Occupational benefits insurance

Operating statement 2017

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There are many types of insur-ance. But what matters to us is that we work together with you to find the solution that is best for you. This is why we are always glad to advise you in person.

AXA is focusing on semi-autonomous Pillar 2 solutions

As Switzerland's biggest insurer of SMEs, AXA will be focusing entirely on semi-autonomous solutions in the future and from 2019 onwards, will no longer be offering full-value insurance, which is becoming increasingly unattractive for customers. Companies and their employees will enjoy better conditions thanks to this reorientation, while at the same time it will be possible to improve generational fairness within the second pillar.

Ongoing low interest rates, a growing redistribution to the detriment of the working population, and a tight investment corset have resulted in increasingly unfavorable value for money for companies and their employees with full-value insurance in recent years. More and more companies have therefore already chosen a semi-autonomous pension solution in the past few years. In addition, full-value insurance policies are only being underwritten selectively by life insurers across the industry.

AXA and the responsible trustees have therefore decided to no longer offer full-value insurance in the future and to convert the existing full-value insurance foundations into semi-autonomous foundations as of the start of 2019. This decision was communicated on April 10, 2018.

"Under the changed conditions, semi-autonomous solutions are more attractive, fairer and more flexible for our customers. By making this change, we can restore growth in occupational benefits insurance and remain a strong partner of Swiss SMEs into the future," says Fabrizio Petrillo, CEO of AXA Switzerland.

Thomas Gerber
Head of Occupational Benefits and
Member of the Executive Board

An interview with Thomas Gerber

Thomas Gerber, why will AXA no longer be offering full-value insurance in the future?
We are convinced that the change to semi-autonomous solutions is the best choice for our customers under the changed circumstances. Ongoing low interest rates, a growing redistribution to the detriment of the working population, and a tight investment corset have resulted in increasingly poor value for money for our customers with full-value insurance in recent years. Under these circumstances, semi-autonomous solutions are more attractive, fairer and more flexible. They offer better possibilities for realizing earnings, opening the way for insured persons to have the prospect of higher pensions when they retire. They will therefore benefit from increased long-term security for their old age – and they will pay less for it. This also limits the incongruous cross-financing from the younger to the older generation and from extra-mandatory to mandatory benefits.

Why don't you let your customers decide for themselves which pension solution they would like to have?
Overall conditions have changed. As I've already mentioned, interest rates are persistently low, redistribution is constantly increasing and the tight investment corset restricts our options for earning attractive returns for our customers. This has brought us to the point where full-value insurance is no longer an attractive option in the long term. It is too expensive and has ceased to be sustainable. This is why we are adapting our strategy. We are convinced that semi-autonomous solutions offer our customers added value and greater security for their old age.

But isn't it the case that full-value insurance offers the greatest possible security?
Full-value insurance guarantees 100 % of the vested benefits at all times, and the interest and investment risks are fully covered. But this comes at a high price. The changed overall conditions only allow small returns. This makes a high premium necessary in order to finance the guarantees and annuitization losses. At the same time, interest and conversion rates have been in constant decline, leading to reduced benefits as well. Viewed over the longer term, this is not sustainable.

> **"Semi-autonomous solutions are more attractive, fairer and more flexible for our customers."**

So how secure are semi-autonomous solutions?
The new semi-autonomous AXA foundations start out with a solid reserve that will enable them to compensate for market fluctuations over time. The coverage ratio is about 111 %, based on a conservative technical interest rate of 2 %. Temporary underfunding is possible with semi-autonomous solutions, which is not the case with full-value insurance. This allows more scope for the investment strategy, opening up better possibilities for realizing earnings. Nevertheless, the portfolio remains geared toward security and AXA will continue to manage the investments as an experienced asset manager. Restructuring measures would only have to be considered if relevant underfunding continued for a lengthy period. But all the financial crises in the past show that underfunding can be rectified over time, without restructuring contributions, provided that the foundation is managed soundly. Furthermore, the new foundations are being launched with no ongoing pension liabilities; this gives them additional structural risk capacity. For the new foundations, therefore, the risk of considerable underfunding over a lengthy period is very low.

Why didn't you implement the changeover at an earlier stage if you are so convinced that there is no future for full-value insurance?
Especially in recent years, the problems with full-value insurance have become far more serious. For example, the incongruous cross-financing from the younger to the older generation and from extra-mandatory to mandatory benefits amounted to more than CHF *3.4 billion between 2012 and 2017 – at AXA alone.

After an in-depth analysis, we have therefore reached the conclusion, together with the trustees, that semi-autonomous solutions are more attractive, fairer and more flexible for our customers under the changed circumstances. We are convinced that now is the right time for a reorientation.

We have already been offering semi-autonomous solutions for several years. They are constantly gaining popularity with our customers. In 2017, they already accounted for more than 50 % of our new business.

* Conversion rate losses in the current year and strengthening of the technical provisions for retirement pensioners.

An interview with Constance Reschke

Constance Reschke, even with AXA's move to semi-autonomy, the problems of cross-financing and generational fairness are still not solved, are they?

The gap in occupational benefits insurance is constantly becoming wider. On the one hand, people are living longer, which results in pension obligations lasting longer. On the other hand, low interest rates and regulatory provisions are squeezing the earnings required to fund these pension benefits. Unfortunately, corresponding changes to current legislation on mandatory BVG benefits have long since failed to command a political majority. This has led to an incongruous redistribution of ever growing intensity. The change to a semi-autonomous model will help to stem this redistribution. The excessively high conversion rate will also remain in place for the semi-autonomous solution; since the new semi-autonomous AXA foundations are being launched with no ongoing pension liabilities, however, annuitization losses will see a significant reduction as compared to full-value insurance.

So for AXA's solutions, exactly how much does the redistribution amount to?

The incongruous cross-financing from the younger to the older generation and from extra-mandatory to mandatory benefits amounted to more than CHF *3.4 billion between 2012 and 2017 – at AXA alone. The active contributors are the losers in this development: Interest rates on extra-mandatory benefits are being kept low in order to cover the high obligations due for mandatory benefits. Furthermore, the working population must also do without a considerable portion of the returns on their savings capital and pay risk premiums that are too high so that pensioners' pensions can be guaranteed despite missing investment returns.

Why is redistribution higher with full-value insurance than with other solutions?

In contrast to other Pillar 2 solutions, full-value insurance not only covers the risks of death and disability but in this case, the life insurance also bears the investment risk. Life insurers who offer full-value insurance must maintain capital coverage at all times for their entire pension obligations, including the minimum interest, and must underpin the corresponding investments with additional risk capital. This tight corset necessitates a cautious investment strategy, leading to much poorer earnings opportunities than exist for pension funds and semi-autonomous collective foundations. This in turn leads to even higher levels of redistribution. For life insurers, low interest rates also result in a greater risk of loss, which in turn leads to yet higher capital requirements and correspondingly higher premiums for customers. Under these conditions, full-value insurance customers are paying an ever higher price for increasingly fewer benefits.

