

## Elo Interim Report 1 January–30 June 2017

The comparison figures in brackets are figures for 30 June 2016.

- **Return on Elo's investments was 4.4%. The market value of Elo's investments was EUR 22.6 billion.**
- **Solvency strengthened; the solvency ratio was 126.1% and solvency capital was 1.7 times the solvency limit.**
- **The overall result was EUR 437 million.**
- **The expense loading ratio was 82.8%. Premium loading profits are burdened by a 7 per cent decrease in calculation basis applicable to all employment pension companies, so the loading ratio is not comparable with previous years. In the future, the loading profit will be distributed to customers in full instead of the previous 50 per cent.**

	1.1.–30.6.2017	1.1.–30.6.2016	1.1.–31.12.2016
Premiums written, EUR million	1,694.8	1,633.2	3,321.5
Net investment income at current value, EUR million	967.3	198.7	1,147.4
Net return from investment on capital employed, %	4.4 %	1.0 %	5.6 %

	30.6.2017	30.6.2016	31.12.2016
Technical provisions, EUR million	19,440.8	18,154.4	18,527.4
Solvency capital, EUR million	4,709.3	3,870.4	4,270.9
ratio to solvency limit	1.7	1.9	1.8
Pension assets, EUR million <sup>2)</sup>	22,771.9	20,924.3	21,825.3
% of technical provisions <sup>1)</sup>	126.1 %	122.7 %	124.3 %
TyEL payroll, EUR million <sup>3)</sup>	12,194.1	11,658.0	11,943.7
YEL earned income sum, EUR million <sup>3)</sup>	1,871.9	1,873.3	1,861.6

<sup>1)</sup> Ratio calculated as percentage of the technical provisions used in the calculation of the solvency limit

<sup>2)</sup> Technical provisions + valuation difference

<sup>3)</sup> Estimate of policyholders' salary and reported earnings for the full year

### Economic environment and development of the investment market

Global economic growth accelerated slightly during the first half of the year compared to the previous year. The consensus estimate of global economic growth for 2017 is now 3.3 per cent, while last year it was 3.1 per cent. Consumer confidence has continued to be strong, and companies' relatively good performance has also been reflected as a growth in investments to some extent.

High unemployment rates in the euro economies is in decline while growth in the euro zone is picking up to a level of two per cent per year. With the picking of global growth and growth in the euro zone in particular, expectations of the growth of Finland's exports-driven national economy for the current year have been increasing during the first half of the year and already amount to approximately 2.5 per cent. The growth has also begun to be visible as improved employment rate, but the unemployment rate is still far too high, almost 9 per cent, with regard to our national economy's long-term view.

Growth has also picked up slightly compared to last year in emerging economies and Japan. In the United States, the new administration's expectations of significantly higher growth have remained unseen, at least for the time being, and the IMF, for example, has decreased the US growth outlook for this and the next year to 2.1 per cent.

In spite of the improved growth, the ascending trend of inflation rates stopped during the first half of the year after a couple of years, with both the actual inflation rate and expectations of inflation decreased in the OECD area and in particular in the United States. In the euro zone, five-year inflation expectations have remained low for a long time, only slightly over one per cent, which is clearly below the two per cent goal set by the European Central Bank.

Central banks' support for the markets has continued, and they are still aiming to safeguard economic growth. In the United States, however, there have been two rate hikes since the beginning of the year, and the US Federal

Reserve has announced that it will begin to reduce its balance sheet bloated with purchases of securities during the remainder of the year. In the euro zone and Japan, on the other hand, monetary policy has continued to be stimulating, significantly supporting the global financial and investment markets.

The global investment market, especially the equity market, has yielded extremely good returns since March 2009. This has been the second-longest streak of good returns from investments since World War II. During the first half of the year, the investment market developed positively again. The returns from most asset classes, such as the equity market and corporate bond investments, were positive in local currency terms. Of currencies, the US dollar in particular weakened quite strongly, which resulted in the returns from many asset classes turning negative when converted into euros.

