Q4 2015 Earnings Call

Company Participants

- Dieter Wemmer, Chief Financial Officer
- Maximilian Zimmerer, Member-Management Board
- Oliver Bäte, Chief Executive Officer
- Oliver Schmidt, Head-Investor Relations

Other Participants

- Andrew J. Ritchie, Analyst
- Farooq Hanif, Analyst
- James A. Shuck, Analyst
- Johannes J. Reich, Chief Executive Officer
- Michael Haid, Analyst
- Michael I. Huttner, Analyst
- Nick Holmes, Analyst
- Paul De'Ath, Analyst
- Peter D. Eliot, Analyst
- Thomas Seidl, Analyst
- Vinit Malhotra, Analyst

MANAGEMENT DISCUSSION SECTION

Operator

Ladies and gentlemen, welcome to the Allianz Conference Call on the Financial Results 2015. For your information, this conference is being recorded.

At this time, I'd like to turn the call over to your host today, Mr. Oliver Schmidt, Head of Investor Relations. Please go ahead, sir.

Oliver Schmidt {BIO 2473131 <GO>}

Yeah. Thank you, Alex. Good afternoon from my side as well, and welcome to our conference call. As you know, we have three presenters today. Oliver will kick it off and share his views on the result of 2015 and our way forward. Then as always, Dieter will go through all the details and, finally, Max will talk about our investments.

We have scheduled two hours for the call. That should give us about one hour for Q&A. In case that's not enough to cover your questions, please come and see us at one of our

Analyst Meetings next week. We have scheduled one for Monday in London and one for Wednesday in Frankfurt. That's all from my side.

And with that, I hand over to Oliver. Thank you.

Oliver Bäte

Yeah. Good afternoon, everybody. Good evening to Asia, and good morning to those in the U.S. that are listening in. I'm going to keep it fairly quick before I hand over to Dieter, who, in his usual high quality, will deliver you the details of the financial numbers.

Let me start out on page A2 of the document that you should have been able to download or see on the net where we are giving an overview of the 2015 key figures. And we didn't manage for that, but coincidentally we had the highest revenues ever at €125 billion in the 125th year of our existence, so that was a nice coincidence, up 2.4%, an all-time record. And we've recorded €10.735 billion operating profit, up 3% from prior year.

Shareholder income grew even more strongly, 6.3% to €6.6 billion, which we consider to be a very strong result, given the environment and particularly given how peers in our sector are performing. Dividend per share is up 6.6% based on the proposal that we are making of €7.30, we rounded it up to €7.30. Our solvency ratio stands at a very strong 200% at the end of the year, up about 9 points.

The returns have been good for those that had invested in Allianz properly last year that you see on the right-hand side, but that is the past. But what I would like to summarize looking at the page, you see a very resilient company, very resilient numbers and significant growth potential going forward.

Now let me give you my €0.50 on the performance of the Group as highlighted on page A3 both for the Group and the individual segments, that is Property-Casualty, Life/Health and Asset Management. From an overall perspective, we're happy to record 2.4% growth.

Why it doesn't look like a big number? But you should remember that we had announced last year that we would like to restructure our Life business, in particular the new business very consistently in an environment where interest rates are falling. And therefore, you see in the Life segment a decline in the top line.

Given that, you see strong growth in Property-Casualty, a very strong number that I've hardly seen since I joined Allianz in 2008. And based on the strong U.S. dollar, even Asset Management up despite the outflows at PIMCO. So, overall, a positive number from my personal point of view.

On operating profit, we've been careful and reached the upper end, 3.2% up. And that is a mix of 4.1% growth in P&C, an outstanding 14% growth in Life and Health, and as expected, the decline of profitability in Asset Management in line with the outflows, particularly at PIMCO.

The return on equity remained strong. This is computed on average equity. I remind you, it's down from 13% to 12.5%. On a consistent basis, it basically remains unchanged and is the target. But it also gives you an indication that we would like to focus on earnings growth in the future to make sure that earnings and dividends per share are growing from three sources, underlying, organic growth, external growth and, if need be, share buybacks or other capital measures if that is required. However, that is not our preference. The preference is to have organic business growth and then selective external growth.

Now, when you look at the segments in terms of returns, the P&C segment is at target. And I believe personally there is further upside in terms of managing capital efficiency even in P&C. So you should see over time potentially stronger returns on invested equity.

In the Life and Health segment, we are at 10.8%. That is, as we discussed in the Capital Markets Day, a mix of very good numbers in Germany and some further improvements that are necessary in the rest of the Life portfolio. We're working vigorously on improving the return on invested capital in the Life segment, and you can expect further improvements. And the return on equity in the Asset Management segment remains excellent at 15.2%. So, overall, from my point of view and the board of management, very solid results.

In the P&C segment, driven by very strong results in core Europe where we can really play our scale advantages where we can play our strengths across all channels, but we also have to bear in mind that we had some challenges in the year. Number one, slow progress in LatAm, but I would also like to mention what is not on the page that we had to end the Fireman's Fund saga with some additional reserve strengthening in the beginning of the year that is impacting the AGC&S results. Dieter will address that when he gets to the presentation.

You may have seen in the press announcements that we are getting rid of €1 billion of our long-term reserves in the U.S. That is, by the way, happening at book values which tells you that the reserve level that we've achieved in the U.S. now are strong enough to be accepted for transfers, which tells you we have really fixed the reserve issues. And that should give you a lot of comfort that that is under control. In LatAm, we have to make significantly more progress next year, but there we are also confident that we're turning the dial.

On Life and Health, let me reiterate that we are very proud to have successfully executed our new product strategy. There's more to come. But all the budgets in terms of shifting business from traditional products in new business have been overperformed. Let me really compliment our German colleagues, our Italian colleagues, and our French colleagues. In France, we now have 50% unit-linked share in new business that was unthinkable a few years ago. So, at this point in time, thank you to our colleagues, and that will continue.

The second thing that we're addressing is the in-force business. And in particular, where we have negative spreads, we're working very actively to address these books. This is not just an issue of profitability drag, but these books consume a lot of solvency capital and have a lot of interest rate sensitivity that we are trying to get rid of, because that makes capital management more efficient. And that is really the objective of us addressing our back books, to make capital more efficient, make solvency more stable and be able to lift capital out where we can.

On Asset Management, Allianz Global Investors' operating profit is at a new high. Let me compliment the colleagues here, therefore, also supported them in the latest acquisition of Rogge. They're, I think, doing a great job. At PIMCO, the net outflows are stabilizing. We have to further work on profitability, but that is underway and recent outflows are more or less in line with the industry. And as you can see from the performance fees that we were able to collect, that in effect means that we're doing really well on our alternative strategy, and we are only getting performance fees, of course, if we are over-performing relative to investor expectations. So that is good news. And there are more performance fees to come this year.

So, overall, a solid year that prepares us well for this very volatile environment that we believe offers great opportunities for a stable company like us that can balance volatility across the segments and across the markets.

Now let me also remind you on page A4 that we do have an attractive dividend policy that is – payout ratio that we increased to 50%. Let me also remind you of the ratchet that we have introduced, and that we will pay out unused M&A budget if we don't use it. And just as a general comment, because there are lingering questions all the time, no, we're not planning outside acquisitions. We're not planning to do M&A that is not accretive or doesn't meet our return hurdles, whether that is cost of capital or long-term 13% ROE question, in case do you have that on your mind. That is, however, a long-term average.

We're looking – if we do something for bolt-on consistently with the record that we've built over the last few years. And therefore, we would also like to point out dividend per share growth has been 6.6% and is proposed to be 7.30%, as you can see on the page.

Page A5 gives you the overview of where we are relative to the original ranges that we have provided. While Asset Management is more towards the lower boundary, Life has outperformed, and P&C is exactly in the middle so that overall, the Group was trending towards the upper boundary.

Some people have said that historically we've always outperformed our lower boundary. Let me remind you, the laws of physics hold. You cannot continuously just go over the top. We have a boundary, and we have these corridors because given financial markets and given the economic environment, there is volatility, and we need to take care of that.

That's why our outlook for the next year is also more cautious. It would be absolutely not prudent if we would not reflect in our outlook what's going on in the outside world. And I'm going to talk about it in a second.