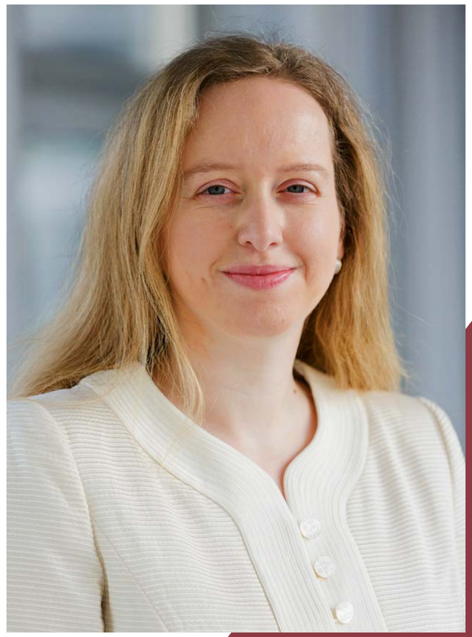
> **"Since 2012, the cross-financing amounted to over CHF 3.4 billion – at AXA alone."**

Who will benefit from the change to semi-autonomous solutions, and how?

Around 40,000 customers and their insured persons – about 260,000 in number – in the existing foundations which will be converted into semi-autonomous foundations as of the start of 2019. In April, they received a personal letter outlining the background to the reorientation and their new conditions. The risk premiums they pay will be 30% less on average; the exact premium depends on the sector to which the employer belongs and the risk experience. At the same time, the new solution offers the potential for better investment results, leading to higher interest on retirement assets and therefore higher benefits in old age and higher vested benefits. This gives customers a significantly better price/value ratio.

The risks of death and disability are still covered with AXA, while responsibility for the investment strategy and the investment risk is transferred to the foundations. AXA remains responsible for managing the investments and, as a globally renowned asset manager, offers the best conditions for the secure investment of savings and adequate interest payments.

* Conversion rate losses in the current year and strengthening of the technical provisions for retirement pensioners.



Constance Reschke
Head of Collective Foundation Operations
AXA Switzerland

Patricia Mattle
Head of Autonomous Market
AXA Switzerland

An interview with Patricia Mattle

In addition to the collective foundations business, AXA is also active in the reinsurance business for pension funds. How satisfied are you with AXA's performance in this market segment during the reporting year?

We have been able to grow substantially in an intensely competitive market environment. The reinsurance market continues to be fiercely contested and highly competitive. Our competitors are life insurers who have specialized in the pension fund reinsurance business. To survive in this market, it's essential to offer a fully integrated range of products at competitive prices. We succeeded very well in this regard during 2017. At the same time, we have successfully established our market position as a provider of modular solutions. One key success factor here was the reinsurance solution with risk coverage of the regulations.

> **"We have successfully established our position as a provider of modular solutions."**

You mentioned the modular approach. What do you mean by that?

In all cases, the reinsurance solution also includes services that directly impact an occupational benefits institution's risk management. This is why we adopt a holistic advisory approach. A crucial point here is that the question of optimum risk reinsurance should not merely be reduced to financial, biometric or portfolio-related factors.
Management aspects also play a part in the decision. This is why our reinsurance solutions have a modular structure so that they can be optimally matched to our customers' requirements.

At the same time, we have continued to expand our range of products so that we can offer even more individual responses to our customers' requirements. Our new offerings include "Case Management" and legal protection insurance for pension funds.

Which challenges do you anticipate?

For years, our focus in the reinsurance business has clearly been on pure risk coverage without savings and longevity, but the fundamental problems of occupational benefits insurance also impact the reinsurance business. We shall present alternative options to company-owned foundations that have full-value insurance with us: for example, affiliation to a collective foundation and new investment possibilities. And we shall offer them full support during the transformation process. As a longstanding partner of company-owned foundations, we are responsible for offering them a sustainable reinsurance solution. And we shall gladly fulfill that responsibility.

And what will happen as regards inter-company solutions?

Most inter-company customers also have full-value insurance with us in addition to risk reinsurance. As in the case of the collective foundations, we shall present the attractive new models to these customers and work with them to develop the solution that is ideal for them. We shall actively support them in the transformation process. Our aim is to develop optimal solutions for these customers and their affiliated companies, and to continue the excellent customer relationships that have been built up over the years.

Moving toward semi-autonomy

In April this year, AXA announced that it will no longer offer full-value insurance as of the start of 2019, and will convert the existing full-value insurance foundations into semi-autonomous foundations. What changes will there be at AXA Life and the foundations because of this step?

Until now, AXA Life has offered its customers full-value insurance solutions through three collective foundations, and in other ways. The investment risks and the risks of old age, death and disability were each covered by AXA Life, so the full-value insurance collective foundations and the affiliated customers bore no risks.

In addition to full-value insurance, AXA Life has also been offering semi-autonomous pension solutions for about 20 years. So the company has many years' experience of collaborating with semi-autonomous foundations.

As was announced on April 10, 2018, AXA Life has decided, together with the trustees of the full-value insurance collective foundations, to transfer the full-value insurance collective foundations into semi-autonomy. As part of this transformation, the risk of old age and the investment risks and/or the savings process will be transferred to the semi-autonomous collective foundations. This includes interest on retirement assets as well as new retirement pensions to be added as from January 1, 2019. The existing retirement pensioners remain in AXA's existing customer base and for this reason, the new foundations are being launched with an extremely attractive age structure. Accordingly, customers of the semi-autonomous collective foundations will benefit from higher returns in the long term, because semi-autonomous solutions offer more scope for the investment policy than full-value insurance. But at the same time, the customers also participate in bearing the investment risks. This means that the semi-autonomous foundations could become underfunded. Such underfunding is permitted on a temporary basis without an immediate need for restructuring measures, whereas this is not the case with full-value insurance.

The foundations are equipped with a solid coverage ratio of about 111 % (calculation as at December 31, 2017), so they will have fluctuation reserves of around 11 % at their disposal. These reserves can help to compensate for market fluctuations over time.

In the future too, AXA will cover the risks of disability and death, as well as all current retirement and survivors' pension benefits

	Full-value insurance	Semi-autonomous solution
Risks of disability and death	AXA	AXA
Investment strategy / investment risks	AXA	Foundation
Asset management	AXA	AXA
Current pension benefits	AXA	AXA
Future pension benefits	AXA	Foundation
Administration	AXA	AXA
Supervisory authority*	FINMA	BVS/FINMA

* The BVG and Foundation Supervision of the Canton of Zurich (BVS) will supervise the new semi-autonomous foundations. Current retirement and survivors' pensions as at December 31, 2018 as well as the risk tariff, risk pensions and the minimum distribution ratio will remain under the supervision of the Swiss Financial Market Supervisory Authority (FINMA).