### **Employment pension system**

The pension reform took effect at the start of 2017 and introduced two new types of pension: the partial early old-age pension and the career pension. The first career pensions will be issued in 2018. The partial early old-age pension has attracted particular attention, and it has been very popular. The popularity can be partially attributed to the fact that an increasing number of age groups are applying for the new pension at the same time. There have been unemployed people among the applicants.

The solvency requirement and the principles for determining it changed as of the beginning of 2017, and the method of presenting the key figures also changed at the same time. The presentation of solvency ratio changed so that it now shows how much the assets exceed the technical provision. The solvency limit is presented as euros instead of the former percentage.

The calculation of employment pension companies' expense loading was amended as of the beginning of 2017. The expense loading of employment pension premiums was decreased by approximately 7 per cent compared to the previous year as of the beginning of 2017. Therefore, the loading profit for 2017 is lower than for previous years, and the expense loading ratio is not directly comparable with previous years.

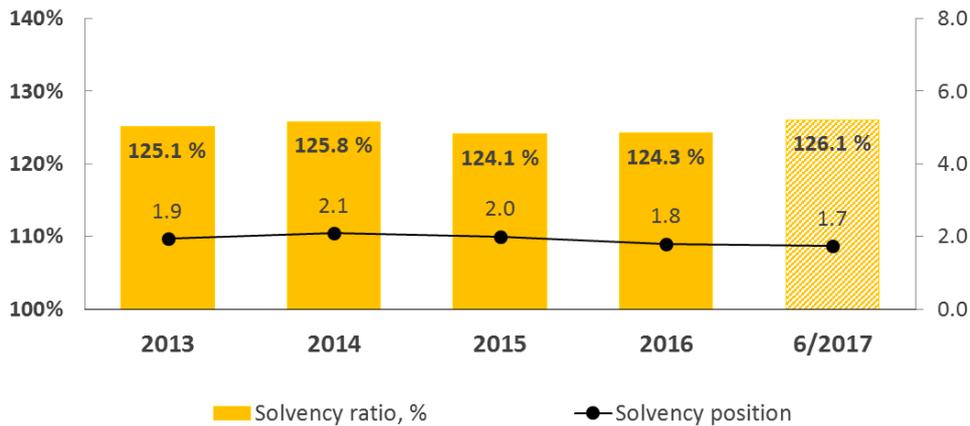
The Ministry of Social Affairs and Health confirmed the new pension employment company-specific customer bonus principles early in the year. The customer bonus is the part of the result of the employment pension company credited to the customer. The employment pension company's solvency and operational efficiency influence the amount of the customer bonus. Thanks to the reform, a pension employment company can transfer its entire loading profit to bonuses. The reform will be actually visible to customers after a transition period in 2019.

Elo's bonus principles are based on fairness. Elo distributes the loading profit resulting from operational efficiency to the customers that have contributed to it and takes the customer's full history into account in distributing the profit resulting from solvency. The company continues to reward long-term customers, but following the reform, newer and growing customers will accrue bonuses faster than before. Elo's customers will continue to receive competitive bonuses in the future.

During 2017, the Finnish Centre for Pensions announced an idea to reform the determination of entrepreneurs' pension cover. In terms of its main principles, YEL is still similar to what it was when the relevant act was prescribed in 1970. However, entrepreneurship has diversified in recent years, and it is perhaps the time to think about new solutions for entrepreneurs' pension cover. The customers of invoicing service companies, who are currently often left completely without pension cover, gave rise to particular debate.

### **Result and solvency**

The amount of solvency capital grew by EUR 438 million from the beginning of the year to EUR 4,709.0 million (EUR 3,870 million). The ratio of pension assets to technical provisions, i.e. the solvency ratio, was 126.1 per cent (22.7 per cent). The solvency capital was 1.7 (1.9) times the solvency limit.