We are aiming at 5.5% as a middle ground for P&C, 3.6% as a middle of the band, and 2.2% in Asset Management. So, on Asset Management, given the volatility in the markets, we are more cautious. That is not a mistrust in the businesses. That is just reflecting volatility and impact of lowering asset values that we are taking into account. Again, everything else would be not professional.

Why do we believe that? Page A7 gives you an overview. If it wasn't enough that in our industry, we are challenged through digitalization, low interest rates, the change of the business model and increasing consumerism, conduct is a major issue that we are debating with regulators on top of all of the things that we continuously around Solvency II. By the way, as a side comment, it would be great if we could stop continuously inventing new charges, new risk capital ideas, but just let – move on after 10 years and apply the model.

But we also have significant political and regulation uncertainty not just within Europe and the Middle East, but in many parts of the world, tensions are rising. In particular, in commodity-dependent countries, the social environment is not benign. Therefore, the expectations for growth are rather moderate and we expect that volatility in financial markets is going to continue.

While we believe equity markets should recuperate and interest rates have to go higher, we saw an all-time low in the bond today, which has nothing to do with underlying economics. It's just reflecting fear. We need to expect that markets will remain challenging both on an interest rate perspective and an equity market perspective.

And I'd also like to remind you, as we told you in November, that is our base case. We are not seeing this as a tail scenario. Allianz is planning and is basing its strategy on an environment of ultra-low rates and high volatility going forward. We believe that is providing huge opportunities for us. As you look around in the sector, you see a lot of people that are weakened, and that should provide us with opportunities in many ways.

So, therefore, let me turn your attention to page A8. Just think about three core elements of our strengths that are very important as you consider investment recommendations and investment decisions. The first one is scale. We absolutely believe this industry will prove that scale matters both nationally but globally as well. Digitalization is the true force behind it. The ability, however, to also command outstanding performance in investment management – Max is going to talk about it – will make all the difference in the future. We're outperforming our peers in terms of providing better-than-benchmark returns to our clients. And our global lines are growing in importance with €3.3 billion operating profit in 2015, the major source of future growth.

On top of that, you have resilience. We have three segments with multi-billion euro earnings power that is very important, as we had the boom on the Asset Management side that nicely balanced temporary weakness we had in Germany and other places on P&C. Now that we had the changes in Asset Management, the P&C and Life segments are picking up. You rarely see that in other places. And now, our capital is extremely strong. It's not just Solvency II in our rating. Please take a look at the source and the quality of our capital.

We're one of the few companies that do not need huge amounts of interestingly computed value in force to support our capitalization. We have a very high quality of core capital. And while we are having equivalence, we are one of the companies that have the lowest benefit from equivalence rules for our overall capitalization as compared to almost any peer. So it's not just the level of capital, but also the quality of capital that is stronger in Allianz and in almost most of the places that I know.

On top of that, we have really top global brands. We just mentioned in the BrandFinance Global 500 ranking as the only one in the top 50 that is an insurer, and we are very proud of that.

So if scale and resilience were not enough, we also outperform on skills. When we've changed the order, historically we would have talked about underwriting claims excellence that remains important. The number one thing we're looking at, the key steering metric, is going to be customer satisfaction and centricity. That's the transition we are making because in the world that is moving from a push industry to a pull industry, that will separate the winners from the losers.

We aim for a top-quartile position here, and I'm confident we'll achieve that. On top of that, technical excellence will be at the forefront of what we do. We have very low combined ratio volatility. And mind you, again, we have, with our [REAL] program, taken a lot of the external reinsurance and internalized it. And despite that, our volatility on the combined ratio has been fairly low.

And last but not least, our people are outstanding, and the motivation of our people is outstanding, as we showed you on the Capital Markets Day. Therefore, our ambition for the next three years remains unchanged despite all the volatility as you can see on A9, 13% ROE which means capital has to be used efficiently. Earnings per share growth has a three-year average of 5%. By the way, the number for 2015 was 8%, and the health of the business is as important as the financials. Maybe not for you and at least for some people's spreadsheets, but for the long-term success of Allianz, customer satisfaction to have 75% of our business being better than market and having employees that get ever-more motivated will make the difference for us in the future.

And page A10 gives you a couple of details that I'd like to reiterate both around performance and around health. We have a strongly pronounced regional and sectorial diversification with a number of very important leadership positions. We have low earnings volatility. I mentioned capital strengths not just in terms of its level but also the high quality of its components.

A conservative yet very innovative investment policy, Max is going to talk about it. Our ability to access alternative assets, I think, is almost unmatched. We have very limited exposure to peripheral sovereign debt commodities, energy and banking sectors, very unlike it was in the early 2000s. We are pushing for innovation. The Baidu joint venture, Allianz1 and many things are coming online now and we're really moving our balance sheet, we're changing the Life and Health business mix, and we are working on the back book. So that gives you a lot of trust that performance in the future will be even better than in the past.

While at the same time, we are banking on strong health of the company, as a strong brand, focusing on customer satisfaction, having performance management moving from top down to a horizontal approach and making sure it's consistent and making sure that leadership in Allianz is tied to how well we run our people not just our numbers and making sure that our people stay motivated.

And with that, I thank you for listening and turn it over to Dieter.

Dieter Wemmer {BIO 4755450 <GO>}

Thanks very much, Oliver. And also from me, good afternoon and good morning to everybody on the call. The B section of the presentation that is what we use. Every quarter starts with a qualitative page on the renewal agenda and finish with a quantitative page on the renewal agenda. Just that you have more time for questions, I will directly jump to page B5 and go into the numbers.

So you have already heard all the headline figures. The P&C segment certainly contributed with a good increase in 2015 and then the stellar performance comes from the Life and Health segment where actually Asset Management shows anticipated reduction in profitability, and the Corporate segment that is mainly an internal accounting issue with corporate with our own pension which I will talk about later.

So, net income at €6.6 billion, 6.3% up. We had a non-cash item in Q4 to book, that is Korean or Asian life goodwill, which amounted to €171 million, and then wipes out all life goodwill we had for our Asian operation. That is probably the number you were looking for and we've created the miss.

So let's look at the fourth quarter. Actually a very good quarter in total on operating profitability, despite the fact that we had some headwinds to overcome, in particular on the P&C side with man-made losses and some cat events I will talk about later.

Let's go to page nine. Shareholders' equity, €63 billion. It's actually a new high for our net asset value. The average return on equity, excluding the unrealized gains, a small drop of 40 basis points, more explained by the strong growth of average equity and not the movement of the net income, which you have seen, went up more than 6%.

Sticking to our 50% payout ratio, so actually we are proposing to pay slightly more than the 50% because 7.3% is the rounded number up. So I think we are, when you look just on the first pages, I would call it delivery on all promises. And I said actually in the third quarter earnings call that I would expect a good single-digit increase in dividend and net income.

So page 11 shows Solvency II capitalization actually stays completely flat compared to Q3. Why did it not go up where interest rates slightly moved up in Q4? Yeah, that's a very relevant reaction and also the right question. I asked the same question, and we got some last minute changes in the calculation format driven by EIOPA technical paper.

Number one was a change in the interest rate curve for Korea, so they moved the last liquid point earlier. The next one was the same change for the Swiss franc interest rate curve. And thirdly, they adjusted the calculation methodology for the risk margin. And all three changes together, it cost us about all equally the same, so in total, we lost 4 points in our Solvency. So, the one-off who would have expected 203%, 204% were right to the spot because that was also my back-of-the-envelope calculation.

So, sensitivities are unfortunately, on the interest rate curve, up compared to our Q3 number and that has exactly the same explanation. The uptick in the interest rate sensitivity is driven by Switzerland and Korea life, and the change of the underlying interest rate curves.

So, probably a lot of you are now trying to guess what happened in the first six, seven weeks of the year 2016. When you just use all the disclosed sensitivities, you can say, well, equity markets obviously down; interest rates down; credit spreads up on government bonds; credit spreads up on other bonds. The only offsetting element is that volatility adjuster is also up, which offsets a little bit of the impact, but still without doing anything. So that means when you assume we are a sleepy management, then it would go about 20 points as we are working every day and not sleepy. We are working on compensating for it. And you will then see with the Q1 disclosure how awake we worked.