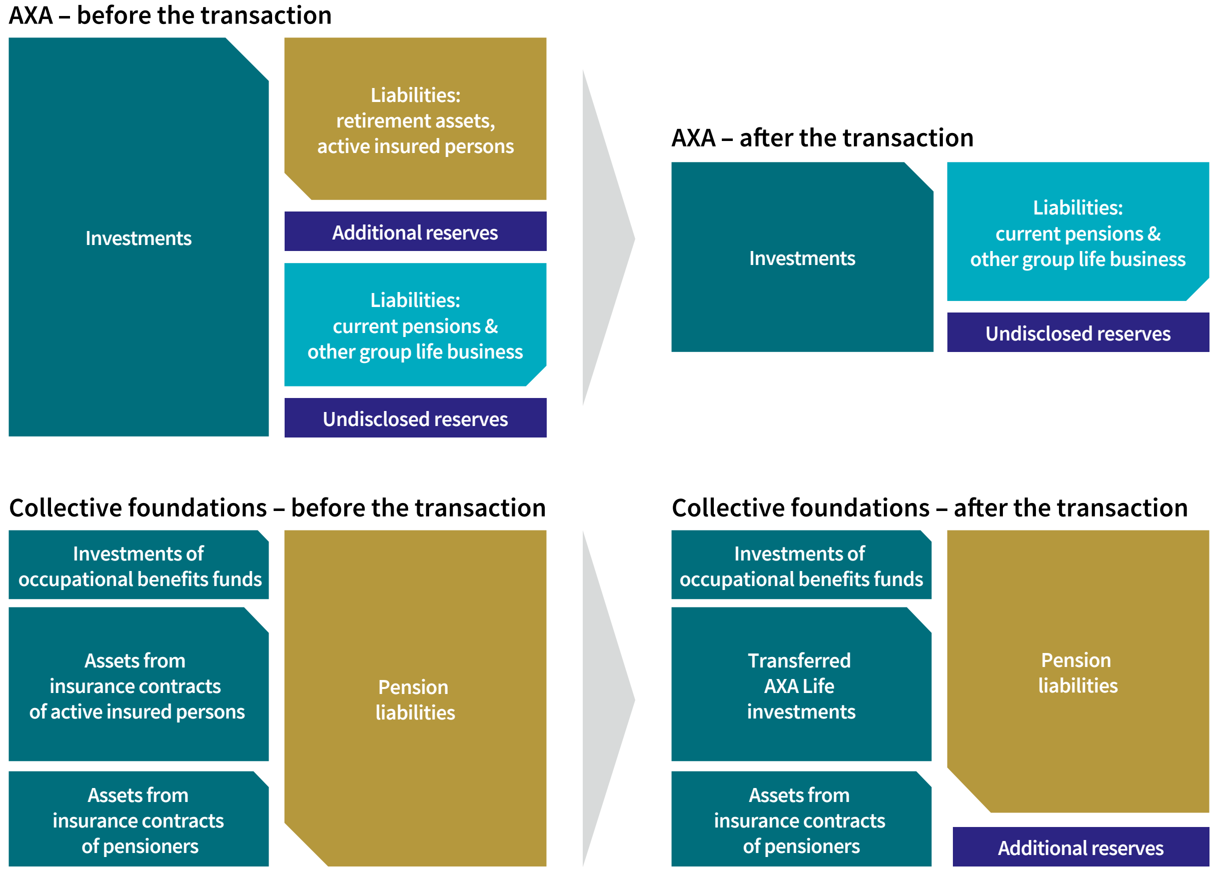
With 85 % of the retirement assets of AXA Life, a substantial portion of the Group Life portfolio will move from the AXA Life balance sheet onto the balance sheets of the relevant foundations as of January 1, 2019. The foundations already carry the retirement assets on their books as pension liabilities. From January 2019 onwards, the corresponding securities will be transferred to the foundations. The undisclosed investment reserves implicitly involved in the transfer are to be used by the foundations to form (or strengthen) the additional reserves.

When allocating the investments, AXA Life will pay particular attention to ensure that all policyholders receive fair and equal treatment. It will take care to ensure adequate funding for the remaining retirement and survivors' pensions.

For AXA, the cession of the risks for active insured persons frees up not only the retirement assets but also additional reserves that are no longer required and, in accordance with the provisions of supervisory law, these are to be transferred to the foundations' additional reserves for the specified purposes. AXA will continue to make its investment expertise available to the collective foundations and, as already mentioned, will handle asset management for the investments.

The move to the semi-autonomous solution decided upon by AXA Life and the responsible trustees has taken place in consultation with the BVS. The Financial Market Supervisory Authority (FINMA) has examined compliance with requirements under insurance supervision legislation.

Transfer of funds to the foundations



Key data

Number of insured persons
At the end of 2017, AXA had 590,025 insured persons with occupational benefits insurance. This figure includes 402,300 active insured persons, 70,121 pension recipients and 117,605 vested benefits policies.

The portfolio of insured persons decreased by 10,934 or 1.8 % year-on-year. The declining number of vested benefits policies accounted for most of this downturn. In 2017, for example, credit balances from 7,431 vested benefits policies were transferred to the new occupational benefits institution of the insured persons concerned.

AXA will continue to audit and streamline the portfolio of vested benefits policies, so the number of such policies will decrease again next year.

Conversion rates
The statutory pension conversion rate for mandatory benefits remains high at 6.8 %. On the other hand, life insurers have some leeway as regards the conversion rate for extra-mandatory benefits. The reduction of the conversion rate to 5 % by 2018 as announced by AXA in spring 2015 had a positive impact again in 2017, as was already the case in the prior year; this relieved pressure on losses due to pension conversions.

Costs for active insured persons
Operating expense for active insured persons decreased from CHF 182 million in the prior year to CHF 181 million, and costs per active insured person showed a slight increase of 0.4 % to reach CHF 450. This increase is due to the smaller number of active insured persons.

AXA focuses particular attention on operating expense and aims to continue optimizing this figure in the future by boosting efficiency.

