Results of operations, financial position and net assets

Property and casualty reinsurance

- Sustained competition in property and casualty reinsurance
- Solid outcome of treaty renewals as at 1 January 2017
- Large loss expenditure sharply higher in the first quarter compared to corresponding period
- Group net income up 5.4% to EUR 215.4 million

The situation in worldwide property and casualty reinsurance was little changed overall from the previous year. The increased loss expenditure in 2016 had positive implications for reinsurance premiums only on a local level, with the result that the intense competition prevailing in the markets was largely sustained. The supply of reinsurance capacity still clearly exceeds demand, even though the decline in prices was less marked than in the previous year. This was also evident in the treaty renewals as at 1 January 2017, when roughly 64% of our property and casualty reinsurance portfolio was renegotiated. We maintained our rigorous underwriting discipline and focused on high-quality existing business, complemented by opportunities in niche and specialty segments. Once again we benefited from our excellent financial ratings and our long-standing customer relationships. Attractive possibilities to enlarge our portfolio opened up primarily in North America, including for example in the area of cyber covers. Overall, the pressure on rates in North America eased; signs of a bottoming out in prices could be detected here across the various lines of business. Furthermore, the treaty renewals in Canada also passed off very favourably; appreciable rate increases were booked in property business under virtually all programmes. Last year's heavy losses from the devastating forest fires in the province of Alberta were the driving factor here.

In the aviation line as well as in parts of Eastern Europe and in China we scaled back our shares in view of inadequate prices. The treaty renewals in credit and surety reinsurance, on the other hand, were satisfactory. In credit reinsurance, in particular, we were able to enlarge some existing sizeable customer accounts and acquire new clients, hence boosting the premium volume in this line. In the area of structured reinsurance demand for solutions offering solvency relief was thoroughly pleasing: we booked significant premium growth here from Europe, North America and Latin America.

Reflecting these developments, gross premium for our Property & Casualty reinsurance business group rose by 12.5% to EUR 2.8 billion (EUR 2.5 billion). At constant exchange rates growth would have come in at 11.3%. The level of retained premium climbed to 88.6% (87.9%). Net premium earned increased by 10.4% to EUR 2.2 billion (EUR 2.0 billion); adjusted for exchange rate effects, it would have grown by 8.8%.

Losses in the first quarter were significantly heavier than in the corresponding quarter of the previous year. Net expenditure on major losses totalled EUR 133.7 million (EUR 55.5 million), a figure that was nevertheless still within the envisaged quarterly budget. The largest individual loss – at around EUR 50 million – was Cyclone Debbie, which caused severe damage and subsequent flooding in Australia.

The insurance industry was also impacted by the decision of the UK government to cut the discount rate for personal injury compensation payments ("Ogden rate") from 2.5% to -0.75% effective March 2017. This means that compensation amounts will rise sharply in cases where claimants receive a lump-sum payment to compensate claims that involve an ongoing, long-lasting financial burden – such as care costs. Severe personal injury claims, e. g. as a consequence of a car accident, may therefore become quite substantially more expensive, resulting in higher payments under liability insurance covers that will have particularly serious implications for non-proportional reinsurance. Given that this move not only affects future claims but also past claims that have still to be run off, it compels insurers and reinsurers to set aside substantial additional reserves. In the first quarter Hannover Re booked additional loss reserves of EUR 126 million for this purpose. In view of the very adequate level of the IBNR reserves (for claims that have been incurred but not yet reported), however, this did not result in any run-off losses. It is to be anticipated that the change in the Ogden rate will require further additional reserves to be set aside in the course of the year. Nevertheless, these should also be absorbed by the IBNR reserves that have been constituted.

The underwriting result for total property and casualty reinsurance fell short of the previous year's very good quarter on account of higher losses; it amounted to EUR 90.7 million (EUR 100.3 million) as at 31 March 2017. The combined ratio stood at 95.6% (94.7%) and is thus in line with our goal of staying below 96% for the full year.

