

IFRS 8 Operating Segments

Implementation in the Munich Re Group





1. IFRS Regulations

2. Implementation in the Munich Re Group

3. The new income statement format for 2008-figures in segments

Comparison of the rules (I)

IAS 14 Segment Reporting (applicable until 31.12.2008)

IFRS 8 Operating Segments (starting from 1.1.2009)

Segmentation

- Risk and reward approach to segmentation required
- Segmentation according to products/services and regions
- A segment is defined as a distinguishable component of an enterprise with a homogeneous risk and return structure
- **Two-tier segmentation** through company-specific definition of primary and secondary segments
- Primary and secondary segmentation depending on whether risks and return on equity are influenced mainly by products/services or geographical regions

- Identification of segments to be based on internal reporting
- A segment is determined according to the "**only internal view**", i.e. it is defined as a component of an entity
 - that engages in business activities from which it may earn revenues and incur expenses;
 - whose operating results are regularly reviewed by the management to make decisions about resources to be allocated to the segment and assess its performance; and
 - for which discrete financial information is available
- No distinction between primary and secondary segments

In both cases, there are additional quantitative thresholds for defining reportable segments

Comparison of the rules (II)

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Measure of segment result

- Segment disclosure on the basis of IFRS principles of recognition and measurement
- No need for reconciliation but also no insight into the company's internal organisational structure

- Segment disclosures stem from internal reporting, i.e. are not necessarily IFRS-based
- As a rule, need to reconcile the measure of segment result to the standardized IFRS measure

Focus on comparability and transparency of results of different companies

Focus on internally relevant performance measures

Motivation

- Usefulness for investors focuses on comparability and segmentation according to risks and rewards
- Segment reporting based on external reporting

- Usefulness for investors focuses on management's information basis
- Enhanced transparency with regard to corporate management

Summary

Segmentation according to the
risk and reward approach

Segmentation according to the
management approach

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Implications of IFRS 8 for the Munich Re Group – Overview

***The management approach of IFRS 8 requires segment disclosure
in line with internal management***

Disclosure of internally used performance measures
Segmentation according to management logic

***Owing to the different types of segment and the differentiated management logic required
(reinsurance and primary insurance, life and non-life), the management system within the
Munich Re Group is naturally heterogeneous***

Matrix management of insurance companies within the business segments
(underwriting vs. investment responsibility)
Value-added calculation in property-casualty and health reinsurance versus Market-Consistent
Embedded Value in life and health primary insurance

Discussion of the following aspects

Segmentation

Consideration of
International Health in the segmentation

**Segment disclosure according
to internal reporting**

Changes in structure of the income statement

Segmentation for International Health (IH)

International Health

- IH does not meet quantitative thresholds under IFRS 8 yet; organisation and reporting structure under development
- In reinsurance (RI), continued disclosure of health together with life
- In primary insurance (PI), separation of life and health owing to high volume of health, but no separation into German business and international operations
- Disclosure of separate IH business segment when the quantitative thresholds are reached

Munich Re Group					
Reinsurance		Primary insurance			Asset management
Life and health	Property-casualty	Life	Health	Property-casualty	–

As soon as quantitative threshold is reached

Munich Re Group						
Reinsurance		International Health	Primary insurance			Asset management
Life	Property-casualty	–	Life	Health ¹	Property-casualty	–

¹ Amendment as of April 24th, 2009: predominantly German health business but also health business of international ERGO-composite-insurers which is managed by ERGO and therefore remains in the segment Primary insurance Health.

