IFRS 17 / IFRS 9

A first glance

Clemens Jungsthöfel, Chief Financial Officer
25th International Investors' Day 2022
London, 6 October 2022

hannover re®

Agenda

1

Introduction IFRS 17 / 9

2

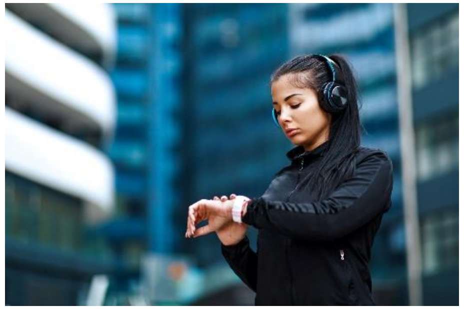
Approach to transition

3

Impact on equity, earnings and KPIs

4

Timeline



5

Key takeaways

1

Introduction
IFRS 17 / 9

somewhat different

hannover re®

IFRS 17 significantly changes the structure of the balance sheet
IFRS 9 changes the classification and measurement of financial instruments

IAS 39 / IFRS 4 (US GAAP)

Assets

Retro share in technical provisions

Deferred Acquisition Costs

Receivables from reinsurance business

Investments IAS 39
Amortised Cost
- Held to Maturity
- Loans, Receivables

Fair Value
- Available for Sale
- Fair Value Option/ Trading

Liabilities

Equity

Technical provisions for insurance liabilities:
- Provisions for unearned premiums
- Premium reserve
- Provisions for premium refund
- Other technical provisions

Provision for outstanding claims

Other liabilities

IFRS 9 / 17

Assets

Retro-LRC
Retro-LIC

Investments IFRS 9
- Amortised Cost
- Fair Value OCI
- Fair Value PL

Liabilities

Equity

"Insurance Contract Liability":

LRC without Loss Component
- Cash flows
- Discounting
- Risk adjustment
- CSM

LRC Loss Component

LIC
- Cash flows
- Discounting
- Risk adjustment

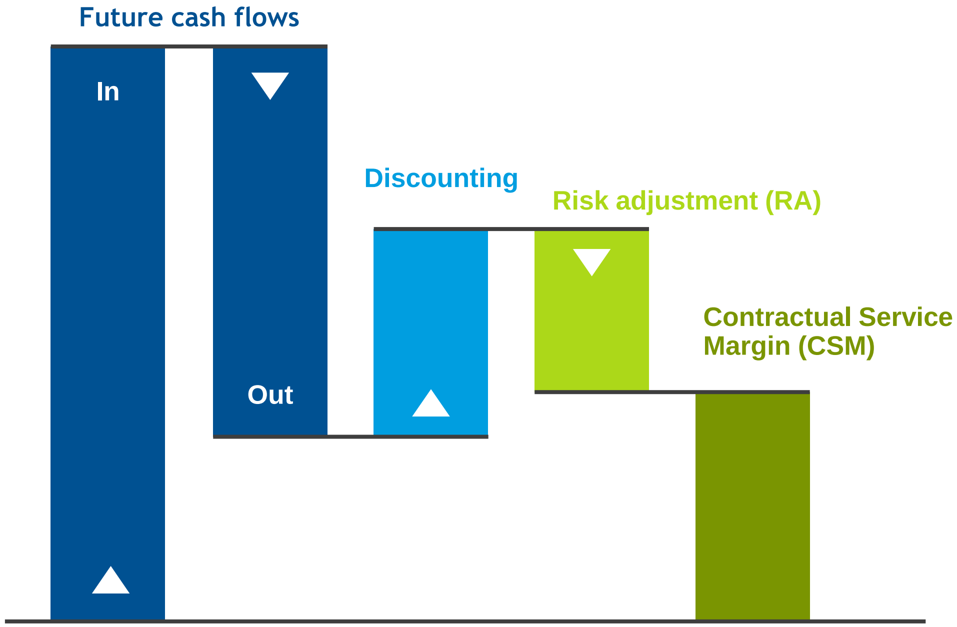
Other liabilities

hannover re®

IFRS 17 - Full adoption of GMM allows to steer business on a consistent basis

Ensuring transparency and bridging the GA(A)P to economic view

Full adoption of General Measurement Model (GMM) for entire business (P&C and L&H)



