ZURICH®

Risk review 2013

Zurich Insurance Group
Annual Report 2013

Risk review

Zurich's approach to risk management aims to protect the Group's capital, enhance value creation, optimize its risk-return profile, support decision making and protect Zurich's reputation and brand. The Risk review describes the Group's risk management framework and risk governance, presents an analysis of its main risks, and reports on capital management and capital adequacy.

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The Risk review is an integral part of the Consolidated financial statements (except for the "Swiss Solvency Test Requirement," "Internal Model Capital Adequacy" and "Conclusion" sections presented on pages 169–177). Certain comparative figures have been restated, as set out in note 1 of the Consolidated financial statements.

Risk review *continued*

Risk management

Mission and objectives of risk management

The mission of risk management at Zurich Insurance Group (Zurich, or the Group) is to promptly identify, measure, manage, report and monitor risks that affect the achievement of strategic, operational and financial objectives. This includes adjusting the risk profile in line with the Group's stated risk tolerance to respond to new threats and opportunities in order to optimize returns.

The Group's major risk management objectives are to:

- Protect the capital base by monitoring that risks are not taken beyond the Group's risk tolerance
- Enhance value creation and contribute to an optimal risk-return profile by providing the basis for an efficient capital deployment
- Support the Group's decision-making processes by providing consistent, reliable and timely risk information
- Protect Zurich's reputation and brand by promoting a sound culture of risk awareness and disciplined and informed risk taking

Risk management framework

In order to achieve its mission and objectives, the Group relies on its risk management framework.

Risk management framework

At the heart of the risk management framework is a governance process with clear responsibilities for taking, managing, monitoring and reporting risks. The Group articulates the roles and responsibilities for risk management throughout the organization, from the Board of Directors and the Chief Executive Officer (CEO) to its businesses and functional areas, thus embedding risk management in the business. See the "Risk governance and risk management organization" section.

To support the governance process, the Group relies on documented policies and guidelines. The Zurich Risk Policy is the Group's main risk governance document; it specifies the Group's risk tolerance, risk limits and authorities, reporting requirements, procedures to approve any exceptions and procedures for referring risk issues to senior management and the Board of Directors. Limits are specified per risk type, reflecting the Group's willingness and ability to take risk, considering earnings stability, economic capital adequacy, financial flexibility and liquidity, franchise value and reputation, the Group's strategic direction and operational plan, and a reasonable balance between risk and return, aligned with economic and financial objectives. The Group regularly enhances the Zurich Risk Policy to reflect new insights and changes in the Group's environment and to reflect changes to the Group's risk tolerance. In 2013, the Zurich Risk Policy was updated and strengthened for various areas, including market risk, project risk, as well as the management of asset/liability risk. Related procedures and risk controls were strengthened or clarified for these areas. As an ongoing process, adherence to requirements stated in the Zurich Risk Policy is assessed.

One of the key elements of the Group's risk management framework is to foster risk transparency by establishing risk reporting standards throughout the Group. The Group regularly reports on its risk profile, current risk issues, adherence to its risk policies and improvement actions both at a local and on a Group level. The Group has procedures in place for the timely referral of risk issues to senior management and the Board of Directors.

Various governance and control functions coordinate to help ensure that objectives are being achieved, risks are identified and appropriately managed and internal controls are in place and operating effectively. This coordination is referred to as "integrated assessment and assurance."

Risk management is not only embedded in Zurich's business but is also aligned with the Group's strategic and operational planning process. The Group assesses risks systematically and from a strategic perspective through its proprietary Total Risk Profiling™ (TRP) process, which allows Zurich to identify and then evaluate the probability of a risk scenario occurring, as well as the severity of the consequences should it occur. The Group then develops, implements and monitors appropriate improvement actions. The TRP process is integral to how Zurich deals with change, and is particularly suited for evaluating strategic risks as well as risks to Zurich's reputation. At Group level this process is performed annually, reviewed regularly and tied to the planning process.

In addition to this qualitative approach, the Group regularly measures and quantifies material risks to which it is exposed. The Zurich Economic Capital Model (Z-ECM) provides a key input into the Group's strategic planning process as it allows an assessment as to whether the Group's risk profile is in line with the Group's risk tolerance. Z-ECM forms the basis for optimizing the Group's risk-return profile by providing consistent risk measurement across the Group. See "Internal model capital adequacy (unaudited)" for more information about the Group's risk tolerance.

The operations relating to Zurich Santander (the long-term alliance with Banco Santander S.A., entered into in 2011) continue to be integrated into the Zurich risk management framework. In addition, these operations continue to leverage their existing internal control system while introducing Zurich's internal control system. In 2013, Zurich Santander began to conduct Total Risk Profiling™ assessments as well as to monitor adherence to the Zurich Risk Policy.

An important element of the Group's risk management framework is a well-balanced and effectively managed remuneration program. This includes a Group-wide remuneration philosophy, robust short- and long-term incentive plans, strong governance and links to the business planning, performance management and risk policies of the Group. Based on the Group's Remuneration Rules, the Board of Directors establishes the structure and design of the remuneration arrangements so that they do not encourage inappropriate risk taking. The Group Chief Risk Officer (Group CRO) consults with the other assurance, control and governance functions to provide the CEO with a review of risk factors to consider in the annual process to determine variable compensation. Also in consultation with these functions, the Group CRO provides an individual assessment of Group Key Risk Takers as part of their annual individual performance assessment. For more information on Zurich's remuneration system, see the "Remuneration report (unaudited)."

Through these processes, responsibilities and policies, Zurich embeds a culture of disciplined risk taking across the Group. The Group continues to consciously take risks for which it expects an adequate return. This approach requires sound judgment and an acceptance that certain risks can and will materialize in the future.

External environment

Various external stakeholders, among them regulators, rating agencies, investors and accounting bodies, place emphasis on the importance of sound risk management in the insurance industry. Zurich monitors developments in the external environment and assesses the impact on the Group's business, the insurance industry, and the communities in which the Group operates.

Regulatory perspective

Regulatory regimes, such as the Swiss Solvency Test in Switzerland and the regulatory principles of Solvency II in the European Union, emphasize a risk-based and economic approach, based on comprehensive quantitative and qualitative assessments and reports.

In 2013, the timeline for the roll-out of Solvency II in the European Union was further specified. The introduction of the complete framework is expected for January 1, 2016. In the context of systemic risk, the Financial Stability Board announced a list of Global Systemically Important Insurers, Zurich not being among them.

See "Analysis of capital adequacy" for more information about regulatory requirements.

Risk review *continued*

Rating-agency perspective

Rating agencies' assessment of an insurance company's risk management is an integral part of their financial strength credit analysis. Standard & Poor's (S&P) has a separate rating for Enterprise Risk Management. S&P's rating for Zurich's overall enterprise risk management is "strong." This reflects its positive view of the Group's risk management culture, risk controls, and strategic and emerging risk management. S&P regards these capabilities as enabling the Group to further optimize capital allocation and earnings.

Economic and geopolitical perspective

In the first half of 2013, after the U.S. fiscal crisis was averted, economic conditions improved in advanced markets. The new leadership in China maintained support for the economy, and there has been a welcome shift in policy towards strengthening domestic demand. Overall, risk assets started the year 2013 on a strong footing, supported by better economic data, reduced political risks and a notable shift in investor sentiment toward these asset classes.

In the second half of 2013, the global recovery appeared to have entered a more robust stage, both in advanced and emerging markets. The economic expansion was supported by continued loose monetary policy, while headwinds from elevated debt levels and fiscal austerity weakened. Geopolitically, the second half of 2013 was dominated by conflicts in the Middle East and North Africa and the situation in the region has remained very volatile.

During 2013, politics in the U.S. and in the Eurozone remained the key risk to the economic outlook. While the risk of a Eurozone breakdown receded, following decisive action from the European Central Bank and the marked improvements in peripheral funding conditions, longer-term uncertainty has remained. A further adjustment of debt and increased competitiveness is required in a number of countries. Also, U.S. fiscal policy remained a concern throughout the year.

External interactions

The Group maintains close working relationship with such stakeholders as external organizations and expert groups.

Zurich is a major contributor to the Global Risk Report that is produced by the World Economic Forum in cooperation with other WEF partners. The report's assessment of the most pressing global risks and the interconnections among them provides valuable information for risk mitigation across the globe. Supporting the report by sharing Zurich's expertise is also part of Zurich's commitment to corporate responsibility.

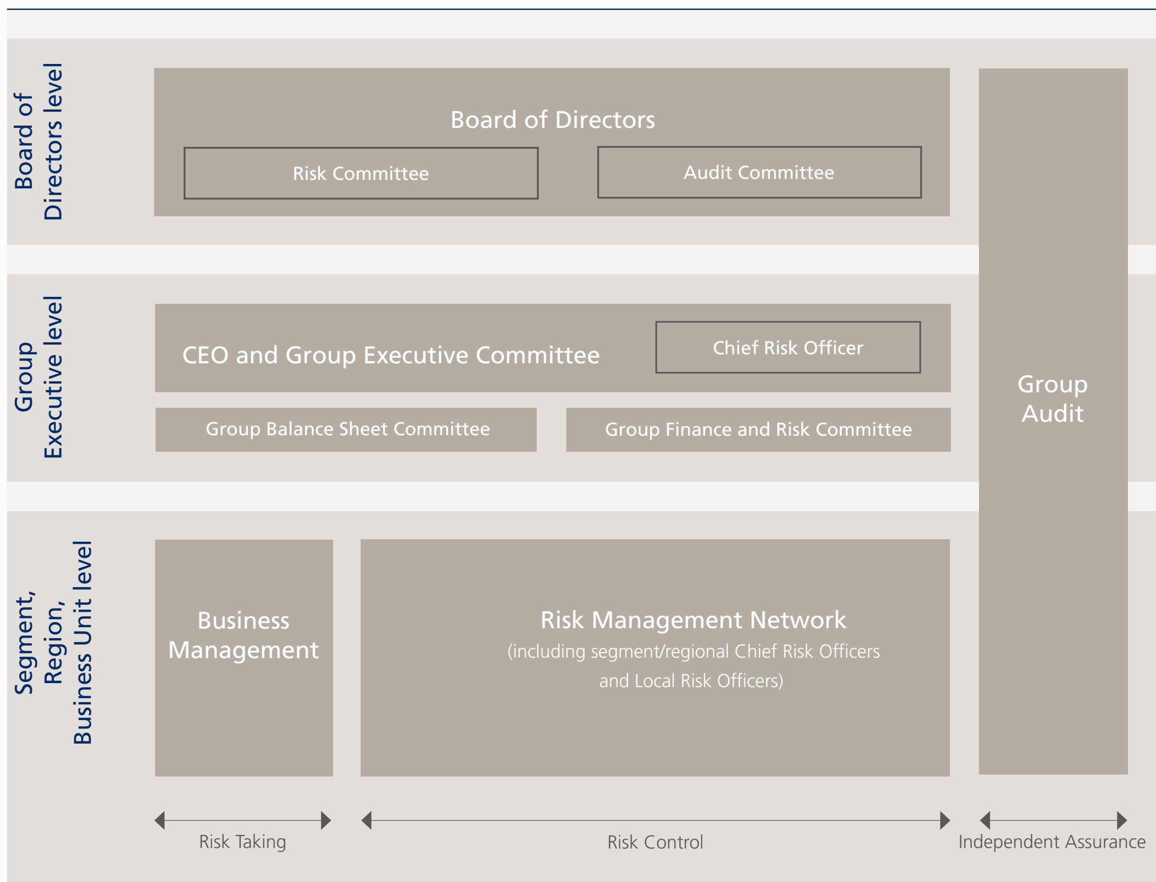
The Group is also involved in a number of international industry organizations engaged in advancing the regulatory dialogue and sound risk management practices. Zurich is a standing member of and actively contributes to the Emerging Risk Initiative of the CRO Forum (an organization composed of the chief risk officers of major insurance companies and financial conglomerates that focuses on developing and promoting insurance industry best practices in risk management).

The Group seeks external expertise from its International Advisory Council and Natural Catastrophe Advisory Council to better understand and assess risks, particularly regarding areas of complex change. For more information on these councils, see the "Corporate governance report (unaudited)." In addition, the Investment Management Advisory Council provides feedback to Investment Management on achieving superior risk-adjusted returns versus liabilities for the Group's invested assets.

Risk governance and risk management organization

The section below gives an overview of the Group's risk governance and risk management organization.

Risk governance overview



The overview above highlights only key elements of the governance framework that specifically relate to risk management.

Board of Directors level

The Board of Directors of Zurich Insurance Group Ltd has ultimate oversight responsibility for the Group's risk management. It establishes the guidelines for the Group's risk management framework and key principles, particularly as articulated in the Zurich Risk Policy, and approves changes to such guidelines and key principles, as well as transactions reaching specified thresholds.

The Risk Committee of the Board serves as a focal point for oversight regarding the Group's risk management, in particular the Group's risk tolerance, including agreed limits that the Board regards as acceptable for Zurich to bear, the aggregation of these limits across the Group, the measurement of adherence to risk limits, and the Group's risk tolerance in relation to anticipated capital levels. The Risk Committee further oversees the Group-wide risk governance framework, including risk management and control, risk policies and their implementation, as well as risk strategy and the monitoring of operational risks. The Risk Committee also reviews the methodologies for risk measurement and the Group's adherence to risk limits. The Risk Committee further reviews, with business management and the Group Risk Management function, the Group's general policies and procedures and satisfies itself that effective systems of risk management are established and maintained. It receives regular reports from Group Risk Management and assesses whether significant issues of a risk management and control nature are being appropriately addressed by management in a timely manner. The Risk Committee assesses the independence and objectivity of the Group Risk Management function, approves its terms of reference, reviews the activities, plans, organization and quality of the function, and reviews key risk management principles and procedures.

Risk review *continued*

To facilitate information exchange between the Audit Committee of the Board and the Risk Committee of the Board, at least one board member is a member of both committees. The Risk Committee met seven times in 2013 (once jointly with the Remuneration Committee).

To foster transparency about risk, the Board receives quarterly risk reports and additional updates. In 2013, reporting was further enhanced. Reports included in-depth risk insights into topics such as the development of new global capital standards and political risks in Latin America as well as emerging risks.

Group Executive level

The CEO, together with the Group Executive Committee (GEC), oversees the Group's performance with regard to risk management and control, strategic, financial and business policy issues of Group-wide relevance. This includes monitoring adherence to and further development of the Group's risk management policies and procedures. The Group Balance Sheet Committee and the Group Finance and Risk Committee regularly review and make recommendations on the Group's risk profile and significant risk-related issues.

The Chief Risk Officer is a member of the GEC and reports directly to the CEO and the Risk Committee of the Board. He is a member of each of the management committees listed below, in order to provide a common and integrated approach to risk management, to allow for appropriate assessment and, where necessary, mitigation of risks identified in these committees.

At a Group level the management committees dealing with risks are:

- Group Balance Sheet Committee (GBSC) – acts as a cross-functional body whose main function is to review and make recommendations regarding the activities that materially affect the balance sheets of the Group and its subsidiaries. The GBSC is charged with setting the annual capital and balance sheet plans for the Group based on the Group's strategy and financial plans, as well as recommending specific transactions or unplanned business changes to the Group's balance sheet. The GBSC has oversight of all main levers of the balance sheet, including capital management, reinsurance, asset/liability management, and liquidity. The GBSC reviews and recommends the Group's overall risk tolerance. It is chaired by the CEO.
- Group Finance and Risk Committee (GFRC) – acts as a cross-functional body for financial and risk management matters in the context of the strategy and the overall business activity of the Group. The GFRC oversees financial implications of business decisions and the effective management of the Group's overall risk profile, including risks related to insurance, financial markets and asset/liability, credit and operational risks as well as their interactions. The GFRC proposes remedial actions based on regular briefings from Group Risk Management on the risk profile of the Group. It reviews and formulates recommendations for future courses of action with respect to potential merger and acquisition (M&A) transactions, changes to the Zurich Risk Policy, internal insurance programs for the Group, material changes to the Group's risk-based capital methodology and the overall risk tolerance. The GFRC is chaired by the Chief Financial Officer, while the Chief Risk Officer acts as deputy.

The management committees rely on output provided by technical committees, including:

- Asset/Liability Management Investment Committee – deals with the Group's asset/liability exposure and investment strategies and is chaired by the Chief Investment Officer.
- General Insurance Global Underwriting Committee – acts as a focal point for underwriting policy and related risk controls for General Insurance and is chaired by the Global Chief Underwriting Officer for General Insurance.
- Group Reinsurance Committee – defines the Group's reinsurance strategy in alignment with the Group's risk framework and is chaired by the Global Head of Group Reinsurance.

Representatives of Group Risk Management are members of all these technical committees.

Group Risk Management organization

The Chief Risk Officer leads the Group Risk Management function, which develops methods and processes for identifying, measuring, managing, monitoring and reporting risks throughout the Group. Group Risk Management proposes changes to the risk management framework and the Group's risk policies; it makes recommendations on the Group's risk tolerance and assesses the risk profile. The Chief Risk Officer is responsible for the oversight of risks across the Group; he regularly reports risk matters to the Chief Executive Officer, senior management committees and the Risk Committee of the Board.

The Group Risk Management organization consists of central functions at Group level and a decentralized risk management network at segment, regional, business unit and functional levels.

At Group level there are two centers of expertise: risk analytics and risk and control. The risk analytics department quantitatively assesses insurance, financial market and asset/liability, credit and operational risks and is the Group's center of excellence for risk quantification and modeling. The risk and control department includes operational risk management, risk reporting, risk governance, and risk operations. The risk management network consists of the Chief Risk Officers (CROs) of the Group's segments and regions, and the Local Risk Officers (LROs) of the business units and functions and their staff. While their primary focus is on operational and business-related risks, they are responsible for providing a holistic view of risk for their area. The risk officers are part of the management teams in their respective businesses and therefore are embedded in the business. The LROs also report to the segment or regional CROs, who in turn report to the Group's Chief Risk Officer. The CROs of the Group's segments and regions are members of the leadership team of the Group's Chief Risk Officer.

In addition to the risk management network, the Group has audit and oversight committees at the major business and regional levels. The committees are responsible for providing oversight of the risk management and control functions. This includes monitoring adherence to policies and periodic risk reporting. At the local level, these oversight activities are conducted through risk and control committees or quarterly meetings between senior executives and the local heads of governance functions.

Risk review *continued*

Analysis by risk type

Risk type description

In order to enable a consistent, systematic and disciplined approach to risk management, Zurich categorizes its main risks as follows:

- Strategic – unintended risk that can result as a by-product of planning or executing the strategy
- Insurance – risk associated with the inherent uncertainty regarding the occurrence, amount or timing of insurance liabilities
- Market – risk associated with the Group's balance sheet positions where the value or cash flow depends on financial markets
- Credit – risk associated with a loss or potential loss from counterparties failing to fulfill their financial obligations
- Liquidity – risk that the Group does not have sufficient liquidity to meet its obligations when they fall due, or would have to incur excessive costs to do so
- Operational – risk associated with the people, processes and systems of the Group, and external events such as outsourcing, catastrophes, legislation, or external fraud
- Reputation – risk that an act or omission by the Group or any of its employees could result in damage to the Group's reputation or loss of trust among its stakeholders

The Zurich Economic Capital Model quantifies the internal capital for insurance, market, credit and operational risks. See "Internal model capital adequacy (unaudited)" for more information.