So, on page 13, the internal growth figure at 2.9%. That's actually almost a 3%, our mid-term strategic target internal growth of 3%, pretty great achievement. In particular, what I think is a great start into 2016, the price effects in Q4 were stronger than in previous quarters so that even the average moved from the 0.5% we had before to the 0.8%. I believe that is a very good start, good for most of our key markets, still not got enough for some of the underperforming markets, which Oliver addressed already. And here, I think Latin America, I will touch on also a little bit later.

Let's move on to page 15. The operating profit of the P&C segment and the combined ratio, underwriting results more or less flat. Well, actually our underlying net and premium is more than 6% up, so certainly a good driver for profit. In particular, when you still see that we have small upside against our 94% target in the combined ratio. Combined ratio at 94.6%. I believe it is a very good one. The last quarter ended at 96.3%. So some of you might have been disappointed. But actually compared to other announcements, I think that it's a great result, and I don't want to hide behind the peer comparison. That is also a great result on a stand-alone basis.

We had 6.4% of large losses of man-made nature in Q4, and a couple of – more than 2 percentage points in cat losses. So, cat losses are obvious, it's the Irish flooding, two UK floodings and the hailstorm in Australia. The man-made losses is one large Southern

European credit loss and a Brazilian water dam and an uptick in the Tianjin port fire, which seems to become one of the largest man-made insurance events in history.

Run-off results, 4.1%. Is this a big number? Yes, it is clearly above our long-term average of 3.2%. But we are ending the year with a very strong balance sheet, so we are not harvesting our future. And actually, it is not so far off on last year when you compare it OE by OE.

We had in 2014 more Fireman's Fund reserve increases, and in 2015, we had a substantial catch-up for Brazil and Russia. The catch-up for Brazil and Russia did not repeat. So when you actually do the negative OEs out, the other who contribute was positive run-off pretty much same level as the year before. And as I said, very strong balance sheet on December 31.

Also being confirmed by the announced Enstar deal from yesterday, we have quota-shared 50% of our long-tail liabilities in the U.S. that includes run-off from Fireman's Fund, asbestosis workers' comp, and some other lines. And it was quota-shared at book value. That means also the external provider likes our reserving strength. And both together in this partnership, we hope that in our joint work we can run-off the old claims slightly better than anticipated so that we both create a win-win out of the transaction.

So if we move on to the page showing the individual countries and their Property-Casualty results, clearly, Germany reconfirming its strong last year combined ratio. Actually, Q4 has started with or ended the year with a 90% combined ratio, which is really positive, and also the pricing environment is still friendly.

Italy, another strong year, €1 billion operating profit out of our Italian P&C shop is really a fantastic result. But France, also catching up in size. AGCS looks, at first glance, poor with 102.9% combined ratio. But please, remember that they have taken up the cleanup work of Fireman's Fund. And the Fireman's Fund combined ratio standalone, actually, worsened because we sold the stable personal lines business and we have only now half of the portfolio in commercial.

We've strengthened reserves there. We have built a lot of restructuring charges and we are really cleaning up. So, the old Fireman's Fund commercial business ended the year with 124% combined, embedded in this 102.9% of AGCS. If you carve it out the AGCS business, as you have seen it before is at a 94% combined which is, actually, a very strong result in a very difficult market, and they continue to do a great job here.

Latin America, a very disappointing result altogether, €150 million loss. The only thing what has changed compared to the previous year, the worst country moved from Brazil further south and it is now Argentina. Brazil is in a turnaround, a slowed down turnaround, because of the poor economic environment. And Argentina, we are doing a reset for the business we are doing and have really cleaned it up in Q4 very strongly.

Let me also point out that actually the worsening in Spain is explained that for Baremo, that are the new tables for bodily injury in Spain, we have already put this in our existing reserves for all open claims, which might potentially be affected by Baremo tables in future. So another demonstration of sound balance sheet work.

Short overview of the investment results, page 19 of the P&C segment, yes, current yields going down as expected in the interest rate environment. However, average assets up as you have already seen in previous quarters and the non-interest rate items are just small or negative than the year before, so that the overall investment income is up.

Moving to the Life segment, same story as last quarter, continued progress in the mix change of new business, hence, 5% less revenues and 1.5% less new business volumes than the year before. However, in better quality, as I will show you on the new business margin page in a minute. Therefore, we are happy with all the numbers, of course, for the U.S., we would really like to see even more growth than we have. We just couldn't repeat the great sales campaign of our FRA product. We are still running at a very high volume, as you will also see in a minute when we look now on the operating profit.

Page 23. €3.8 billion is a very big operating profit. And in the last quarter, it was a contribution of €1.1 billion. Well, is there actually a lot of one-off in it? Yes, but the one-off in realized gains was pretty much in the first quarter. Q3 and Q4 saw quite some offsetting effects on trading results, on FX and other derivatives. So, when you look at the last six months in total, it looks much more stable.

And an important driver actually of our investment margin is actually the U.S. In the meantime, we are making in fixed-index annuity alone close to $1 billion of operating profit. $1 billion of operating profit that is double-digit growth over the year before and additionally the dollar is 20% higher value than the year before. So, in our investment margin, you see really a clear boost from our U.S. Life business. And now, you understand even more why we like fixed-indexed annuity more than other products and that we want to continue.

The other movements in the profit by source is not a lot to mention. Sure, when you have, as we did in Q1, more realized gains, in particular in Continental Europe, you always get the offsetting impact from change in DAC, that is a faster amortization of your deferred acquisition costs. Hence, despite the high volume of new business, we don't have a growing DAC. We have, actually, a shrinking DAC as you can see in the table of minus €332 million.

And, I think, that – well, probably, the next question is, what would you say is the normal outlook for 2016? Well, when I take out the investment margin back to normal, I would say, it probably goes down to 3.5%, then we have the year-end new business and the new business of the year 2016, so around 3.6%, would be for me, the midpoint for the following year, as I assume that's a strong contribution from the U.S. continues with further growth.

Now moving to the new business margin. The value of new business in-force, around at €1,200 and that is number post tax and post cost of capital. So, when you compare this to the operating profit number, we have actually a pretty high replacement value of our operating profit. Operating profit is roughly 2.5 years to 3 years of pre-tax value of new business, so that should certainly be a strong positive outlook for the future.

If you look at the new business margin, a completely different story between the first six months and the second six months. First two quarters, we are running at 1.5% new business margin, Q3 at 3.0%, Q4 at 2.8%. So, with an average of 2.1%. And in particular, the last six months, a very good starting point for our 3% commitment in our strategic renewal agenda.

So, I think, overall, the Life business is in good shape. Yes, and maybe I should also have mentioned that in the operating profit, we had to consume more than €200 million loss recognition in Korea, and that is in the operating profit outside of the goodwill impairment, which I mentioned. But that was at earlier quarter, not at Q4. Q4 had no special elements.

Page 27 is always the demonstration that our investment margin and our current yields are big enough to cover our guarantees because there is always the fear of everybody that we are running out of investment income and can't service the guarantees anymore. I think when you follow this page over the last years, we could demonstrate quarter-after-quarter that we are in very good shape here. And this fear is not justified.

And as I've said before, a normalized margin, I would say, at 85 bps, higher than we said in the past, that we had it more at 80 bps, but that is a higher weighting of our U.S. business which provides this normalized number up.

And now, we move on page 29 to the first step into the asset management sector, asset management – well, U.S. dollar is compensating for the high outflows, altogether where the high outflows, I think, are clearly going down. I told you in the last earnings call that PIMCO had even a small positive month in October. For the full quarter Q4, PIMCO saw €11 billion outflows with €3 billion to €4 billion inflows at Allianz Global Investors, actually for the segments, the net outflows were €8 billion. Still a big number, but I think where we started 15 months ago, great progress. And therefore, we are quite happy that we achieved what we achieved for the year.

Now, looking at the revenue development; continuing pretty much the story of previous quarters. PIMCO's fee margin has stabilized at the €39 billion level. We are dancing around the €39 billion and ended the last quarter with €39.2 billion, so slightly lower than the previous quarter. Also, Allianz Global Investors' stable between 53 bps and 54 bps. So, resulting for Allianz Global Investors in 12% internal growth and 20% nominal and at PIMCO, 20% drop, or corrected with dollar, a 4% drop.