The investment income booked for property and casualty reinsurance from assets under own management grew by 17.3% to EUR 238.2 million (EUR 203.1 million).

The operating profit (EBIT) for property and casualty reinsurance as at 31 March 2017 improved again slightly on the already very good level of the previous year's quarter to reach EUR 309.8 million (EUR 299.7 million). The EBIT margin stood at 14.3% (15.3%) and thus again beat our minimum target of 10%. Group net income rose by 5.4% to EUR 215.4 million (EUR 204.3 million). Earnings per share amounted to EUR 1.79 (EUR 1.69).

Key figures for property and casualty reinsurance

in EUR million	2017		2016
	1.1.–31.3.	+/– previous year	1.1.–31.3.
Gross written premium	2,814.7	+12.5%	2,502.1
Net premium earned	2,165.7	+10.4%	1,961.3
Underwriting result	90.7	-9.6%	100.3
Net investment income	243.4	+17.5%	207.2
Operating result (EBIT)	309.8	+3.4%	299.7
Group net income	215.4	+5.4%	204.3
Earnings per share in EUR	1.79	+5.4%	1.69
EBIT margin[1]	14.3%		15.3%
Combined ratio[2]	95.6%		94.7%
Retention	88.6%		87.9%

[1] Operating result (EBIT)/net premium earned
[2] Including funds withheld

Life and health reinsurance

- Gross premium income develops as planned
- Strong interest in reinsurance solutions designed to optimise the increased capital requirements associated with regulatory solvency standards
- Life and health reinsurance delivers solid contribution to Group net income

Life and health reinsurance developed in line with expectations in the first quarter of 2017. The challenging state of the German insurance market, both on the life and health side and with respect to longevity covers, remained unchanged: the guaranteed interest rate, which had last been adjusted in 2015, was reduced from 1.25% to 0.9% as at 1 January 2017, thereby further diminishing the appeal of traditional life insurance products. The new long-term care definition, which now differentiates between five grades of care, was adopted at the start of 2017. In the financial year just ended we had worked intensively on a new LTC table that we were then able to make available to our customers in time for implementation. Owing to the more demanding solvency requirements imposed by Solvency II, some primary insurers continue to need financing assistance for the supplementary reserves that have to be set aside for life products promising guaranteed returns in excess of the official reference rate ("Zinszusatzreserve"). In this respect we are engaged in a dialogue with our primary insurance clients with an eye to potential reinsurance solutions that can provide capital relief.

Results in our US mortality business again came under strain in the period under review from a higher-than-expected mortality in older underwriting years. Financial solutions business, on the other hand, developed exceptionally favourably as anticipated and delivered a clearly positive profit contribution.

In the United Kingdom the life insurance market continued to be dominated by pricing pressure, especially on the mortality side. Despite this, our longevity portfolio in the UK fared well. We were able to write new treaties and at the same time secured additional new business for the future with our existing customers. Demand from UK insurers and pension funds remains strong with an eye to fulfilment of exacting Solvency II capital requirements for longevity risks. The market is, however, also extremely competitive and price-sensitive. In the international arena we are receiving numerous inquiries from life and pension insurers seeking capital relief. Particularly in Canada and Japan, the longevity market showed very vigorous growth. Furthermore, we registered

a surge in interest in the Scandinavian markets, Germany, Israel, Korea and South Africa. Based on our long-standing expertise – especially with longevity risks – , we have already successfully transferred reinsurance solutions to international markets in the past and we expect global longevity business to develop favourably.

In Asia we observed an extremely dynamic development on the various markets. In Malaysia and Shanghai, for example, we noted strong demand with promising business opportunities in the morbidity sector. In Korea we were successful in writing life reinsurance business. What is more, our new branch in India commenced its operational activities.

Viewed from an overall perspective, life and health reinsurance in Australia, Africa as well as the Middle East and Scandinavian markets developed in line with our expectations. In addition, we received very positive feedback from our customers on our two underwriting tools hr | ReFlex and hr | Quirc.