Strategic risk

Strategic risk corresponds to the unintended risk that can result as a by-product of planning or executing the strategy. A strategy is a long term plan of action designed to allow the Group to achieve its goals and aspirations. Strategic risks can arise from:

- Inadequate assessment of strategic plans
- Improper implementation of strategic plans
- Unexpected changes to assumptions underlying strategic plans

Risk considerations are a key element in the strategic decision-making process. The Group assesses the implications of strategic decisions on risk-based return measures and risk-based capital in order to optimize the risk-return profile and to take advantage of economically profitable growth opportunities as they arise.

The Group works on reducing the unintended risks of strategic business decisions through its risk assessment processes and tools, including the Total Risk Profiling™ process. The Group Executive Committee regularly assesses key strategic risk scenarios for the Group as a whole, including scenarios for emerging risks and their strategic implications.

The Group specifically evaluates the risks of M&A transactions both from a quantitative and a qualitative perspective. The Group conducts risk assessments of M&A transactions to evaluate risks specifically related to the integration of acquired businesses.

Insurance risk

Section highlights
- In 2013, the Group restructured its reinsurance covers for natural catastrophe events. While the retention for the regional catastrophe treaties was increased, the co-participation was reduced to 10 percent.
- The cession rate for both General Insurance and Global Life remained stable. Due to its strong balance sheet, Zurich is able to structure and align its reinsurance programs to achieve an optimum risk/reward ratio.

Insurance risk is the inherent uncertainty regarding the occurrence, amount or timing of insurance liabilities. The exposure is transferred to Zurich through the underwriting process. Zurich actively seeks to write those risks it understands and that provide a reasonable opportunity to earn an acceptable profit. As Zurich assumes certain customer risks, it aims to manage that transfer of risk, and minimize unintended underwriting risks, through such means as:

- Establishing limits for underwriting authority
- Requiring specific approvals for transactions involving new products or, where established, limits of size and complexity may be exceeded
- Using a variety of reserving and modeling methods to address the various insurance risks inherent in the Group's insurance business
- Ceding insurance risk through proportional, non-proportional and facultative reinsurance treaties. The Group centrally manages reinsurance treaties.

General insurance risk

General insurance risk includes the reasonable possibility of significant loss due to uncertainty in the frequency of the occurrence of the insured events as well as in the severity of the resulting claims. The following provides an overview of the Group's main lines of business:

- Motor includes automobile physical damage, loss of the insured vehicle and automobile third party liability insurance.
- Property includes fire risks (for example fire, explosion and business interruption), natural perils (for example earthquake, windstorm and flood), engineering lines (for example boiler explosion, machinery breakdown and construction) and marine (cargo and hull).
- Liability includes general/public and product liability, excess and umbrella liability, professional liability including medical malpractice, and errors and omissions liability.
- Special lines include directors and officers, credit and surety, crime and fidelity, accident and health, and crop.
- Worker injury includes workers compensation and employers liability.

The Group's underwriting strategy is to take advantage of the diversification of general insurance risks across lines of business and geographic regions. The Group seeks to optimize shareholder value by achieving its mid-term return on equity goals. Doing so necessitates a prudent, stable underwriting philosophy that aims to take advantage of its competitive strengths while avoiding risks with disruptive volatility. At the core of the Group's underwriting is a robust governance process. The Group's four major processes for underwriting governance – underwriting strategy, authorities, referrals and reviews – are implemented at Group and local levels.

A fundamental component of managing insurance risk is underwriting discipline. The Group sets limits on underwriting capacity, and cascades authority to individuals based on their specific expertise. The Group sets appropriate pricing guidelines with a focus on consistent technical pricing across the organization. As part of these guidelines, the Group requires the setting of a technical price according to common standards. The technical price is set in a way that allows a return on risk-based capital in line with the Group's target. The ratio of actual premium to technical price is a key performance metric, which is monitored regularly. Technical reviews confirm whether underwriters perform within authorities and adhere to underwriting philosophies and policies. The Group's global line of business networks share best practices across the globe, providing additional guidance and governance. The Group has governance procedures to review and approve potential new products to evaluate whether the risks are well understood and justified by the potential rewards.

The Group faces the risk that actual losses emerging on claims provisions may be higher than anticipated. Because of this uncertainty, general insurance reserves are regularly measured, reviewed and monitored. The total loss and loss

Risk review *continued*

adjustment expense reserves are based on work performed by qualified and experienced actuaries at the local, regional and Group level.

To arrive at their reserve estimates, the actuaries take into consideration, among other things, the latest available facts, historical trends and patterns of loss payments, exposure growth, court decisions, economic conditions, in particular inflation, and public attitudes that may affect the ultimate cost of settlement. Inflation is monitored on a country basis; the monitoring process relies on both Zurich's economic view on inflation and specific claims activity, and feeds into actuarial models and Zurich's underwriting processes such as technical price reviews.

In most instances, these actuarial analyses are conducted at least twice a year for on-going business according to agreed timetables. Analyses are performed by product line, type and extent of coverage and year of occurrence. The Group has reserve committees to facilitate communications and reporting regarding reserve opinions. A series of reserve committees feed from the local level to regions and segments and into a Group reserve committee, where the Group's total loss and loss adjustment expense reserves are consolidated and recommended for approval by Group management. As with any projection, there is an inherent uncertainty in the estimation of claim reserves due to the fact that the ultimate liability for claims will be impacted by trends as yet unknown, including future changes in the likelihood of claimants bringing suit, the size of court awards, and the attitudes of claimants toward settlement of their claims.

The Group closely monitors potential new emerging risk exposures. Zurich has an Emerging Risk Group, with cross-functional expertise from core insurance functions such as underwriting, claims and risk in order to identify, assess and recommend actions for such risks.

In addition to the specific risks insured, each line of business could expose the Group to losses that could arise from natural and man-made catastrophes. The main concentrations of risks arising from such potential catastrophes are regularly reported to senior management. The most important peril regions and risks are United States and Caribbean tropical cyclone, Europe windstorm and California earthquake, as well as potential terrorism exposures.

Tables 1.a and 1.b show the Group's concentration of risk within the General Insurance business by region and line of business based on direct written premiums before reinsurance. The Group's exposure to general insurance risks varies significantly by geographic region and may change over time. General insurance premiums ceded to reinsurers (including retrocessions) amounted to USD 6.0 billion and USD 5.9 billion for the years ended December 31, 2013 and 2012, respectively. Reinsurance programs such as catastrophe covers are managed on a global basis, and therefore, net premium after reinsurance is monitored on an aggregated basis.

General Insurance – Direct written premiums and policy fees by line of business and by region – current period

Table 1.a

in USD millions, for the year ended December 31, 2013	Motor	Property	Liability	Special lines	Worker injury	Total
North America	1,414	3,501	3,454	1,695	2,558	12,621
Europe	5,827	4,657	2,441	2,067	467	15,458
Other regions[1]	2,505	1,938	480	1,045	193	6,161
Total	**9,746**	**10,095**	**6,376**	**4,806**	**3,217**	**34,240**

[1] Including intercompany eliminations

General Insurance – Direct written premiums and policy fees by line of business and by region – prior period

Table 1.b

in USD millions, for the year ended December 31, 2012	Motor	Property	Liability	Special lines	Worker injury	Total
North America	1,372	3,225	3,313	1,628	2,463	12,000
Europe	5,854	4,613	2,400	2,029	437	15,333
Other regions[1]	2,364	1,943	462	1,114	176	6,060
Total	**9,590**	**9,782**	**6,175**	**4,771**	**3,075**	**33,393**

[1] Including intercompany eliminations

Sensitivities analysis for general insurance risk

Tables 2.a and 2.b show the sensitivity of net income before tax and the sensitivity of net assets, using the Group effective income tax rate, as a result of adverse development in the net loss ratio by one percentage point. Such an increase could arise from either higher frequency of the occurrence of the insured events or from an increase in the severity of resulting claims or from a combination of frequency and severity. The sensitivities do not indicate a probability of such an event and do not consider any non-linear effects of reinsurance. Based on the assumptions applied in the presentation of the sensitivity analysis in tables 2.a and 2.b, each additional percentage point increase in the loss ratio would lead to a linear impact on net income before tax and net assets. In addition, the Group monitors insurance risk by evaluating extreme scenarios, taking into account non-linear effects of reinsurance contracts.

Table 2.a

Insurance risk sensitivity for the General Insurance business – current period

in USD millions, for the year ended December 31, 2013	Global Corporate	North America Commercial	Europe	International Markets
+1% in net loss ratio				
Net income before tax	(61)	(76)	(116)	(45)
Net assets	(46)	(57)	(87)	(34)

Table 2.b

Insurance risk sensitivity for the General Insurance business – prior period

in USD millions, for the year ended December 31, 2012	Global Corporate	North America Commercial	Europe	International Markets
+1% in net loss ratio				
Net income before tax	(55)	(76)	(118)	(43)
Net assets	(41)	(57)	(88)	(32)

Modeling natural catastrophes

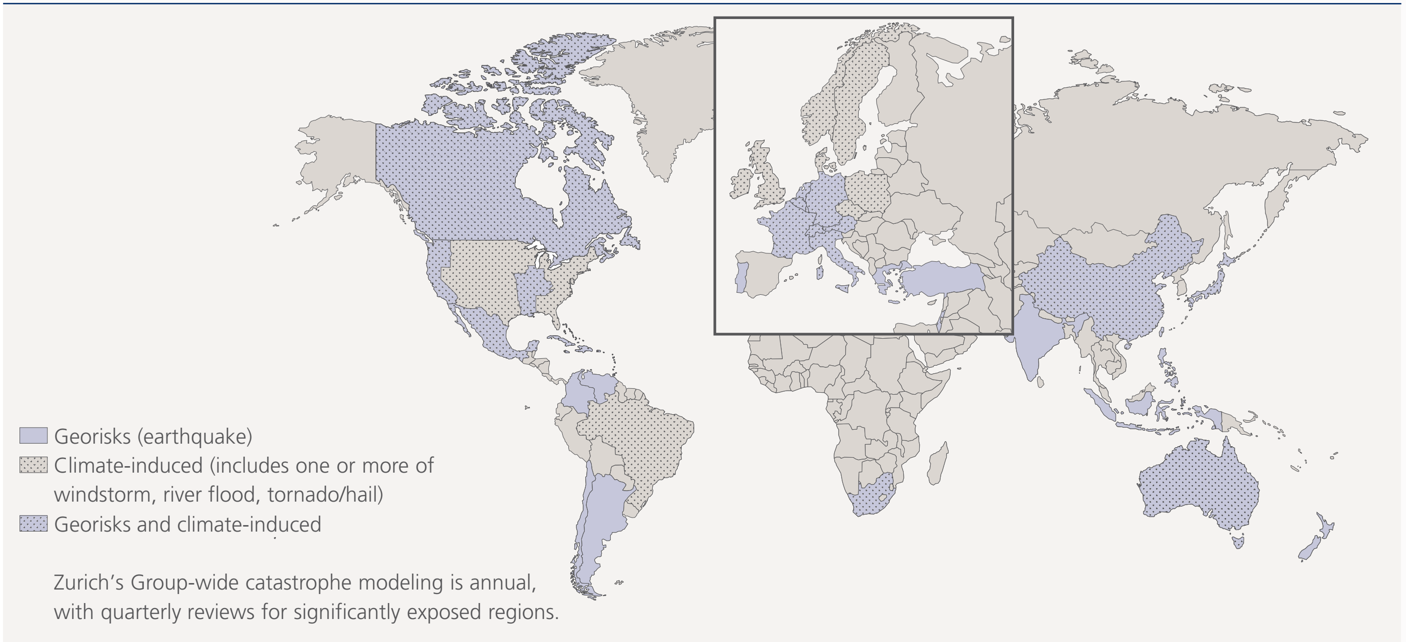
Understanding the potential effects of natural catastrophes is a critical component of risk management for general insurance. While specific catastrophes are unpredictable, modeling helps to determine potential losses should catastrophes occur. The Group uses a combination of third-party and in-house models to manage its underwriting and accumulations in modeled areas to stay within intended exposure limits and to guide the levels of reinsurance Zurich buys.

The Group models exposures in a center of excellence for consistency in approach and to form a global perspective on accumulations. The center of excellence works with the local businesses to help improve the overall quality of data, by analyzing and comparing data quality levels, providing priorities for data quality improvements and supporting implementation with advice and external data, where required. The Group models potential losses from property policies located in hazard-prone areas with material exposure and from workers' compensation policies covering earthquakes in California. Other non-property related losses are quantified based on adjustments. The risk modelling principally addresses climate-induced perils such as windstorms, river floods, tornadoes and hail, and geologically induced perils such as earthquakes. The Group constantly seeks to improve its modeling, fill in gaps in models with additional assessments and increase the granularity of data collection in order to enhance the accuracy and utility of the information.

With an expanded catastrophe research and development team, the Group continues to improve the "Zurich view" of catastrophe risk by using output from multiple catastrophe models, by using internal and external expertise, for instance through the Natural Catastrophe Advisory Council, a group of scientists associated with research organizations such as the U.S. National Center for Atmospheric Research, the United States Geological Survey and the Intergovernmental Panel on Climate Change. Zurich further validates modeling results through comparisons with claims experience. In addition, Zurich continues its effort to extend assessments by evaluating potential non-modeled catastrophe hotspots and including appropriate modeling or loadings for non-modeled lines.

Risk review *continued*

Peril regions assessed for 2013



Risks from man-made catastrophes

Man-made catastrophes include such risks as industrial accidents and terrorism attacks. Zurich's experience in monitoring potential exposures from natural catastrophes is also applicable to threats posed by man-made catastrophes, particularly terrorism.

The Group reviews and aggregates worker injury and property exposures to identify areas of significant concentration. The Group also assesses other lines of business, such as liability and auto, although the potential exposure is not as significant. The resulting data allows underwriters to evaluate how insuring a particular customer's risk might affect Zurich's overall exposure. In North America, Zurich uses a vendor-provided catastrophe model to evaluate potential exposures in every major U.S. city. The Group undertakes more detailed and frequent analytics for cities in which Zurich has greater exposure, and continues to refine its reporting about such risks.

Although the Group's analysis has shown its exposures outside North America are lower, in large part due to government-provided pools; the Group has extended its approach to improve its view of the risk for countries with the next greatest potential net exposure. The Group periodically monitors accumulation limits for these and other areas, and continues to refine its analytics.

Life insurance risk

The risks associated with life insurance include:

- Mortality – risk that actual policyholder death experience on life insurance policies is higher than expected.
- Longevity – risk that annuitants live longer than expected.
- Morbidity – risk that policyholder health-related claims are higher than expected.
- Policyholder behavior – risk that policyholders' behavior in discontinuing and reducing contributions or withdrawing benefits prior to the maturity of contracts is worse than expected. Poor persistency rates may lead to fewer policies remaining on the books to defray future fixed expenses and therefore reduce the future positive cash flows from the business written, potentially impacting its ability to recover deferred acquisition expenses.
- Expense – risk that expenses incurred in acquiring and administering policies are higher than expected.
- Market – risk associated with the Group's balance sheet positions where the value or cash flow depends on financial markets, which is analyzed in the "Market risk" section.
- Credit – risk associated with a loss or potential loss from counterparties failing to fulfill their financial obligations, which is analyzed in the "Credit risk" section.

A more diversified portfolio of risks is less likely to be affected across the board by a change in any subset of the risks. As a result, the offsetting effects between unit-linked and traditional business reduce some of the risk associated with the Global Life business.

The Group has local product development committees and a Group-level product approval committee, under the leadership of the Global Life Chief Risk Officer, for potential new life products that could significantly increase or change the nature of its risks. Such reviews allow Zurich to manage new risks inherent in its new business propositions. The Group regularly reviews the continued suitability and the potential risks of existing life products.

The Group's use of market-consistent embedded value reporting principles allows Zurich to further understand and report on the risk profile of its life products and how risks would change in differing market conditions. Embedded value is the measure that markets use to value life businesses. For more information, see the "Embedded value report."

From a risk-management perspective, unit-linked products have been designed in order to reduce much of the market and credit risk associated with traditional business for the Group. Those risks inherent in these products are largely passed on to the policyholder, although a portion of the Group's management fees are linked to the value of funds under management and hence are at risk if the fund values decrease. Unit-linked products carry mortality/morbidity risk and market risk to the extent that there are guarantees built into the product design. Contracts may have minimum guaranteed death benefits where the sum at risk depends on the fair value of the underlying investments. For certain contracts these risks are mitigated by explicit mortality and morbidity charges.

Other life insurance liabilities include traditional life insurance products, which include protection products and life annuity products. Protection products carry mortality, longevity and morbidity risk as well as market and credit risk. The most significant factors that could increase the frequency of mortality claims are epidemics, such as strains of influenza, or lifestyle changes such as eating, drinking and exercise habits, resulting in earlier or more claims than expected. Morbidity claims experience would not only be affected by the factors mentioned above, but because disability is defined in terms of the ability to perform an occupation, it could also be affected by economic conditions. In order to reduce cross-subsidies in the pricing basis, premiums are differentiated, where permitted, for example by product, age, gender and smoker status. The policy terms and conditions and the disclosure requirements contained in insurance applications are designed to mitigate the risk arising from non-standard and unpredictable risks that may result in severe financial loss.

In the life annuity business, the most significant insurance risk is continued medical advances and improvement in social conditions that lead to increases in longevity. Annuitant mortality assumptions include allowance for future mortality improvements.

In addition to the specific risks listed above, the Group is exposed to policyholder behavior and expense risks. Policyholder behavior risk is mitigated by product designs that match revenue and expenses associated with the contract as closely as possible. Expense risk is mitigated by careful control of expenses and by regular expense analyses and allocation exercises.

Risk review *continued*

Certain life insurance contracts contain guarantees for which liabilities have been recorded for additional benefits and minimum guarantees. These arise primarily in the subsidiary Zurich American Life Insurance Company (ZALICO) which in the past wrote variable annuity contracts that provide policyholders with certain guarantees related to minimum death and income benefits. After 2001, ZALICO no longer issued new policies with such features. The Group has a dynamic hedging strategy to manage its economic exposure and reduce the volatility associated with its closed book of variable annuities products within its U.S. life business. New Life products developed with financial guarantees are subject to review and approval by the Group-level product approval committee. The Group is also exposed to risks arising out of Bank Owned Life Insurance contracts sold in the U.S. See heading "other contracts" in note 7 of the Consolidated financial statements for additional information.

The Group defines concentration risk in the Global Life business as the risk of exposure to increased losses associated with inadequately diversified portfolios of assets or obligations. Concentration risk for a life insurer may arise with respect to investments in a geographical area, economic sector, or individual issuers, or due to a concentration of business written within a geographical area, of a policy type, or of underlying risks covered.

Zurich is exposed to two main types of concentration risk in its Global Life business:

- From a market risk perspective, interest rate guarantees in Germany and Switzerland expose Zurich to financial losses that may arise as a result of adverse movements in interest rates. The Group also wrote a small book of variable annuity business in the U.S. with minimum guaranteed death benefits, but ceased writing new business in 2012. The management of these guarantees is a combination of asset-liability matching and hedging; see the "Market risk" section.
- From an insurance risk perspective, the main factors that would affect concentration risk include mortality risk, morbidity risk, longevity risk, policyholder behavior risk (lapse, anti-selection) and expense risk. There is diversification across geographical regions, lines of business and even across the different insurance risk factors such that Zurich is not exposed to significant concentrations of insurance risk.