Overview: Impact on the income statement

Improvement of IFRS disclosure to increase transparency of the segments

Breakdown of operating result

TECHNICAL RESULT

Underwriting items plus
income from
technical interest

NON-TECHNICAL RESULT

Investment result and other non-technical
result components, deduction of
income from technical interest

Separated out from operating result

Other non-operating result
(e.g. foreign exchange losses)

Finance costs

Impairment losses of goodwill

Tax

Impact on the income statement – Operating result (I)

The operating result is not a normalised measure of result

Reasons:

- No smoothing of the operating result to eliminate extraordinary components of the investment result because
 - we regard all components of the investment result as linked with our core business and thus as operating components (e.g. owing to the requisite policyholder participation in extraordinary earnings components as well);
 - such smoothing would require a host of differentiations, some of them arbitrary, and we see it as basically immaterial from which result sources the earnings on investments derive;
 - it would lead to a number of inconsistencies with other income-statement items directly dependent on the investment result and thus also on the result of disposals and the write-downs of investments (e.g. the item "expenses for claims and benefits" would then have to be adjusted in the same way).
- Similarly, there is no smoothing of random fluctuations in claims experience, since these constitute a component of the underwriting business

Deliberate refraining from normalisation in order to avoid
arbitrariness and limited transparency of disclosure


The income from technical interest, however, produces greater stabilisation of the technical result in the
segments life and health primary insurance (cf. slide 11)

Impact on the income statement – Operating result (II)

"Operating result" as a uniform measure of segment result

Reasons:

- Use of different performance measures: Market-Consistent Embedded Value (MCEV) in life and health primary insurance, and multi-year value-based management (VBM) performance measures on a gross basis in non-life
- Decision makers' focus is also on the business fields' IFRS result contributions
- In the case of different internal performance measures, IFRS 8 states that those most consistent with IFRS accounting measures should be used



Therefore, "primary" performance measures (MCEV, VBM) are replaced by the "secondary" measure operating result (cf. definition on slide 15)

Distinction between operating and non-operating result

- All income and expenses that are not plannable or clearly generated by ordinary operations (e.g. currency gains and losses, restructuring expenses, expenses for other services and system infrastructure) are deducted (cf. slide 15).
- All other result components (including non-regular income and expenses related to investments) are classified as part of the operating result

Impact on the income statement – Sub-results and income from technical interest

Disclosure of sub-results

- Within the operating result, a technical result and a non-technical result are disclosed
- The technical result embraces the result components assignable to the operative underwriting business
- The investment result and the other operating income and expenses are shown in the non-technical result

Logic and benefits of disclosing income from technical interest

- Via the income on technical interest, the investment earnings and other income linked to the underwriting business are recognized and allocated to the technical result.
- In the property-casualty segments for primary insurance and reinsurance, income from technical interest essentially corresponds to the risk-free interest to be earned on the technical provisions.
- In the segment “life and health reinsurance”, income from technical interest is the interest on the provisions mainly based on contractual agreements (income from deposits retained on assumed reinsurance).
- In the segments “life” and “health” in primary insurance,
 - the income from technical interest also includes – via the allocation to provisions for premium refunds – portions of other operating income as well as regular and extraordinary investment earnings. Therefore, the corresponding expenses for technical interest are disclosed below the other operating-result sources (cf. p. 13)
 - the income from technical interest and the expenses for claims and benefits produce substantial stabilization of the technical result on balance. Therefore a normalization of the policyholder participation, with the inconsistencies that would ensue (especially regarding transparency of expenses for claims and benefits), has been dispensed with.

The income from technical interest makes possible an adequate breakdown into the two sub-result measures "technical result" and "non-technical result" appropriate to each business segment

Impact on the segment income statement – structure until 31.12.2008

Old structure of segment income statement (until 31.12.2008)

<i>Gross premiums written</i>	5. Investment income
- <i>From insurance transactions with other segments</i>	Investment expenses
- <i>From insurance transactions with external third parties</i>	Investment result
1. Gross earned premiums	<i>Thereof:</i>
Ceded	- <i>Income from associates</i>
Net earned premiums	6. Other income
2. Gross expenses for claims and benefits	7. Other expenses
Ceded share	8. Operating result
Net expenses for claims and benefits	9. Amortisation of goodwill
4. Gross operating expenses	10. Finance costs
Ceded share	11. Taxes on income
Net operating expenses	12. Consolidated result

Impact on the income statement – structure applicable from 1.1.2009

New structure of segment income statement (from 1.1.2009)