Gross premium income of EUR 1.7 billion (EUR 1.8 billion) was generated in life and health reinsurance as at 31 March 2017, equivalent to a modest decline of 1.7%. The decrease would have similarly been 1.7% adjusted for exchange rate effects.

The level of retained premium stood at 91.3% (90.5%). Net premium earned consequently fell slightly by 0.9% to EUR 1.6 billion (EUR 1.6 billion). At constant exchange rates, a contraction of 1.3% would have been booked.

Investment income from our assets under own management rose by 3.2% to EUR 80.6 million (EUR 78.1 million). Income from securities held for our account by ceding companies fell slightly short of the previous year's level at EUR 67.7 million (EUR 79.5 million).

The operating result (EBIT) totalled EUR 89.8 million (EUR 105.5 million), a drop of 14.9% compared to the previous year's strong performance. This decline can be attributed principally to the comparatively poorer result of the existing book of US mortality business. With an EBIT margin of 33.0% financial solutions business comfortably beat the 2% target. For longevity business, too, the 2% target was fulfilled with an EBIT margin of 2%. Mortality and morbidity business delivered an EBIT margin of 0.9%, thereby failing to reach the targeted 6% mark. Group net income contracted by 22.2% to EUR 60.6 million (EUR 77.9 million). Earnings per share amounted to EUR 0.50 (EUR 0.65).

Key figures for life and health reinsurance

in EUR million	2017		2016
	1.1.–31.3.	+/– previous year	1.1.–31.3.
Gross written premium	1,731.9	-1.7%	1,761.4
Net premium earned	1,566.4	-0.9%	1,580.7
Investment income	148.3	-5.9%	157.6
Operating result (EBIT)	89.8	-14.9%	105.5
Net income after tax	60.6	-22.2%	77.9
Earnings per share in EUR	0.50	-22.2%	0.65
Retention	91.3%		90.5%
EBIT margin[1]	5.7%		6.7%

[1] Operating result (EBIT)/net premium earned

Investments

- High-quality diversified investment portfolio maintained
- Ordinary investment income exceeds previous year's level
- Return on investment at 3.0% well on track to meet year-end target

Despite widespread disquiet on both the geopolitical level and in domestic political spheres, the investment environment was nevertheless relatively stable in the period under review; it was, however, notable for a continued low interest rate level and relatively low risk premiums on corporate bonds. While modest yield increases were widely observed on German government bonds, the general level of rates was still very low overall. German government bonds continue to be sold at negative returns well into the medium maturity segment. In the case of US Treasuries, a slight rotation of the yield curve was observed overall against a backdrop of modest yield declines in the medium to long maturity ranges.

Credit spreads on European and US corporate bonds were very largely stable in most rating classes, with the result that they too remained on a stubbornly low level overall. In total, the unrealised gains on our fixed-income securities as at 31 March 2017 increased slightly to EUR 1,119.9 million (EUR 1,098.1 million). After the already significant growth recorded in 2016, our portfolio of assets under own management increased to EUR 42.0 billion (31 December 2016: EUR 41.8 billion). We scarcely changed the allocation of our assets to the individual classes of securities in the first quarter. The reorganisation of the rating structure of our USD fixed-income portfolio was partially suspended because we considered the risk/return ratio of some classes of securities in the lower rating segment to be no longer adequate. We shall observe the development of the market here before potentially continuing with this move. In the other classes of securities and on the euro side, where the situation is more attractive in this regard, we pressed ahead with the restructuring accordingly. In this way we shall be able to increase the liquidity of our portfolio while maintaining the overall risk level of our fixed-income holdings virtually unchanged and continuing to generate stable returns. In addition, we modestly reduced our real estate portfolio by selling an office property in the United States. Compared to the previous year, we adjusted the modified duration of our portfolio of fixed-income securities merely insignificantly to 4.9 (5.0).