Table 3 shows the Group's concentration of risk within the life business by region and line of business based on reserves for life insurance on a net basis. The Group's exposure to life insurance risks varies significantly by geographic region and line of business and may change over time. See note 8 of the Consolidated financial statements for additional information on reserves for insurance contracts.

Reserves, net of reinsurance, by region

Table 3

in USD millions, as of December 31	Unit-linked insurance contracts		Other life insurance liabilities		Total reserves	
	2013	2012	**2013**	2012	**2013**	2012
Global Life						
North America	730	627	5,473	5,307	6,204	5,934
Latin America	9,416	10,256	5,336	5,204	14,751	15,460
Europe	48,939	47,979	82,007	80,468	130,945	128,447
United Kingdom	26,452	28,719	5,001	5,200	31,453	33,919
Germany	13,437	11,095	43,728	43,084	57,165	54,179
Switzerland	767	708	20,074	19,741	20,841	20,450
Ireland	2,660	1,731	1,971	1,727	4,631	3,458
Spain	4,737	4,808	6,189	5,981	10,926	10,789
Rest of Europe	885	918	5,044	4,734	5,929	5,652
Asia-Pacific and Middle East	3,927	3,371	2,860	3,035	6,787	6,406
Other	16	10	350	284	366	294
Eliminations	–	–	–	4	–	4
Subtotal	**63,028**	62,243	**96,025**	94,302	**159,053**	156,545
Other segments[1]	11,844	11,874	4,076	4,915	15,921	16,789
Total	**74,873**	74,117	**100,101**	99,217	**174,974**	173,334

[1] See note 28 of the Consolidated financial statements for additional information on the Group's segments.

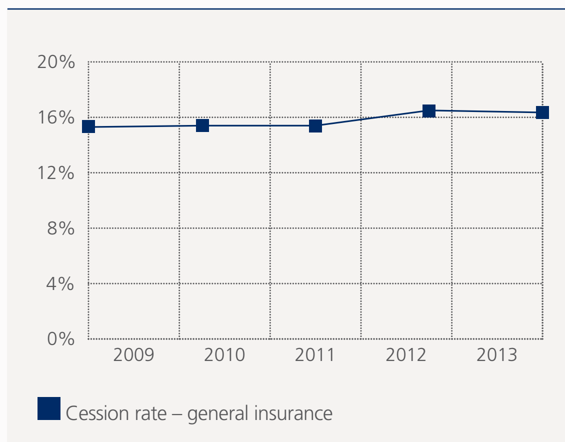
Sensitivities analysis for life insurance risk
The Group reports sensitivities for the Global Life business on Embedded Value and New Business Value to changes in economic and operating risk factors. The operating factors include discontinuance rates, expenses, mortality and morbidity. The embedded value methodology adopted by the Group is based on a market-consistent approach to allow explicitly for market risks. See the "Embedded value report" for more information on the sensitivities for the Global Life business to economic and operating risk factors.

Reinsurance for general insurance and life insurance

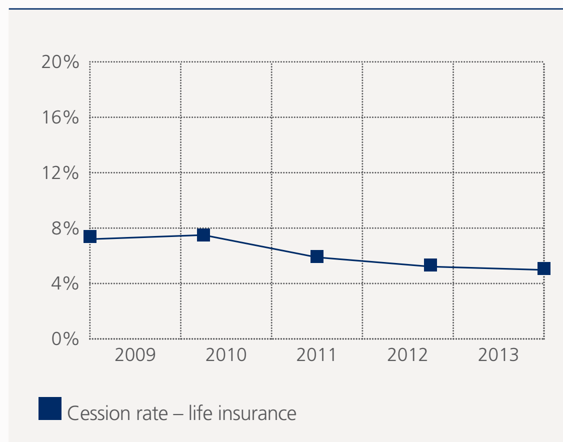
The Group's objectives for purchasing reinsurance are to provide market-leading capacity for customers while protecting the balance sheet and optimizing the Group's capital efficiency. The Group follows a centralized purchasing strategy for both segments, General Insurance and Global Life, and bundles programs, where appropriate, to benefit from diversification and economies of scale. These efforts for General Insurance have led to a decreasing expenditure for treaty reinsurance while growth in the General Insurance Global Corporate business has increased premium cessions to captives and co-reinsurers, resulting in an overall stable cession rate.

Due to its strong balance sheet, Zurich is able to structure and align its reinsurance programs to achieve an optimum risk/reward ratio. Zurich manages its central reinsurance purchasing according to these principles. The Group is therefore able to manage its risks to retain a significant and stable portion of its gross written premiums, as shown in the charts below.

Ceded premium – trend
(% of general insurance gross written premiums ceded to reinsurers)



Ceded premium – trend
(% of life insurance gross written premiums ceded to reinsurers)



The Group continues to use traditional reinsurance markets and other alternatives, such as catastrophe bonds, to protect against extreme single events and increased frequency of events. The Group is able to use its global reach in particular for catastrophe protection. It has in place a combination of per event and annual aggregate covers, which protects the Group's business both per event and by region, and also for multiple events across regions. This helps to reduce the risks posed by the frequency of catastrophes, as well as their severity.

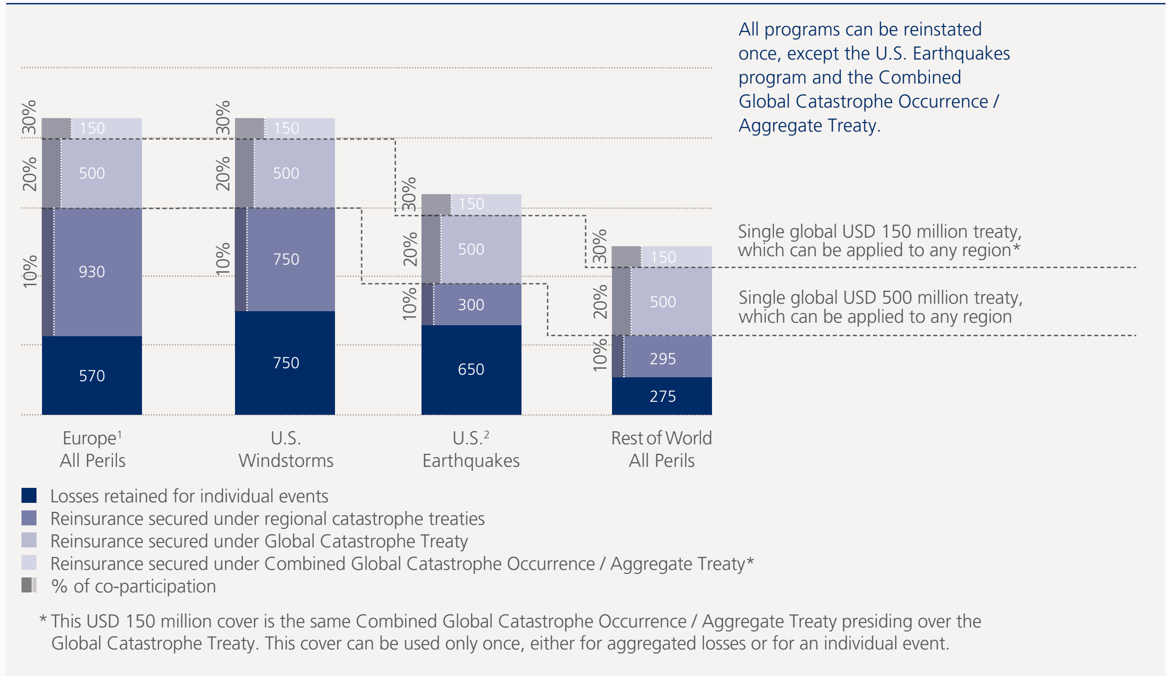
The Group uses reinsurance to manage risk to unusually severe or unusually frequent events, as illustrated on the following page, through the main in-force reinsurance covers as of December 31, 2013 for natural catastrophe events.

The Group participates in the underlying risks through its retention and through its co-participation in the excess layers. The contracts are on a loss-occurrence basis except the aggregate catastrophe cover Lakeside Re III Cat bond which operate on an annual aggregate basis. In addition to these covers, the Group has per risk programs, local catastrophe covers, a bilateral risk swap and a catastrophe bond in place. These covers are reviewed continuously and are subject to change going forward. The current covers are placed annually: January 1 for the U.S. Program and the Global Aggregate Catastrophe Cover; April 1 for the European Program and July 1 for the Rest of the World Program.

In 2013, the Group restructured its reinsurance covers for natural catastrophe events. While the retention for the regional catastrophe treaties was increased, the co-participation was reduced to 10 percent. A new Global Catastrophe Treaty covering extreme single events and a Combined Global Catastrophe Occurrence / Aggregate Treaty covering either aggregate losses or individual large events have been put in place.

Risk review *continued*

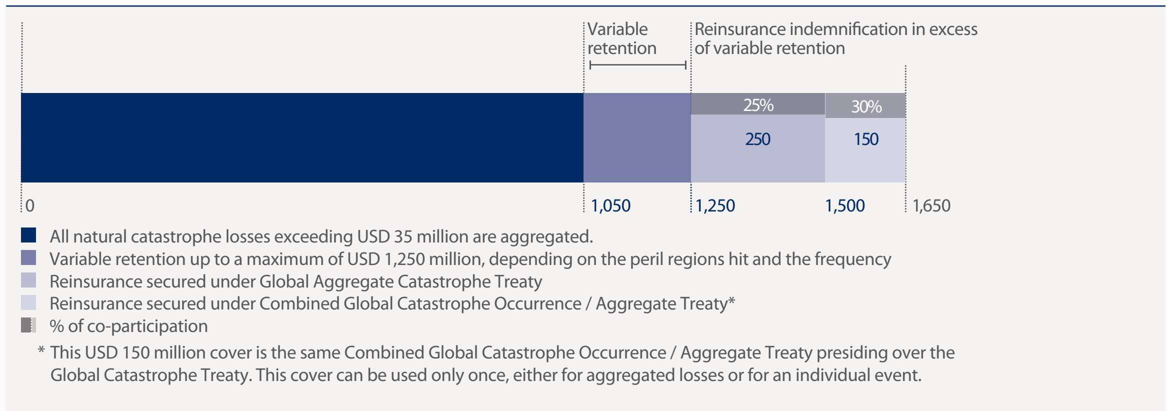
Reinsurance for natural catastrophes by region – unusually severe catastrophe events
(in USD millions, as of December 31, 2013)



* This USD 150 million cover is the same Combined Global Catastrophe Occurrence / Aggregate Treaty presiding over the Global Catastrophe Treaty. This cover can be used only once, either for aggregated losses or for an individual event.

[1] Original cover is in EUR. Conversion rate EUR/USD 1.345 has been applied to calculate the corresponding USD amount.
[2] Lakeside Re III - Cat Bond

Reinsurance for natural catastrophes, aggregated – unusually frequent catastrophe events
(in USD millions, as of December 31, 2013)



* This USD 150 million cover is the same Combined Global Catastrophe Occurrence / Aggregate Treaty presiding over the Global Catastrophe Treaty. This cover can be used only once, either for aggregated losses or for an individual event.

Market risk

Section highlights

- The Group has slightly increased its investments in equity markets, in particular in the second part of the year, as the financial markets continued to recover. Risks from interest rates and credit spreads have remained stable.

Market risk is the risk associated with the Group's balance sheet positions where the value or cash flow depends on financial markets. Fluctuating risk drivers resulting in market risk include:

- Equity market prices
- Real estate market prices
- Interest rates and credit spreads
- Currency exchange rates

The Group manages the market risk of assets relative to liabilities on an economic total balance sheet basis. It strives to maximize the economic risk-adjusted excess return of assets relative to the liability benchmark taking into account the Group's risk tolerance as well as local regulatory constraints.

The Group has policies and limits to manage market risk. It aligns its strategic asset allocation to its risk-taking capacity. Zurich centralizes management of certain asset classes to control aggregation of risk, and provides a consistent approach to constructing portfolios and selecting external asset managers. It also diversifies portfolios, investments and asset managers. Zurich regularly measures and manages market risk exposure. The Group has established limits on concentration in investments by single issuers and certain asset classes as well as deviations of asset interest rate sensitivities from liability interest rate sensitivities, and the Group limits investments that are illiquid.

The Group Balance Sheet Committee reviews and recommends the Group's capital allocation to market risk, while the Asset/Liability Management Investment Committee reviews and monitors the Group's strategic asset allocation and tactical boundaries and monitors the Group's asset/liability exposure. The Group oversees the activities of local Asset/Liability Management Investment Committees and regularly assesses market risks both at a Group and at a local business level. Risk assessment includes quantification of the contributions to financial market risk from major risk drivers. The economic effect of potential extreme market moves is regularly examined and considered when setting the asset allocation.

Risk assessment reviews include the analysis of the management of interest rate risk for each major maturity bucket and adherence to the aggregate positions with risk limits. The Group applies processes to manage market risks and to analyze market risk hotspots. Risk mitigation actions are taken if necessary to manage fluctuations affecting asset/liability mismatch and risk-based capital.

The Group uses derivative financial instruments to limit market risks arising from changes in currency exchange rates, interest rates and equity prices, from credit quality of assets and liabilities and commitments to third parties. The Group enters into derivative financial instruments mostly for economic hedging purposes and, in limited circumstances, the instruments may also meet the definition of an effective hedge for accounting purposes. The latter include cross-currency interest rate swaps in fair value hedges and cross-currency swaps in cash flow hedges of Zurich's borrowings, in order to mitigate exposure to foreign currency and interest rate risk. In compliance with Swiss insurance regulation, the Group's policy prohibits speculative trading in derivatives, meaning a pattern of "in and out" activity without reference to an underlying position. Derivatives are complex financial transactions; therefore, the Group addresses the risks arising from derivatives through a stringent policy that requires approval of a derivative program before transactions are initiated, and by subsequent regular monitoring by Group Risk Management of open positions and annual reviews of derivative programs.

For more information on the Group's investment result, including impairments and the treatment of selected financial instruments, see note 6 of the Consolidated financial statements. For more information on derivative financial instruments and hedge accounting, see note 7 of the Consolidated financial statements.

Risk review *continued*

Risk from equity securities and real estate

The Group is exposed to various risks resulting from price fluctuations on equity securities and real estate. Risks arising from equity securities and real estate could affect the Group's liquidity, reported income, surplus and regulatory capital position. The exposure to equity risk includes common stocks, including equity unit trusts, common stock portfolios backing participating-with-profit policyholder contracts, and equities held for employee benefit plans. The exposure to real estate risk includes direct holdings in real estate, listed real estate company shares and funds, as well as real estate debt securities such as commercial and residential mortgages, commercial and residential mortgage-backed securities and mezzanine debt. Returns on unit-linked contracts, whether classified as insurance or investment contracts, may be exposed to risks from equity and real estate, but these risks are borne by policyholders. However, the Group is indirectly exposed to market movements from unit-linked contracts both with respect to earnings and with respect to economic capital. Market movements impact the amount of fee income earned when the fee income level is dependent on the valuation of the asset base. Therefore, the value of in-force business for unit-linked business can be negatively impacted by adverse movements in equity and real estate markets.

The Group manages its risks from equity securities and real estate as part of the overall investment risk management process, and applies limits as expressed in policies and guidelines. Specifically, Zurich has limits for holdings in equities, real estate and alternative investments.

For additional information on equity securities and real estate held for investment, see note 6 of the Consolidated financial statements.

Risk from interest rate and credit spread

Interest rate risk is the risk of loss resulting from changes in interest rates, including changes in the shape of yield curves. The Group is exposed to interest rate risk including from debt securities, reserves for insurance contracts, liabilities for investment contracts, employee benefit plans and loans and receivables. Changes in interest rates affect the Group's held-to-maturity floating-rate debt securities and unhedged floating-rate borrowings through fluctuations in interest income and interest expense. Changes in interest rates affect the Group's held-for-trading debt securities and fair value hedged borrowings through periodic recognition of changes in their fair values through the income statement. Changes in interest rates affect the Group's available-for-sale debt securities through periodic recognition of changes in their fair values through shareholders' equity. Zurich has limits on holdings in real assets and limits on deviations of asset interest rate sensitivities from liability interest rate sensitivities. The Group also manages credit spread risk, which describes the sensitivity of the values of assets and liabilities due to changes in the level or the volatility of credit spreads over the risk-free interest rate yield curves.

Returns on unit-linked contracts, whether classified as insurance or investment contracts, are at the risk of the policyholder; however, the Group is exposed to fluctuations in interest rates in so far as they impact the amount of fee income earned if the fee income level is dependent on the valuation of the asset base.

Risk management initiatives during 2013

The Group unwound part of its euro receiver swaptions program in the first half of 2013 following the decrease in interest rate exposure in its German life business. The Group has slightly increased its investments in equity markets, in particular in the second part of the year, as the financial markets continued to recover. Risks from interest rates and credit spread have remained stable.

Analysis of market risk sensitivities

Basis of presentation – General Insurance and rest of the businesses

The basis of the presentation below is an economic valuation represented by the fair value for Group investments, IFRS insurance liabilities discounted at risk-free market rates (the Group describes risk-free market rates as swap rates) to reflect the present value of insurance liability cash flows and other liabilities, for example own debt. In the sensitivities, own debt does not include subordinated debt, which Zurich considers available to protect policyholders in a worst-case scenario.

Tables 4.a, 4.b, 6.a and 6.b show the estimated economic market risk sensitivities of Group investments, including real estate for own use, liabilities, including insurance and financial liabilities, and the net impact for General Insurance and the rest of the businesses. Positive values represent an increase of the balance, whereas values in parentheses represent a decrease of the balance. Mismatches in changes in value of assets relative to liabilities represent an economic risk to the Group. The net impact is the difference between the impact on Group investments and liabilities. It represents the economic risk the Group faces related to changes in market risk factors.

In determining the sensitivities, investments and liabilities are fully re-valued in the given scenarios. Each instrument is re-valued separately taking the relevant product features into account. Non-linear effects, where they exist, are reflected in the model. The sensitivities are shown after tax. They do not include the impact of Group-internal transactions.

Tables 6.a and 6.b show sensitivities for the rest of the businesses include Farmers, Other Operating Businesses and Non-Core Businesses. Where Non-Core Businesses includes business with life insurance characteristics, the analysis is based on market-consistent embedded value market risk sensitivities. See the "Embedded value report" for more details on the market risk sensitivities specifications.

Limitations of the analysis:

- The sensitivity analysis does not take into account actions that might be taken to mitigate losses. This strategy may involve changing the asset allocation, for example through selling and buying assets.
- The sensitivities show the effects of a change of certain risk factors, while other assumptions remain unchanged.
- The interest rate scenarios assume a parallel shift of all interest rates in the respective currencies. They do not take into account the possibility that interest rate changes might differ by rating class; these are disclosed separately as credit spreads risk sensitivities.
- The equity market scenarios assume a concurrent movement of all stock markets.
- The sensitivities do not indicate a probability of such events occurring in the future. They do not necessarily represent the Group's view of expected future market changes. In addition to the sensitivities, management uses stress scenarios to assess the impact of more severe market movements on the Group's financial condition. For more information on stress scenarios, see table "Sensivities for the Z-ECM ratio (unaudited)".
- The sensitivity analysis is based on economic net assets, and not on shareholders' equity or net income as set out in the Consolidated financial statements.
- The sensitivity analysis is calculated after tax; the Group effective tax rate is 24.9 percent for 2013 and 24.7 percent for 2012.