The net return on investment operations at fair values stood at EUR 967 million (EUR 199 million). The return credited in technical provisions for the same period was EUR 528 million (EUR 297 million), of which technical provisions linked to equity income accounted for EUR 160 million (EUR –49 million). The result of investment operations at current value was thus EUR 440 million (EUR –98 million).

The loading profit came to EUR 10 million (EUR 14 million). The insurance business surplus was EUR –13 million (EUR –36 million), and other income EUR 0.2 million. Elo’s combined total result at current value was EUR 437 million (EUR –120 million).

Solvency capital	30.6.2017	30.6.2016	31.12.2016
Solvency limit, EUR million	2,719.4	2,046.5	2,367.6
Maximum amount of solvency capital, EUR million	8,158.1	8,186.0	9,470.6
Solvency capital, EUR million	4,709.3	3,870.4	4,270.9
Solvency ratio, % <sup>1)</sup>	126.1	122.7	124.3
Solvency capital/Solvency limit <sup>2)</sup>	1.7	1.9	1.8

<sup>1)</sup> Pension assets in relation to technical provisions as referred to in Section 11, item 10, of the Ministry of Social Affairs and Health’s decree 614/2008. All years are presented according to the new presentation method.

<sup>2)</sup> Solvency capital in relation to solvency limit

## Insurance business

Elo is the market leader in both TyEL and YEL pension insurance in terms of the number of policies. At the end of June, Elo administered 44,700 TyEL (46,000) and 84,000 YEL (84,600) insurance policies. The total number of self-employed persons and employees insured by Elo at the end of the reporting period was 484,200 (476,600), or almost half a million.

## Customer accounts

Policyholders are free to transfer their pension cover to another pension insurance company on four dates every year, provided they have waited one year from the previous transfer. Elo’s profit from this transfer business has been the largest ever so far. A total of 312 (316) TyEL and 514 (1,274) YEL insurance policies were transferred to Elo during the reporting period. The premiums written for TyEL insurance policies grew by EUR 12.2 million (EUR 5.3 million). During the reporting period, Elo gained 2,753 (2,796) TyEL and 4,225 (4,352) YEL insurance policies through new customer prospecting.

Elo works in close co-operation with Fennia, LocalTapiola and Turva and serves as the employment pension partner for all three companies. Elo’s services are available locally everywhere in Finland through our partners’

service networks. Successful and effective collaboration with the partners has significantly helped Elo to reinforce its position as the most popular employment pension company in Finland.

During the reporting period, Elo built new features for the customers' wellbeing at work online service, which are due to deployment in autumn 2017. The working capacity management online service will provide customers with access to diverse monitoring and reporting features for working capacity management and development in the future.

In May, Elo signed a unique cooperation agreement with the Finnish Institute of Occupational Health. The aim of the agreement is to provide Elo's customer companies with working capacity management services based on Finnish research. In addition, we will develop new kinds of solutions for supporting wellbeing at work and coping at work in cooperation with the Finnish Institute of Occupational Health for our customers.

Elo's statistics show that one in three entrepreneurs have confirmed their income as so low that it does not provide genuine cover for old age or, for example, unemployment. Therefore, Elo decided to focus particularly on communicating about the YEL insurance cover for entrepreneurs in 2017. In spring 2017, Elo opened the discussion of entrepreneurs YEL insurance cover through active communications. The message also attracted attention from the media, and the theme was discussed in several media channels. The discussion was also visible in Elo's customer service and website, as the number of contacts and related use of services increased considerably. Elo has carried out long-term development work to make the use of services easier. An example of this is the entrepreneurs' mobile application published in late 2016, whose user volumes and use have increased at a steady rate.

### **Pension services**

Elo issued a total of approximately 14,300 pension decisions on the basis of applications during the first half of the year. The partial early old-age, which was introduced at the beginning of the year, was a particularly popular form of pension. During the first half of the year, such pensions were issued to 1,536 customers.

The volumes of the new partial early old-age pension were higher than expected, but Elo succeeded in keeping its average pension processing time the quickest in the industry.