Valuation methods and rationale

- Cash flows and economics of reinsurance business will remain unchanged
- IFRS 17, in particular **GMM** as default model, is complex with significantly increased data and other requirements
- However, we have taken a broader, long-term view and aim to use the change in accounting as **transformational** in order to
  - increase transparency on **earning patterns** and **value creation**, incl. comparability between lines of business
  - improve alignment with both Solvency II and internal performance measures (IVC: Intrinsic Value Creation)
  - review our data and IT infrastructure, streamline processes and increase automation
  - solve systematic IFRS4 accounting mismatches and reward asset-liability management efforts
  - improve steering and managing of our portfolios
- Adoption of **OCI option** for large parts of our portfolio to match investment valuation will reduce volatility from interest rate movements
- **Prudent reserving approach** will be maintained and – together with CSM and RA at transition – help to manage potential increased volatility

hannover re®

IFRS 9 - Fundamental revision of accounting rules for financial instruments

Higher share of assets at Fair Value through P&L

Classification and valuation

- Majority of investments in **scope of IFRS 9** (direct real estates out of scope)
- IAS 39 **categories** HtM, L&R, AfS, FVPL will change to
  - Amortised Costs (AC)
  - Fair Value through P&L (FVPL)
  - Fair Value through OCI (FVOCI)
  - Fair Value through OCI w/o recycling (FVOCI non-recycling)
- Reduced flexibility in assigning financial instruments to valuation categories (**"SPPI"** criteria)
- Business model **„Hold & Sell"** has been applied, i.e. most financial instruments **continue to be classified as FVOCI** (~ 93%)
- **FVPL** volume rises significantly
- **Expected Credit Loss** (ECL) becomes new P&L component
- Existing **currency accounting mismatch** (monetary vs. non-monetary items) will be mitigated with changes in FV of investment funds (incl. Private-Equity, Real-Estate, fixed-income funds and the respective f/x effects) now being recognised in P&L (previously OCI)
- Minor effect on **equity** at transition (amortised costs instruments)

SPPI = Solely payment of principle interest

Assets categorised Fair Value P&L

- Main asset classes: Private-Equity, Real-Estate, fixed-income funds

IAS 39	IFRS 9
<1%	~7.5%

Introduction of Expected Credit Loss (ECL)

- ECL is measured at acquisition for all fixed-income instruments categorised Amortised Cost or Fair Value OCI
- In case of a significant change in credit quality, probability of default changes from 1 year to remaining maturity

Stage 1	Stage 2	Stage 3
Expected loss within one year	Expected loss until maturity	Impairment (based on market value)

2 Approach to transition

somewhat different

hannover re®

Our transition is focused on ensuring sustainable future earnings

IFRS 17 - Approach to transition

How to measure in-force business when applying IFRS 17

Impracticable to use the full retrospective approach?

- Yes → Full Retrospective Approach FRA
- No → Modified Retrospective Approach MRA
- No → Fair Value Approach FVA

Business with application of FVA has biggest impact in transition

- The CSM or loss component of the LRC at the transition date is determined as the difference between the fair value of a group of insurance contracts at transition and the fulfilment cash flows measured at that date
- IFRS 13 defines fair value as "the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date"

Transition principles

- Hannover Re has used all available approaches at transition: full retrospective (FRA), modified retrospective (MRA) and fair value approach (FVA)
- Main limitation for FRA ("impracticability") is usually data availability (e.g. segmentation, granularity, initial recognition)

