Solvency and Financial Condition Report 2019

ERGO Insurance NV/SA

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EXECUTIVE SUMMARY

ERGO Insurance NV/SA (hereafter the “company”) is part of the ERGO Group that in turn is part of the Munich Re Group. The company provides life insurance products with a focus on pension savings and long term savings.

This document is the Solvency and Financial Condition Report (“SFCR”) of ERGO Insurance NV/SA. Munich Re prepares a consolidated SFCR at Group level. The published report for the 2019 financial year can be found at www.munichre.com/en/ir/result-center/index.html.

The purpose of this report is to assist policyholders and other stakeholders to understand the solvency and financial position of ERGO Insurance NV/SA as at 31 December 2019 (i.e. reporting period is 1 January 2019 to 31 December 2019). Data contained in this report are subject to data quality monitoring.

Section A - Business and Performance

The company’s mission is to take good care of the savings our customers have entrusted us with and to protect their pension savings and financial health for the full duration of their contracts.

In 2019, ERGO Insurance NV/SA progressed significantly in its implementation of the New Strategy. In Q4 2019, the Board of Directors approved the closing of the program with remaining activities managed by business departments. The Management of the company monitors the evolution of its policy portfolios as well as the financial capacity of the company. Decisions taken earlier in 2017 and 2018 on capital management and investment strategy are delivering expected results in 2019 and as such are supporting the solvency position. The Solvency II ratio at year-end 2019 is established at 259% compared to 273% at year-end 2018.

Underwriting performance

The underwriting performance is based on the premiums the company receives, the claims paid out to clients and the different expenses related to administration and commercialization of policies.

In 2019, the following key developments occurred:

- Following the progress made in the implementation of the run-off strategy, the **Gross Written Premium** declined by 19% (-56,5 ml €), from 353,7 ml € in 2018 to 297,2 ml € in 2019.
- The overall **claims** incurred increased by 24% (+84,8 ml €), driven by Insurance with Profit Participation policies, where claims increased by 28% (+72,1 ml €). Other life insurance and Index-linked and unit-linked insurance claims increased by 16% (+4,2 ml €) and by 6% (+3,6 ml €), respectively.
- **Personnel and general expenses** are established at 47,2 ml € in 2019, compared to 51,5 ml € in 2018. The total expenses before cost allocation, excluding paid restructuring expenses provisioned in 2016, are 4,4 ml € lower compared to 2018.

Investment performance

The net income from investments decreased from 127 ml € in 2018 to 86 ml € in 2019, mainly driven by a decrease in the extraordinary investment result from 31,5 ml € in 2018 to -1,8 ml € in 2019. This is explained by the realisation of valuation reserves on fixed income investments in 2018.

Section B – System of Governance

The most important governing bodies in the System of Governance include: the Board of Directors; Audit and Risk Committee; the Nomination and Remuneration Committee, and the Management Committee.

During 2019, the onboarding of new Management Committee members reinforced the culture for sound risk management within ERGO Insurance NV/SA. The management of Independent Control Functions remained largely unchanged, providing stability in actuarial controlling, risk and compliance controlling and audit oversight. The company's Risk Management System is built to identify, assess and measure, steer as well as monitor and report risks. Continued focus remained on ensuring effective governance and further embedding an appropriate risk culture across the company, in line with the risk appetite set by the Board of Directors.

Section C - Risk Profile

The Risk Profile of the company provides at a given point in time a view on all the risks to which the company is exposed to, for instance:

- Underwriting risk: As is typical for an insurance company, underwriting risk represents the potential loss arising from entering into or underwriting insurance policies. Because of ERGO insurance N.V.'s business model and activities, its main underwriting risks are life risk and to a lesser extent health risk. In 2019, the decrease of interest rates led to a higher underwriting risk.
- Market risk: As is typical for a life insurance company, market risk is the major risk contributor to the company's Risk Profile. Market risk is the risk of a loss that may be caused by fluctuations in the prices of the financial instruments in a portfolio. The various risk factors are the interest rate, credit spreads, exchange rates, share prices or property prices. Movements in these various elements form the foundation of market risk. In 2019, a strong performance of the equity markets led to an increase in equity risk and also to higher unit-linked reserves and hence higher expected profits on those reserves. Interest rate risk decreased significantly, which is partly related to the very low interest rates by Q4 2019. The low interest rate risk is also the result of a good asset-liability matching.
- Operational Risk: The exposure to Operational Risk has significantly decreased in 2019 compared to 2018, mainly driven by a significant reinforcement of control activities in Operations, successful developments of system functionalities to automate processes, development of new applications such as Customer Support Platform providing a 360° view on clients, migration of old systems and actions taken to manage legacy risks.