On page 33, yes, the normal fee income is down almost €1 billion, just following the outflows at PIMCO, and that is before currency movement. Performance fees up to €607 million, not only that we had some individual performance fees, also the payback of the private fund Bravo I is clearly going as continuous as predicted. And with €600 million, I think we have reached a very good level of performance fees, resulting in the overall expected number. We probably would have expected from a timing that more of the performance fees would already accrue or realize in 2015, but, yes, they are not lost and the rest will accrue in 2016.

As you have seen already in previous quarters, we are summarizing the whole FX effect in the last column, which gives us then the additional €300 million, and we are overall, with the Asset Management sector, within our target range. So, the page on the corporate segment, that was €100 million lower in the quarter than the previous two quarters now, resulting into a loss of €945 million. That is actually more an internal accounting and consolidation issue because the additional €100 million for pension accruals is then offset in the other German OEs across all segments, because in the consolidated statement, that is all covered under the IFRS 19, and there is no P&L impact. So, it is more how we account for intercompany transactions.

So, I would, hence, expect for – for the year 2016 that we are getting closer back to our 2014 number. Also, I should mention that our Indian operations, which contributes close to about €40 million operating profit, we had in the past an operating – in the corporate segment, they are in 2015 in the Asia-Pacific region.

So, altogether, banking also slightly up, also I think holding and treasury, nothing very spectacular, pretty much business as usual. Now, coming to the summary page, how to move from operating profit to shareholders net income. I think I should highlight here the amortization of intangible assets. There is a small ongoing increase in this line coming also from the Unipol acquisition, but, otherwise, the one-off of €171 million of goodwill impairment for the cash generating unit, Asia-Pacific Life and Health.

And that are the biggest events. Therefore, when you would have expected a tax rate of around 30% instead of the 31%, yeah, well, a write-down of goodwill is, of course, tax exempt, so you are not making any tax reimbursement on this one. Hence, the tax rate is one notch higher and this explains already most of the figures and then I would like to close the presentation with the future page we are using to give you one page of the overview where we stand with our 2018 ambition.

Left-hand side's all the cons, right-hand side all the health indicators, and I consider the Solvency II interest rate sensitivity, also a health indicator because that is a demonstration of how fast we move the mix of our Life new business and how fast are we getting out of long-term guarantees.

And with this – and then, I refer actually to page 40 with the detailed definitions. But I think that is for your reading. We use exactly this definition to define the numbers and I hope we can then talk in the future more about it, here that is just establishing the starting point.

Last page and then I'm done. Financial reporting from 2016 on, we want to make use of the EU Transparency Directive and adjust our quarterly releases. We will continue every quarter with an analyst presentation, a press release, and, of course, the analyst call and our call with journalists. However, we will stop producing interim reports for Q1 and Q3. That means we will only do half year accounts then with all the footnotes and disclosures. I hope that finds your agreement, but happy to get your feedback on this, also, on the road show.

And with this one, I hand over to Max.

Maximilian Zimmerer {BIO 2557503 <GO>}

Good afternoon. I will tell you something about the investment side, to start with a very boring page, that's C3, where you can see the segmentation of the overall investment portfolio. Nearly, no changes, but there were a lot of changes behind the curtain. On the Life business as such, grown by 4% and P&C by 2%. Debt instrument by weighting is nearly the same, only gradual changes on the duration.

And Dieter already explained some changes on the liability side due to model changes. Overall, there was an increase of 0.5 years. And what we did on the asset side, we go for longer – went for a longer duration. Overall, that means we increased it by active measures a little bit by more than half a year overall.

Now, going to page C4, and what you can see here that, overall, we cope very well with the declining interest rates by extending the duration. That's a safeguarding measure for our Solvency II position, in general, and it allowed us, in general, also, to increase our share in alternative assets, and I will come to that in a moment. I think that's the most interesting part on the investment side, in general, because that's the part where you can earn some extra money. And if you think of the very low interest rates, that is very much needed overall.

Now, getting to page C5, that is now showing the overall Allianz Investment, but not according to IFRS, but according to the real market values. That means it includes, also, real estate own use, the hidden reserves on the real estate portfolio and some accrued interest on the debt portfolio, that means size-wise, it's a little bit, let's say, €30 billion higher than the IFRS view overall.

What you can see that we have now invested €92 billion in so-called return to investments. What do I mean by return to investments? These are all investments which are not listed in the stock exchange, but it's important. That means it includes real estate, infrastructure, equity, and debt renewables, but also private equity and also the mortgage part.

What are the expected returns? You can see them on right-hand side. That is very much important. If we do not see these kind of returns, we will not grow overall the assets. But we can say, right now, although there are some tightening going on, it's still possible to earn a decent extra return there and that made it possible to grow the overall portfolio by €18 billion. Only to remind you that last year, we had only an increase of €10 billion. That means, right now, the production is really up and running. We have very good portfolio managers, especially on the Allianz Capital Partners' side, but also at AGI. And it means it's now possible really to differentiate also against the competition.

Going to page C6. There you can see which part of the business we have grown significantly. And as you can see, nearly everything. Private equity is a little bit more difficult. We invest in private equity funds. But as you know, unfortunately, there are some paybacks over time. And therefore, it's more difficult to grow that part overall of a business then in the very long-term holdings we have, for example, on the infrastructure side, where every new deal usually is also growing the overall portfolio.

There is a lot of work I can tell you because it's cost us around 100 transactions. And you do them not in one second as buying an equity stock. It's more that you need a head time of 6 months to 12 months. And that means it's really important that you start early with this kind of business. There are some examples, as you can see, on the right hand side of our investments.

Only what I would like to mention, on the renewables part, we have concentrated mainly on Europe but now, we're also going to the U.S. It's a very interesting market for us. It's a totally different regime. That means you can see also some diversification in that respect. And that's very often possible that you will work without the subsidies from the state. If you are a long-term buyer in the form of energy, that means you can already lock in the prices for the energy.

Now, going to page C7. What you can see, we tried to come up with a comparison versus our peer group, the peers which are best compared against us. By that, I mean the European peers – Generali, AXA, and Zurich. I think that's a very interesting exercise. We have to rely mainly on the public numbers, but also the numbers for the analysts, if we have access to them. And because, since 2007, you are obliged to publish also the market value of the assets, you can try to calculate also the investment performance or total return. That is very interesting. That means not only book yields, but also changes in hidden reserves on the assets that makes it possible at least to come up with an assessment of the overall investment performance.

And as you can see, in the years 2007 to 2014, in the eight years, we have achieved an overall total return of 5.2% against the competition of 4.7%. I think that's a large difference. I can't promise that for the future, but I think this is at least very promising. What is important that we have not achieved this wonderful performance with a lower credit quality, we also compare the credit quality by rating and the loss ratios, which are behind the credit rating. We are a little bit above the average of the peers, in general. Our current year is higher than that of competition, which is also very nice.

And I see the main reason is that we have advantages due to the very professional in-house asset management that's not only PIMCO and AGI, it's also Allianz Global Partners and Allianz Real Estate. And what we can see and what we are difficult to compare and we are also way better diversified also for single sovereign bonds, we really worked against these clusters in the last years. And I think that we made a lot of progress in that respect, too.

Now, coming to page C8. This is now the yield that is measured by IFRS. It means what we take into account is the current income of the group and then the realized gains and losses, but also the changes in the book reserves. And if you add that up overall, you come up with a total performance of 1.2%. Is it a nice number? It could be higher. But to be frank, the year before, we had a total performance of 11.8%. The main reason was that in 2014, the interest rates had fallen significantly. That means a lot of funny money from unrealized reserves. Now, it went the other way around.

In the year 2015, there was a small increase in interest rates, especially in the longer-term bonds that means you had some losses on the bonds as such. And therefore, the total performance of 1.2% is okay. If we measure against benchmark indices, what we do internally as bund is relevant for us, then you would see there was also an outperformance, but only a small one.

Now, turning to page C9. There you can see the new investment yields, a little bit lower than the year before, but still strong if you think of the current investment environment. The P&C side on average 2.2%. On the Life side, it's 2.5%. Only to compare that to the bund yield right now, it's 22 basis points for 10 years. Hopefully, they will go up a little bit during the year. But if you compare again the risk-free rates, still I think these are attractive yields overall.