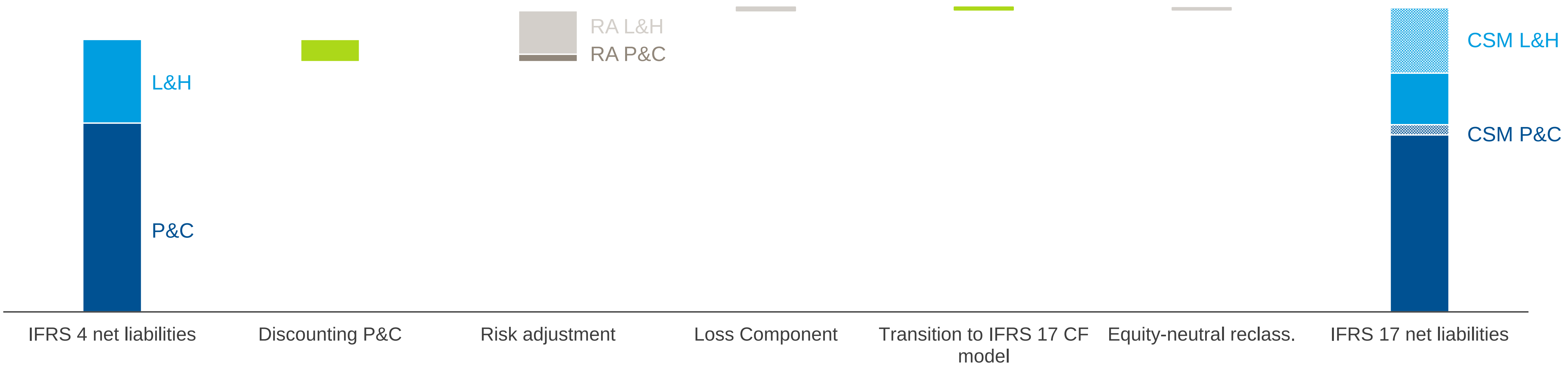
Transition to IFRS 17 generally does not change the economic assumptions, but results in an unlocking of IFRS 4 assumptions (best estimate liability and interest rates)

hannover re®

Our transition is focused on ensuring sustainable future earnings

IFRS 17 - Approach to transition

Revaluation of net liabilities (illustrative)



HR Transition to IFRS 17 enables economic measurement of net liabilities and establishes substantial profit / risk margins to ensure sustainable future earnings

Ensuring transparency and bridging the GA(A)P to economic view

IFRS 17 - Approach to transition

P&C

- Discounting reflects time value of money in measurement of technical liabilities; effect is mainly driven by long-tail segments
- Prudent reserving level maintained within LIC (resiliency reserves); may result in loss component / onerous business at initial recognition
- Establishment of RA (as additional level of prudence) and CSM increases liabilities
- Use of FVA for older underwriting years

Prudent reserving approach maintained

Discounting effect will be more pronounced in 2022/23 due to higher interest rates