	2017		2016	
Existing customer base at end of accounting year	590,025		600,959	
Number of active insured persons	402,300		406,183	
Number of pension recipients	70,121		69,740	
Number of vested benefits policies	117,605		125,036	
Interest and conversion rates	Mandatory benefits	Extra-mandatory benefits	Mandatory benefits	Extra-mandatory benefits
Effective interest rate including surplus participation	1.00 %	0.50 %	1.25 %	1.25 %
Interest rate applied to retirement assets	1.00 %	0.00 %	1.25 %	0.50 %
Pension conversion rate for men retiring at age 65	6.80 %	5.17 %	6.80 %	5.39 %
Pension conversion rate for women retiring at age 64	6.80 %	5.05 %	6.80 %	5.26 %
Technical interest rate for valuation of the pension liabilities	1.35 %		1.50 %	
	Total in millions	per capita	Total in millions	per capita
Total cost premium	190		192	
Active insured persons	190	473	192	472
Vested benefits policies / per policy	0	0	0	0
Other cost premiums	0	0	0	0
Total operating expense	217		217	
Active insured persons	181	450	182	448
Pension recipients	30	433	30	425
Vested benefits policies	5	46	6	46
Operating expense for other cost units	0	0	0	0

Monetary amounts in CHF

Income statement

Income	2017	2016
Contributions to retirement assets	2,508	2,481
Retirement assets transferred in (transferred individually)	2,678	2,888
Retirement assets transferred in (transferred in connection with new affiliations)	540	567
Deposits for transferred retirement and survivors' pensions	40	46
Deposits for transferred disability pensions	30	32
Deposits for vested benefits policies	3	53
Savings premiums	5,799	6,066
Risk premiums	580	606
Cost premiums	190	192
Total premiums	**6,569**	**6,864**
Direct earnings from investments	1,634	1,661
Result from disposals	329	115
Currency result	– 442	– 331
Balance from write-ups and write-downs	– 113	357
Interest expense	– 22	– 21
Asset management costs	– 218	– 197
Total investment income, net	**1,167**	**1,583**
Other earnings (total)	**10**	**10**
Reinsurance result	**– 20**	**– 13**
Total income	**7,726**	**8,444**

Expenditure	2017	2016
Retirement, death and disability benefits	2,014	1,989
Vested benefits	3,546	3,743
Surrender values	1,189	1,497
Expenses for processing benefits	30	30
Total insurance benefits, gross	**6,779**	**7,259**
Retirement assets	– 82	15
Actuarial reserves for current retirement and survivors' pensions	662	689
Actuarial reserves for current disability pensions	– 108	– 104
Actuarial reserves for vested benefits policies	– 241	– 488
Provision for insurance cases which have occurred but have not yet been settled	– 10	8
Other technical provisions	209	572
Total change in technical provisions, gross	**430**	**692**
Acquisition and administrative expenses, gross	**187**	**188**
Other expenses (total)	**10**	**11**
Surplus participation allocated to surplus fund	**144**	**79**
Operating result	**176**	**215**
Total expenditure	**7,726**	**8,444**

Monetary amounts in CHF

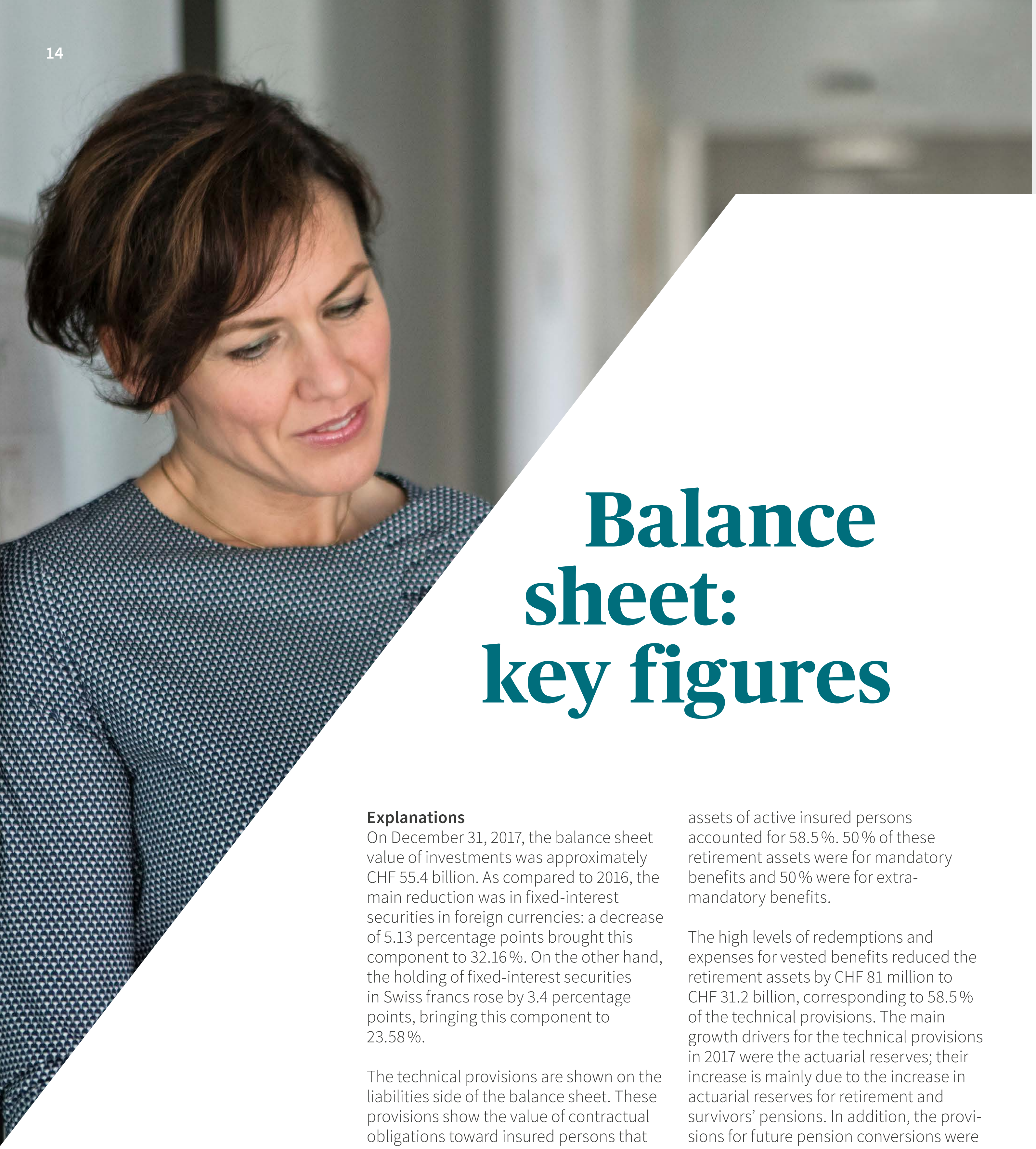
Explanations
In occupational benefits insurance, the total income consists mainly of savings premiums, risk premiums and cost premiums together with investment income. This figure decreased by 8.5% year-on-year. Premium income in Group Life fell by 4.3% or CHF 295 million to CHF 6.6 billion – single premiums decreased by 8.2% to CHF 3.3 billion while annual premiums were stagnant at CHF 3.3 billion. Investment income decreased by CHF 416 million year-on-year.