Basis of presentation – Global Life

Tables 5.a and 5.b show the estimated economic sensitivity of the Embedded Value of the Global Life business to financial market movements. In modeling these exposures, where appropriate, allowance has been made for dynamic actions that would be taken by management or by policyholders. For contracts with financial options and guarantees, such as some participating business, movements in financial markets can change the nature and value of these benefits. The dynamics of these liabilities are captured so that this exposure is quantified, monitored, managed and where appropriate, mitigated.

Limitations of the analysis:

- The sensitivities show the effects of a change in certain risk factors, while other assumptions remain unchanged, except where they are directly affected by the revised conditions.
- The market risk scenarios assume a concurrent movement of all stock markets and an unrelated parallel shift of all interest rates in different currencies.
- The assumptions on policyholder behavior, such as lapsing of policies, included in the sensitivity analysis for Global Life may be different from actual behavior. Therefore, the actual impact may deviate from the analysis.

For more information, see the "Embedded value report."

Risk review *continued*

Analysis of economic sensitivities for interest rate risk

Tables 4.a to 6.b show the estimated impacts of a 100 basis point increase/decrease in yield curves of the major currencies U.S. dollar (USD), euro (EUR), British pound (GBP), Swiss franc (CHF) and "other currencies" after consideration of hedges in place, as of December 31, 2013 and 2012, respectively.

Table 4.a

Economic interest rate sensitivities for the General Insurance business - current period

in USD millions, as of December 31, 2013	USD	EUR	GBP	CHF	Other currencies	Total
100 basis points increase in the interest rate yield curves						
Group investments	(1,346)	(636)	(316)	(328)	(187)	**(2,813)**
Liabilities	(915)	(469)	(309)	(294)	(148)	**(2,136)**
Net impact before tax	(430)	(168)	(7)	(34)	(39)	**(677)**
Tax impact	107	42	2	8	10	**169**
Net impact after tax	(323)	(126)	(5)	(25)	(29)	**(509)**
100 basis points decrease in the interest rate yield curves						
Group investments	1,324	625	342	288	186	**2,766**
Liabilities	922	456	341	317	152	**2,188**
Net impact before tax	402	169	–	(29)	34	**577**
Tax impact	(100)	(42)	–	7	(9)	**(144)**
Net impact after tax	302	127	–	(21)	26	**434**

Table 4.b

Economic interest rate sensitivities for the General Insurance business - prior period

in USD millions, as of December 31, 2012	USD	EUR	GBP	CHF	Other currencies	Total
100 basis points increase in the interest rate yield curves						
Group investments	(1,314)	(578)	(352)	(341)	(186)	**(2,772)**
Liabilities	(1,146)	(411)	(368)	(364)	(109)	**(2,397)**
Net impact before tax	(168)	(167)	16	22	(78)	**(375)**
Tax impact	42	41	(4)	(6)	19	**93**
Net impact after tax	(127)	(126)	12	17	(59)	**(282)**
100 basis points decrease in the interest rate yield curves						
Group investments	1,005	490	351	237	184	**2,266**
Liabilities	1,049	342	391	334	111	**2,228**
Net impact before tax	(44)	147	(41)	(97)	73	**38**
Tax impact	11	(36)	10	24	(18)	**(9)**
Net impact after tax	(33)	111	(31)	(73)	55	**29**

Table 5.a

Economic interest rate sensitivities for the Global Life business - current period

in USD millions, as of December 31, 2013	USD	EUR	GBP	CHF	Other currencies	Total
100 basis points increase in the interest rate yield curves						
Total impact on Embedded Value	(211)	(195)	(72)	(4)	57	**(425)**
100 basis points decrease in the interest rate yield curves						
Total impact on Embedded Value	162	213	55	(37)	44	**437**

Economic interest rate sensitivities for the Global Life business - prior period

Table 5.b

in USD millions, as of December 31, 2012	USD	EUR	GBP	CHF	Other currencies	Total
100 basis points increase in the interest rate yield curves						
Total impact on Embedded Value	(130)	(165)	(98)	142	(100)	**(350)**
100 basis points decrease in the interest rate yield curves						
Total impact on Embedded Value	61	365	111	(140)	68	**465**

Economic interest rate sensitivities for the rest of the businesses - current period

Table 6.a

in USD millions, as of December 31, 2013	USD	EUR	GBP	CHF	Other currencies	Total
100 basis points increase in the interest rate yield curves						
Group investments	(798)	(112)	1	(56)	–	**(966)**
Liabilities	(390)	(194)	(21)	(131)	–	**(736)**
Net impact before tax	(409)	82	22	75	–	**(230)**
Tax impact	102	(21)	(5)	(19)	–	**57**
Net impact after tax	(307)	62	16	57	–	**(172)**
100 basis points decrease in the interest rate yield curves						
Group investments	896	94	(3)	62	1	**1,050**
Liabilities	475	163	21	80	–	**738**
Net impact before tax	421	(69)	(24)	(18)	1	**311**
Tax impact	(105)	17	6	5	–	**(78)**
Net impact after tax	316	(52)	(18)	(14)	–	**234**

Economic interest rate sensitivities for the rest of the businesses - prior period

Table 6.b

in USD millions, as of December 31, 2012	USD	EUR	GBP	CHF	Other currencies	Total
100 basis points increase in the interest rate yield curves						
Group investments	(831)	(148)	(22)	(36)	(1)	**(1,037)**
Liabilities	(585)	(166)	(28)	(117)	–	**(898)**
Net impact before tax	(246)	19	7	82	(1)	**(139)**
Tax impact	66	(5)	(2)	(20)	–	**39**
Net impact after tax	(180)	14	5	61	–	**(100)**
100 basis points decrease in the interest rate yield curves						
Group investments	895	111	22	26	1	**1,055**
Liabilities	643	140	28	34	–	**845**
Net impact before tax	252	(29)	(6)	(8)	1	**210**
Tax impact	(64)	7	2	2	–	**(53)**
Net impact after tax	189	(22)	(5)	(6)	–	**157**

Analysis of economic sensitivities for equity risk

Tables 7 to 9 show the estimated impacts from a 10 percent decline in stock markets, after consideration of hedges in place, as of December 31, 2013 and 2012, respectively.

Risk review *continued*

Economic equity price sensitivities for the General Insurance business

Table 7

in USD millions, as of December 31	2013	2012
10% decline in stock markets		
Group investments	(525)	(456)
Liabilities	–	–
Net impact before tax	(525)	(456)
Tax impact	131	113
Net impact after tax	(394)	(343)

Economic equity price sensitivities for the Global Life business

Table 8

in USD millions, as of December 31	2013	2012
10% decline in stock markets		
Total impact on Embedded Value	(279)	(246)

Economic equity price sensitivities for the rest of the businesses

Table 9

in USD millions, as of December 31	2013	2012
10% decline in stock markets		
Group investments	(83)	(171)
Liabilities	31	34
Net impact before tax	(113)	(205)
Tax impact	28	49
Net impact after tax	(85)	(156)

Analysis of economic sensitivities for credit spread risk

Tables 10.a to 12.b show the estimated impacts from a 100 basis points increase in corporate credit spreads, as of December 31, 2013 and 2012, respectively.

Economic credit spread sensitivities for the General Insurance business – current period

Table 10.a

in USD millions, as of December 31, 2013	USD	EUR	GBP	CHF	Other currencies	Total
100 basis points increase in credit spreads						
Net impact before tax	(1,001)	(332)	(178)	(144)	(89)	**(1,744)**
Tax impact	249	83	44	36	22	**434**
Net impact after tax	(752)	(249)	(134)	(108)	(67)	**(1,310)**

Economic credit spread sensitivities for the General Insurance business – prior period

Table 10.b

in USD millions, as of December 31, 2012	USD	EUR	GBP	CHF	Other currencies	Total
100 basis points increase in credit spreads						
Net impact before tax	(939)	(278)	(198)	(160)	(102)	**(1,677)**
Tax impact	232	69	49	39	25	**414**
Net impact after tax	(707)	(209)	(149)	(120)	(77)	**(1,262)**

Economic credit spread sensitivities for the Global Life business – current period

Table 11.a

in USD millions, as of December 31, 2013	USD	EUR	GBP	CHF	Other currencies	Total
100 basis points increase in credit spreads						
Total Impact on Embedded Value	(174)	(262)	(86)	(234)	(145)	**(901)**

Economic credit spread sensitivities for the Global Life business – prior period

Table 11.b

in USD millions, as of December 31, 2012	USD	EUR	GBP	CHF	Other currencies	Total
100 basis points increase in credit spreads						
Total impact on Embedded Value	(189)	(282)	(100)	(250)	(130)	**(951)**

Economic credit spread sensitivities for the rest of the businesses – current period

Table 12.a

in USD millions, as of December 31, 2013	USD	EUR	GBP	CHF	Other currencies	Total
100 basis points increase in credit spreads						
Net impact before tax	(339)	(49)	5	4	–	**(380)**
Tax impact	84	12	(1)	(1)	–	**95**
Net impact after tax	(254)	(37)	4	3	–	**(285)**

Economic credit spread sensitivities for the rest of the businesses – prior period

Table 12.b

in USD millions, as of December 31, 2012	USD	EUR	GBP	CHF	Other currencies	Total
100 basis points increase in credit spreads						
Net impact before tax	(320)	(74)	2	(3)	–	**(396)**
Tax impact	89	18	–	1	–	**108**
Net impact after tax	(231)	(56)	1	(3)	–	**(288)**

Risk review *continued*

Currency risk

Currency risk is the risk of loss resulting from changes in exchange rates. The Group operates internationally and therefore is exposed to the financial impact arising from changes in the exchange rates of various currencies. The Group's presentation currency is the U.S. dollar, but its assets, liabilities, income and expenses are denominated in many currencies, with significant amounts in the euro, Swiss franc, British pound, as well as the U.S. dollar.

On local balance sheets there is the risk that a currency mismatch may lead to fluctuations in a balance sheet's net asset value, either through income or directly through equity. The Group manages this risk by matching foreign currency positions on local balance sheets within prescribed limits. Residual local mismatches are reported centrally in order to make use of the netting effect across the Group. Zurich then hedges residual mismatches from local balance sheets through a central balance sheet within an established limit. The monetary currency risk exposure on local balance sheets is considered immaterial.

Because the Group has chosen the U.S. dollar as its presentation currency, differences arise when functional currencies are translated into the presentation currency. The Group applies net investment hedge accounting in order to protect against the effects of changes in certain exchange rates on selected net investments. The Group does not take speculative positions on foreign currency market movements. Using constant exchange rates from one year to the next, the Group's 2013 net income attributable to shareholders would have been lower by USD 6 million (applying 2012 exchange rates to the 2013 result). In 2012, the result would have been higher by USD 45 million (applying 2011 exchange rates to the 2012 results).

Table 13 shows the sensitivity of the total IFRS equity to changes in exchange rates for the main functional currencies to which the Group is exposed. Positive values represent an increase in the value of the Group's total equity. The sensitivity analysis does not take into account management actions that might be taken to mitigate such changes. The sensitivities show the effects of a change of the exchange rates only, while other assumptions remain unchanged. The sensitivities do not indicate a probability of such events occurring in the future. They do not necessarily represent Zurich's view of expected future market changes. While table 13 shows the effect of a 10 percent increase in currency exchange rates, a decrease of 10 percent would have the converse effect.

See notes 1, 3 and 7 of the Consolidated financial statements for additional information on foreign currency translation and transactions.

Table 13

Sensitivity of the Group's total IFRS equity to exchange rate fluctuations

in USD millions, as of December 31	**2013**	2012
10% increase in		
EUR/USD rate	915	904
GPB/USD rate	311	362
CHF/USD rate	(382)	(253)
Other currencies/USD rates	760	787

Credit risk

Section highlights
- During 2013, the intensity of the euro crisis eased despite areas of negative growth and high unemployment. The U.S. remains vulnerable to both domestic and global risks.
- The risk-weighted average issuer credit rating of the Group's debt securities portfolio is "BBB+". The largest concentration in the Group's debt securities portfolio is in government, supranationals and similar debt securities at 48.4 percent.

Credit risk is the risk associated with a loss or potential loss from counterparties failing to fulfill their financial obligations. The Group's exposure to credit risk is derived from the following main categories of assets:

- Cash and cash equivalents
- Debt securities
- Reinsurance assets
- Mortgage loans
- Other loans
- Receivables
- Derivatives

The Group manages individual exposures as well as credit risk concentrations. The Group's objective in managing credit risk exposures is to maintain them within parameters that reflect the Group's strategic objectives and risk tolerance. Sources of credit risk are assessed and monitored, and the Group has policies to manage the specific risks within the various subcategories of credit risk. To assess counterparty credit risk, the Group uses the ratings assigned by external rating agencies, qualified third parties, such as asset managers, and internal rating assessments. When there is a difference among external rating agencies, the Group assesses the reasons for the inconsistencies and applies the lowest of the respective ratings unless other indicators of credit quality justify the assignment of alternative internal credit ratings. The Group maintains counterparty credit risk databases, which record external and internal sources of credit intelligence.

The Group regularly tests and analyzes credit risk scenarios and prepares possible contingency measures, which may be implemented should the credit risk environment worsen. Zurich adjusts the scenarios if market conditions warrant.

Although the Group actively uses collateral to mitigate credit risks, the principle is nevertheless to manage the underlying credit risks independently from the collateral. The Group has limits and quality criteria to identify acceptable letter-of-credit providers. Letters of credit enable Zurich to limit the risks embedded in reinsurance captives, deductibles, trade credit and surety.

Macro review of the credit risk environment

During 2013, the intensity of the euro crisis eased despite areas of negative growth and high unemployment. Unresolved high government and private debt levels in Europe continued to drive negative rating actions on governments – even beyond the peripheral countries. Even though credit conditions are more favorable in the U.S., it remains vulnerable to both domestic and global risks such as fiscal policy challenges, developments in the Eurozone and the tapering of the U.S. Federal Reserve System's expansive policy.

Financial institutions have been slowly re-establishing levels of profitability and asset quality seen prior to the crisis. They have overall built up capital and liquidity and improved their operating flexibility. Therefore, on the one hand, the credit outlook for banks slightly improved and the potential for rating downgrades decreased. On the other hand, Zurich expects government support for financial institutions to decrease over time. For example, the European Union has developed a new directive for the recovery and resolution of troubled banks that would allow losses to be imposed on a broad range of liabilities, including senior unsecured debt. Such aspects of new regulations negatively impact the credit outlook of financial institutions.

Risk review *continued*

Credit risk concentration

The Group limits and regularly monitors credit exposures by individual counterparty and related counterparties by the aggregated exposure across various types of credit risk for that counterparty. The Group's exposure to counterparties' parent companies and subsidiaries across sources of credit risk is aggregated to include reinsurance assets, investments, certain insurance products and derivatives. Best estimates, based on statistical data and own assessments, are used to assign loss-given-default percentages and loss dependency factors reflecting, for example, double default events. The aggregated exposure information is compared with the Group's credit limits. The limits vary based on the underlying rating category of the counterparty. There was no material exposure in excess of the Group's limits for counterparty aggregation as of December 31, 2013 or December 31, 2012. In line with the Group's overall risk appetite, additional investments in Italy were exceptionally approved in order to benefit from slight credit improvements in the European "periphery."

The maximum exposure to credit risk consists mainly of on-balance sheet exposures. Off-balance sheet exposures are primarily related to collateral, such as letters of credit, used to protect the underlying credit exposures on the balance sheet. The Group also has off-balance sheet exposures related to undrawn loan commitments of USD 8 million and USD 20 million as of December 31, 2013 and 2012, respectively. See note 24 of the Consolidated financial statements for undrawn loan commitments.

Credit risk related to cash and cash equivalents

The Group has significant exposure to cash and cash equivalents across the globe. In order to mitigate concentration, settlement and operational risks related to cash and cash equivalents, the Group limits the maximum cash amount that can be deposited with a single counterparty. In addition, the Group maintains an authorized list of acceptable cash counterparties based on current ratings and outlook, taking the analysis of fundamentals and market indicators into account.

Cash and cash equivalents amounted to USD 7.2 billion as of December 31, 2013 and USD 9.1 billion as of December 31, 2012. The risk-weighted average rating of the overall cash portfolio has decreased from "A" to "BBB+" in 2013 due to a change in the rating methodology. Applying the changed methodology retrospectively, the risk-weighted average rating for 2012 would have been "BBB+". 61 percent of the total was with the ten largest global banks, whose average rating was "A-" as of December 31, 2013, down from "A" as of December 31, 2012.

Credit risk related to debt securities

The Group is exposed to credit risk from third party counterparties where the Group holds securities issued by those entities. Table 14 shows the credit risk exposure on debt securities, by issuer credit rating.

Table 14

Debt securities by rating of issuer

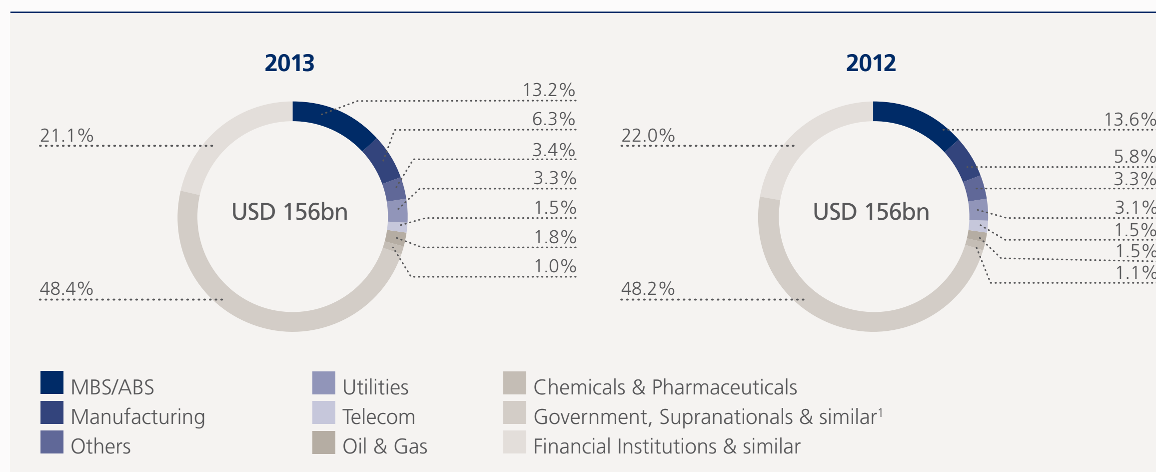
as of December 31	2013		2012	
	USD millions	% of total	USD millions	% of total
Rating				
AAA	37,010	23.7%	48,526	31.2%
AA	57,985	37.1%	48,032	30.9%
A	26,992	17.2%	27,135	17.4%
BBB	31,170	19.9%	29,021	18.6%
BB and below	2,360	1.5%	2,448	1.6%
Unrated	939	0.6%	432	0.3%
Total	**156,456**	**100.0%**	**155,594**	**100.0%**

As of December 31, 2013, investment grade securities comprise 97.9 percent of the Group's debt securities, and 23.7 percent were rated "AAA." The downgrades of several Eurozone governments and related entities caused breaches of internal rating category limits, which were managed as circumstances allowed. The migration from AAA to AA is mostly due to the downgrade of UK governments. As of December 31, 2012, investment grade securities comprised 98.1 percent of debt securities, and 31.2 percent were rated "AAA." The Group's investment policy prohibits speculative grade investments, unless specifically authorized and under exceptional circumstances. Where the Group identifies investments expected to be downgraded to below investment grade, it implements appropriate corrective actions.

