SwissLife

Management summary in English

regarding the "Solvabilität" (Solvency) chapter of the Swiss Life Financial Condition Report 2017

This management summary provides relevant solvency information for Swiss Life Group in English. The information listed in this summary is taken from the "Bericht über die Finanzlage 2017" chapter "Solvabilität" for Swiss Life Group. For additional information, please see "Bericht über die Finanzlage 2017".

Please note that this summary is not intended to be a pure translation of the original text published in German. The original German text is binding.

Management summary in English regarding the "Solvency" chapter of the Swiss Life Financial Condition Report 2017

Solvency of Swiss Life Group

SST ratio

Solvency of Swiss Life Group

CHF m	01.01.2017	Prior-year adjustment	**01.01.2018**
Risk-bearing capital	31 914		**36 225**
Target capital	21 477		**22 972**
Market value margin	4 319		**4 077**
A = Risk-bearing capital – market value margin	27 595		**32 148**
B = Target capital – market value margin	17 158		**18 894**
SST RATIO (A/B) in %	161%		170%

The solvency of the Swiss Life Group as of 1 January 2018 amounted to 170%.

Compared with 1 January 2017, the target capital of Swiss Life Group has increased by CHF 1.5 bn to CHF 23.0 bn, while the risk-bearing capital has risen by CHF 4.3 bn to CHF 36.2 bn. The SST ratio increased by 9 percentage points to 170%.

The SST ratio is calculated from the risk-bearing capital less the market value margin divided by the target capital less the market value margin.

The market value margin is the cost of capital for the risk-bearing capital required to be held by the insurance company while fulfilling its insurance liabilities.

The current information on solvency (risk-bearing capital, target capital) corresponds to the reporting to FINMA. This information is subject to a regulatory review.

SST model

Swiss Life calculates its SST ratio as of 1 January 2017 and as of 1 January 2018 using an internal model that has been approved by FINMA with conditions.

One condition is that future non-guaranteed policyholder bonuses are recognised as risk-bearing capital. Consistently, the target capital is calculated without the effects of the risk-sharing by the policyholder.

A further condition concerns the diversification between market and credit risk. According to FINMA, no diversification between market and credit risk may be taken into account. The results presented in this report have therefore been calculated excluding this diversification benefit.

The approved internal SST model of Swiss Life primarily differs from the former standard FINMA model in terms of the following aspects:

- Fully simulation-based calculation of the target capital including credit risk and guarantees. By contrast, the credit risk in the standard model is calculated with a factor-based model according to Basel III.

- The target capital includes the expected financial result from the life insurance business, as the potential changes in value of the risk-bearing capital over one year have to be considered.

- The standard FINMA models are calibrated for the Swiss market. However, Swiss Life is substantially active in foreign markets. The internal SST model is more granular in terms of risks factors in comparison with the former standard FINMA model (e.g. risks abroad).

Risk-bearing capital

The risk-bearing capital comprises the core capital and the supplementary capital.

The supplementary capital consists of risk-absorbing capital instruments that can be allocated to the risk-bearing capital. In the case of Swiss Life this corresponds to the market value of the hybrid instruments.

The core capital comprises the market-consistent value of the assets minus the sum of the best estimate value of the insurance liabilities and the market-consistent value of the remaining liabilities. Planned dividends and capital repayments, treasury shares held directly by the insurance company at its own risk, intangible assets and latent property taxes must be deducted to the extent that they cannot be offset.

Risk-bearing capital

CHF m	01.01.2017	Prior-year adjustment	**01.01.2018**
Market-consistent value of assets minus total from best estimate liabilities plus market-consistent value of other liabilities	29 192		**33 207**
Deductions	-458		**-579**
CORE CAPITAL	28 735		**32 628**
Supplementary capital	3 180		**3 597**
RISK-BEARING CAPITAL	31 914		**36 225**

The risk-bearing capital of the Swiss Life Group has increased by CHF 4.3 bn from prior year level and amounted to CHF 36.2 bn as of 1 January 2018.

The increase in the risk-bearing capital of the Swiss Life Group is largely driven by the positive capital market and positive business development. The periodic update of the parameters and regulatory changes had a negative effect on the risk-bearing capital in 2017.

Reconciliation of risk-bearing capital of Swiss Life Group and Swiss Life Ltd

CHF bn	Swiss Life Group	Swiss Life Ltd
As of 01/01/2017	31.9	29.8
Regulatory changes	-0.4	-0.4
Business development	1.3	0.6
Parameter updates	-0.7	-0.7
Capital markets development	4.1	4.0
AS OF 01/01/2018	36.2	33.4

Regulatory changes

According to FINMA requirements, the Ultimate Forward Rate (UFR) is reduced for the currencies CHF, EUR, USD and GBP by 15 basis points each a year, which reduced the risk-bearing capital. Swiss Life did not use the new alternative, available from 1 January 2018, of valuing EU units with Solvency II valuation curves.