<i>Gross premiums written</i>	6. Investment income
- <i>From insurance transactions with other segments</i>	Investment expenses
- <i>From insurance transactions with external third parties</i>	Investment result
1. Gross earned premiums	<i>Thereof:</i>
Ceded	- <i>Income from associates</i>
Net earned premiums	7. Other operating income
2. Income from technical interest	8. Other operating expenses
3. Gross expenses for claims and benefits	9. Deduction of income from technical interest
Ceded share	10. Non-technical result
Net expenses for claims and benefits	11. Operating result
4. Gross operating expenses	12. Other non-operating result, impairment losses of goodwill and finance costs
Ceded share	
Net operating expenses	13. Taxes on income
5. Technical result	14. Consolidated result

Important definitions (I)

Definition and explanation of important terms in connection with IFRS 8

Income from technical interest

The income from technical interest is the amount which the insurance business assumed earns from risk-free investment. This amount is reallocated from the non-technical business. In detail:

- RI property-casualty and PI property-casualty: The risk-free interest on the technical provisions, i.e. a normalized investment result is allocated to the technical result via the income from technical interest
- RI Life/Health: income from technical interest is the interest on the provisions mainly based on contractual agreements (income from deposits retained on assumed reinsurance)
- PI life, PI health: policyholders' participation in the form of guaranteed interest rate/actuarial interest and profit sharing (provision for current and deferred premium refunds) plus net unrealized gains and losses from unit-linked life insurance

Technical interest

- The technical result comprises all items of income and expense directly attributable to the operating insurance business, i.e.
- Net earned premiums
 - + Income from technical interest
 - Net expenses for claims and benefits
 - Net operating expenses

Important definitions (II)

Definition and explanation of important terms in connection with IFRS 8

Non-technical result

- The non-technical result represents the shareholders' share of the other business, i.e.
- Investment result
 - + Other operating income
 - Other operating expenses
 - Deduction of income from technical interest

Operating result

- Sum of underwriting and non-technical result

Other non-operating result

- Breakdown of previous "other income" and "other expenses" into an operating and a non-operating component
- "Non-operating" are foreign exchange gains/losses, income and expenses in respect of other intangible assets, other non-technical income/expenses (e.g. income and expenses unrelated to the accounting period, project costs, and large portions of ERGO AG's holding-company expenses)

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Income statement

Group

€m	Q1 2008	Q2 2008	Q3 2008	Q4 2008	Q1–4 2008
Gross premiums written	9,842	9,011	9,270	9,706	37,829
1. Net earned premiums	8,543	8,697	8,857	9,627	35,724
2. Income from technical interest	1,101	1,205	1,142	1,356	4,804
3. Net expenses for claims and benefits	6,933	7,085	6,956	7,745	28,719
4. Net operating expenses	2,108	2,104	2,227	2,604	9,043
5. Technical result	603	713	816	634	2,766
6. Investment result	1,675	1,586	662	1,923	5,846
7. Other operating income	174	126	229	179	708
8. Other operating expenses	158	132	192	259	741
9. Deduction of income from technical interest	–1,101	–1,205	–1,142	–1,356	–4,804
10. Non-technical result	590	375	–443	487	1,009
11. Operating result	1,193	1,088	373	1,121	3,775
12. Other non-operating result	–53	–55	–128	–110	–346
13. Impairment losses of goodwill	–	–	–	167	167
14. Finance costs	86	95	91	89	361
15. Taxes on income	277	310	152	634	1,373
16. Consolidated result	777	628	2	121	1,528

Income statement

Reinsurance life and health

€m	Q1 2008	Q2 2008	Q3 2008	Q4 2008
Gross premiums written	1,676	1,713	1,794	1,947
1. Net earned premiums	1,585	1,662	1,705	1,823
2. Income from technical interest	168	169	151	100
3. Net expenses for claims and benefits	1,254	1,320	1,311	1,419
4. Net operating expenses	385	442	471	523
5. Technical result	114	69	74	-19
6. Investment result	362	480	154	256
7. Other operating income	32	21	44	52
8. Other operating expenses	19	25	28	62
9. Deduction of income from technical interest	-168	-169	-151	-100
10. Non-technical result	207	307	19	146
11. Operating result	321	376	93	127
12. Other non-operating result, impairment losses of goodwill and finance costs	-20	-45	-30	-8
13. Taxes on income	-19	-2	29	115
14. Consolidated result	320	333	34	4