The Group measures the average issuer credit rating both with a linear and a risk-weighted scale. Despite the ongoing de-risking of the fixed income portfolio, the risk-weighted average issuer credit rating of the Group's debt securities

portfolio was "BBB+" (2012: "A–/BBB+"). This is mainly due to both downgrades of governments and government-related financial institutions in 2013 and higher exposures due to the tightening of credit spreads. Based on the linear scale, the average rating was"AA–"(2012: "AA–") and therefore in line with the "AA–" target rating as set out in the Group's risk policy.

Debt securities – credit risk concentration by industry
(%, as of December 31)



[1] 2012 figures exclude government agency debt.

As of December 31, 2013, the largest concentration in the Group's debt securities portfolio is in governments, supranationals and similar debt securities at 48.4 percent. In all other categories, a total of USD 37.9 billion or 47 percent is secured. As of December 31, 2012, 48.2 percent of the Group's debt portfolio was invested in governments, suprationals and similiar. In all other categories, a total of USD 40.3 billion or 49.5 percent was secured.

The Group's debt exposure to Eurozone governments and supranationals & similar

Table 15

in USD millions, as of December 31	**2013**	2012
Germany	7,873	9,282
France	5,191	4,638
Austria	3,108	2,892
Belgium	2,305	1,959
Netherlands	2,093	2,122
Peripheral countries	14,351	11,301
Greece	–	–
Ireland	491	243
Italy	8,885	6,646
Portugal	530	531
Spain	4,445	3,881
Rest of Eurozone	1,147	974
Eurozone supranationals and similar	679	1,058
Total	**36,747**	**34,226**

As shown in table 15, the Group had debt exposure to Eurozone governments of USD 36.8 billion and USD 34.2 billion as of December 31, 2013 and 2012, respectively. Exposure to Greece, Ireland, Italy, Portugal and Spain amounted to USD 14.4 billion and USD 11.3 billion as of December 31, 2013 and 2012, respectively. This increase was primarily driven by switches in investments from Germany into Italy to benefit from improvements in credit quality and from the spread differential.

In addition to the debt exposure, the Group had sovereign loan exposure of USD 4.2 billion and USD 4.7 billion to Germany as of December 31, 2013 and 2012, respectively.

Risk review *continued*

The second largest concentration in the Group's debt securities portfolio is to financial institutions (including banks), at 21.1 percent, of which 44.5 percent is secured. In response to the European government-debt crisis, the Group identified and selectively reduced unsecured and subordinated credit exposure issued by banks with weak credit profiles, and credit exposure to banks supported by weaker governments.

The third largest concentration in the Group's debt securities portfolio is to structured finance securities (mortgage-backed securities (MBS)/asset-backed securities (ABS) and similar). Although credit risks of the underlying securities are diverse in nature, the Group also considers macro impacts that may affect structured finance sub-categories (e.g. auto or credit card ABS's) in its credit assessments. Structured finance exposures are assessed on a look-through basis prior to acquisition and not merely on the strength of prevailing credit ratings or credit profiles.

Credit risk related to reinsurance assets

As part of its overall risk management strategy, the Group cedes insurance risk through proportional, non-proportional and facultative reinsurance treaties. While these cessions mitigate insurance risk, the recoverables from reinsurers and receivables arising from ceded reinsurance expose the Group to credit risk.

The Group's Corporate Reinsurance Security Committee manages the credit quality of cessions and reinsurance assets. The Group typically cedes new business to authorized reinsurers with a minimum rating of "A–." 59 percent and 58 percent of the business ceded to reinsurers that fall below "A–" or are not rated is collateralized, as of December 31, 2013 and 2012, respectively. Of these percentages, 55 percent and 50 percent are ceded to captive insurance companies, in 2013 and 2012, respectively.

Reinsurance assets include reinsurance recoverables of USD 18.1 billion and USD 19.9 billion as of December 31, 2013 and 2012, respectively, which are the reinsurers' share of reserves for insurance contracts, and receivables arising from ceded reinsurance, gross of allowances for impairment, of USD 1.1 billion and USD 1.1 billion as of December 31, 2013 and 2012, respectively. Reserves for potentially uncollectible amounts of reinsurance assets amount to USD 174 million as of December 31, 2013 and USD 206 million as of December 31, 2012. The Group's policy on impairment charges takes into account both specific charges for known situations (e.g. financial distress or litigation) and a general, prudent provision for unanticipated impairments.

Reinsurance assets in table 16 are shown before taking into account collateral such as cash or letters of credit from banks rated at least "A," which can be converted into cash, and deposits received under ceded reinsurance contracts.

Compared to December 31, 2012, collateral decreased by USD 414 million to USD 7.6 billion.

The risk-weighted average credit quality of reinsurance assets (including receivables, but after deduction of collateral) was "A" as of December 31, 2013 and 2012. Credit factors to determine the risk-weighted average credit quality of reinsurance assets are based on historical insurance impairment statistics, consistent with the prior year. For credit risk assessment purposes, collateral has been taken into account at nominal value as an approximation for fair value. For collateral, the Group applies minimum requirements, such as a minimum rating for the issuers of letters of credit and guarantees, and for pledged assets a minimum coverage ratio of 100 percent.

Table 16 shows reinsurance premiums ceded and reinsurance assets split by rating.

Table 16

Reinsurance premiums ceded and reinsurance assets by rating of reinsurer and captive

as of December 31	2013				2012			
	Premiums ceded		**Reinsurance assets**		Premiums ceded		Reinsurance assets	
	USD millions	**% of total**	**USD millions**	**% of total**	USD millions	% of total	USD millions	% of total
Rating								
AAA	88	1.3%	38	0.2%	77	1.2%	42	0.2%
AA	1,484	22.6%	7,672	40.3%	1,434	22.1%	8,852	42.6%
A	2,152	32.8%	6,681	35.1%	2,279	35.2%	6,959	33.5%
BBB	1,071	16.3%	2,058	10.8%	800	12.4%	2,080	10.0%
BB	387	5.9%	656	3.4%	213	3.3%	425	2.0%
B	51	0.8%	33	0.2%	34	0.5%	42	0.2%
Unrated	1,313	20.2%	1,890	9.9%	1,644	25.4%	2,390	11.5%
Total	**6,546**	**100.0%**	**19,027** [1]	**100.0%**	**6,481**	**100.0%**	**20,791** [1]	**100.0%**

[1] The value of the collateral received amounts to USD 7.6 billion and USD 8.0 billion as of December 31, 2013 and 2012, respectively.

Credit risk related to mortgage loans

Mortgage loans expose the Group to credit risk. The mortgage business is dependent on local property market conditions and local legislation. Investment portfolio allocations made to mortgages consider these factors and are within the framework of the strategic asset allocation defined by the Group and adapted and approved by local investment committees. Conservative lending criteria (i.e. maximum mortgage loan to property value ratios) and the diversification of loans across many single borrowers, particularly in Germany and in Switzerland, help reduce potential loss. Dunbar Assets Ireland (formerly Zurich Bank) has, however, suffered from concentrations to a smaller number and type of borrowers, such as property developers and investors. Furthermore, business units are required to clearly state criteria for determining borrower and collateral quality in their local mortgage policies. The Group specifies requirements for the local policies and sets monitoring and reporting standards. The Group closely monitors the performance of the portfolios in terms of impairments and losses.

The Group's largest mortgage loan portfolios are in Germany (USD 4.5 billion) and in Switzerland (USD 3.9 billion); these are predominantly secured against residential property. In Switzerland, the underlying properties backing individual loans are revalued every 10 years. In Germany, the property valuation is not generally reassessed after the granting of the mortgage loan. A less frequent or no revaluation of the underlying property means that reported loan-to-value (LTV) ratios will be higher (lower) than they would be if property prices have risen (fallen) since their valuation.

In Switzerland, the residential property market has seen steady price growth since 2000 and fast growth in the past six years, raising concerns about the development of a price bubble. Residential property price increases have been strongest in the main economic centers and more moderate in the rest of the country; residential prices in the Lake Geneva region and in the Canton of Zug have more than doubled since 2000, and in the Canton of Zurich have increased by 76% in the same period. In 2013, outstanding mortgages in the Lake Geneva region represent approximately 33% of the Swiss portfolio. Mortgages in the Canton of Zurich and in the Canton of Zug represent 35% and 1.3% of the Swiss portfolio respectively. The bulk of those mortgages was granted before 2008 and is therefore not affected by price developments in the last six years. In Germany, residential prices are increasing in the major cities, however in line with the Group's investment policy, mortgage exposure has been reduced. To mitigate the impact of potential bubbles in the portfolio, the Group has a process to regularly review regional property markets, and to tighten underwriting standards in areas with strong price appreciation. Zurich's German and Swiss mortgage portfolios remain strong and well managed; LTV lending buffers are generally strong, and loss impairments and losses remain low.

Risk review *continued*

The next largest portfolio comprises loans granted by Dunbar Assets Ireland (including the UK property loans of Dunbar Assets plc) of USD 864 million (after provisions) in the UK and Ireland. They consist of residential and commercial property development financing or investment loans, secured as either property under development or completed developments. In 2010, these entities ceased originating new business in these markets following the significant deterioration in economic conditions and the drop in property values in the UK and Ireland. Provisions at Dunbar Assets Ireland now stand at a significant USD 761 million (USD 713 million in 2012) or 47 percent and 39 percent of the portfolio as of December 31, 2013 and December 31, 2012 respectively; this accordingly reduces the carrying balance of net loans outstanding. Dunbar Assets Ireland regularly reviews its property valuations as part of the continual assessment of the appropriateness of provisioning on a portfolio that is largely impaired. For more details, see table 18.a and 18.b.

Credit risk related to other loans

The credit risk arising from other loans is assessed and monitored together with the fixed income securities portfolio. 63.1 percent of the reported loans are to Government, Supranationals and similar or government or supranational institutions, of which 99.4 percent are to the German Central Government or the German Federal States. Table 17 shows the composition of the loan portfolio by rating class. As of December 31, 2013, a total of USD 7.9 billion or 66.7 percent of loans are secured. As of December 31, 2012, a total of USD 8.0 billion or 68.3 percent of loans were secured.

Table 17

Other loans by rating of issuer

as of December 31	2013		2012	
	USD millions	**% of total**	USD millions	% of total
Rating				
AAA	6,185	52.5%	6,851	51.2%
AA	1,293	11.0%	2,315	17.3%
A	2,257	19.1%	2,113	15.8%
BBB and below	1,167	9.9%	1,524	11.4%
Unrated	887	7.5%	582	4.3%
Total	**11,789**	**100.0%**	**13,385**	**100.0%**

Credit risk related to receivables

The Group's largest credit risk exposure to receivables is from third party agents, brokers and other intermediaries; the risk arises where they collect premiums from customers to be paid to the Group or pay claims to customers on behalf of the Group. The Group has policies and standards to manage and monitor credit risk from intermediaries with a focus on day-to-day monitoring of the largest positions. As part of these standards, the Group requires that intermediaries maintain segregated cash accounts for policyholder money. Additionally, the Group requires intermediaries to satisfy minimum requirements in terms of their capitalization, reputation and experience as well as providing short-dated business credit terms.

Past due but not impaired receivables should be regarded as unsecured, but some of these receivable positions may be offset by collateral. The Group reports internally on Group past due receivable balances and strives to keep the balance of past due positions as low as possible, while taking into account customer satisfaction. In 2013, the Group continued efforts to reduce past due receivables through both short- and long-term initiatives to improve processes and systems.

Receivables from ceded reinsurance form part of the reinsurance assets and are managed accordingly.

See note 17 of the Consolidated financial statements for additional information on receivables.

Credit risk related to derivatives

The positive replacement value of outstanding derivatives, such as interest rate, currency, total return and equity swaps, forward contracts and purchased options represents a credit risk to the Group. In addition there is a potential exposure arising from possible changes in replacement value. The Group regularly monitors credit risk exposures arising from derivative transactions. Outstanding positions with external counterparties are managed through an approval process embedded in derivative programs.

To limit credit risk, derivative financial instruments are typically executed with counterparties rated "A–" or better by an external rating agency. In addition, it is the Group standard to only transact derivatives with counterparties where the Group has an ISDA Master Agreement with a Credit Support Annex in place. This mitigates credit exposures from over-the-counter transactions due to close-out netting and requires the counterparty to post collateral when the derivative position is beyond an agreed threshold. The Group mitigates credit exposures from derivative transactions further by using exchange-traded instruments whenever possible.

Analysis of financial assets

Tables 18.a to 19.b provide an analysis, for non unit-linked businesses, of the age of financial assets that are past due but not impaired and of financial assets that are individually determined to be impaired.

Analysis of financial assets - current period

Table 18.a

in USD millions, as of December 31, 2013	Debt securities	Mortgage loans	Other loans	Receivables and other financial assets	Total
Neither past due nor impaired financial assets	**156,181**	**8,825**	**11,787**	**15,016**	**191,809**
Past due but not impaired financial assets. Past due by:					
1 to 90 days	–	131	–	1,477	1,608
91 to 180 days	–	38	–	304	343
181 to 365 days	–	22	–	182	203
> 365 days	–	114	–	285	399
Past due but not impaired financial assets	**–**	**304**	**1**	**2,248**	**2,553**
Financial assets impaired	**275**	**1,456**	**20**	**162**	**1,914**
Gross carrying value	**156,456**	**10,585**	**11,808**	**17,426**	**196,276**
Less: impairment allowance					
Impairment allowances on individually assessed financial assets	–	726	19	89	835
Impairment allowances on collectively assessed financial assets	–	61	–	208	269
Net carrying value	**156,456** [1]	**9,798** [2]	**11,789**	**17,130**	**195,172**

[1] Available-for-sale debt securities are included net of USD 2 million of impairment charges recognized during the year.
[2] USD 158 million past due but not impaired and USD 1.4 billion impaired mortage loans relate to the run-off property loans at Dunbar Assets Ireland.

Risk review *continued*

Table 18.b

Analysis of financial assets - prior period

in USD millions, as of December 31, 2012	Debt securities	Mortgage loans	Other loans	Receivables and other financial assets	Total
Neither past due nor impaired financial assets	**155,182**	**9,318**	**13,385**	**14,492**	**192,376**
Past due but not impaired financial assets. Past due by:					
1 to 90 days	–	185	–	1,207	1,392
91 to 180 days	–	80	–	290	370
181 to 365 days	–	107	–	223	330
> 365 days	–	165	–	305	469
Past due but not impaired financial assets	**–**	**537**	**–**	**2,024**	**2,561**
Financial assets impaired	**412**	**1,397**	**1**	**248**	**2,057**
Gross carrying value	**155,594**	**11,252**	**13,386**	**16,764**	**196,995**
Less: impairment allowance					
Impairment allowances on individually assessed financial assets	–	696	–	117	814
Impairment allowances on collectively assessed financial assets	–	37	–	210	247
Net carrying value	**155,594** [1]	**10,519** [2]	**13,385**	**16,437**	**195,934**

[1] Available-for-sale debt securities are included net of USD 12 million of impairment charges recognized during the year.
[2] USD 385 million past due but not impaired and USD 1.4 billion impaired mortage loans relate to the run-off property loans at Dunbar Assets Ireland.

Tables 19.a and 19.b show how the allowances for impairments of financial assets in tables 18.a and 18.b have developed during the periods ended December 31, 2013 and 2012, respectively.

Table 19.a

Development of allowance for impairments – current period

in USD millions	Mortgage loans	Other loans	Receivables
As of January 1, 2013	733	–	327
Increase/(Decrease) in allowance for impairments	92	20	12
Amounts written-off	(62)	(1)	(38)
Foreign currency translation effects	24	–	(5)
As of December 31, 2013	**787**	**20**	**297**

Table 19.b

Development of allowance for impairments - prior period

in USD millions	Mortgage loans	Other loans	Receivables
As of January 1, 2012	645	–	320
Increase/(Decrease) in allowance for impairments	69	13	39
Amounts written-off	(4)	(13)	(37)
Foreign currency translation effects	23	–	5
As of December 31, 2012	**733**	**–**	**327**

Liquidity risk

Section highlights

- The Group maintains internal liquidity sources that cover the Group's potential liquidity needs, including those that might arise under stressed conditions.

Liquidity risk is the risk that the Group may not have sufficient liquid financial resources to meet its obligations when they fall due, or would have to incur excessive costs to do so. Zurich's policy is to maintain adequate liquidity and contingent liquidity to meet its liquidity needs under both normal and stressed conditions. To achieve this, the Group assesses, monitors and manages its liquidity needs on an ongoing basis.

The Group has Group-wide liquidity management policies and specific guidelines as to how local businesses have to plan, manage and report their local liquidity. These include regularly conducting stress tests for all major carriers within the Group. The stress tests use a standardized set of internally defined stress events, and are designed to provide an overview of the potential liquidity drain the Group would face if it had to recapitalize local balance sheets.

At the Group level, similar guidelines apply and detailed liquidity forecasts based on the local businesses' input and the Group's own forecasts are regularly performed. As part of its liquidity management, the Group maintains sufficient cash and cash equivalents and high quality, liquid investment portfolios to meet expected outflows including those for maturing debt obligations. In addition, the Group maintains internal liquidity sources that cover the Group's potential liquidity needs, including those that might arise under stressed conditions. The Group takes into account the amount, permanence of availability and speed of accessibility of the sources. The Group centrally maintains committed borrowing facilities, as well as access to diverse funding sources to cover contingencies. Funding sources include asset sales, external debt issuances and use of letters of credit. The Group maintains a broad range of maturities for external debt securities. A possible liquidity risk could arise from a downgrade of the Group's credit rating. This could impact the Group's commitments and guarantees, thus potentially increasing the Group's liquidity needs. This risk and potential mitigating actions are assessed on an ongoing basis within the Group's liquidity framework.

The Group limits the percentage of the investment portfolio that is not readily realizable, and regularly monitors exposures to take action if necessary to maintain an appropriate level of asset liquidity. During 2013, the Group was within its limits for asset liquidity. The fair value hierarchy tables in note 25 of the Consolidated financial statements segregate financial assets into three levels to reflect the basis of the determination of fair value. These tables indicate the high liquidity of the Group's investments.

See note 20 of the Consolidated financial statements for additional information on debt obligation maturities and on credit facilities and note 24 of the Consolidated financial statements for information on commitments and guarantees. The Group's regular liquidity monitoring includes monthly reporting to the executive management and quarterly reporting to the Risk Committee of the Board, covering aspects such as the Group's actual and forecasted liquidity, possible adverse scenarios that could affect the Group's liquidity and possible liquidity needs from the Group's main subsidiaries, including under stressed conditions.