The decision to discontinue offering vested benefits policies was followed through consistently in 2017, leading to a decrease in single payments for vested benefits of CHF 50 million. Other single payments decreased by CHF 245 million, principally because fewer retirement assets were transferred in. In keeping with its strategy, AXA continued to pursue a selective underwriting policy in new full-value insurance business.

The most important items making up overall expenditure are benefits for insured persons, technical provisions, administrative expenses, and insured persons' participation in the surplus allocated to the surplus fund. Indemnities decreased by 6.6% or CHF 480 million to CHF 6.8 billion in the reporting year. This decrease is due to lower expenditure for redemptions and vested benefits.

The increase of CHF 0.4 billion in technical provisions during 2017 was less pronounced than in the prior year (CHF 0.7 billion). Retirement assets decreased by CHF 82 million because of numerous outflows due to vested benefits and redemptions (prior year: increase of CHF 15 million). Provisions for vested benefits policies could be reduced by a further CHF 241 million thanks to the smaller portfolio (prior year: reduction of CHF 488 million). Other technical provisions were strengthened again due to the sustained low interest rate environment, with the exception of provisions for current disability pensions; in this case, a further reduction was possible thanks to a higher rate of return to active status.

In 2017, acquisition and administrative expenses together with other expenses were unchanged from the prior year, at CHF 197 million. The allocation to the surplus fund in favor of insured persons rose to about CHF 144 million. The operating result for 2017 amounted to CHF 176 million (before tax). The decrease of CHF 39 million is mainly attributable to a lower investment result.



Balance sheet: key figures

Explanations
On December 31, 2017, the balance sheet value of investments was approximately CHF 55.4 billion. As compared to 2016, the main reduction was in fixed-interest securities in foreign currencies: a decrease of 5.13 percentage points brought this component to 32.16 %. On the other hand, the holding of fixed-interest securities in Swiss francs rose by 3.4 percentage points, bringing this component to 23.58 %.

The technical provisions are shown on the liabilities side of the balance sheet. These provisions show the value of contractual obligations toward insured persons that must be guaranteed in the long term. Insurers are obliged to form adequate provisions and to review their adequacy regularly on the basis of the currently applicable mathematical parameters.

As at December 31, 2017, the technical provisions amounted to around CHF 53.4 billion, corresponding to the guarantees we have provided for our insured persons. Of this figure, retirement assets of active insured persons accounted for 58.5 %. 50 % of these retirement assets were for mandatory benefits and 50 % were for extra-mandatory benefits.

The high levels of redemptions and expenses for vested benefits reduced the retirement assets by CHF 81 million to CHF 31.2 billion, corresponding to 58.5 % of the technical provisions. The main growth drivers for the technical provisions in 2017 were the actuarial reserves; their increase is mainly due to the increase in actuarial reserves for retirement and survivors' pensions. In addition, the provisions for future pension conversions were increased by CHF 200 million.

Asset items

Asset items	2017		2016	
Cash and cash equivalents, time deposits	1,475	2.66 %	510	0.88 %
Fixed-interest securities in Swiss francs	13,065	23.58 %	11,662	20.18 %
Fixed-interest securities in foreign currencies	17,821	32.16 %	21,556	37.29 %
Mortgages and other claims on nominal values	8,198	14.79 %	8,544	14.78 %
Swiss and foreign equities	1,320	2.38 %	1,178	2.04 %
Investment fund units	87	0.16 %	106	0.18 %
Private equity and hedge funds	3,791	6.84 %	3,705	6.41 %
Credit balances from derivative financial instruments	1,233	2.23 %	1,720	2.98 %
Investments in participations and associated companies	0	0.00 %	0	0.00 %
Real estate	8,420	15.20 %	8,820	15.26 %
Other investments	0	0.00 %	0	0.00 %
Total investments	55,411	100.00 %	57,801	100.00 %
Other assets	2,464		1,721	
Total net assets	57,875		59,522	

Liability items

Liability items	2017		2016	
Retirement assets	31,239	58.47 %	31,320	59.10 %
of which mandatory benefits	15,655		15,981	
of which extra-mandatory benefits	15,584		15,339	
Additional provision for future pension conversions	910	1.70 %	710	1.34 %
of which mandatory benefits	839		710	
of which extra-mandatory benefits	71		0	
Actuarial reserves for current retirement and survivors' pensions	13,380	25.04 %	12,717	24.00 %
of which mandatory benefits	7,286		6,875	
of which extra-mandatory benefits	6,094		5,842	
Actuarial reserves for current disability pensions	1,650	3.09 %	1,758	3.32 %
of which mandatory benefits	959		1,041	
of which extra-mandatory benefits	691		717	
Strengthening of actuarial reserves for current pensions	3,180	5.95 %	3,164	5.97 %
of which mandatory benefits	1,598		1,617	
of which extra-mandatory benefits	1,581		1,547	
Actuarial reserves for vested benefits policies	1,767	3.31 %	2,008	3.79 %
Provision for insurance cases which have occurred but have not yet been settled	386	0.72 %	396	0.75 %
Cost-of-living (COL) fund	651	1.22 %	650	1.23 %
Credited surplus portions	0	0.00 %	0	0.00 %
Other technical provisions	266	0.50 %	274	0.52 %
Total technical provisions, gross	53,429	100.00 %	52,997	100.00 %
Surplus fund	251		237	
Other obligations	2,770		3,519	
Other liabilities	1,426		2,768	
Total net assets	57,875		59,522	

Monetary amounts in CHF millions

Investments

AXA aims to achieve the optimum combination of profitability, liquidity and security when managing its investments. It has been investing for some years now to enhance its asset-liability management (ALM) capability. The analyses and findings from this process provide the basis for an investment strategy that aims to optimize the risk-return ratio of the portfolio as well as the level of risk capital. It is vital to ensure that, despite fluctuations in the value of investments, there is always enough equity available to meet the company's obligations at all times.

Investments broken down by asset class
In line with our principle of security, the majority of funds are invested in fixed-interest securities, with the focus on top-quality and corporate bonds. Top-quality bonds include Swiss government bonds and mortgage bonds. As they are considered to be virtually risk-free, they offer correspondingly low returns.

The decrease in fixed-interest securities is mainly attributable to a reduction in foreign currencies. The real estate portfolio also decreased slightly due to sales. In view of the positive market assessment, however, the equities and private equity component was increased again in 2017.

Net credit balances from derivative financial instruments mainly comprise derivatives for currency hedging and the corresponding collateral deposited.