Now, coming to page C10. You know this comparison very well, and we always compare for the Life and Health business. The total yields what we achieve on the assets, but more so on the reserves because we hold more assets than reserves, that brings us in the year 2015 to 5.1%, and that compares with a minimum guarantee of 2.3% that's still a very nice spread. That means all of the guarantees are very much secure. And the same holds true if you think of the new business. The new business guarantees for the business with any guarantee is at 0.8% and the reinvestment yield, as already explained, at 2.5%. Also, they have still a nice buffer.

Now, coming to page C11, that's more for the Q&A. Perhaps, that leaves me with not many questions to that. The overall question is right now, what is our exposure to the oil and gas sector? That is not so much interesting because of ESG, I think, but more because of the very low oil prices and at least there's assumption that we will see more default on the oil sector as such in oil and gas sector. And what you can see in our overall exposure is pretty small, it's only 2% of the overall investment portfolio, that means 5% of our equity portfolio, that's €1.6 billion. And on the fixed income side, it's €10.7 billion. If lower, that means 2% overall. And if you think of the ratings, they are pretty much okay, too. That means, in general, no large risks on oil exposure.

To summarize it, more interesting, I think, was the development of the market this year. We have seen a lot of volatility and this in all market segments. That means on the equity side, the maximum was a minus – depending on the index between 10% and 18% right now, still we are at minus 10% to 12% in most of the equity markets. And on the interest rate side, unfortunately, very low interest rates, bund yields as I already mentioned, was 22 basis points, 10-year swap rates are 56 basis points right now. That means also very, very low.

And in addition to that, also higher credit spreads, what I like very much. But Solvency II-wise, it means all three things are working against the Solvency II numbers. That means we have to make sure that we can stand these kind of perfect storms. And overall, I think we implemented some measures also to lower the overall volatility. As Dieter already mentioned, there's still something what we plan to do in that respect.

Overall, my outlook for the year is still a positive one. I think equity markets are too cheap. Therefore, I'm optimistic that we will see some recovery. That goes also for the interest rates. But to be fair, this can last a little bit longer because of the things that Mr. Dragi already has announced. At least, there are some expectations around the market. But it could also happen similar thing what we have seen last year – until April, very low interest rates and then a big shock on the interest rate markets, where the markets went up by nearly 1 percentage point in three months. But let's wait for that. We have to prepare for all these scenarios, that's for sure. What we would like to do in general is to invest more in alternative assets to also get some additional liquidity spreads. I think that's very much important for us, too. Thank you very much.

Oliver Schmidt {BIO 2473131 <GO>}

All right. Thank you, Oliver, Dieter, and Max. And with this, we are now happy to take your questions.

Q&A

Operator

Thank you. And we will take an opening question from James Shuck of UBS. Please go ahead. Your line is open.

Q - James A. Shuck {BIO 3680082 <GO>}

Good afternoon, everybody. Thank you for taking my questions. I had two questions, please. Firstly, could you just talk me through what your expected level of capital generation would be in any normal year? I'm kind of thinking about the pre-dividend accrual level of capital generation. And in particular, I'm trying to – if you're able to split that out for me and tell me what the Life and Health contribution is in euro terms. Obviously, we transitioned from the old Solvency I basis of capital generation, which we can see from the MCEV disclosure, into a Solvency II world. I'm interested to see how the Life and Health side of things in particular compares on to the new basis. That's my first question.

Second question is around the rollout of the digital agency. At the time when you presented on the German digital agency, you talked about the potential for 25% increase in productivity. And I'm keen to know where you are with that, whether those productivity levels are holding up as you had initially envisaged? And also the status of other countries as you rolled out the digital agency in the latter part of 2015 and into the first half of this year, please. Thank you.

A - Dieter Wemmer {BIO 4755450 <GO>}

James, it's Dieter here. The expected level of capital generation, that is a very difficult question to answer, because even when we now create a formula, I bet with you there will not be a single quarter where we can demonstrate that it works like this because there is so much volatility for many parameters. So, actually, any number we give to you is then always being offset by the reality. And I'm afraid that, that would actually create a misled to all of you, and that it's much better when you just focus on our 2018 financial targets because we are committed to manage the balance sheet and the growth of the business in the right direction.

Maybe over the years, when we have more average quarters to produce, we can distill it down to a more useful guidance. But at the moment, I think that would be too early.

A - Operator

On the digital agency, I think we have so far not yet a lot of experience how the first pilots are running. And we would give in summer when we have a Capital Markets Day about the digital-only, we would give then some more details on this one.

Q - James A. Shuck {BIO 3680082 <GO>}

Okay. Thank you very much.

Operator

We will take our next question from Peter Eliot of Kepler Cheuvreux. Please go ahead. Your line is open.

Q - Peter D. Eliot {BIO 7556214 <GO>}

Thank you very much. I guess, you highlighted the reasons for being a bit prudent on the growth outlook for operating profits. And, obviously, the midpoint of your outlook is, I guess, 1% higher than it was last year. So I'm just wondering if you could help us on the translation to EPS. Obviously, any excess capital, which would help bridge the gap to 5%. But I was just wondering if you could share your expectations on developments for the non-operating profit and also the impact of recent market volatility on the starting point there?

Second question was just on the underperforming non-Life businesses. Yeah, you highlighted that Brazil might take a bit longer to turn around. But on Fireman's Fund, where you've obviously taken some restructuring charges in Argentina, where there's been reserve increases, would it be too optimistic to assume something quicker? Just wondering if you could share your thoughts there. Thank you.

A - Operator

Sure. On Argentina and Fireman's Fund, we look for a quicker resolution. On the outlook and EPS growth, well, I think that is equating with EPS that it has more input parameters than just operating profit. I think I pointed already a little bit towards the tax rate, but also

– look, we have promised that we will either use our M&A budget or return it. The M&A budget unused end of 2015 is some €1.67 billion. M&A budget end of 2016, assuming we wouldn't buy anything as close to €3 billion, when you take €3 billion and whether you use it for M&A or you return it to shareholders, creates already an EPS enhancement of some 4 points, 5 points. So, actually, I think we are well set to deliver the number.

And please, we said clearly, our EPS gross target is in aggregate 5% a year. That means we are interested to move the current €14.6 earnings per share to €16 or close to €17 in 2018. We are not planning to show a 1.25% progress by quote. So, that is certainly not in a strategic plan that you really schedule it like a Swiss claim.

And then – I think I have answered both questions.

Q - Peter D. Eliot {BIO 7556214 <GO>}

Thank you.

Operator

We will take our next question from Paul De'Ath of RBC. Please go ahead. Your line is open.

Q - Paul De'Ath

Yeah. Hi, there, and thanks for taking my questions. Couple of points, please. Firstly, on the kind of Life business and new product development, I know you, obviously, had great success in the U.S. with the FIA product, and you talked previously about potentially trying to build an FIA product for Europe. I'm just wondering how that's going, and if there's anything you can talk about on how that is progressing.

And then, the second point is just on the Asset Management business and the purchase that you've made recently in AGI of the Rogge business. I was just wondering if you could expand a little on the thinking behind that. It's fixed income, and also it wasn't necessarily the greatest business in old mutuals portfolio. So, I was just wondering why you think it's going to be better on the AGI if it wasn't on the old mutual? Thanks.

A - Maximilian Zimmerer {BIO 2557503 <GO>}

Hello. It's Max. I wanted to start the question on the Life side. Fixed index annuities, we do not sell only in the U.S. We sell it's also successfully in Germany and in Austria, and the name is Index Select. And there's also now, I think, growing interest into these products, but right now, it's around 10% of the overall production there. And the main reason for that is its base rates are very small and, therefore, there's a also yearly guarantee on that one. That means it's really attractive for us to get some upside result this vigorous for the customers.

It is not so easy to copy that product for other OEs because the main importance is you have also a very sound back book to start with these kind of products. What we're doing, because we think most of the customers do not want only pure unit-linked products and want to carry all the risk, what we do – is coming up with other hybrid products with some forms of guarantees included. And also, there is a new product we are planning for Southern Europe, it's a unit-linked product with guarantees, at least where the overall risk per year is limited to a maximum of 10%. And because we think that is the future, overall, of the market, in usual traditional products with pure fixed-income investments and the very low rates you have right now after costs, there's nearly nothing in it for the customers. And therefore, you'll need some upside. That means the overall idea of fixed income annuities, we tried to copy that one and bring that also to other markets, but these are mostly other forms of products.