Income statement

Reinsurance property-casualty

€m	Q1 2008	Q2 2008	Q3 2008	Q4 2008
Gross premiums written	3,874	3,477	3,683	3,705
1. Net earned premiums	3,251	3,188	3,333	3,676
2. Income from technical interest	326	313	321	322
3. Net expenses for claims and benefits	2,449	2,173	2,396	2,390
4. Net operating expenses	939	876	987	1,200
5. Technical result	189	452	271	408
6. Investment result	631	1,268	83	824
7. Other operating income	62	28	93	25
8. Other operating expenses	33	27	72	84
9. Deduction of income from technical interest	–326	–313	–321	–322
10. Non-technical result	334	956	–217	443
11. Operating result	523	1,408	54	851
12. Other non-operating result, impairment losses of goodwill and finance costs	–51	–109	–81	20
13. Taxes on income	213	190	48	524
14. Consolidated result	259	1,109	–75	347

Income statement

Primary insurance life

€m	Q1 2008	Q2 2008	Q3 2008	Q4 2008
Gross premiums written	1,432	1,473	1,382	1,765
1. Net earned premiums	1,280	1,334	1,241	1,603
2. Income from technical interest	382	494	408	652
3. Net expenses for claims and benefits	1,420	1,577	1,330	2,019
4. Net operating expenses	204	200	181	317
5. Technical result	38	51	138	-81
6. Investment result	455	534	361	835
7. Other operating income	132	123	130	141
8. Other operating expenses	139	137	162	122
9. Deduction of income from technical interest	-382	-494	-408	-652
10. Non-technical result	66	26	-79	202
11. Operating result	104	77	59	121
12. Other non-operating result, impairment losses of goodwill and finance costs	-23	33	-54	-199
13. Taxes on income	31	66	7	10
14. Consolidated result	50	44	-2	-88



Income statement

Primary insurance health

€m	Q1 2008	Q2 2008	Q3 2008	Q4 2008
Gross premiums written	1,554	1,423	1,436	1,427
1. Net earned premiums	1,351	1,387	1,414	1,394
2. Income from technical interest	247	254	262	248
3. Net expenses for claims and benefits	1,258	1,350	1,284	1,232
4. Net operating expenses	207	202	186	192
5. Technical result	133	89	206	218
6. Investment result	159	208	70	120
7. Other operating income	18	18	16	29
8. Other operating expenses	26	23	31	41
9. Deduction of income from technical interest	–247	–254	–262	–248
10. Non-technical result	–96	–51	–207	–140
11. Operating result	37	38	–1	78
12. Other non-operating result, impairment losses of goodwill and finance costs	–18	1	–22	–67
13. Taxes on income	7	19	–2	6
14. Consolidated result	12	20	–21	5

Income statement

Primary insurance property-casualty

€m	Q1 2008	Q2 2008	Q3 2008	Q4 2008
Gross premiums written	1,623	1,163	1,220	1,100
1. Net earned premiums	1,076	1,126	1,164	1,131
2. Income from technical interest	55	55	61	48
3. Net expenses for claims and benefits	599	714	671	717
4. Net operating expenses	360	359	384	360
5. Technical result	172	108	170	102
6. Investment result	103	147	66	–20
7. Other operating income	110	103	142	128
8. Other operating expenses	157	147	135	183
9. Deduction of income from technical interest	–55	–55	–61	–48
10. Non-technical result	1	48	12	–123
11. Operating result	173	156	182	–21
12. Other non-operating result, impairment losses of goodwill and finance costs	–25	–27	–51	–126
13. Taxes on income	39	34	64	–33
14. Consolidated result	109	95	67	–114



Implications of IFRS 8 for the Munich Re Group Summary

Segmentation

Two-step concept for the business field
of International Health

Separation of life and health
in primary insurance

Measure of segment result

Focus on
operating result

Breakdown into technical result
and non-technical result in line
with the internal reporting

More detailed disclosure of
other result