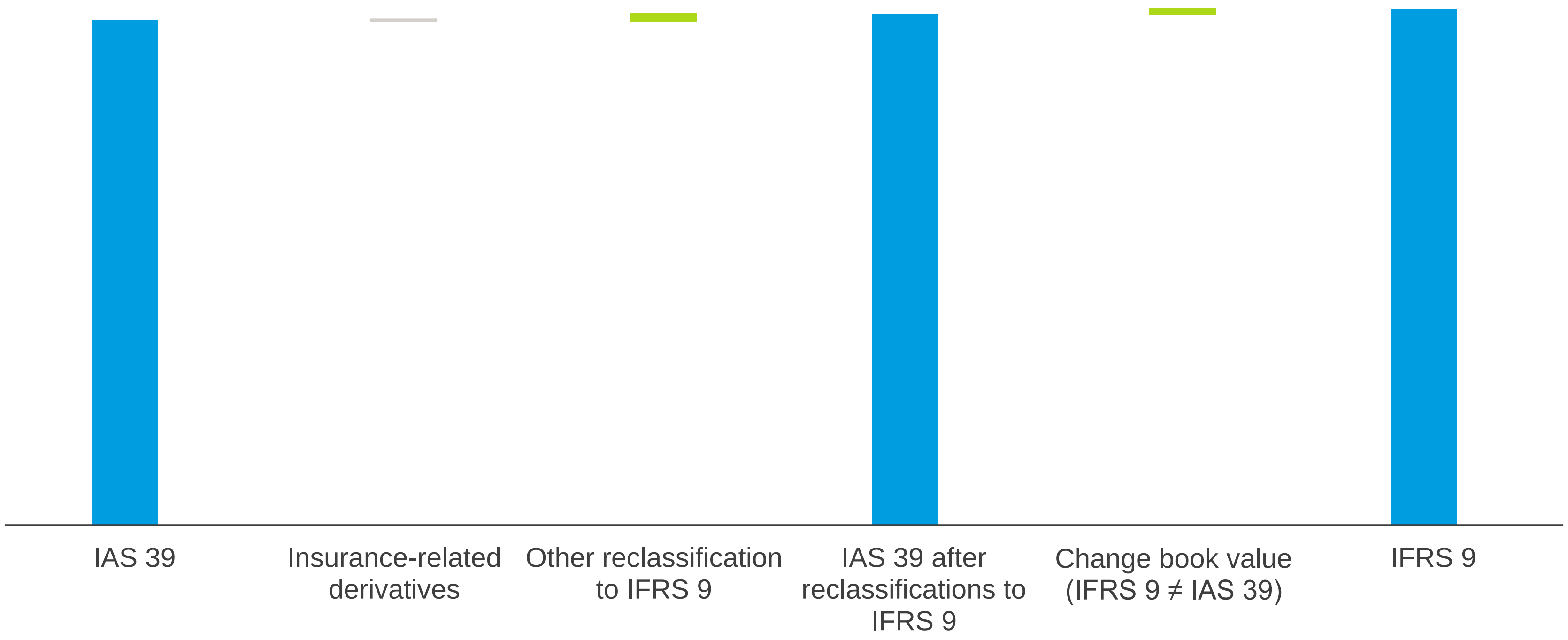
L&H

- Application of IFRS 17 with limited impact on overall level of liabilities for large parts of L&H business
- Increase in liabilities for mortality business with long durations, due to unlocking of best estimate liability and unlocking of discount rates to current interest rates
- Establishment of substantial CSM and RA at transition

No changes in economic assumptions at transition, impact on liabilities driven by transition principles

Investments: Limited impact on asset volume from change to IFRS 9

Revaluation of investments (illustrative)



Insurance-related derivatives will be part of LRC

Change in book value includes IAS39 off-balance sheet valuation reserves for HTM and loans

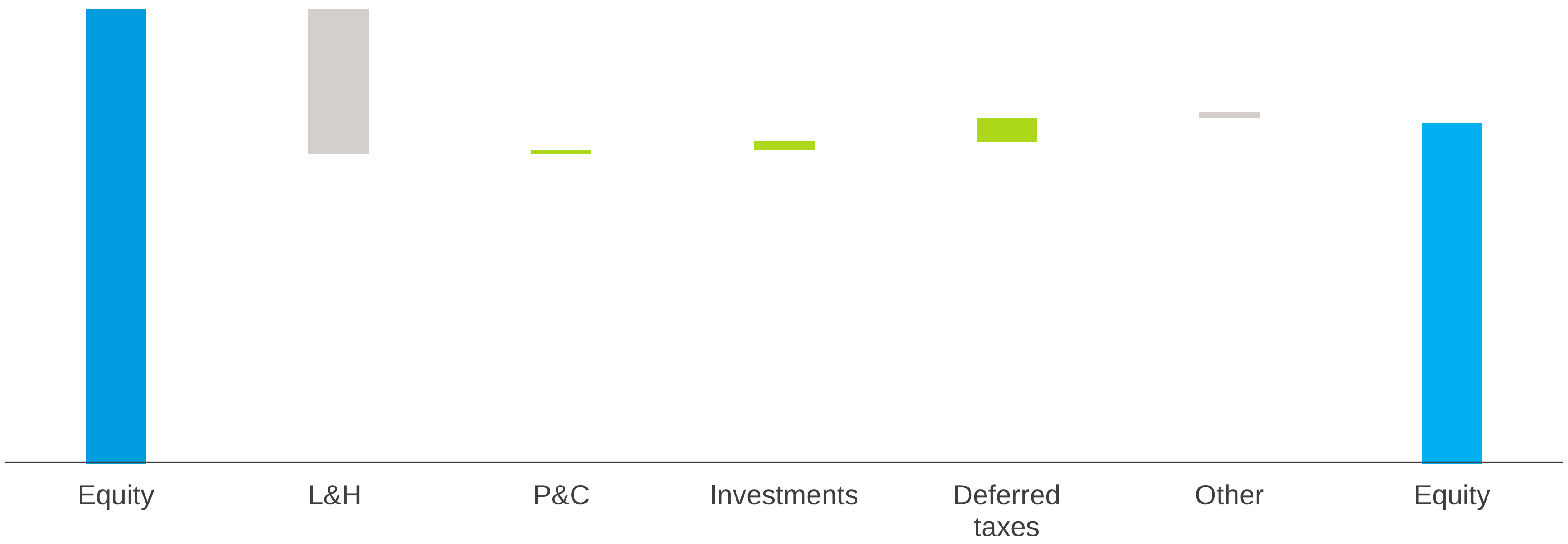
Increased share of assets at Fair Value P&L potentially results in higher P&L volatility

