

# IFRS 8 Operating Segments

## Implementation in the Munich Re Group

May 2009



**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)

### IAS 14 Segment Reporting

(applicable until 31.12.2008)

### IFRS 8 Operating Segments

(starting from 1.1.2009)

#### 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 <sup>1</sup>	Property-casualty	–

<sup>1</sup> Amendment as of April 24<sup>th</sup>, 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>	<b>Investment result</b>
1. Gross earned premiums	<i>Thereof:</i>
Ceded	- <i>Income from associates</i>
<b>Net earned premiums</b>	6. <b>Other income</b>
2. Gross expenses for claims and benefits	7. <b>Other expenses</b>
Ceded share	<b>8. Operating result</b>
<b>Net expenses for claims and benefits</b>	9. Amortisation of goodwill
4. Gross operating expenses	10. <b>Finance costs</b>
Ceded share	11. Taxes on income
<b>Net operating expenses</b>	<b>12. Consolidated result</b>

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

## 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
<b>5. Technical result</b>	<b>603</b>	<b>713</b>	<b>816</b>	<b>634</b>	<b>2,766</b>
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
<b>10. Non-technical result</b>	<b>590</b>	<b>375</b>	<b>-443</b>	<b>487</b>	<b>1,009</b>
<b>11. Operating result</b>	<b>1,193</b>	<b>1,088</b>	<b>373</b>	<b>1,121</b>	<b>3,775</b>
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
<b>16. Consolidated result</b>	<b>777</b>	<b>628</b>	<b>2</b>	<b>121</b>	<b>1,528</b>

## 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
<b>5. Technical result</b>	<b>114</b>	<b>69</b>	<b>74</b>	<b>-19</b>
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
<b>10. Non-technical result</b>	<b>207</b>	<b>307</b>	<b>19</b>	<b>146</b>
<b>11. Operating result</b>	<b>321</b>	<b>376</b>	<b>93</b>	<b>127</b>
12. Other non-operating result, impairment losses of goodwill and finance costs	-20	-45	-30	-8
13. Taxes on income	-19	-2	29	115
<b>14. Consolidated result</b>	<b>320</b>	<b>333</b>	<b>34</b>	<b>4</b>

## 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
<b>5. Technical result</b>	<b>189</b>	<b>452</b>	<b>271</b>	<b>408</b>
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
<b>10. Non-technical result</b>	<b>334</b>	<b>956</b>	<b>-217</b>	<b>443</b>
<b>11. Operating result</b>	<b>523</b>	<b>1,408</b>	<b>54</b>	<b>851</b>
12. Other non-operating result, impairment losses of goodwill and finance costs	-51	-109	-81	20
13. Taxes on income	213	190	48	524
<b>14. Consolidated result</b>	<b>259</b>	<b>1,109</b>	<b>-75</b>	<b>347</b>

## 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
<b>5. Technical result</b>	<b>38</b>	<b>51</b>	<b>138</b>	<b>-81</b>
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
<b>10. Non-technical result</b>	<b>66</b>	<b>26</b>	<b>-79</b>	<b>202</b>
<b>11. Operating result</b>	<b>104</b>	<b>77</b>	<b>59</b>	<b>121</b>
12. Other non-operating result, impairment losses of goodwill and finance costs	-23	33	-54	-199
13. Taxes on income	31	66	7	10
<b>14. Consolidated result</b>	<b>50</b>	<b>44</b>	<b>-2</b>	<b>-88</b>

## 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
<b>5. Technical result</b>	<b>133</b>	<b>89</b>	<b>206</b>	<b>218</b>
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
<b>10. Non-technical result</b>	<b>-96</b>	<b>-51</b>	<b>-207</b>	<b>-140</b>
<b>11. Operating result</b>	<b>37</b>	<b>38</b>	<b>-1</b>	<b>78</b>
12. Other non-operating result, impairment losses of goodwill and finance costs	-18	1	-22	-67
13. Taxes on income	7	19	-2	6
<b>14. Consolidated result</b>	<b>12</b>	<b>20</b>	<b>-21</b>	<b>5</b>

## 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
<b>5. Technical result</b>	<b>172</b>	<b>108</b>	<b>170</b>	<b>102</b>
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
<b>10. Non-technical result</b>	<b>1</b>	<b>48</b>	<b>12</b>	<b>-123</b>
<b>11. Operating result</b>	<b>173</b>	<b>156</b>	<b>182</b>	<b>-21</b>
12. Other non-operating result, impairment losses of goodwill and finance costs	-25	-27	-51	-126
13. Taxes on income	39	34	64	-33
<b>14. Consolidated result</b>	<b>109</b>	<b>95</b>	<b>67</b>	<b>-114</b>

# 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