According to a survey by Elo, those receiving partial old-age pension from Elo are aware of the impacts of this new type of pension on the amount of their final old-age pension, and they are satisfied with the service they have received. The average processing time of partial old-age pensions was 7 days, which is 60 per cent faster than the industry average.

Approximately 223,300 pensioners were paid their pensions by Elo at the end of June. A total of EUR 1,551 million was paid in pensions during the first half of the year, of which old-age pensions accounted for EUR 1,294 (the figure includes partial early old-age pensions).

### **Digitalisation at Elo**

Digitalisation is increasingly visible in our customers' as well as Elo's operations. Elo considers digitalisation to be an essential and inseparable part of business and, in particular, its development. Digital competence will thus be part of each Elo employee's basic skills.

Increasing operational efficiency through robotics was investigated in pension and insurance services in early 2017. Based on an experiment, it has been found that the utilisation of analytics and artificial intelligence can refine many processes and sub-processes of pension insurance, and the pilot will go live before the end of 2017. The utilisation of digitalisation is increasingly strongly visible in investment activities in portfolio management as well as more efficient investment processes.

The completion of the national income register towards the end of the decade will result in changes in the customer interface. Elo has prepared for the change by revising its electronic services to be multi-channel for both private and corporate customers.

Elo has transitioned to the use of agile operating models in development work, and we procure as many services flexibly from cloud as possible. In the networking world, the importance of data security is increasing year by year, and Elo's investments in data security have also grown.

With the growth in digital services, Elo is also preparing for operating in new ecosystems which are not necessarily administered by Elo. The ability to connect to the customer's business process through interfaces will be essential in this respect. We estimate that employment pension companies will be part of the platform economy already in the next couple of years, and the opening of interfaces will also take place in the employment pension business.

### **Focal points of investment asset classes**

Investments in emerging markets in both equities and bonds yielded excellent returns again, and the share of such investments was visible in the result. In all, the returns from Elo's investment portfolios did well against the benchmark indices set for them.

Of equity markets, the best returns were achieved in Finland and emerging markets in both local currencies and euros. The pricing of equity markets has increased to a high level, but the profit growth expectations have also remained high. Elo's equity investments succeeded particularly well in emerging markets and Europe. The bond market developed positively during the first half of the year, and the investments with the highest risks yielded the best returns. The return from Elo's bond portfolio was reasonable due to Elo's emphasis on higher-risk investments.

With regard to currencies, the US dollar weakened by over 8 per cent against the euro, which slightly decreased Elo's return on investments. The share of Elo's open currency risk and the US dollar in particular of investments has, however, been kept relatively moderate during the first half of the year.

The demand for real investments continued to be strong in the investment market in spite of their high prices and valuation. However, the continued low interest rates maintains their appeal. The return on Elo's real estate investments remained steady and comprised of stable rental income and increase in the value of housing investments. Sales of EUR 160 million of real estate were connected to the formation of the seed portfolio of Agore Oy, a joint venture with Första AP Fonden and Trevian investing in real estate in the provinces. The biggest new investment commitments were made in Exilion's new hotel fund, which simultaneously concluded agreements on future hotel projects in Tripla in Pasila and the Helsinki railway station square.

The accelerated growth of Finland's economy was seen in Elo's corporate financing in the form of growing demand for loans. At the same time, the general supply of loan money to companies is at a good level and also provides an adequate foundation for the commencement of investments.

At the end of June, the value of Elo's investments was EUR 22,607 million (EUR 20,827 million). Return on investments was 4.4 per cent (1.0 per cent) during the first half of the year. From the beginning of the year, the asset class with the highest return was unlisted equities, with a return of 9.4 per cent (4.6 per cent).