3 Impact on Shareholders' Equity, future earnings and KPIs

Shareholders' equity: Discounting proves more meaningful economic view

Interest rate changes 2022 clearly demonstrate accounting mismatch under IFRS 4

Revaluation of equity (illustrative)



Unlocking of best-estimate liabilities and interest rates increases liabilities in L&H

Positive impact from discounting of P&C liabilities partly offset by establishment of CSM and RA

Limited impact from IFRS 9

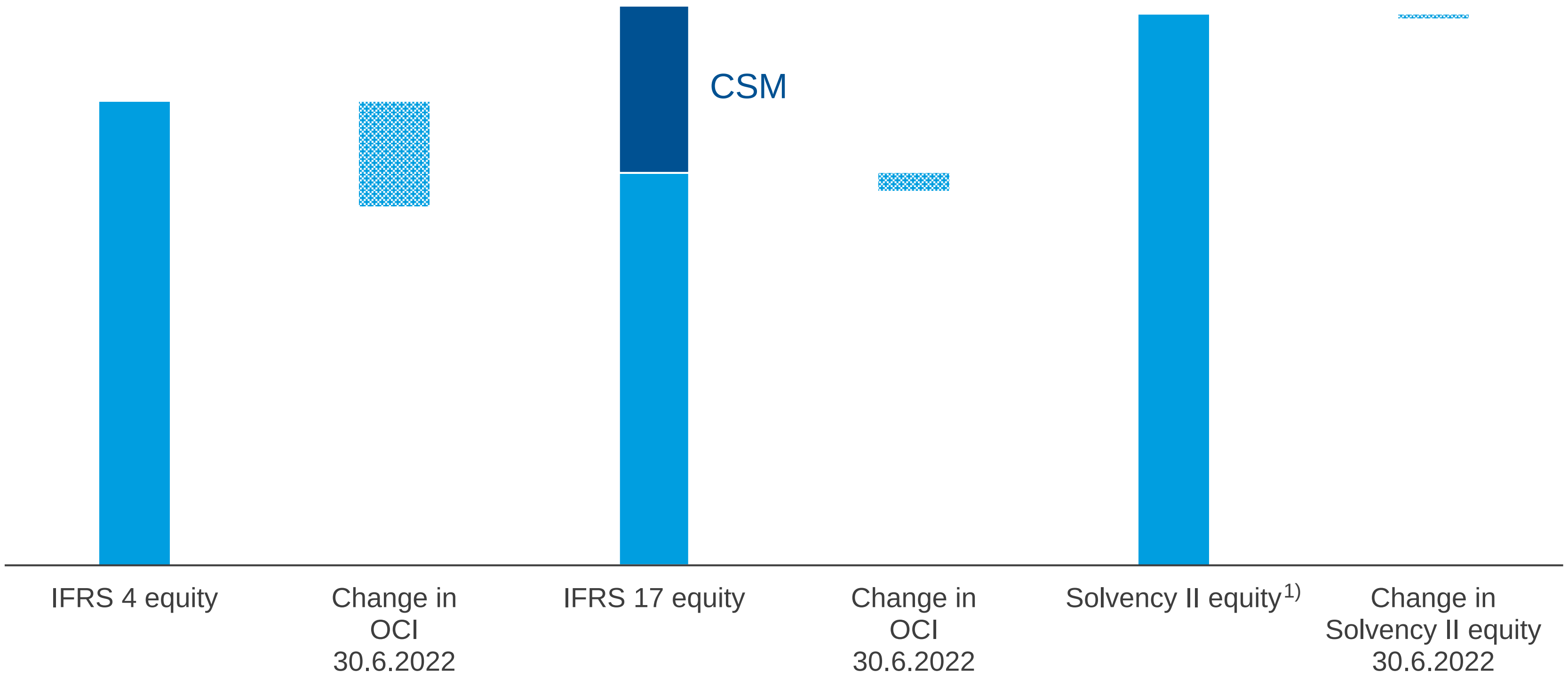
Change in Equity from discounting significantly smaller with higher interest-rate level when IFRS 17 will become effective in 2023