Business development in 2017

The expected return on Swiss Life assets above the risk-free interest rate and the new business had a positive impact on the business development in 2017. Moreover, the full conversion of the Swiss Life Holding convertible bond had a positive effect on the risk-bearing capital of Swiss Life Group while having no impact on Swiss Life Ltd. The proposed dividend for payment in April 2018 reduces the risk-bearing capital with effect from 1 January 2018. Repayment of the EUR 590 million hybrid bond in April 2017 was already considered in the risk-bearing capital as of 1 January 2017 and thus has no impact by comparison with the previous year.

Parameter updates

The update of the insurance parameters, particularly the updated best estimate assumptions for the Swiss group life business along with additional updates reduced the overall risk-bearing capital for the reporting period.

Capital market developments

Capital market developments were positive overall in 2017. Lower credit spreads and the strong appreciation of the euro relative to the Swiss franc made a particular contribution to the positive development. Risk-bearing capital as of 1 January 2018 was also increased through the positive development of equities, interest rates and real estate.

Target capital

The required capital (target capital) is determined in consideration of possible losses over a time horizon of one year in unfavourable circumstances for the company. This takes place in the internal Swiss Life SST model in a simulation-based manner with regard to market, credit and insurance risks.

In addition, the market value margin, extreme scenarios and the expected financial result are also taken into account for determining the target capital. The latter effect generally reduces the target capital.

Target capital

CHF m	01.01.2017	Prior-year adjustment	**01.01.2018**
Market risk	13 626		**16 055**
Insurance risk	3 352		**3 302**
Diversification	-3 122		**-3 101**
Credit risk	3 891		**3 988**
Market value margin and other effects on target capital	3 729		**2 728**
thereof market value margin	4 319		**4 077**
thereof other effects	-590		**-1 349**
TARGET CAPITAL	21 477		**22 972**

Compared with 1 January 2017, the target capital of the Swiss Life Group has risen by CHF 1.5 bn to CHF 23.0 bn.

As illustrated in the following table, the change in the market risk is primarily decisive for the development of the target capital in the reporting period.

Reconciliation of target capital of Swiss Life Group and Swiss Life Ltd

CHF bn	Swiss Life Group	Swiss Life Ltd
As of 01/01/2017	21.5	19.5
Change of market risk	2.4	2.4
Change of credit risk	0.1	0.1
Change of insurance risk	-0.1	-0.1
Change of market value margin and other effects	-1.0	-1.1
AS OF 01/01/2018	23.0	20.8

Change of market risk

The rise in market risk results partially from the increase in the duration gap. In addition, the market risk of equities and real estate increased due to higher exposure. Lower credit spreads and the resulting higher market values of fixed income investments also increased the target capital.

Change of credit risk

The increase in the credit risk is mainly due to the rise in the market values of fixed income investments resulting from lower interest rates and spreads. This effect was partly offset through risk-mitigating portfolio adjustments and partly by the effect of the annual parameter update.

Change of insurance risk

The regularly updated insurance parameters lead to a small decrease in insurance risk capital, which is partially offset by the lower diversification effects between the market and insurance risk. Changes in diversification effects are included under change of market value margin and other effects.

Change of market value margin and other effects

The regularly updated insurance parameters reduce the market value margin between 1 January 2017 and 1 January 2018. Moreover, the revised definition of the pandemic scenario also reduces the target capital.

Components of the market risk

CHF m	01.01.2017	Prior-year adjustment	**01.01.2018**
Market risk of interest rates	6 965		**9 546**
Market risk of spreads	5 492		**5 746**
Market risk of currency exchange rates	3 362		**4 014**
Market risk of equities	3 585		**4 273**
Market risk of real estate	4 070		**4 532**
Market risk of participations	90		**74**
Diversification effects of market risk	-9 937		**-12 131**
MARKET RISK	13 626		**16 055**

Components of insurance risk

CHF m	01.01.2017	Prior-year adjustment	**01.01.2018**
Insurance risk of mortality	2 246		**2 154**
Insurance risk of longevity	1 160		**853**
Insurance risk of disability	427		**418**
Insurance risk of reactivation rate	243		**268**
Insurance risk of costs	1 440		**1 640**
Insurance risk of lapses	2 167		**2 221**
Insurance risk of option exercise	1 934		**1 932**
Insurance risk of non-life	245		**274**
Diversification effects of insurance risk	- 6 510		**-6 458**
INSURANCE RISK	3 352		**3 302**

Valuation

The assets and liabilities disclosed for solvency purposes in the financial condition report are measured at market value. If compared to the annual report of Swiss Life Group, valuation differences of assets and liabilities arise due to the market-consistent valuation for solvency purposes, while other valuation methods are also used according to IFRS.

Classification differences, valuation differences and the future non-guaranteed policyholder bonuses to be recognised as risk-bearing capital in accordance with FINMA requirements explain the key differences in the SST reporting and the annual IFRS report of the Swiss Life Group.

General note to Swiss Life Ltd

Swiss Life Ltd is the major subsidiary of Swiss Life Holding and plays a major role within the Swiss Life Group.

The SST ratio of the Swiss Life Group is therefore largely driven by Swiss Life Ltd, while effects from other companies only exert a minor additional impact. The SST solvency model of Swiss Life Ltd corresponds to that of the Swiss Life Group.

The solvency ratio of Swiss Life Ltd as of 1 January 2018 amounted to 174%.