The "Other investments" item comprises mortgages, loans, and cash and cash equivalents. The higher figure here is due to an increase in cash and cash equivalents.

The valuation reserves show the difference between market and book values. The sharp increase is caused mainly by the ongoing increase in real estate values and the positive trend on the equity markets in the reporting year.

Investments

	2017		2016	
	Book value	Market value	Book value	Market value
Real property and buildings	8,222	10,912	8,621	10,566
Shares in real estate companies	198	324	198	317
Shares in associated companies	0	0	0	0
Participations	0	0	0	0
Equities and units in investment funds	1,408	1,869	1,284	1,540
Other non-fixed-interest securities	0	0	0	0
Own equities	0	0	0	0
Fixed-interest securities	30,887	33,105	33,219	35,576
Hedge funds	1,763	2,015	1,944	2,157
Private equity	2,028	2,351	1,761	2,035
Net credit balances from derivative financial instruments	199	199	225	225
Other investments	9,673	9,673	9,054	9,054
Total investments	**54,378**	**60,448**	**56,306**	**61,470**
Share of collective investments		4.69 %		3.81 %
Share of investments with non-specified costs		2.73 %		3.19 %
Valuation reserves at the end of the accounting year		**6,070**		**5,164**
Change in valuation reserves compared to previous year		**906**		**159**

Monetary amounts in CHF millions

Return earned and performance of investments
The gross return on investments of CHF 1.385 billion corresponds to a return on book values of 2.50 % (prior year: 3.22 %). After deduction of asset management costs, the net return was 2.11 %. The reduction in book yield was due mainly to higher write-downs on real estate and equity hedging derivatives.

Trend of return on investments

	2017		2016	
Direct earnings from investments	1,634		1,661	
Other investment income	– 248		120	
Result from disposals	329		115	
Currency result	– 442		– 331	
Balance of write-ups and write-downs	– 113		357	
Interest expense	– 22		– 21	
Investment income, gross	**1,385**		**1,779**	
Asset management costs	– 218		– 197	
Investment income, net	**1,167**		**1,583**	
Asset management without real estate maintenance	– 218	– 0.36 %	– 197	– 0.33 %
Maintenance and servicing of real estate*	– 83	– 0.14 %	– 83	– 0.14 %
Total asset management costs	**– 302**	**– 0.49 %**	**– 279**	**– 0.46 %**

Monetary amounts in CHF millions

* Costs of maintenance and servicing of real estate are directly offset in the income statement against real estate earnings (net view).

Gross market yield is the market yield before deduction of asset management costs; Total Expense Ratio costs (TER costs) are already deducted from the net market yield. Net market yield rose by 3.40 % year-on-year. In addition to equities, alternative investments such as hedge funds and private equity as well as convertible bonds should be singled out for their very good performance. Furthermore, the real estate portfolio benefited not only from stable rental income with a high occupancy rate, but also from the continuing increase in market values.

In 2017, asset management costs amounted to CHF 302 million. The year-on-year increase of CHF 23 million is due to an increase in transaction costs for direct investments together with higher asset management costs for single-level collective investments. At CHF 83 million, real estate maintenance costs were unchanged year-on-year.

Return and performance

	2017		2016	
	Gross	Net	Gross	Net
Total return on book values	2.50 %	2.11 %	3.22 %	2.86 %
Market value performance	3.76 %	3.40 %	3.21 %	2.88 %

Investment returns for 2017 by investment category

	Market value performance	Return on book values	Contribution to total return
Fixed-interest investments and other investments	2.59 %	2.72 %	1.71 %
Convertible bonds	6.26 %	6.81 %	0.18 %
Equities	18.99 %	9.81 %	0.51 %
Hedge funds	7.81 %	6.18 %	0.26 %
Private equity	10.91 %	10.67 %	0.37 %
Real estate	11.39 %	5.88 %	2.07 %
Others	– 1.94 %	– 1.76 %	– 1.34 %
Total return, gross	3.76 %	2.50 %	3.76 %
Minus asset management costs	– 0.36 %	– 0.39 %	– 0.36 %
Total return, net	3.40 %	2.11 %	3.40 %

Asset management costs, 2017

	Market value	Costs caused			
		TER costs	TTC costs	SC costs	Total
Direct investments	55,964	– 181	– 35		– 216
Single-level collective investments	2,699	– 60	0		– 60
Multiple-level collective investments	138	– 9	0		– 9
Investments with non-specified costs	1,647	0	0		0
Total market value / Total before capitalization	60,449	– 249	– 35	– 19	– 304
Capitalized costs		0	2	0	2
Total recognized in income		– 249	– 33	– 19	– 302

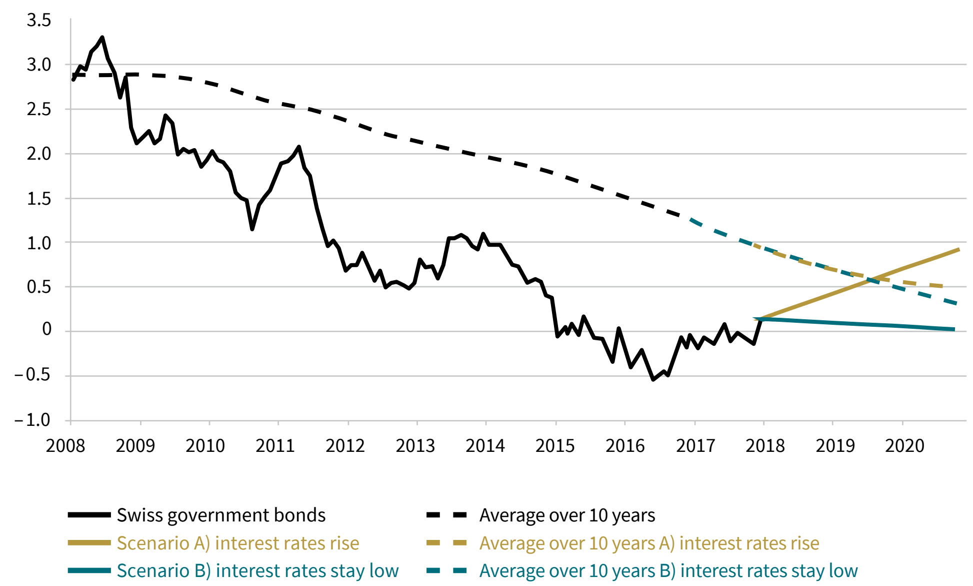
Monetary amounts in CHF millions

TER costs: Costs of administration and management (internal and external)
TTC costs: Transaction costs
SC costs: Costs that cannot be allocated to individual investments

Outlook for 2018

2018 will again see the investment market influenced by global macroeconomic uncertainties, volatile commodity prices, interventions by various central banks and political events. The interest rate level recovered slightly at the start of 2018 but it remains very low and continues to present a major challenge. At the end of 2017, interest rates for Swiss government bonds with a maturity of 10 years were at the low level of minus 0.15 %. Even if interest rates should rise again, the average yield on fixed-interest securities will continue to decline in the near future due to low interest rates in preceding years. If interest rates on risk-free investments remain at their current low level, the decline in average returns will be accentuated, as the chart opposite illustrates. In order to mitigate the effects of low interest rates, AXA is adhering to its tried-and-tested strategy of diversified investment.