At transition insurance liabilities will increase and equity decrease due to risk adjustments and CSM, which will contribute to earnings over time

IFRS 17 equity + CSM at similar level to Solvency II equity

Accounting mismatch for interest-rate movements largely mitigated

Equity (illustrative)



From an economic perspective shareholders' equity needs to be seen in conjunction with contractual service margin (CSM) and risk adjustment (RA)

Reduction in equity at transition (1.1.2022) will be by far more than compensated for by CSM and RA

Sum of equity and CSM (after tax) will be comparable to Solvency II equity

Development of OCI in 1H/2022 confirms more economic view of IFRS17

Financial leverage to be viewed in relation to shareholders' equity + CSM

1) Solvency II excess of assets over liabilities

hannover re®

Transition approach expected to lead to sustainable earnings level

IFRS 17 income statement

Reinsurance revenue
Reinsurance service expenses
Net expenses from reinsurance contracts held
Reinsurance service result

Net finance income / expenses from reinsurance contracts issued
Net finance income / expenses from reinsurance contracts held
Net reinsurance finance result

Net income from investments under own management

Net currency result
Other income and expenses

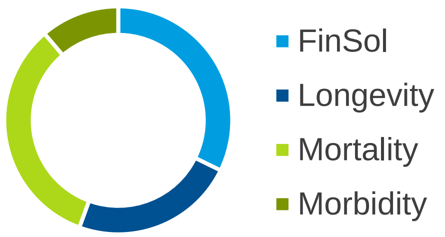
EBIT
Tax
Net income

Reinsurance service result

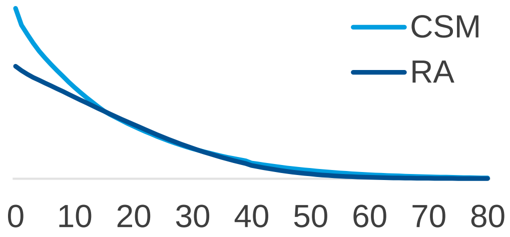
- Actual vs. expected claims + expenses
- Release of CSM and RA
- Change in LIC (includes P&C reserve runoff)
- Loss component and release of loss component
- Deposit-accounting business in Financial Solutions will largely be recognised in reinsurance service result

CSM	Risk adjustment
P&C ~ 15% / L&H ~ 85%	P&C ~ 15% / L&H ~ 85%

L&H CSM is well diversified



Release of L&H CSM and RA



P&C

- Well diversified by line of business and region
- Release of CSM largely within two years

hannover re®

Potential KPIs

Return on equity	**P&C combined ratio** Cost Ratio (gross) + Loss Ratio (gross) + Reinsurance Ratio = Combined Ratio
EBIT growth P&C and L&H	**Solvency II ratio**
xRoCA P&C and L&H	**Reinsurance revenue growth**
CSM growth	**New business CSM (incl. loss component)**