The share of fixed income investments totalled 39.1 per cent (43.7 per cent) and return at fair values -1.0 per cent (3.0 per cent). Their market value totalled EUR 8,835 million (EUR 9,102 million). The share of bonds, which are included in fixed income investments, of investment assets totalled 30.0 per cent (37.0 per cent) and return -1.3 per cent (3.5 per cent). Other financial market instruments and deposits are part of fixed income investments and they totalled EUR 1,542 million (EUR 878 million), accounting for 6.8 per cent (4.2 per cent), and return was 0.0 per cent (0.0 per cent). The modified duration of bonds was 3.8 (3.7) years.

Equity investments accounted for 36.2 per cent (30.8 per cent) of investments, their value was EUR 8,183 million (EUR 6,412 million) and return 8.0 per cent (-2.2 per cent). Of this, listed shares accounted for 28.8 per cent (23.9 per cent) and their market value was EUR 6,508 million (EUR 4,980 million). Return on listed equities was 8.9 per cent (-4.0 per cent). The share of capital investments included in equities totalled 5.9 per cent (5.5 per cent) of investment assets and return at fair values 3.4 per cent (5.2 per cent). The market value of unlisted equities amounted to EUR 336 million (EUR 289 million), accounting for 1.5 per cent (1.4 per cent), and return was 9.4 per cent (4.6 per cent).

At the end of the six-month period, the value of Elo's real estate investments was EUR 2,784 million (EUR 2,689 million). They accounted for 12.3 per cent (12.9 per cent) of all investments, of which indirect investments accounted for 3.3 per cent (3.3 per cent). In total, the return on real estate investments was 3.1 per cent (3.7 per cent) and the return on direct real estate investments was 3.7 per cent (4.0 per cent).

Hedge fund investments accounted for 11.9 per cent (12.6 per cent) of the market value of investment assets, or EUR 2,681 million (EUR 2,619 million). Their return on capital employed was -2.1 per cent (-0.7 per cent).

The average 5-year real return of Elo's investments was 6.9 per cent and average 10-year nominal return was 4.6 per cent. The average 5-year real return of was 6.1 per cent and average 10-year real return was 3.0 per cent. The figures used in the calculations for 2007–2013 are the return on investments for LocalTapiola Mutual Pension Insurance Company.

The net return on investment operations at fair values stood at EUR 967 million (EUR 199 million). The result of investment operations at current value was EUR 440 million (EUR -98 million).

### Asset allocation and returns

	Basic allocation by market value		Actual risk position		Return	Volatility
	EUR million	%	EUR million	%	%	%
<b>Fixed-income investments</b>	<b>8,835.0</b>	<b>39.1</b>	<b>8,844.3</b>	<b>39.1</b>	<b>-1.0</b>	
Loans	508.1	2.2	508.1	2.2	1.3	
Bonds	6,784.5	30.0	6,793.8	30.1	-1.3	2.8
Bonds of public corporations	3,209.5	14.2	3,338.8	14.8	-3.1	
Bonds of other corporations	3,575.0	15.8	3,455.0	15.3	0.3	
Other money market instruments and deposits inc. any receivables and liabilities related to investments	1,542.3	6.8	1,542.3	6.8	0.0	
<b>Equities</b>	<b>8,183.2</b>	<b>36.2</b>	<b>8,826.4</b>	<b>39.0</b>	<b>8.0</b>	
Listed equities	6,507.5	28.8	7,150.7	31.6	8.9	13.5
Private equity investments	1,340.1	5.9	1,340.1	5.9	3.4	
Unlisted equity investments	335.5	1.5	335.5	1.5	9.4	
<b>Real estate</b>	<b>2,784.3</b>	<b>12.3</b>	<b>2,784.3</b>	<b>12.3</b>	<b>3.1</b>	
Direct real estate investments	2,030.1	9.0	2,030.1	9.0	3.7	
Real estate funds and joint investment companies	754.2	3.3	754.2	3.3	1.2	
<b>Other investments</b>	<b>2,804.2</b>	<b>12.4</b>	<b>2,814.4</b>	<b>12.4</b>	<b>14.1</b>	
Hedge fund investments	2,680.9	11.9	2,680.9	11.9	-2.1	2.6
Commodity investments	-0.2	0.0	15.2	-0.1	-	
Other investments	123.5	0.5	118.2	0.5	-	
<b>Total investments</b>	<b>22,606.7</b>	<b>100.0</b>	<b>23,269.4</b>	<b>102.9</b>	<b>4.4</b>	<b>3.9</b>
Effect of derivatives			-662.6	-2.9		
<b>Total</b>	<b>22,606.7</b>	<b>100.0</b>	<b>22,606.7</b>	<b>100.0</b>		