Tables 20.a and 20.b provide an analysis of the expected maturity profile of reserves for insurance contracts, net of reinsurance, based on expected cash flows without considering the surrender values as of December 31, 2013 and 2012. Reserves for unit-linked insurance contracts amounting to USD 74.9 billion and USD 74.1 billion as of December 31, 2013 and 2012, respectively, are not included, as policyholders can generally surrender their contracts at any time, at which point the underlying unit-linked assets would be liquidated. Risks from the liquidation of unit-linked assets are largely borne by the policyholders of unit-linked contracts.

Risk review *continued*

Table 20.a

Expected maturity profile for reserves for insurance contracts, net of reinsurance – current period

in USD millions, as of December 31, 2013	Reserves for losses and loss adjustment expenses	Future life policyholders' benefits	Policyholders' contract deposits and other funds	Total
< 1 year	17,338	9,017	1,386	27,742
1 to 5 years	23,511	21,918	2,432	47,861
5 to 10 years	8,279	14,966	1,931	25,176
10 to 20 years	5,509	17,083	2,542	25,134
> 20 years	2,681	18,990	9,834	31,506
Total	**57,319**	**81,975**	**18,126**	**157,420**

Table 20.b

Expected maturity profile for reserves for insurance contracts, net of reinsurance – prior period

in USD millions, as of December 31, 2012	Reserves for losses and loss adjustment expenses	Future life policyholders' benefits	Policyholders' contract deposits and other funds	Total
< 1 year	17,288	8,188	1,370	26,846
1 to 5 years	23,688	20,807	2,208	46,704
5 to 10 years	8,465	14,448	1,859	24,772
10 to 20 years	5,612	18,896	2,361	26,869
> 20 years	2,332	18,960	10,119	31,411
Total	**57,385**	**81,300**	**17,917**	**156,602**

For additional information on reserves for insurance contracts, see note 8 of the Consolidated financial statements.

Tables 21.a and 21.b provide an analysis of the maturity of liabilities for investment contracts based on expected cash flows as of December 31, 2013 and 2012. The undiscounted contractual cash flows for liabilities for investment contracts are USD 67.4 billion and USD 57.6 billion as of December 31, 2013 and December 31, 2012, respectively. Liabilities for unit-linked investment contracts amount to USD 59.5 billion and USD 50.2 billion as at December 31, 2013 and 2012, respectively. The policyholders of unit-linked investment contracts can generally surrender their contracts at any time, at which point the underlying unit-linked assets would be liquidated. Risks from the liquidation of unit-linked assets are borne by the policyholders of unit-linked investment contracts. Certain non-unit-linked contracts also allow for surrender of the contract by the policyholder at any time. Liabilities for such contracts amounted to USD 922 million and USD 958 million as of December 31, 2013 and 2012 respectively. The Group actively manages the Global Life in-force business to improve persistency and retention.

Table 21.a

Expected maturity profile for liabilities for investment contracts – current period

in USD millions, as of December 31, 2013	Liabilities related to unit-linked investment contracts	Liabilities related to investment contracts (amortized cost)	Liabilities related to investment contracts with discretionary participation features	Total
< 1 year	5,663	182	344	6,189
1 to 5 years	6,853	559	1,330	8,742
5 to 10 years	7,548	151	1,301	8,999
10 to 20 years	10,499	96	1,094	11,690
> 20 years	28,905	43	2,545	31,493
Total	**59,469**	**1,030**	**6,614**	**67,113**

Table 21.b

Expected maturity profile for liabilities for investment contracts – prior period

in USD millions, as of December 31, 2012	Liabilities related to unit-linked investment contracts	Liabilities related to investment contracts (amortized cost)	Liabilities related to investment contracts with discretionary participation features	Total
< 1 year	4,383	172	295	4,850
1 to 5 years	6,253	799	1,333	8,385
5 to 10 years	6,757	173	1,068	7,998
10 to 20 years	9,258	115	940	10,313
> 20 years	23,579	46	2,267	25,892
Total	**50,229**	**1,305**	**5,903**	**57,437**

See note 20 of the Consolidated financial statements for information on the maturities of total debt issued. For more information on the Group's other financial liabilities, see note 18 of the Consolidated financial statements.

See note 6 of the Consolidated financial statements for information on the maturity of debt securities for total investments.

The Group has committed to contribute capital to subsidiaries and third parties that engage in making investments in direct private equity and private equity funds. Commitments may be called by the counterparty over the term of the investment (generally three to five years) and must be funded by the Group on a timely basis. See note 24 of the Consolidated financial statements.

Risk review *continued*

Operational risk

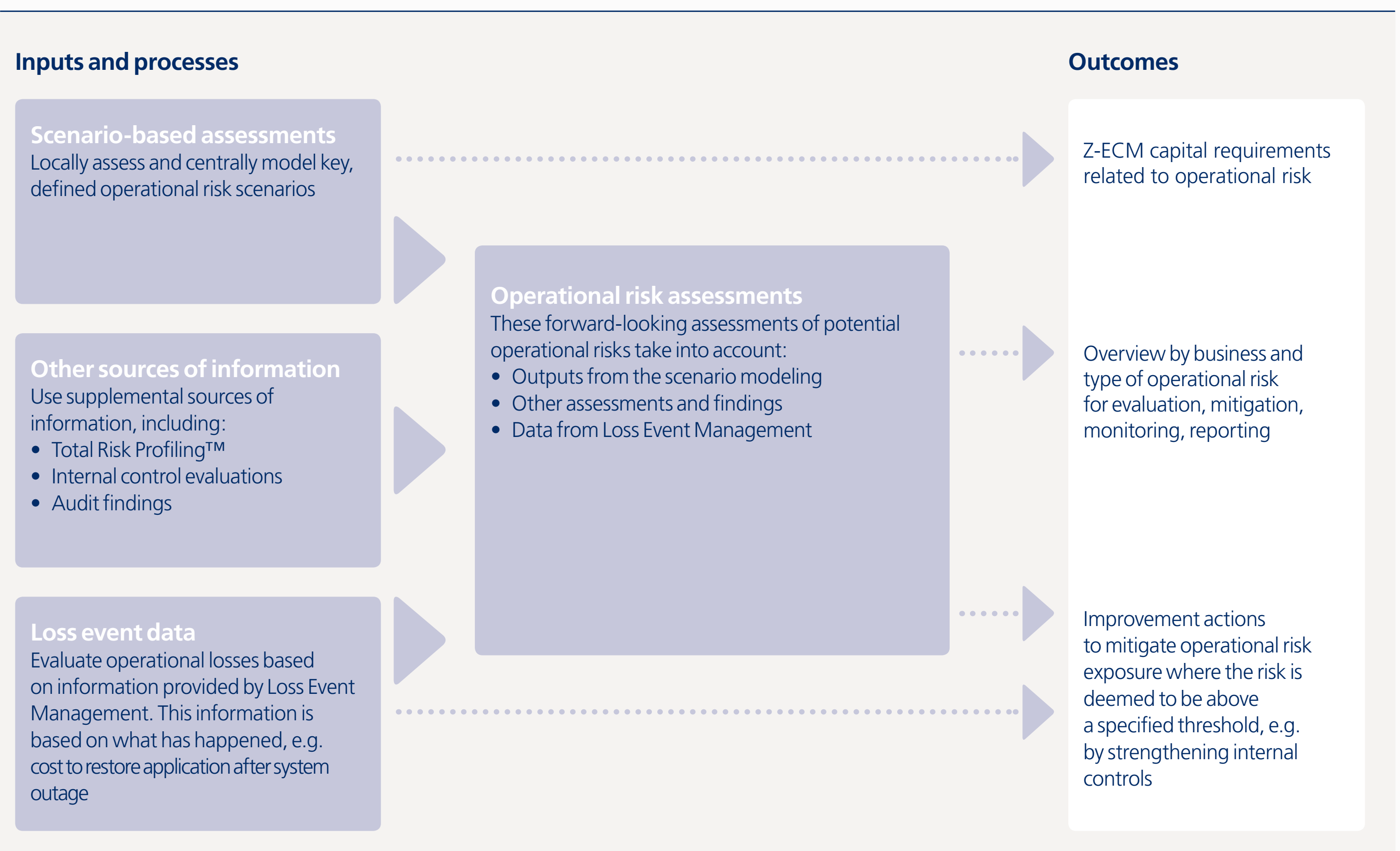
Section highlights

- Zurich regularly reviews projects to identify significant risks that may threaten successful project delivery, and mitigates these risks.
- In 2013, this area was strengthened by adding to the Zurich Risk Policy specific requirements to manage project risks.

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people, systems or from external events such as outsourcing, catastrophes, legislation, or external fraud.

Zurich has a comprehensive framework with a common approach to identify, assess, quantify, mitigate, monitor and report operational risk within the Group as summarized below.

Operational risk



Within this framework, the Group:

- Uses a scenario-based approach to assess, model and quantify the capital required for operational risk for business units under extreme circumstances (internal model calibrated to a confidence level of 99.95 percent over a one-year time horizon). This approach allows comparison of information across the Group and highlights the main scenarios contributing to the Z-ECM capital required. See chart "Z-ECM capital required for operational risk split by risk scenarios (unaudited)" for more information.

- Documents and evaluates loss events above a threshold determined by the Zurich Risk Policy, in a Group-wide database. Improvement actions are put in place to avoid recurrence of such operational loss events.
- Conducts operational risk assessments through which operational risks are identified for key business areas and are qualitatively assessed. Risks identified and assessed above a certain threshold must be mitigated, and escalated in specific reports at the Group level. Plans for improvement actions are documented and tracked on an ongoing basis. The Group uses a scoping exercise to determine which business units and Group-wide functional areas conduct operational risk assessments. In the assessments, the Group uses such sources of information as Total Risk Profiling™, internal control assessments, and audit findings, as well as scenario modeling and loss event data.

The Group has specific processes and systems in place to focus on high priority operational matters such as managing information security, business continuity and project risks as well as combating fraud.

In the area of information security the Group continued to focus on its global improvement program with special emphasis on protecting customer information, improving security with its suppliers and monitoring that access to information is properly controlled. This helps the Group to better protect information assets and ensure compliance with regulation and policies.

A key task is maintaining and developing the Group's business continuity capability with an emphasis on recovery from events such as natural catastrophes, significant operational interruptions and the possibility of a pandemic. In order to achieve this The Group has continued to further implement a more globally consistent approach to business continuity and crisis management.

Addressing the risk of claims and non-claims fraud continues to be of importance. In 2013, the Group continued its global anti-fraud initiative to further improve the Group's ability to prevent, detect and respond to fraud. While claims fraud is calculated as part of insurance risk and non-claims fraud is calculated as part of operational risk for risk-based capital, both are part of the common framework for assessing and managing operational risks.

Zurich regularly reviews projects to identify significant risks that may threaten successful project delivery, and mitigates these risks. In 2013, this area was strengthened by adding to the Zurich Risk Policy specific requirements to manage project risks. The Group Chief Risk Officer reports regularly on the status and development of significant project risks to the CEO, senior management committees and the Risk Committee of the Board.

The Group considers controls to be key instruments for monitoring and managing operational risk. Although primarily focused on important controls over financial reporting, internal control efforts also include related operational and compliance controls. Therefore, the Group continues to strengthen the robustness, consistency, documentation and assessment of internal controls for significant entities and business processes. Operational effectiveness of key controls is assessed by self assessment and independent testing on controls supporting the financial statements. For more details, see the "Risk management and internal control statement" in the "Corporate governance report (unaudited)."

Risks to the Group's reputation

Risks to the Group's reputation include the risk that an act or omission by the Group or any of its employees could result in damage to the Group's reputation or loss of trust among its stakeholders. Every risk type has potential consequences for Zurich's reputation, and therefore, effectively managing each type of risk helps Zurich reduce threats to its reputation.

Additionally, the Group endeavors to preserve its reputation by adhering to applicable laws and regulations, and by following the core values and principles of Zurich Basics, the Group's code of conduct, which includes integrity and good business practice. The Group centrally manages certain aspects of reputation risk, for example, communications, through functions with the appropriate expertise.

Risk review *continued*

Capital management and analysis of capital adequacy

Capital management

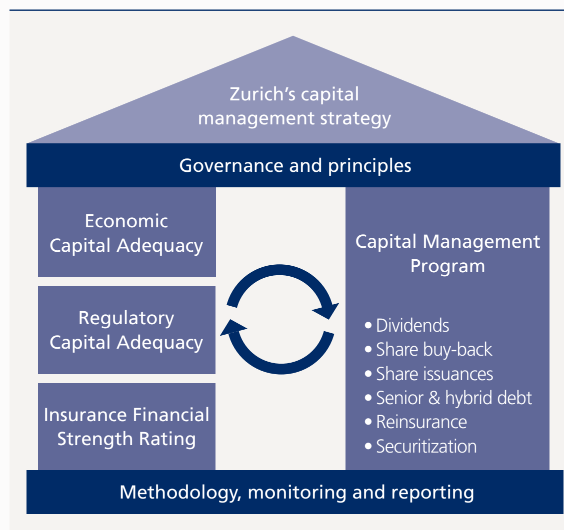
The Group's capital management strategy is to maximize long term shareholder value by optimizing capital allocation while managing the balance sheet at "AA" level and in accordance with regulatory, solvency and rating agency requirements. In particular, the Group endeavors to manage its capital such that the Group and all of its regulated entities are adequately capitalized in compliance with the relevant regulatory capital adequacy requirements.

Further, Zurich strives to simplify the Group's legal entity structure in order to reduce complexity and increase fungibility of capital. The Group also wants to minimize constraints to capital fungibility by pooling risk, capital and liquidity centrally as much as possible.

Capital management framework

The Group's capital management framework forms the basis for actively managing capital within Zurich. Major elements are economic, regulatory, and rating agency capital adequacy.

Capital management framework



Zurich's policy is to manage its capital position by allocating capital to businesses earning the highest risk-adjusted returns and pooling risks and capital as much as possible to operationalize its global risk diversification, subject to local and Group regulatory solvency requirements and rating agency capital adequacy constraints.

The Group manages capital and solvency through an integrated and comprehensive framework. The Group Balance Sheet Committee defines the capital management strategy and sets the principles, standards and policies for the execution of the strategy. Group Treasury and Capital Management is responsible for the execution of the capital management strategy within the mandate set by the Group Balance Sheet Committee.

Within these defined principles, the Group manages its capital using a number of different capital models taking into account economic, regulatory, and rating agency constraints. The Group's capital and solvency position is monitored and reported regularly. Based on the results of the capital models and defined standards and principles, Group Treasury and Capital Management has a set of measures and tools available to manage capital within the defined constraints. This tool set is referred to as the capital management program.

Capital management program

The Group's capital management program comprises various actions to optimize shareholders' total return and to meet capital needs, while enabling Zurich to take advantage of growth opportunities as they arise. Such actions are performed as and when required and include dividends, capital repayments, share buy-backs, issuances of shares, issuance of senior and hybrid debt, securitization and purchase of reinsurance.

The Group seeks to maintain the balance between higher returns for shareholders on equity held, which may be possible with higher levels of borrowing, and the security provided by a sound capital position. The payment of dividends, share buy-backs, and issuances and redemption of debt have an important influence on capital levels. In 2013, the Group paid a dividend out of the capital contribution reserve, and replaced maturing senior debt and callable hybrid debt with new senior and hybrid debt.

Zurich Insurance Group Ltd is not subject to legal restrictions on the amount of dividends it may pay to its shareholders other than under the Swiss Code of Obligations. The Swiss Code of Obligations provides that dividends may only be paid out of freely distributable reserves or retained earnings and that 5 percent of annual retained earnings must be allocated to a general legal reserve until such reserve in the aggregate has reached 20 percent of the paid-in share capital; therefore the earnings allocated to those reserves are restricted. As of December 31, 2013, the amount of the general legal reserve exceeded 20 percent of the paid-in share capital of the Group. Similarly, company laws in many countries in which the Group's subsidiaries operate may restrict the amount of dividends payable by those subsidiaries to their parent companies.

The ability of the Group's subsidiaries to pay dividends may be restricted or – while dividend payments as such may be legally permitted – may be indirectly influenced by minimum capital and solvency requirements imposed by insurance and other regulators in the countries in which the subsidiaries operate. Other limitations, such as foreign exchange control restrictions, exist in some countries.

In the U.S., restrictions on the payment of dividends that apply to insurance companies may be imposed by the insurance laws or regulations of an insurer's state of domicile. For general insurance subsidiaries, dividends are generally limited over a 12 month period to the lesser of 10 percent of the policyholders' surplus or adjusted net investment income. For life, accident and health insurance subsidiaries, dividends are generally limited over a 12 month period to 10 percent of the previous year's policyholders' surplus or the previous year's net gain from operations. Dividends paid in excess of statutory limitations require prior approval from the Insurance Commissioner in the insurer's state of domicile.

For details on dividend payments, and issuances and redemptions of debt, see notes 20 and 21 of the Consolidated financial statements.

Analysis of capital adequacy

Insurance Financial Strength Rating

The Group maintains interactive relationships with three global rating agencies: Standard & Poor's, Moody's and A.M. Best. The Insurance Financial Strength Rating (IFSR) of the Group's main operating entity is an important element of Zurich's competitive position. Moreover, the Group's credit ratings derived from the financial strength ratings affect the cost of capital.

The Group maintained its strong rating level and its stable outlook in 2013. As of December 31, 2013 the IFSR of Zurich Insurance Company Ltd, the main operating entity of the Group, was "AA–/stable" by Standard and Poor's, "Aa3/stable" by Moody's and "A+ (superior)/stable" by A.M. Best.

Regulatory capital adequacy

The Group endeavors to manage its capital such that all of its regulated entities meet local regulatory capital requirements at all times.

In each country in which the Group operates, the local regulator specifies the minimum amount and type of capital that each of the regulated entities must hold in addition to their liabilities. The Group targets to hold, in addition to the minimum capital required to comply with the solvency requirements, an adequate buffer to ensure that each of its regulated subsidiaries meets the local capital requirements. The Group is subject to different capital requirements depending on the country in which it operates.

At a Group level, Zurich endeavors to pool risk and capital as much as possible and thereby create diversification benefits for the Group. This also allows the Group to take into account the benefits that arise from this pooling in those regions where these benefits are recognized under the capital adequacy regime, e.g., in the U.S., Ireland, and Switzerland.

Risk review *continued*

Regulatory requirements in Switzerland

In Switzerland, under the Swiss Solvency Test (SST), groups, conglomerates and reinsurers are required to use company-specific internal models to calculate risk-bearing and target capital. Internal models must be approved by the Swiss Financial Market Supervisory Authority (FINMA). In 2013, Zurich continued to further enhance and refine its internal model to meet evolving regulatory requirements. The model approval process continues with FINMA, which has approved on a provisional basis the use of Zurich's internal model for 2013, without prejudicing the final approval of the internal model. Zurich has filed an SST ratio with FINMA in excess of the regulatory requirements, both as of January 1, 2013 and as of July 1, 2013 (subject to FINMA approval). For more details, see the "Swiss Solvency Test requirement (unaudited)" section.