A - Oliver Bäte

Okay. And then, the Rogge question. Well, first of all, Allianz Global Investors needs to see that they are establishing a global footprint. UK is so far one of our weakest markets. So, with the acquisition, I think we expand in the UK. That means we see also there then cost saving opportunities on the top line. That is maybe lesser points Old Mutual can claim where they have such a strong footprint in the UK, so quite a different situation.

And I think also the global fixed income strategies which are being added by this RGP are filling a right spot in the AGI's capability profile. And you can be assured that the past performance has been reflected in the purchase price, so therefore, I think we are ticking all three boxes.

Q - Paul De'Ath

Okay. Great.

Operator

We would take our next question from Farooq Hanif of Citi. Please go ahead. Your line is open.

Q - Farooq Hanif {BIO 4780978 <GO>}

Hi. Thank you. I'm assuming that you haven't been asleep year-to-date as markets have fallen. So, I was wondering if you could give us a guide to the kinds of management actions that you've been taking, because, naturally, what's going to happen is, as you get into 180% to 190% range, everyone's going to speculate that, what's the risk Allianz falls below 180%, et cetera, et cetera. So, I wondered if you could talk about that.

Secondly, in the alternative portfolio, how much of that is – can we think of being allocated to Life and how much to non-Life? Is that important? Because – just wanted to understand the yield implications of where the alternative portfolio is allocated in the business?

And I guess, lastly, partly to Paul's question, we've seen a deceleration of net flows, sales as well have been weak in Life, and that's understandable given what you're doing in that business. But are we going to be facing this for a few years now as you shift to the new business mix? Or can we see some revenue, top line, net flow recovery coming by the end of the year? Thank you.

A - Dieter Wemmer {BIO 4755450 <GO>}

Well, when I start with your last point, actually, when you see that 2015 over 2014, on average, our Life results, that means the basis for the earnings is 8% higher. So, we have a natural source also here of income even when the net inflows were very strong in the unit-linked space, but we had outflows in traditional which is actually not so bad.

The volatility in Solvency II that is actually – and here it simplifies our organization that is really a one segment topic. So we are only dealing with our Life and Health segment in this question. P&C, it is really not very material, and therefore, not relevant to do it. We do a full suite of activities. And as usual, we really like to talk about it when we have done it and when that is the next reporting date with the Q1 results.

We are not making any announcement of what we are doing and not doing because, also, why would we set up a financial market on movements we might plan that it's just volume we are acting on that would be really a bad message to the market. But I can also tell you that we are a pretty quiet investor and not panicking over the current volatility of the market.

A - Maximilian Zimmerer {BIO 2557503 <GO>}

Yeah. It's Max. Only to add that, at least I can give you the ratio of puts we have in place for the equities. This is 28%, only that you know that in overall that means there are some measures in place. That is not new. Only to say that we're always working with puts overall, but only to prevent us if there's a real quest that we have to fire sale something.

And then to the question of the alternatives, I do not have the number here in front of me. I can give you only some guidance in that respect. If you think of the mortgage business, mortgage business is usually long term, 10 years plus. That's mainly with the Life business. Private placement is also the same, mainly Life business, not P&C, infrastructure, debt. There is some shortage of debt, but most of debt is also long-dated and long-dated goes always into the Life portfolios.

Real estate, we have both, that means on P&C and on the Life side, and that's where it's split. Private equity, also, we do it in the P&C and in the Life business. Infrastructure equity is usually also purely for the Life business. And renewals, it's the same, that's mainly – that goes only with the Life business, only to give you an idea, yes?

Q - Farooq Hanif {BIO 4780978 <GO>}

Okay. Thank you.

Operator

We will take our next question from Vinit Malhotra of Mediobanca. Please go ahead. Your line is open.

Q - Vinit Malhotra {BIO 16184491 <GO>}

Good afternoon. Hi. Thank you. So, just on the Life, the first question is on the technical margins. It seems to me that the quarterly run rate hasn't been really going as high as the outlook is progressing. And Dieter, I just wanted to double check, you did try to suggest that it wasn't really investment income driven, this increase in outlook. But we aren't really seeing the trend in the technical margin. So, I just wanted, obviously, to understand a bit more about the outlook increase, but also whether it is technical margin-driven or loadings-driven or investment margin-driven. That's the first question.

Second question is just on the alternative assets, again, for Max. I remember in the Investor Day, a slightly smaller number, maybe €86 billion was shown, and we suddenly see €92 billion. Is it all mark-to-market or has there been a lot of activity in the last few months at Allianz?

Lastly, if I may, just ask, on the M&A strategy, is it a fair understanding that there was a bit more – not emphasis, but a bit more talk about it at the Investor Day when these targets were presented? And is it the volatile markets which have caused you to tone it down a bit? So, just a very quick comment. Thank you.

A - Dieter Wemmer {BIO 4755450 <GO>}

I'll start with the Life outlook. Well, the technical margin will certainly grow also. I'm foreseeing an improvement there in 2016 if everything goes to plan. However, the big swing factor in the investment margin is, as I said before, the higher weighting of our U.S. business, because all the profits of a fixed index annuity policy are showing up in the investment margin. There is no technical profit, so to speak. It's all investment income over expenses and customer return. And that is, I think, the biggest driver for the higher base point number I mentioned.

And the rest, we have normalized to a normal flow of turnover in our portfolio, which we had also, in the last two quarters, we had, I think realized gains of around €1.2 billion. And that is just what you almost automatically create with the size of the portfolio and some active management.

A - Maximilian Zimmerer {BIO 2557503 <GO>}

Yeah. Coming to the question to the alternatives, at the Capital Markets Day, I think I've shown the portfolio in the third quarter 2015 that was at €86 billion. Now, we're at €92 billion. The €6 billion, I can't tell you whether that's only transactions or also some additional returns coming from market and valuation.

I assume so, because, overall, for the total year, we do the evaluations for a part of the assets also quarterly. The overall performance of the alternatives and the real estate in this year were double-digits. That means also some price increases, not only new transactions. But I can tell you from the €18 billion, that increase of the alternative investment portfolio, how much was performance and how much was transactions. What I only can say, a little bit more than 10% was the overall yield on the alternatives last year.

Q - Vinit Malhotra {BIO 16184491 <GO>}

Thank you.

A - Oliver Bäte

Let me – Oliver here, the Oliver Bäte, not Oliver Schmidt, talk a little about M&A, because that's lingering on the minds and investors have mentioned that to us and to me specifically. Let me reinforce the following item.

We've, I think, built nicely over the last few year a record of being disciplined on acquisitions. We've said we want to invest in Property-Casualty, particularly in countries where we have strong operations and want to build further scale. And that will consolidate and reinforce our positions over time and where we have management teams that can actually integrate. That remains unchanged.

The second question we get is what are the return hurdles? We have the same return hurdles for acquisitions that we have for our in-force. We want over time to have 15% RoRC or 13% RoE that is also the case for our acquisitions. That is, obviously, a long-term average. And we want to make accretive acquisitions. That's also important.

And we are certainly not interested to acquire something against issuing huge amounts of stock. So, just let me reiterate. So going out and buying a gigantic company at this point in time is not on the agenda, so you don't need to be worried about that. At the same time, we believe this environment will separate the strong from the weak ones. You will particularly, I think, see a lot of conglomerates that have strong home markets, but very weak portfolios outside of the home market disposing of peripheral operations that might be good in the core and might be fit to us. And we're systematically looking at that. We have been looking at that.

In many cases over the last three years, prices were too high. But with valuations coming down and companies being under pressure to clean up their portfolios, to meet Solvency costs and all the other things, we feel we are in the position to take advantage of our relative strength. And that is what we are intending to do. Again, applying strict discipline on the financial criteria, and we expect and hope for your support in that strategy. Thank you.

Q - Vinit Malhotra {BIO 16184491 <GO>}

Thanks, Oliver. Thanks, Dieter. Thank you.

Operator

We will take our next question from Michael Huttner of JPMorgan. Please go ahead. Your line is open.

Q - Michael I. Huttner {BIO 1556863 <GO>}

Fantastic. Thank you very much. On the Solvency, I'm a bit puzzled because you have huge buffers in Germany. So, you have this 300% Solvency there, 200% at a group level. And I just wondered why these buffers are not helping moderate the volatility we're seeing with the ratio now excluding management actions at about 180%, which is at the bottom end of your target range. I just wondered if you could talk about that.