The total return percentage includes income, expenses and operating expenses not allocated to any investment types. Modified duration of bonds 3.8.

The open currency position is 14.2 % of the market value of the investments.

### Preparation for climate change in Elo's investment operations

Elo's investment operations ranked globally in the best AAA category in an assessment by the international climate association AODP. The asset owners in this Leaders category demonstrate elite performance across all capabilities in managing portfolio climate risk. Elo was among the top three per cent and ranked number 10 globally out of 500 investors. The environmental organisation WWF also estimated Elo's investments to be in line with the two-degree objective of the Paris climate change deal.

Elo published a climate strategy for investment operations in March. Elo's aim is that by 2025, a significant share of the investments will support the achievement of the UN's sustainable development goals. Elo continuously develops the assessment of climate change and aims to ensure that the investments do not involve excessive climate risk.

### Corporate governance

Elo's Annual General Meeting elected new members to the Supervisory Board and the company's auditor on 24 April 2017. The Annual General Meeting adopted the financial statements and consolidated financial statements,

resolved on the use of profits in accordance with the proposal of the Board of Directors and discharged the members of the Supervisory Board and Board of Directors and the CEO from liability.

Mikko Leppälä was elected as a new member of the Supervisory Board for the three-year term 2017–2020. In addition, Satu Yrjänen, CEO (Kantar TNS Oy) was elected as a member of the Supervisory Board until the Annual General Meeting of 2018 and Pekka Metsi, CEO (Granlund Oy), Heikki Pesu, CEO (Are Oy), Harri Miettinen, CEO (Kymen Seudun Osuuskauppa) and Tapio Volanen, CEO (CGI Suomi Oy) until the Annual General Meeting of 2019.

With regard to those whose term ended, Vesa Aallosvirta, Maria Hanho, Johanna Heikkilä, Tero Jussila, Pekka Kampman, Olavi Kaukonen, Heikki Kyntäjä, Mikael Pentikäinen Terhi Penttilä, Marko Piirainen, Kimmo Simberg, Mika Varjonen and Olli Vormisto were re-elected.

The Annual General Meeting resolved to keep the annual compensation paid to the Chair and Deputy Chair of the Supervisory Board and the meeting fees paid to the members unchanged. Detailed information about the remuneration is disclosed in the remuneration report published on Elo's website. Ernst & Young Oy, Authorised Public Accountants, was appointed as the company's auditor.

### **Personnel and operating expenses**

Total operating expenses amounted to EUR 66 million (EUR 65 million) for the period under review. The loading profit for the reporting period came to EUR 10 million (EUR 14 million). The average amount of work performed during the first six months of the year was 451 (452) man-years. No substantial changes have taken place in the numbers of employees employed on a permanent and fixed-term basis compared to the previous year.

### **Economic outlook**

The economic outlook for the remainder of the year is optimistic, similarly to the first half. The outlook of the Finnish economy is quite bright at last, driven by recovered domestic demand and exports. Continued and strengthening growth requires that growth in the euro zone and emerging economies will remain at a sufficient level. Measures by central banks and expectations of them continue to have an essential effect on the development of the global economy and investment environment. Political uncertainties in all major economic areas cause risks. In addition to this, the valuation levels of many investments have continued to rise, and central banks' efforts to neutralise their fiscal policies may cause nervousness in the investment market. Interest rates of public loans were still increasing clearly in June, while estimates of a tightening of the fiscal policies of central banks have strengthened in the market.