Regulatory requirements in the European Economic Area

In European countries, insurance entities are required to maintain minimum solvency margins according to the existing Solvency I legislation. Solvency I capital is calculated as a fixed percentage of premiums, claims, reserves and net amounts at risk. The required minimum solvency margin for general insurers is the greater of 16 percent of premiums written for the year or 23 percent of a three-year average of claims incurred, subject to the first tranche (EUR 61 million) of premiums at 18 percent and the first tranche (EUR 43 million) of claims at 26 percent. In these calculations, premiums and claims for certain liability lines are increased by 50 percent. A reduction is given for reinsurance based on reinsurance claims recoveries over three years as a percentage of gross claims in those years, limited to a maximum of 50 percent. Life insurance companies are required to maintain a minimum solvency margin generally of 4 percent of insurance reserves, but reduced to 1 percent of insurance reserves for life insurance where the credit and market risks are carried by policyholders, plus 0.3 percent of the amount at risk under insurance policies. The same minimum capital requirements are applicable for insurance entities operating in Switzerland. In certain European countries, both EU and non-EU, further requirements have been imposed by regulators.

On November 25, 2009 the directive on Solvency II was adopted. Solvency II aims to reflect the latest developments in prudential supervision, actuarial methods and risk management. It includes economic risk-based solvency requirements, which are more risk sensitive and more sophisticated than Solvency I. Solvency II capital requirements also consider all material risks and their interactions. As part of the risk management system, every insurance and reinsurance entities will be required to conduct their own risk and solvency assessment, including the assessment of the overall solvency needs reflecting their specific risk profiles. As part of the disclosure provisions, companies will have to publicly report their solvency and financial condition.

In 2013, the timeline for the roll-out of Solvency II was further specified. The introduction of the complete framework is expected for January 1, 2016. Zurich is fully engaged in an extensive program of work in order to meet Solvency II requirements when they enter into force. The Group intends to use its internal model, which aligns the Solvency II approach with that used for the Z-ECM, for Zurich Insurance plc (Ireland). The Group is in the pre-application process in order to gain regulatory approval for the internal model from the Central Bank of Ireland, the Group's EU lead regulator.

Regulatory requirements in the U.S.

In the U.S., required capital is determined to be the "company action level risk-based capital" calculated with the risk-based capital model of the National Association of Insurance Commissioners. This method, which builds on regulatory accounts, measures the minimum amount of capital for an insurance company to support its overall business operations by taking into account its size and risk profile. The calculation is based on risk-sensitive factors that are applied to various asset, premium, claim, expense and reserve items.

Regulatory requirements in Asia Pacific, Latin America and Middle East and Africa

Every country has a capital standard for insurance companies. Some jurisdictions, including Japan, Mexico and South Africa, have started to review their economical capital requirements, considering similar approaches to Solvency II.

Solvency I requirements at Group level

The Group continues to be subject to Solvency I requirements based on the Swiss Insurance Supervisory Law. Table 22 sets out the Solvency I position as drafted for filing with the Swiss regulator for 2013 and a restated position for 2012. See Note 1 of the Consolidated financial statements for more information.

Table 22

The Group's Solvency I composition

in USD millions, as of December 31	2013	2012[1]
Eligible equity		
Total equity	**34,734**	**36,874**
Net of intangibles and other assets	(7,996)	(8,501)
Free reserves for policyholder dividends	4,954	5,238
Subordinated debt[2]	5,815	5,709
Deferred policyholder acquisition costs non-life insurance	(3,231)	(3,088)
Dividends	(2,817)[3]	(2,730)
Total eligible equity	**31,460**	**33,500**
Total required solvency capital	**12,201**	**12,031**
Excess margin	**19,259**	**21,470**
Solvency I ratio	**258%**	**278%**

[1] December 31, 2012 has been restated as set out in note 1 of the Consolidated financial statements.
[2] Dated subordinated debt issuances are admissible up to 25 percent of the capital requirement, undated issuances up to 50 percent of the capital requirement.
[3] Amount for dividend reflects the proposed dividend for the financial year 2013, not yet approved by the Annual General Meeting.

As of December 31, 2013 and 2012 respectively, the Group and its material, regulated subsidiaries complied with the applicable regulatory minimum capital requirements.

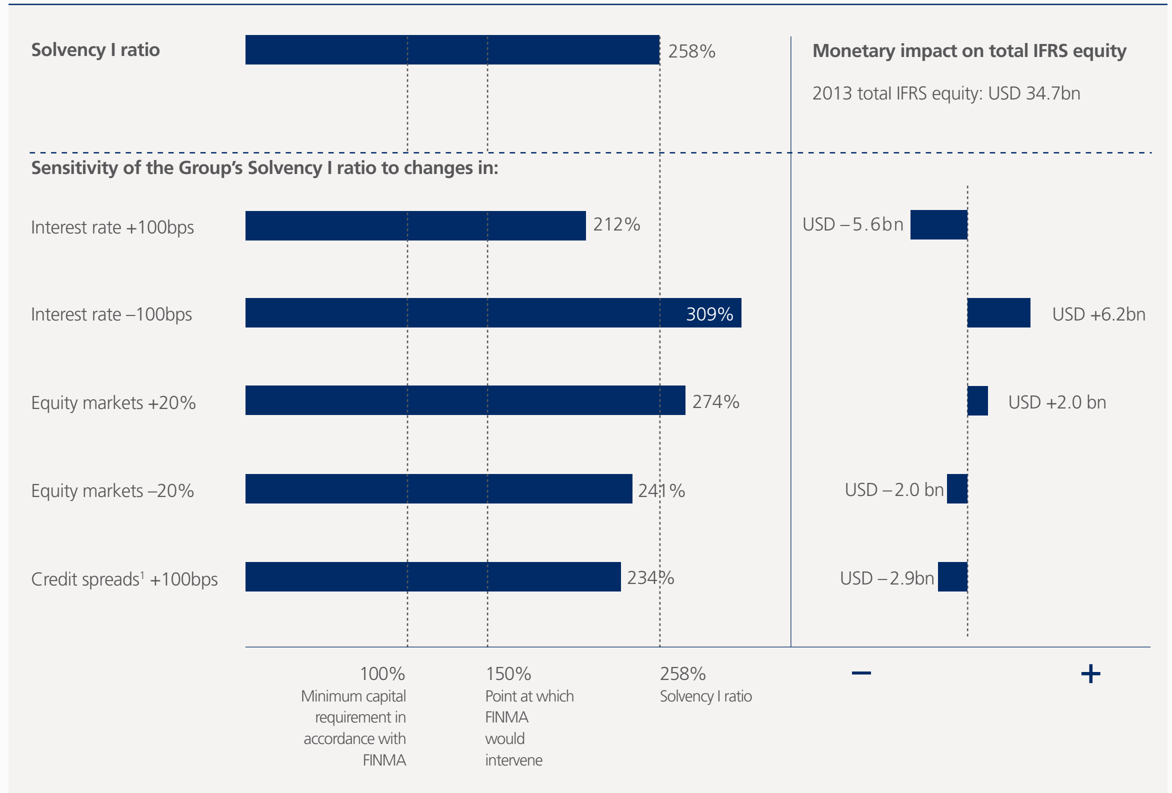
The following chart shows the estimated impact on the Group's solvency position of a one percentage point increase/decrease in yield curves, a separate 20 percent rise/decline in all stock markets, after consideration of hedges in place and a separate one percentage point change in credit spreads, as of December 31, 2013. The sensitivities are considered separate but instantaneous scenarios.

Limitations of the analysis:

- The sensitivity analysis does not take into account actions that might be taken to mitigate losses. The Group uses an active strategy to manage these risks, which may involve changing the asset allocation, for example, through selling and buying assets.
- The sensitivities show the effects from a change of certain risk factors, while other assumptions, such as policyholder assumptions, remain unchanged.
- The interest rate scenarios assume a parallel shift of all interest rates.
- The equity market scenario assumes a concurrent movement of all stock markets.
- The impact on unit-linked business is not included, as policyholders bear the majority of investment risk.
- The impact on changes to the required capital is not included in the sensitivities for the Solvency I ratio.
- The major markets in which the Group invests are the U.S. and Europe. The major interest rate exposures are to U.S. dollar- and euro- denominated assets and liabilities. The sensitivities do not indicate a probability of such events and do not necessarily represent the Group's view of expected future market changes. Debt securities are primarily exposed to interest rate risk, while equity securities are primarily exposed to equity market risk. Debt securities can be affected also by spread widening due to changes in credit quality.
- The Group effective tax rate is assumed to be 24.9 percent in 2013. For the Non-Core Businesses with life insurance characteristics, specific tax rates have been applied.

Risk review *continued*

Sensitivities for the Group's Solvency I ratio and IFRS equity
(as of December 31, 2013)



[1] The credit spread sensitivity is applied to corporate debt, mortgages and euro currency government debt (excluding Germany).

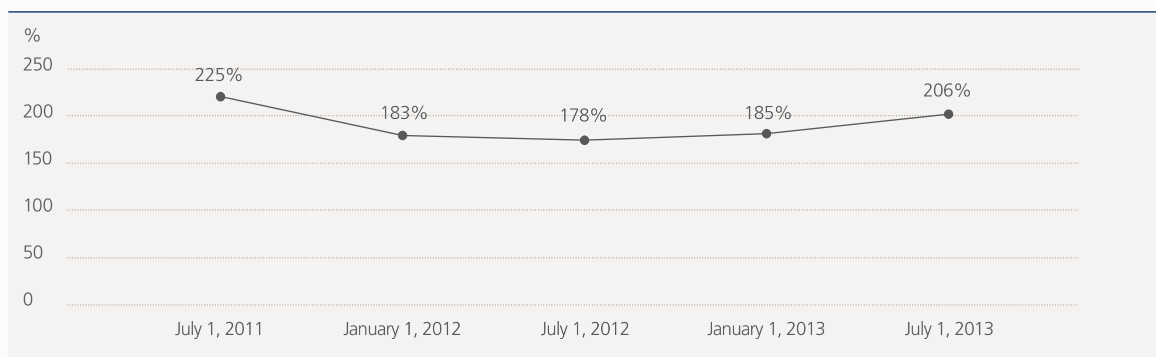
Beginning of unaudited sections.

Swiss Solvency Test requirement

Since January 1, 2011, the Swiss Solvency Test (SST) capital requirements are binding in Switzerland. The Group uses an adaptation of its internal Zurich Economic Capital Model (Z-ECM) to comply with the SST requirements and runs a full SST calculation twice a year. The model is still subject to FINMA approval. For more details about Z-ECM, see the "Internal model capital adequacy (unaudited)" section. For more details about the SST model approval process see the "Regulatory requirements in Switzerland (audited)".

The Group has filed with FINMA an SST ratio of 206 percent as of July 1, 2013.

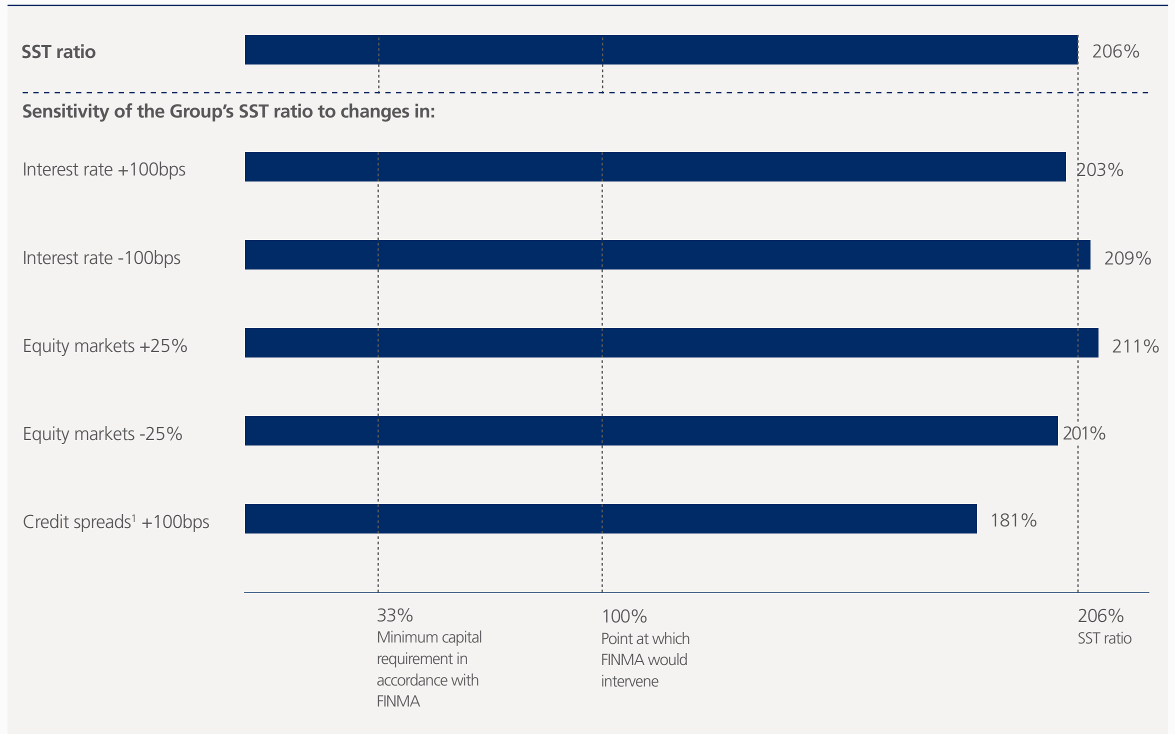
Development of the Group's Swiss Solvency Test ratio
(in %)



Risk review *continued*

The following chart shows the estimated impact on the Group's SST ratio of a one percentage point increase/decrease in yield curves, a separate 25 percent rise/decline in all stock markets, after consideration of hedges in place and a separate one percentage point change in credit spreads, as of July 1, 2013. The sensitivities are considered separate but instantaneous scenarios.

Sensitivities for the Group's Swiss Solvency Test ratio
(as of July 1, 2013)



[1] The credit spread sensitivity is applied to corporate debt, mortgages and Euro currency government debt (excluding Germany). The credit spread sensitivity does not take into account the buffering effect of policyholder participation.

Internal model capital adequacy

Internally, the Group uses its Zurich Economic Capital Model (Z-ECM), which also forms the basis of the SST model. The Z-ECM targets a total capital level that is calibrated to an "AA" financial strength. Zurich defines the Z-ECM capital required as being the capital required to protect the Group's policyholders in order to meet all of their claims with a confidence level of 99.95 percent over a one-year time horizon.

The Group uses Z-ECM to assess the economic capital consumption of its business on a one-balance-sheet approach. The Z-ECM framework is an integral part of how the Group is managed. The Z-ECM framework is embedded in the Group's organization and decision making, and is used in capital allocation, business performance management, pricing, reinsurance purchasing, transaction evaluation, risk optimization, and regulatory, investor, and rating agency communication.

Group's Risk Tolerance

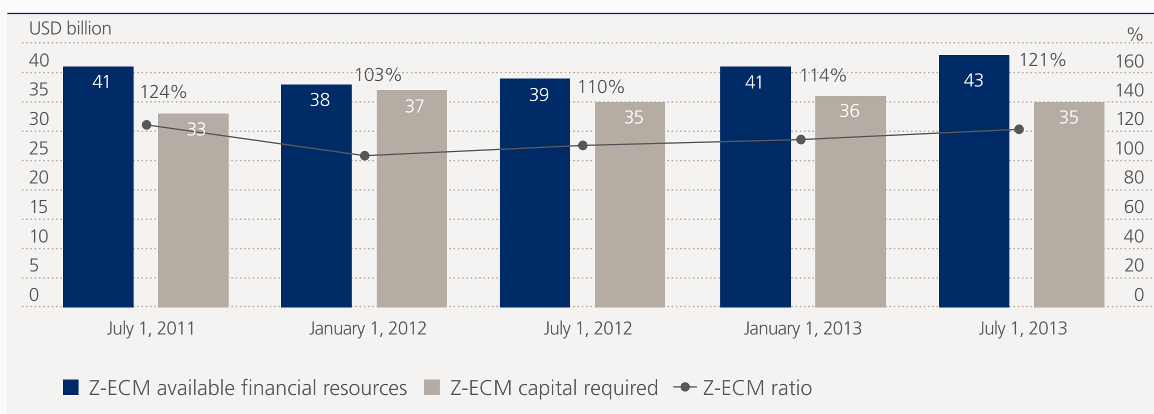
Z-ECM ratio	Range	Action
120%	>120%	Consider increased risk taking or remedial actions
100%	**100-120% "AA" Target Range**	**No action required as within stated objective and equivalent to "AA" rating**
90%	90-100%	Position may be tolerated for a certain time depending on the risk environment
0%	<90%	Z-ECM ratio below Group risk tolerance level, requiring appropriate remedial actions and implementation of de-risking measures

Z-ECM quantifies the capital required for insurance-related risk (including premium and reserve, natural catastrophe, business and life insurance), market risk (market/ALM), credit risk (including reinsurance credit and investment credit) and operational risks.

At the Group level, Zurich compares Z-ECM capital required to the Z-ECM available financial resources (Z-ECM AFR) to derive an Economic Solvency Ratio (Z-ECM ratio). Z-ECM AFR reflects financial resources available to cover policyholder liabilities in excess of their expected value. It is derived by adjusting the IFRS shareholders' equity to reflect the full economic capital base available to absorb any unexpected volatility in the Group's business activities.

The chart below shows the development of the Group's Z-ECM available financial resources, Z-ECM capital required and Z-ECM ratio over time. As of October 1, 2013, the Z-ECM ratio was 120 percent.

Analysis of the Group's Z-ECM available financial resources and Z-ECM capital required
(in USD billions)

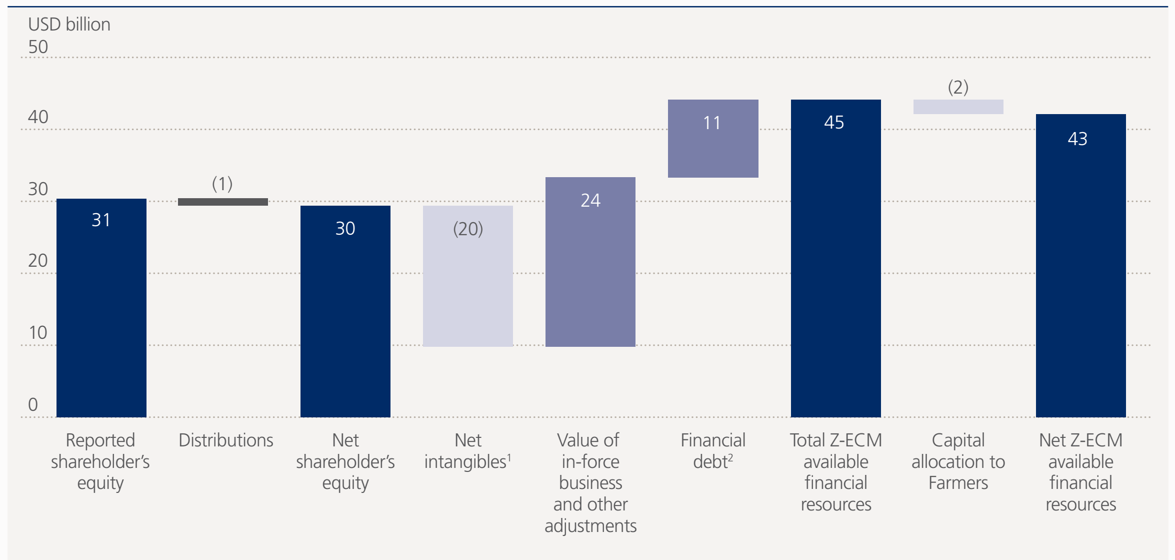


Group performance review

Risk review *continued*

The chart below shows an analysis of the composition of the Group's Z-ECM available financial resources as of July 1, 2013.