On the megadeals, and you just said, Oliver, that you would look forward to our support there and Vinit said yes. What does support mean? Does it mean you'd like us to write nice things, so that's it or does it mean you'll ask shareholders for some money? And then, if I may, a last question. So, in your presentation, Oliver, you repeated or said again, what I understood from the Investor Day, which is that the Life business would shrink the capital allocated or make it more efficient in some way.

And I think Mr. Zimmerer presented the figures, €3 billion, which is not in the kind of budget for the group. So, this would help EPS on top. Can you talk a little bit about that? Sorry. It's three questions. Thank you.

A - Oliver Bäte

Michael, Oliver here. I'll take the easy questions. I'll leave the difficult ones to Dieter and Max. And let me – what I wanted to say is I assume that based also on our investor perception study and support that staying disciplined on the things we have been doing that that is also meeting your expectations. The reason why I'm mentioning that, we occasionally have – get a question around, under all circumstances do pay dividends or do share buybacks. If you take this to an extreme and say that's the only way to run the company, you put a company into runoff.

So, you need to get the balance right between appropriate returns on capital, and we've clearly said that, earnings growth, i.e., and again the way how do you deal with capital that is building up and that you're not using. And we're absolutely committed to not have capital sitting idle in the company, but we also don't want to waste it on M&A.

Now, we cannot wish for the right M&A targets to come at every point in time, when it would be perfect in terms of timing. So, we need some flexibility over time. But as we have said between now and the end of 2018, we'll not accumulate money and have it lying around. So, that discipline, you can expect. But we – as Dieter said earlier, we're not managing these numbers by the day, the month or the quarter. We are in a long-term business, and we're managing for the long-term growth of the business.

So, that is what I wanted to say. If you get consecutive systems where people say, we don't know what to do with your capital and we're, therefore, just paying it out or buying, in fact that's short-term a great message, long-term that's a disaster, I think. Sorry to say.

Q - Michael I. Huttner {BIO 1556863 <GO>}

That's a very good point. Thank you.

A - Dieter Wemmer {BIO 4755450 <GO>}

Michael, you are fully right. There is a dampening effect from the standalone Solvency of Stuttgart, our Life business in Germany to the Group numbers. However, that is already included in the sensitivities we have disclosed so that is, in the end, the net figure which we have calculated for the sensitivities, and therefore, it's already all-in, so to speak.

And when you see that two midsized OEs, Korea and Switzerland, actually, with a change of EIOPA's view how the interest rate curve should be designed, actually we have shown with a lot of capital market material and a lot of base data that the Swiss interest rate curve published by EIOPA is much too conservative and they are actually not following their own rules they apply for other currencies that these two markets are actually moving our interest rate sensitivities three points up, that shows you only how sensitive the Solvency II models are and this calibration question.

And I really hope that we can focus on working with the model and have not to face every now and then an interference from the regulator coming up with some new formula because the people at the regulator have been hired to write technical papers and otherwise they are running out of job. And that is something we have certainly to manage going forward.

Q - Michael I. Huttner {BIO 1556863 <GO>}

You could, I suppose, make their job lighter by instead of letting them be employed by EIOPA, by employing them at Allianz. Sorry about that. Just on the almost €3 billion?

A - Dieter Wemmer {BIO 4755450 <GO>}

Yeah. That was the number which you've picked up from Capital Markets Day slides. We have not explicitly integrated it in any of the targets but it is actually for us, a number which we have demonstrated, that's a 5% EPS growth over the three years. It's not completely unrealistic, and that is a view which has probably not completely transpired in all analyst reports.

Q - Michael I. Huttner {BIO 1556863 <GO>}

So I take this to mean then, although we might not see any of the €3 billion this year, we'll definitely see something next year so that it kind of boosts EPS. Is that fair?

A - Dieter Wemmer {BIO 4755450 <GO>}

Whenever it comes, yeah.

Q - Michael I. Huttner {BIO 1556863 <GO>}

Whenever it comes, okay.

A - Dieter Wemmer {BIO 4755450 <GO>}

I will mention it when we see it.

Q - Michael I. Huttner {BIO 1556863 <GO>}

Okay. So that's fair. Thank you very much. Thanks for answering my questions.

Operator

We will take our next question from Andrew Ritchie of Autonomous. Please go ahead. Your line is open.

Q - Andrew J. Ritchie {BIO 18731996 <GO>}

Hi there. First question on P&C, Dieter. I think you mentioned that large man-mades were 6 points in Q4, discreet Q4. Maybe just for the year as a whole, can you tell us where you think man-made losses were versus some kind of normalized level where you would expect them to be? Again, we've asked this question several quarters, is there a trend here in large losses, is this random? Obviously it's come up for debate a bit more in 2015. But basically I want to know where they are versus a normal year.

Second question, Oliver, you mentioned you're more cautious on the outlook for Asset Management given the market. Can you just give us any sort of qualitative information as to how the market turmoil affected PIMCO year-to-date? Have there been a necessity to build more cash buffers? Has it significantly affected flows? Is there significant mark-to-market issues for some of your liquid credit? But just some color there would be useful.

And a very short question for Max. Max, just looking at the unrealized gains on corporate bonds, even though your energy exposure is quite low, I noticed that this book of unrealized gains fell 25% in the quarter which seems quite high when spreads didn't do an awful lot. Did you realize a lot of gains in corporate bonds in Q4, or was there some sort of asset shift? I'm just surprised this book of unrealized gains on corporate bonds fell so much. Thanks.

A - Oliver Bäte

I'll start with man-made losses because I can give you here a man-made answer. So, 6.4% were the large losses in Q4. Our average for the year was 4.4% and it's actually 0.1% lower than 2014 where we were at 4.5%, and our 10-year average is 4.0%.

It's the trend and it's – I don't think so – we had an Q4 concentrated two losses together of $200 million, and an uptick of the Tianjin port loss. It's seems now that the Tianjin port loss is becoming one of the largest losses ever. Some people are talking that it could, in total, in short losses coming close to September 11, which is an unbelievable size, I feel. And then, our share in it is really, really small. So I think that is – and then we had – well, in 2014, we had more of this – some spectacular airline losses, which made the headings for quite some time. So, is this a trend? No, I don't think so.

A - Maximilian Zimmerer {BIO 2557503 <GO>}

And specifically then, for the year as a whole, man-mades were not particularly unusual either.

A - Dieter Wemmer {BIO 4755450 <GO>}

So, 0.1% lower as a percentage. It is slightly up in absolute number. But our net earned premium grew by more than 6%. So when you divide man-made losses by net earned premium, it moved from 4.5% to 4.4% in 2015.

Q - Andrew J. Ritchie {BIO 18731996 <GO>}

Okay.

A - Maximilian Zimmerer {BIO 2557503 <GO>}

Okay. Coming to the question about unrealized gains and losses and also how you manage this kind of volatility, especially on the Asset Management side, it's true, for example, for PIMCO, it's not so easy to cope with that one, if you have a large mutual fund and there's outflows and especially driven by markets developments, you have to hold more cash than usually necessary. And that's a drag on your overall performance. But what I can tell you at least at PIMCO, although if you think of your total return fund, they had these outflows managed it very well because they had last year a strong outperformance in that respect.

Now coming to the unrealized gains and losses, I can't tell you the split of the minus €17 billion in change and unrealized gains and losses in that number, there's also €3 billion coming from the U.S. business. So, let's say, €14 billion. But I can't just show you. We haven't sold a lot of corporate bonds in the last quarter. There was no necessity to do so. Overall, if you think of the corporate spreads and also of the interest rate movements, the last quarter of 2015 was a pretty quiet one. That means no special actions in that respect.

Q - Andrew J. Ritchie {BIO 18731996 <GO>}

Which is why I'm surprised the unrealized gains fell so much on your corporate bond portfolio.

A - Maximilian Zimmerer {BIO 2557503 <GO>}

You say in one quarter. Where did you pick that number?

Q - Andrew J. Ritchie {BIO 18731996 <GO>}

Just looking at the disclosed unrealized gains on corporate bonds that you give in your appendices every quarter.