Ordinary investment income excluding interest on funds withheld and contract deposits came in higher as at 31 March 2017 than in the comparable period at EUR 319.1 million (EUR 268.5 million). Particularly bearing in mind the continued low level of interest rates, it is highly gratifying that we were able to more than offset the diminished return on our fixed-income securities with what was – by first quarter standards – very strong income from private equity and real estate. Interest on funds withheld and contract deposits retreated to EUR 72.9 million (EUR 83.5 million).

Impairments of altogether just EUR 10.9 million (EUR 13.9 million) were taken. Of this amount, EUR 1.0 million (EUR 4.2 million) was attributable to alternative investments; impairments of EUR 0.4 million (EUR 2.0 million) were recognised on equities. No impairments (EUR 0.7 million) were taken on fixed-income securities. Scheduled depreciation on directly held real estate increased slightly to EUR 7.4 million (EUR 6.9 million), a reflection of our ongoing growing involvement in this area. The impairments were not opposed by any write-ups (EUR 0.1 million).

The net balance of gains realised on disposals stood at EUR 24.1 million (EUR 43.6 million) and was in large measure attributable to regrouping activities as part of regular portfolio maintenance.

We recognise a derivative for the credit risk associated with special life reinsurance treaties (ModCo) under which securities deposits are held by cedants for our account; the performance of this derivative in the period under review gave rise to unrealised gains of EUR 1.3 million (loss of -EUR 1.4 million) recognised in investment income. In economic terms we assume a neutral development for this item over time, and hence the volatility that can occur in specific quarters provides no insight into the actual business development. Altogether, the unrealised gains in our assets recognised at fair value through profit or loss amounted to EUR 10.9 million. This contrasted with unrealised gains of EUR 10.5 million in the corresponding period of the previous year.

Despite a diminished return on our fixed-income securities and lower realised gains, we generated investment income of EUR 392.9 million – a pleasing improvement on the comparable period (EUR 366.2 million) made possible by stronger ordinary income from real estate and private equity. Income from assets under own management accounted for an amount of EUR 320.0 million (EUR 282.7 million), producing an annualised average return (excluding effects from derivatives) of 3.0%. This puts us well on track to achieve our expected target of 2.7% for the full year.

Net investment income

in EUR million	2017		2016
	1.1.–31.3.	+/– previous year	1.1.–31.3.
Ordinary investment income[1]	319.1	+18.9%	268.5
Result from participations in associated companies	4.4		0.7
Realised gains/losses	24.1	-44.7%	43.6
Appreciation	–		0.1
Depreciation, amortisation, impairments[2]	10.9	-21.6%	13.9
Change in fair value of financial instruments[3]	10.9	+4.6%	10.5
Investment expenses	27.6	+3.5%	26.7
Net investment income from assets under own management	320.0	+13.2%	282.7
Net investment income from funds withheld and contract deposits	72.9	-12.8%	83.5
Total investment income	**392.9**	**+7.3%**	**366.2**

[1] Excluding income and expenses on funds withheld and contract deposits
[2] Including depreciation/impairments on real estate
[3] Portfolio at fair value through profit or loss and trading

Rating structure of our fixed-income securities[1]

Rating classes	Government bonds		Securities issued by semi-governmental entities[2]		Corporate bonds		Covered bonds/asset-backed securities	
	in %	in EUR million	in %	in EUR million	in %	in EUR million	in %	in EUR million
AAA	77.3	9,150.8	65.8	4,755.8	1.0	128.9	66.4	2,303.1
AA	11.7	1,385.8	27.7	1,998.1	13.4	1,742.2	14.5	501.6
A	5.1	605.9	2.3	165.3	33.5	4,346.8	5.7	198.2
BBB	4.2	494.5	1.1	81.0	43.0	5,567.2	9.0	312.1
< BBB	1.7	200.3	3.1	222.7	9.1	1,183.1	4.4	152.9
Total	**100.0**	**11,837.3**	**100.0**	**7,222.9**	**100.0**	**12,968.2**	**100.0**	**3,468.0**

[1] Securities held through investment funds are recognised pro rata with their corresponding individual ratings.
[2] Including government-guaranteed corporate bonds