The Risk Management Function maintains a comprehensive record of all risks on which it reports to the Management on a quarterly basis, pointing out new emerging risks, measuring progress on the mitigation actions and analysing behaviour of Key Risk Indicators. Cyber threats arising from the cyber space are identified and managed as part of the quarterly reporting. A specific program is started to improve the maturity to deal with Cyber security risks in general.

Section D - Valuation for Solvency Purposes

The company's economic balance sheet, like that of other insurers, comprises Assets, Technical Provisions and other liabilities. Technical Provisions are reserves for claims and premiums plus a risk margin. Assets, Technical Provisions and other liabilities are valued on a 'fair value' basis according to Solvency II requirements, meaning that the company's financial strength is sensitive to market movements in its value.

The Solvency II Technical Provisions (TP) are defined as the sum of the Best Estimate Liabilities (BE) and the Risk Margin. In 2019, the total Technical Provisions increased to 5,5 Bl € in 2019 from 4,8 Bl € in 2018, mainly due to the lower interest rates. The increase of the risk margin is also largely linked to the interest rate development.

Section E - Capital Management

The current capital management plan primarily aims to maintain a high financial capacity by having a strong solvency position that aims to assure, at all times, that the company can respect minimum regulatory requirements and capital requirements. The primary focus in 2019 was to maintain the attained position since year end 2018.

Nevertheless, where possible, measures were taken for further improvement. The main achievement of 2019 was delivering clearer model governance and further reviews of model and assumptions (most notably on lapses and disability) to calculate the solvency requirements.

The company continued to apply the Volatility Adjustment (VA), which in principle has a stabilizing effect on the solvency capital requirement, especially from market developments on spreads. Relying on its strong financial capacity and a high Solvency II ratio, the company obtained the exemption to further accrue 'flashing light reserves' for 2019.

Mainly as result of market developments, the solvency position slightly decreased, yet still staying at a comfortable level.

The company's Solvency II coverage ratios

Measures and decisions taken by the company were the main drivers to sustain the financial stability of the company:

- Solvency II coverage ratios at year end 2019: **259% of the SCR and 670% of the MCR** (with volatility adjustment)
- Solvency II coverage ratios at year end 2018: **273% of the SCR and 773% of the MCR** (with volatility adjustment)
- Solvency II coverage ratios at year end 2019: **243% of the SCR and 618% of the MCR** (without volatility adjustment)
- Solvency II coverage ratios at year end 2018: **225% of the SCR and 586% of the MCR** (without volatility adjustment)

The amount of the **Solvency Capital Requirement (SCR)** and the eligible amount of own funds to cover the SCR are classified by Tiers as illustrated in Table 1 below:

Item	With VA	Without VA
Eligible own funds to meet SCR	750	712
Tier 1	*606*	*566*
Tier 2 (capped)	*145*	*146*
Tier 3	-	-
SCR	290	293

Table 1: SCR and eligible own funds by tiers in Ml €

The amount of the **Minimum Capital Requirement (MCR)** and the eligible amount of basic own funds to cover the MCR are also classified by tiers as illustrated in the Table 2 below:

Item	With VA	Without VA
Eligible basic own funds to meet MCR	624	585
Tier 1	606	566
Tier 2 (capped)	*19*	*19*
Tier 3	-	-
MCR	93	95

Table 2: MCR and basic own funds by tiers in Ml €

ERGO Insurance NV/SA is monitoring the potential impacts of the Corona / COVID-19 on its capital position. First indications could lead to a manageable drop in the Solvency II ratio as result of changed market circumstances since year end 2019. The exact impact depends on the exact levels of the interest and equity markets as the daily volatile changes in the month of March 2020 imply different impacts. The impact of the equity markets on the own funds is also largely compensated on the solvency ratio by similar impacts on the SCR.