Yield on 10-year Swiss government bonds



Source: Bloomberg; Interest rate trend to February 2018

Minimum distribution ratio (MDR)

Explanations
The majority of group life business is subject to statutory provisions governing the minimum distribution ratio (MDR). These provisions state that at least 90 % of the income generated must be used for the benefit of active insured persons – i.e. for insurance benefits, strengthening reserves, and allocations to the surplus fund. At 91.0 %, AXA's distribution ratio exceeded the statutory minimum in the reporting year.

Explanation of business processes
We distinguish between three basic business processes:

Process	Revenues	Expenses (benefit)
Saving process	Net investment income	• Interest paid on retirement assets and actuarial reserves for current pensions, conversion losses • Formation and reversal of technical provisions for longevity risk, interest guarantees and fluctuations in the value of investments
Risk process	Risk premium	• Payment of death and disability benefits • Formation and reversal of technical provisions for insurance cases reported but not settled, for insurance cases which have occurred but have not yet been reported, for claims fluctuations as well as for rate adjustments and rate restructuring
Cost process	Cost premium	• Administrative and customer advisory services related to occupational pensions and insurance

	2017		2016	
	Subject to MDR	Not subject to MDR	Subject to MDR	Not subject to MDR
Sum of income components	**1,853**	**84**	**2,294**	**87**
Saving process (income from investments)	1,167	0	1,583	0
Risk process (risk premiums)	509	71	533	73
Cost process (cost premiums)	177	13	178	14
Total expenditure	**– 1,361**	**– 41**	**– 1,481**	**– 36**
Saving process (mainly technical interest)	– 898	0	– 999	0
Risk process (mainly death and disability benefits)	– 284	– 33	– 302	– 28
Cost process (mainly administrative costs)	– 179	– 7	– 180	– 8
Gross result, operating statement	**492**	**43**	**813**	**51**
Change in technical provisions in the saving process	**– 227**	**0**	**– 570**	**0**
Longevity risk	– 27	0	– 500	0
Gaps in coverage on conversion into pensions	– 200	0	– 70	0
Interest guarantees	0	0	0	0
Fluctuations in value of investments	0	0	0	0
Change in technical provisions in the risk process	**5**	**7**	**– 2**	**2**
Insurance cases reported but not yet settled	5	7	– 2	2
Insurance cases which have occurred but have not yet been reported	0	0	0	0
Fluctuations in claims	0	0	0	0
Rate adjustments and rate restructuring	0	0	0	0
Total change in technical provisions	**– 222**	**7**	**– 572**	**2**
Cost of raising additional risk capital	**0**	**0**	**0**	**0**
Allocation to surplus fund	**– 103**	**– 41**	**– 35**	**– 44**
Result, operating statement	**167**	**9**	**206**	**9**
Dividend ratio	**91.00 %**	**89.52 %**	**91.00 %**	**89.91 %**
Recapitulation of the operating result				
Share of business subject to MDR	167		206	
Share of total income as %	9.00 %		9.00 %	
Share of business not subject to MDR		9		9
Share of total income as %		10.48 %		10.09 %
Operating result	**176**		**215**	
Share of total income as %	9.06 %		9.04 %	

Monetary amounts in CHF millions

Earnings and expenditure

In occupational benefits insurance, the various elements of income and expense are assigned to the saving, risk and cost processes. Within each of the three processes, certain items of income are posted against certain expense items. Although, as a general rule, each process should function independently, cross-subsidization is possible.

Change to technical provisions

Technical provisions are reserves that AXA uses to strengthen its ability to meet future challenges. In 2017, the technical provisions were strengthened by a total of CHF 222 million, following an increase in the prior year.

In the saving process, technical provisions were increased by CHF 227 million in response to demographic trends and sustained low interest rates. CHF 27 million was set aside for the longevity risk and CHF 200 million for the coverage gap in future pension conversions.

In the risk process, provisions were reduced by CHF 5 million for insurance cases that were reported but not yet settled.

Division of income between insured persons and AXA

AXA's operating result depends directly on the applicable revenue, which consists of the return on investments, the risk premium and the cost premium. It is limited to a maximum of 10 % by the dividend ratio (Legal Quote). For business subject to the minimum ratio regulations, a total of CHF 1.686 billion went to insured persons in 2017 – in the form of indemnities, higher reserves and allocations to the surplus fund. This equates to a dividend ratio of 91.0 %. AXA's profit – the remaining 9 % – was CHF 167 million (before tax) in 2017.

Redistribution

Redistribution	2017	2016	2015	2014	2013	2012	2011
Total	499	811	827	520	416	352	254
Conversion rate loss in the current year	272	241	257	270	196	132	74
Strengthening of provisions for recipients of retirement pensions	227	570	570	250	220	220	180

Monetary amounts in CHF millions

How the minimum distribution ratio is calculated

	2017	2017 Total	2016	2016 Total
Income components				
Saving process – Income from investments	+ 1,167	Total 1,853	+ 1,583	Total 2,294
Risk process – Premium income from death and disability insurance	+ 509		+ 533	
Cost process – Premium income for operations and service	+ 177		+ 178	
At least 90 % of the income components go to insured persons in the form of benefits		91.0 %		91.0 %
Use for the following benefits for insured persons				
1. Interest on retirement assets of insured persons and conversion losses	– 898	Total – 1,361	– 999	Total – 1,481
2. Benefits in the event of disability and death	– 284		– 302	
3. Administration, operations and service	– 179		– 180	
Formation of reserves for future benefits for insured persons				
1. Longevity	– 27	Total – 222	– 500	Total – 572
2. Gap in coverage on conversion into pensions	– 200		– 70	
3. Interest guarantees due to persistent low interest rate phase	0		0	
4. Expected benefit cases due to disability	5		– 2	
Allocation to surplus fund to be used for insured persons		– 103		– 35
Total benefits allocated to insured persons		– 1,686		– 2,088
The profits of life insurers are limited by law and cannot exceed 10 % of the income components		9.0 %		9.0 %
Operating result for AXA Life Ltd. from business subject to MDR (gross before tax)		167		206

