity transaction. Our aim is to arrive at a more sustainable solution for all. I'm pleased to report that the outcomes of both, as negative as they look today, are ultimately positive for clients, for Swiss Re, and especially for you, our shareholders and they enhance the sustainability of our business long-term. These measures were also essential to keep us on track to achieve the target of 10%–12% return on equity for Life & Health by the end of 2015. Life & Health continues to be an attractive business with great growth potential in both mature and developing markets.

Corporate Solutions continued to deliver profitable growth, with net income of USD 319 million and an annual increase in net earned premiums of 18%. Two developments in 2014 will support expansion into high growth markets. The acquisition of Sun Alliance Insurance in China — once approved by the regulator — will enable us to offer corporate insurance directly from mainland China. In Latin America, we acquired 51% ownership of Colombian insurer Confianza, providing us with another foothold in the region in addition to our offices in Mexico and Brazil.

Admin Re® had a good year as well. The unit walked the talk and continued on its path to exit the US market, as evidenced by the sale of the Aurora block of business in the US in October 2014. The sale has a one-time negative impact on our bottom line, but it supports our vision to redeploy capital to areas where we see growth opportunities and attractive shareholder returns.

Finding solutions — together

I hope you share my confidence in our company. In an increasingly global and interconnected environment, we are well positioned to capture opportunities the market offers. We are equally well positioned to rise to meet challenges such as the abundance of capital or the more over-arching challenges of climate change and the insurance protection gap. Our differentiated position, our strong capitalisation, our disciplined underwriting and, last but far from least, our strong client relationships are all the foundation of Swiss Re's profitability. They are the key to our sustainability and, therefore, to Swiss Re generating long-term shareholder value.

With our focus on sustainability it was a particular pleasure that Swiss Re was again named as the insurance sector leader in the 2014 Dow Jones Sustainability Indices, showcasing that sustainability is built into all facets of our management approach.

All these achievements wouldn't be possible if we didn't have the right talent and employees. Please join me in thanking them for their hard work, great engagement and strong 2014 results. Our people are the reason we have a seat at the table with our clients, brokers and business partners. They are also the force for delivering shareholder value to you.

I'd also like to take the opportunity to thank you, dear shareholders, for your confidence in Swiss Re and your trust in us as we continue to plan our way forward. One important step is the introduction of two financial targets which will guide us as of 2016 and beyond (for more information see the box below). They are chosen to continue to focus our efforts on profitability and economic growth and will provide you with the right metrics to measure our success.

Zurich, 19 February 2015

Michel M. Liès
Group Chief Executive Officer

Our next financial targets

Looking at 2016 and beyond, we remain committed to a strong capital position. We will introduce two financial targets for the Group in 2016, focusing on profitability and economic growth.

The first is to deliver a return on equity of 700 basis points above risk-free (as measured by 10-year US Treasury bonds and a basket of rates reflecting our business mix) over the cycle.

The second target is to grow economic net worth (ENW) per share by 10% per annum, also over the cycle.

This timeframe provides a long-term aspiration without being distorted by outlying individual results.