hannover re®

4 Timeline

Timeline for further information

Dec 2022

Further details on IFRS 17 transition and future KPIs

FY 2022 results

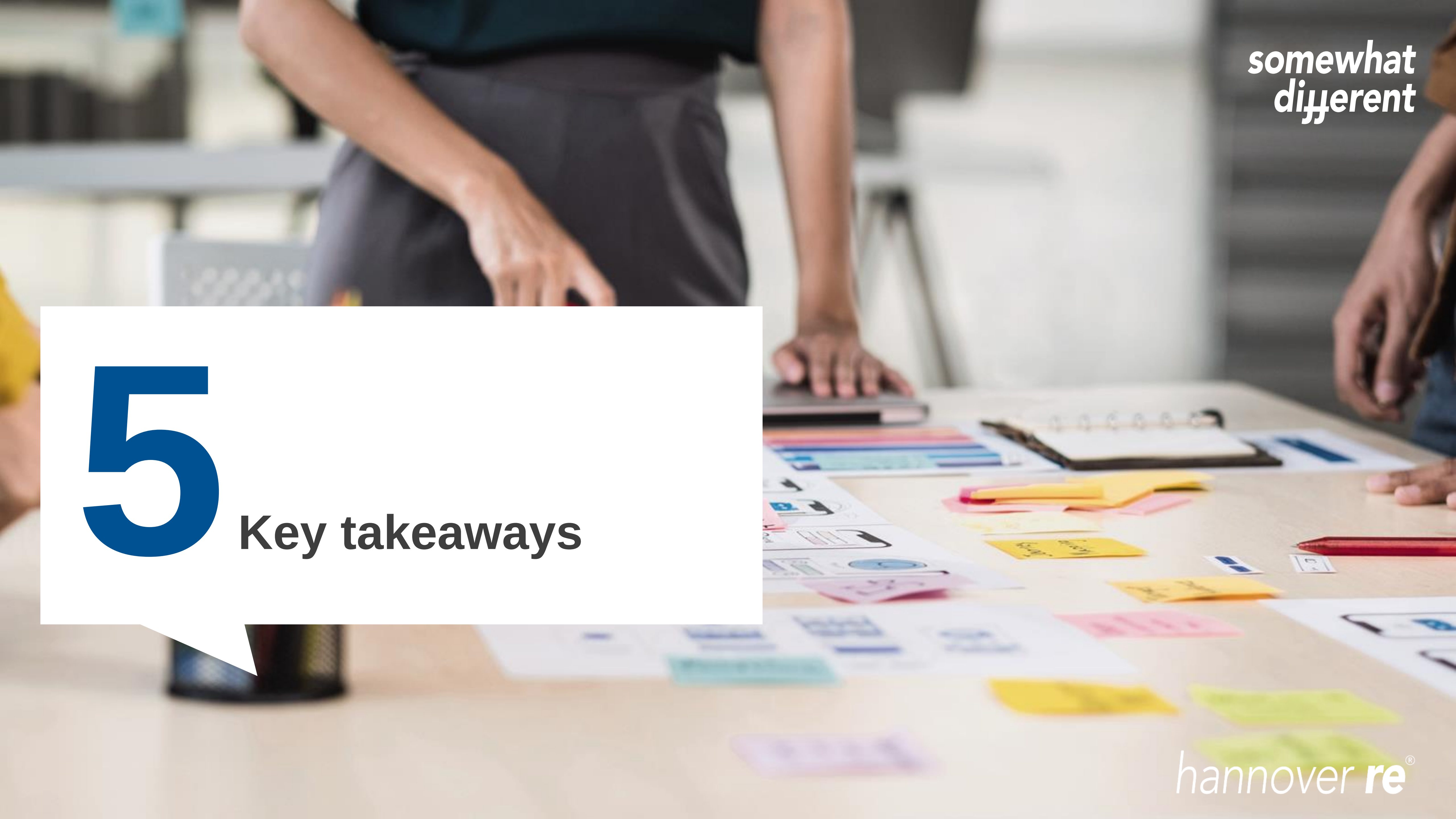
FY 2022 IFRS 4 reporting + IFRS 17 guidance for FY 2023

Q1/2023

First reporting according to IFRS 17

Investors' Day 2023

Publication of targets for new strategy cycle 2024 - 2026



5 Key takeaways

somewhat different

hannover re

Key takeaways

IFRS 17

- Enhancement of presentation and reporting will increase transparency
- Timing of profit recognition will change
  - Establishment of CSM and risk margin
  - No gain at inception, immediate recognition of onerous business
  - Profits will be recognised when earned
- Cash flows and economics will remain unchanged

Main implications IFRS 9

- Classification and hence valuation of asset classes will change
- Impairment rules will change

… for Hannover Re

- Overall limited impact on balance sheet and shareholders' equity
- > 90% of investments categorised as Fair Value OCI
- P&L volatility likely increases due to higher share of assets FVPL
- Minor impacts from introduction of Expected Credit Loss

Implications for Hannover Re

- Strategy and business model will be unaffected
- Strong capitalisation unchanged
- Dividend capacity (German GAAP) remains unchanged
- Prudent reserving approach in P&C will be maintained
- Equity + CSM at similar level to Solvency II equity
- Better reflection of value and earnings of L&H business
- Transformational benefits through review of data, processes, etc.

IFRS 17 will bring accounting view closer to economic view