Monetary amounts in CHF millions

Risk process

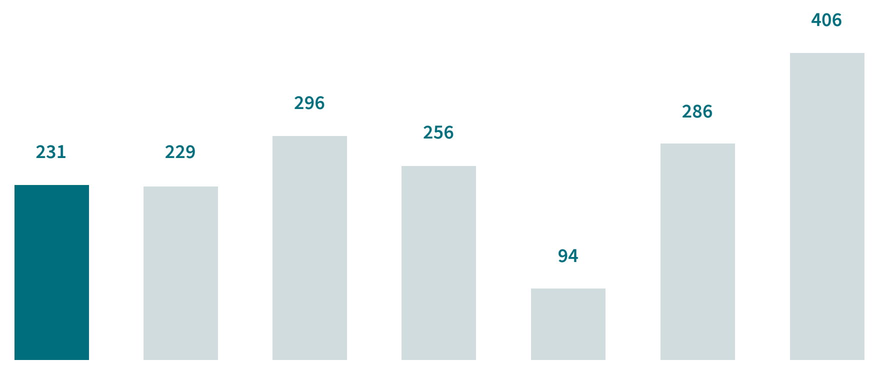
Explanations
The risk process comprises income from risk premiums, expenses in the form of death and disability benefits and also the formation and / or reversal of technical provisions.

By law, AXA is entitled to retain a maximum of 10 % of the risk premiums as its profit share for guaranteeing the risk benefits. 90 % goes to the insured persons in the form of current and future benefits.

The difference between revenues from risk premiums and expenses in the form of benefits and provisions amounted to CHF 231 million in 2017, representing a year-on-year increase of around CHF 2 million. Revenues from risk premiums fell by CHF 24 million while direct benefit payments decreased by CHF 18 million.

In 2017, a large portion of earnings from the risk process was used to cross-subsidize ongoing annuitization losses and to bolster provisions for future conversion losses – always, therefore, in favor of future benefits to the insured persons.

This basic principle applies to business subject to MDR: Higher benefit expenditure and the formation of provisions for future benefits to insured persons result in fewer allocations to the surplus fund, and vice-versa.



Risk process	2017	2016	2015	2014	2013	2012	2011
Risk premiums	509	533	572	568	577	601	617
Risk benefits	– 284	– 302	– 275	– 240	– 322	– 267	– 296
Provisions for expected disability (IV) cases	5	– 2	– 2	– 73	– 160	– 48	85
Result of risk process	231	229	296	256	94	286	406

Monetary amounts in CHF millions

Surplus fund

	2017	2016
As at end of previous year	237	364
Allocated to the surplus fund from the operating account	144	79
Valuation adjustment	0	0
Withdrawn from surplus fund to cover an operating shortfall	0	0
Allocated to occupational benefits institutions	– 131	– 205
As at end of accounting year	251	237

Monetary amounts in CHF millions

Explanations
Life insurers provide security at all times, which is why they calculate their premiums in such a way that all risks can be covered over the long term. As a consequence of this, they generate a surplus (which is allocated to the insured persons) when business performance is good – i.e. when their earnings are greater than their expenses.

By law, no more than two-thirds of the surplus fund may be withdrawn in any one year. Every allocation must be paid out to the insured persons within five years. This mechanism ensures that sufficient funds are available to offset poor results in difficult years and that the fund is built up again in good years, an approach that complies with the principles of sustainability and stability in occupational benefits insurance.

Stability and continuity are AXA's top priority in the context of sharing profits and surpluses. This is why provisions are formed in the surplus fund for future surplus participation. They originate from earnings in the current insurance year, and they reach the insured persons either directly in the form of interest credits on retirement assets or indirectly in the form of premium reductions granted.

In 2017, AXA was able to allocate CHF 144 million to the surplus fund; of this, CHF 103 million originated from business subject to MDR. The total allocation in the reporting year was CHF 65 million above the prior year's figure.

In 2017, CHF 131 million was allocated from the surplus fund to persons insured with AXA; CHF 77 million of this came from business subject to MDR.

Cost-of-living (COL) fund

Explanations
The cost-of-living fund is used to finance future inflation-related adjustments to current disability and survivors' pensions, as stipulated by law. The fund is fed using the cost-of-living premiums of active insured persons, and it also attracts interest. Current pensions are generally adjusted for inflation every two years. A contribution to cost expenses is also taken from the cost-of-living fund.

Survivors' and disability pensions which are paid out for a period of more than three years must be adjusted for inflation in line with the Swiss Consumer Price Index until the recipients reach regular retirement age. The Federal Social Insurance Office publishes the relevant tables annually.

	2017	2016
As at end of previous year	650	639
Cost-of-living premiums received	4	14
Premium interest	0	0
Expenditure for COL increases in risk pensions	0	0
Withdrawal for cost expenses	–3	–3
As at end of accounting year	651	650

Monetary amounts in CHF millions

Operating expense and asset management costs

Breakdown of operating expense	2017		2016	
Commission paid to sales force	36		35	
Commission paid to brokers	29		30	
Other acquisition costs	12		12	
Acquisition costs	77	35.48 %	77	35.48 %
Benefit processing expenses	30	13.82 %	30	13.82 %
Marketing and advertising expenses	3	1.38 %	3	1.38 %
Staff costs	77		73	
Material expenses (including IT costs)	30		35	
Other expenses for general administration	107	49.31 %	108	49.77 %
Reinsurers' share in operating expense	0	0.00 %	0	0.00 %
Total net operating expense	217	100.00 %	217	100.00 %
Costs of asset management without real estate maintenance	–218	–0.36 %	–197	–0.33 %
Costs of maintenance and servicing of real estate*	–83	–0.14 %	–83	–0.14 %
Costs of asset management with real estate maintenance	–302	–0.49 %	–279	–0.46 %

Monetary amounts in CHF millions

* The costs of maintenance and servicing of real estate are offset in the income statement directly against real estate income (net view).

In 2017, asset management costs amounted to CHF 302 million. The year-on-year increase of CHF 23 million is due to an increase in transaction costs for direct investments together with higher transaction costs for single-level collective investments (also see the schedule of TER costs in the Investments section.) Real estate maintenance costs have remained level year-on-year.

The operating and management costs of CHF 217 million include all acquisition and administrative expenses and consulting costs incurred due to AXA's business activities in connection with occupational benefits insurance.

To make the cost process more transparent, acquisition costs are reported in detail, with information provided on acquisition commission for brokers as well as other general administration expenses, broken down by staff costs and material costs.

Operating costs remained stable year-on-year, at CHF 217 million. The increase in staff costs to CHF 77 million is mainly the result of the transfer of employees from the group company AXA Services Switzerland AG. The lower material costs of CHF 30 million are related to the correspondingly lower payment offsets for this company.

Asset management costs do not count toward operating expenses, but are included in the income statement directly as part of the net return on investments.

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