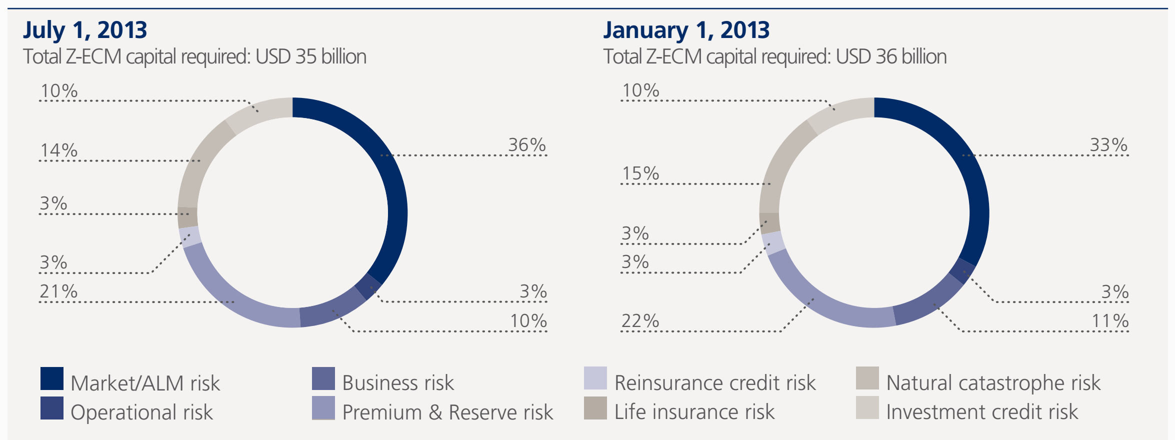
Analysis of the Group's Z-ECM available financial resources
(in USD billions as of July 1, 2013)



[1] Shareholders' intangible assets adjusted for taxes less deferred front-end fees and deferred tax liabilities
[2] All debt issues (senior and subordinated) excluding those classified as operational debt or maturing within one year

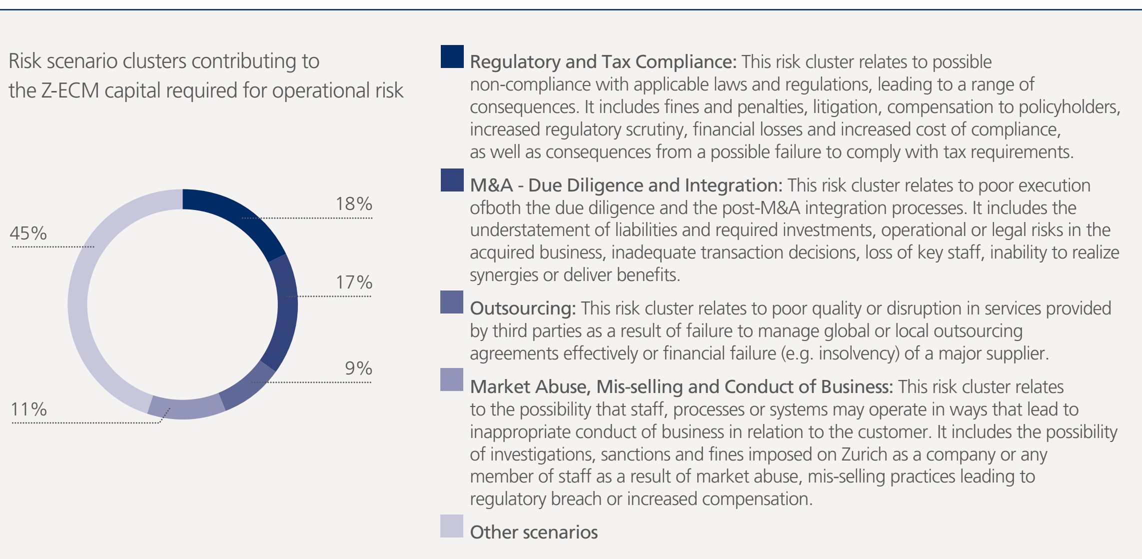
The chart below shows a split of the Z-ECM capital required split by risk type as of July 1 and as of January 1, 2013 respectively. As of July 1, 2013, the largest proportion of Z-ECM capital required arises from Market/ALM risk which comprises 36 percent of the total. Premium & Reserve risk is the second largest, comprising 21 percent.

Z-ECM capital required split by risk type
(%, as of July 1 and January 1, 2013)



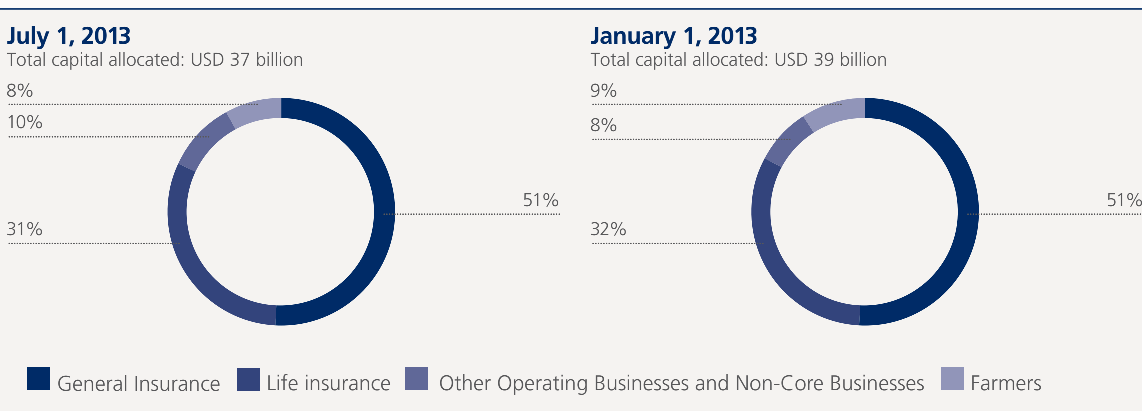
As part of Z-ECM, the Group uses a scenario-based approach to assess, model and quantify the capital required for operational risk for business units under extreme circumstances and a very slight probability of occurrence (internal model calibrated to a confidence level of 99.95 percent over a one-year time horizon). The chart below shows the operational risk scenarios that have the highest impact on Z-ECM capital required. See "Operational risk (audited)" for more information.

Z-ECM capital required for operational risk, split by risk scenario clusters
(as of July 1, 2013)



The following chart shows a split of the Z-ECM capital required allocated to the segments as of July 1 and as of January 1, 2013. As of July 1, 2013, the largest proportion of Z-ECM capital required is allocated to General Insurance, which comprises 51 percent of the total, followed by Global Life with 31 percent of the total. Total allocated capital as of July 1, 2013 equals USD 35 billion Z-ECM capital required plus USD 2 billion direct allocation to Farmers.

Total capital allocated, by segment
(%, as of July 1 and January 1, 2013)



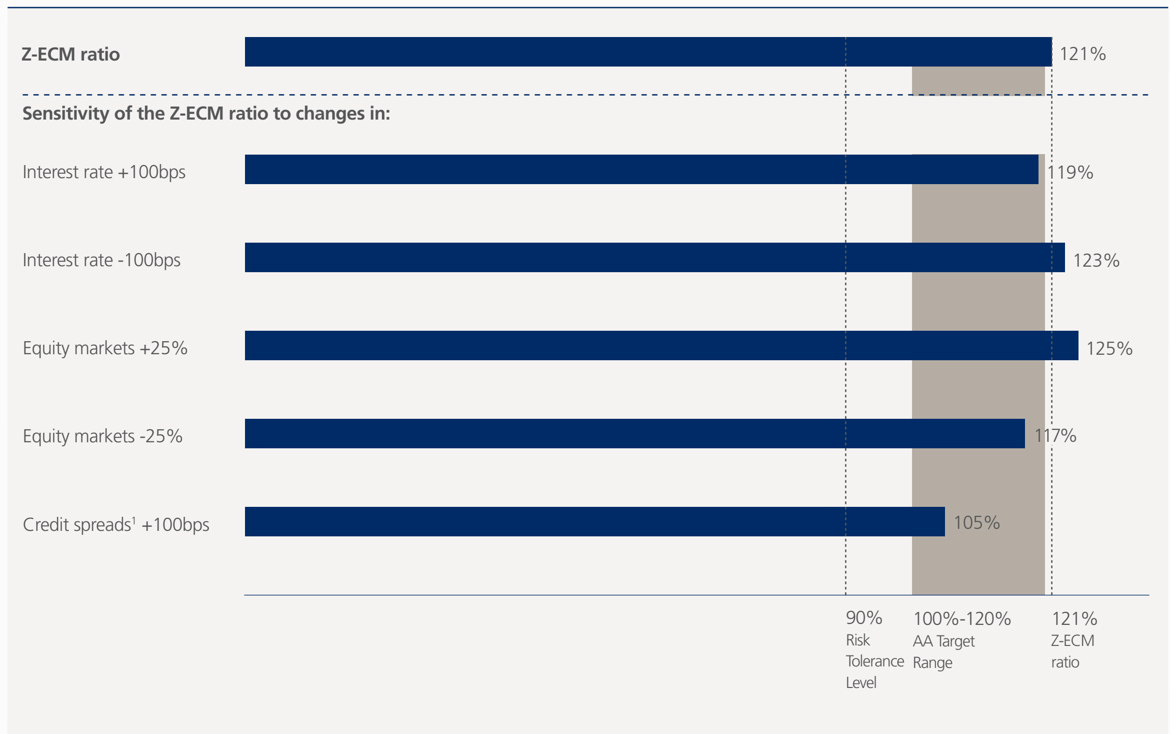
Risk review *continued*

The chart below shows the estimated impact on the Group's Z-ECM ratio of:

- A one percentage point increase/decrease in yield curves
- A 25 percent rise/decline in all stock markets, after consideration of hedges in place
- A one percentage point change in credit spreads

The sensitivities are considered separate but instantaneous scenarios.

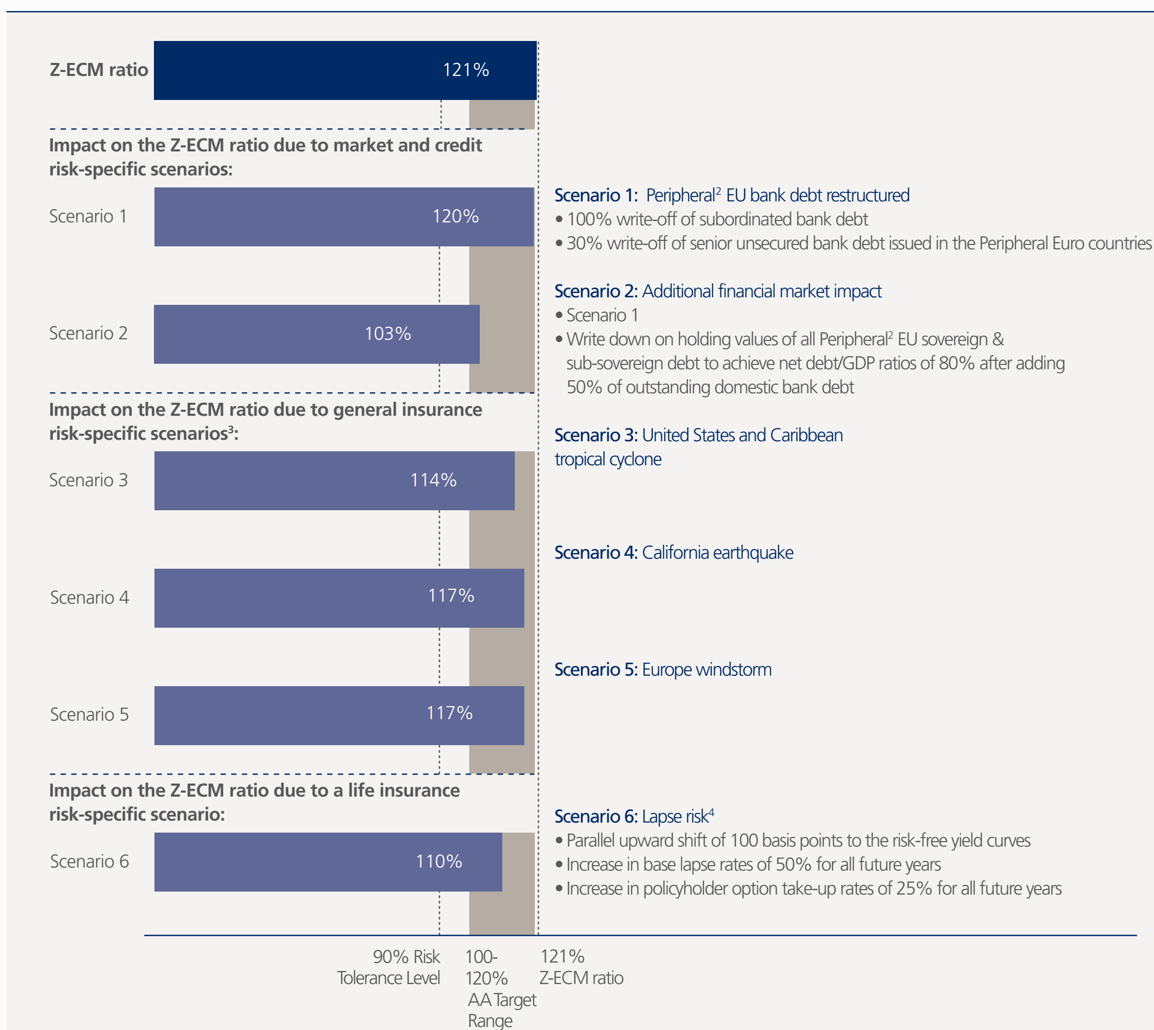
Sensitivites for the Z-ECM ratio
(as of July 1, 2013)



[1] The credit spread sensitivity is applied to corporate debt, mortgages and Euro currency government debt (excluding Germany). The credit spread sensitivity does not take into account the buffering effect of policyholder participation.

In addition to the sensitivities shown above, the Group also evaluates certain stress scenarios on the Z-ECM ratio. Scenarios are defined as events that have a very small probability of occurrence and that could, if realized, negatively affect the Group's Z-ECM available financial resources. The chart on the following page shows three groups of scenarios: market and credit risk-specific, general insurance risk-specific and life insurance risk-specific. In the current market environment, the market and credit risk-specific scenarios particularly focus on peripheral EU debt exposure and adverse financial market impact on equity markets and interest rates in the EU. The general insurance risk-specific scenarios present the three largest natural catastrophe events to which the Group is exposed. Lapse risk represents the Group's largest life insurance risk-specific exposure.

Impact of market, credit, and insurance scenarios on Z-ECM[1]
as of July 1, 2013



[1] The impact of scenarios on changes to the Z-ECM capital required is not included in the sensitivities for the Z-ECM ratio as the impact is expected to be small and positive. Scenario 1 and Scenario 2 do not take into account the buffering effect of policyholder participation.
[2] Greece, Ireland, Italy, Portugal and Spain
[3] The general insurance risk-specific scenarios relate to natural catastrophe events that are estimated on a modeled 250-year net aggregate loss (equivalent to a 99.6% probability of non-exceedance).
[4] The second assumption under the lapse risk scenario, "increase in base lapse rates of 50% for all future years," is applied in a similar manner as the Embedded Value sensitivity, "10% increase in voluntary discontinuance rates"; however the former is pre-tax while the latter is post-tax. (For more details, see the "Embedded value report.") Also, combining the assumptions in the lapse risk scenario introduces potential non-linear effects, which makes it difficult to directly compare the scenario with the Embedded Value sensitivity.

Risk review *continued*

Conclusion

Zurich's risk management framework is well embedded in the business. It sets clear responsibilities for taking, managing, monitoring and reporting risks, and is based on a transparent risk tolerance and risk limit system approved by the Board.

Enterprise risk management

Aligned with the Group's strategic and operational planning process

In 2013 Zurich conducted more than 150 Total Risk Profiling™ exercises, allowing for a systematic assessment of risk from a strategic perspective. The Zurich Risk Policy was strengthened for various areas, including outsourcing.

The Group focused on information security, business continuity management, anti-fraud and internal control initiatives, to manage operational risk.

Processes for a well-balanced and effectively managed remuneration program were strengthened.

More details on pages 128, 129 and 163

Fostering risk culture

Embedding standards and principles Group-wide to promote risk awareness and informed risk-taking

In 2013, Zurich continued to strengthen its risk culture. Risk transparency was enhanced by including in-depth risk insights into topics such as the development of new global capital standards, politcal risks in Latin America, and emerging risks.

The Zurich Risk Policy articulates the Group's approach to risk and its control, and sets standards for effective risk management throughout the Group.

Zurich Remuneration Rules help to root disciplined risk-taking across all levels in the Group

More details on pages 128 – 130 and 132

Regulatory trends

Monitoring developments in the environment in which Zurich operates

Regulatory regimes, such as the Swiss Solvency Test and the regulatory principles of Solvency II, emphasize a risk-based and economic approach, based on comprehensive quantitative and qualitative assessments and reports. In 2013, the timeline for the roll-out of Solvency II was further specified.

Several countries, among them Japan, Mexico and South Africa, started the legislative process to implement regulatory frameworks similar to Solvency II.

To address the topic of systemic risks, the Financial Stability Board announced a list of Global Systemically Important Insurers, Zurich not being among them.

More details on pages 129 and 166

Economic risk profile

Insurance-related and business risks: main drivers of the Group's required capital

As of July 1, 2013, insurance-related and business risks contributes to 48% of the Z-ECM capital required. 51% of the total capital allocated to the segments goes to General Insurance, 31% to Global Life and 8% to Farmers.

More details on pages 172 – 173

Financial condition

Well within the Group's target capital level that is calibrated to a 'AA' financial strength

As of July 1, 2013, the Group had a Zurich Economic Capital Model (Z-ECM) ratio of 121%, and was well above the Swiss Solvency Test requirements with a ratio of 206%. As of December 31, 2013, the Group's Solvency I ratio was 258%.

121%

Z-ECM ratio (as of July 1, 2013)

As of January 1, 2014, Zurich Insurance Company Ltd was rated AA– by Standard and Poor's, with a stable outlook.

AA–/stable

Standard & Poor's financial strength rating of Zurich Insurance Company Ltd (as of December 31, 2013)

More details on pages 165, 167, 169 and 171

Financial condition under stressed perspective

Assessing the potential impact of particularly severe and unlikely scenarios

Zurich assesses the impact of severe events that, while occurring at a very small probability, may have a substantial negative affect on the Group's Z-ECM available financial resources when realized. Depending on the results, the Group develops, implements and monitors improvement actions.

In 2013, the sensitivities for the Z-ECM ratio were analyzed with regard to changes in market and credit conditions. Under all scenarios, the Z-ECM ratio stayed well within the "AA" target range.

Large write-offs on the peripheral EU debt exposure, combined with adverse financial market impact, is one of the worst-case scenarios the Group assessed. If the scenario were realized, the Z-ECM ratio would remain well within the "AA" target range.

More details on page 174

End of unaudited sections.

Risk review *continued*

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