A - Maximilian Zimmerer {BIO 2557503 <GO>}

Okay. I have to look it up, and then let's see whether I find something special in there. You're right. It can't be only the oil exposure, that's for sure, because our exposure is not very large.

Q - Andrew J. Ritchie {BIO 18731996 <GO>}

And just on 10-K, I'm just trying to understand, the additional caution, is that because of the experience to-date in Q4 or is it more...

A - Oliver Bäte

No, it's...

Q - Andrew J. Ritchie {BIO 18731996 <GO>}

...to do with for the year as a whole?

A - Dieter Wemmer {BIO 4755450 <GO>}

No, it's just for the year as a whole. The markets are down 10% whether they're due to AUM in the active Asset Management piece, you know how we're being compensated. So that is a general caution. If volatility goes up and markets go down, that has an effect.

Now we have counter effects on bond portfolios and are having increase in value. And we believe that the precision with which you can make forecast is just lower in this environment than we've had in the past. Nothing in particular about the first six weeks.

Q - Andrew J. Ritchie {BIO 18731996 <GO>}

Okay, thanks. And so, Max, the reference is slide C18 that I'm interested in a follow-up on.

A - Maximilian Zimmerer {BIO 2557503 <GO>}

Sorry. You mean C18 that's a complete year?

Q - Andrew J. Ritchie {BIO 18731996 <GO>}

The stock of unrealized gains on bonds?

A - Maximilian Zimmerer {BIO 2557503 <GO>}

Have you compared – you take only the numbers from C18 or you take also some numbers from the Capital Markets Day? Otherwise, it's only...

Q - Andrew J. Ritchie {BIO 18731996 <GO>}

I'm judging versus the Q3 reported results.

A - Maximilian Zimmerer {BIO 2557503 <GO>}

No, it's a little bit complicated.

Q - Andrew J. Ritchie {BIO 18731996 <GO>}

Okay. Okay. I can follow-up. It's fine.

A - Maximilian Zimmerer {BIO 2557503 <GO>}

Yeah. The Q3 results, at least I need some time to check it, okay?

Q - Andrew J. Ritchie {BIO 18731996 <GO>}

Sure. Okay. It just looks like a big move. But I can follow-up.

A - Maximilian Zimmerer {BIO 2557503 <GO>}

Okay. Thank you.

Q - Andrew J. Ritchie {BIO 18731996 <GO>}

Thanks.

A - Oliver Bäte

Thank you.

Operator

We will take our next question from Thomas Seidl of Bernstein. Please go ahead. Your line is open.

Q - Thomas Seidl {BIO 17755912 <GO>}

Yeah. Thank you. Good afternoon. Three questions. First two on the targets. I come back to the €3 billion Life capital release target. At the Investor Day, I think, you showed us, because of derisking that the required capital had fallen, yet when I look at the numbers now, year-on-year has grown by 9.5% from €20 billion to €22 billion. So my first question is, what keeps you confident that with management action, you can really produce a €3 billion given the headwinds from the macro side?

Second question is on the combined ratio on the P&C, the target is 94%. It seems like it's creeping up now 94.6%, pricing at one, claims frequency up and slow turnarounds in LatAm. Can you give us a flavor or color on how these actions you presented at the Investor Day are coming through in terms of impact, in other words, is the combined ratio of the next two years actually more arising, and then also only towards 2018 falling or what is sort of the dynamics you have in mind there?

And the third question is, on the asset side, you showed the relatively modest exposure to energy, but I think you still have quite some exposure to the financial and the bank sector, and I wonder, given the weakness of the bank sector in Europe, what do you think about the contingent risk Allianz has to some of the weakness in European banks via bond and equities?

A - Oliver Bäte

Okay. I'm starting with all three, and then my colleagues might just end and complete my answer. Yes, for sure, this capital consumption for the Life segment increased Q4 over Q3. And I gave you already the explanation with the changes driven by EIOPA technical changes, which we did not expect when we prepared our Capital Markets Day. However, I believe that our de-risking plans over the years should still hold up. And on something like this, in the end, we can only prove it by delivery and not by – now showing you a list of action we might consider. So it is really proof-point-dependent and that is what we are continuing to do.

On the 94% combined ratio, I mean this 94.6%, you can say overall we are not this far away. Latin America is the first place to pick, but we are working in general on every sub-portfolio, which is above 100% combined. And when we tackle all of them and are only halfway successful on these, then I think you'll see already enough improvement in the combined ratio. So I would not be concerned about these targets. And actually I also would argue that dependency on combined ratio improvement in our industry looking at a recent announcement of big competitors. They are all under pressure to improve combined ratios, which should help from a market competition point of view.

On the asset side, yes, it is true that we have a bigger number against the financial sector banks. But you have to subtract from this all the covered bonds which I would exclude from a direct exposure to the quality of the bank balance sheet and our exposures on subordinated against banks, also equities are fairly modest in relation to the size of our portfolio. But maybe Max can add to this one.

A - Maximilian Zimmerer {BIO 2557503 <GO>}

Perhaps I would first come back to the unrealized gains and losses on the corporate portfolio. It was the number from September 2015 was €4.7 billion as hidden reserves, and it went down to €3.5 billion. That is not very large. If you see the overall size of the portfolio, this was mainly driven by interest rate hikes in the U.S. because we have the long-term corporate bonds and due to the interest rate impact in the last quarter, some of the hidden reserves went out of all the portfolio. It was nothing special that we have sold something or something like that. Banking?

A - Oliver Bäte

Banking.

A - Maximilian Zimmerer {BIO 2557503 <GO>}

Yes, banking – coming back to the banking, 16% of our corporate exposure is in the banking side. This is €32 billion overall, and if you think of the quality in general, it's mainly, what is it, 95% is investment grade, 17% is in BBB and 52% that means the bulk of it is single A. The main reason for that is that most of the banks are in that bracket. And therefore, there's nothing special in that.

What I really can say and I'm really proud of that you're continuously really decreasing our banking exposure. That means within the Corporate segment, we try to reduce the banking exposure as such. The main reason of that is not that we do have trust in the banks, but that banks seem to be some kind of cluster risk.

Q - Thomas Seidl {BIO 17755912 <GO>}

All right. Thank you.

Operator

We will take our question from the line of Nick Holmes of Société Générale. Please go ahead. Your line is open.

Q - Nick Holmes {BIO 3387435 <GO>}

That's great. Thank you very much. Two questions. The first is realized gains in the Life business. Your policy of extending durations this year has obviously generated a lot of gains, really boosted your operating earnings. Now, I know you've already guided that you don't expect Life segment grow very much. But I wanted to ask, how should we expect you to manage the realized gains this year? I mean, the comparative obviously is a very difficult one, which you must therefore bear in mind for your investment strategy.

The second question is, looking at your energy exposure, I noticed that most of it's in the Life segment. I wanted to ask, what sort of guidance would you give to us as to the shareholder exposure? I mean, a lot of that is going to be on a 90%/10% basis, but would it be unwise of us to take something like 90%/10%? Should we be taking more like 50%/50%? Just your thoughts on that would be very much appreciated. Thank you.

A - Dieter Wemmer {BIO 4755450 <GO>}

Okay. Coming to the last question, next – no, it's the same split as usual, there's nothing special in that one. And if you think of the 2% on the quota of the overall portfolio, it would have a minor impact in general. And that means there's no reason why we could not pay any guarantee because there is a default on an energy stock or bond. But that is not what I expect. I provided you also with the rating numbers. That means there's nothing special.

And wanted to remind you, there are very large players in the bucket, take Royal Dutch or Exxon. And I do not see that there's real default risk in general, I only wanted to say that the overall impact of the energy crisis on our portfolio will be a very, very small one in general.

Now, coming to the question, and that is more difficult to answer. How much we would usually realize on the bond reserves, the hidden reserves on the bond side? And it's true, usually this is not driven by, let's say, going for higher operating profit numbers. It's more driven by actions on the fixed income portfolio.

And as you do a duration lengthening, usually you have to sell some bonds. There's no other possibilities. We do not hold so much cash. And because we did that last year, lengthening by 0.5 to 0.6 years actively, you have to sell some bonds.

And as you know, we have still high hidden reserves on the bond side. I would not expect the same amount for every year, only to say that. But I cannot exclude it in general because what we are usually very much hearing is the current yield on our portfolio. And we do not want to spoil the current yield. Overall, every year the current yield on the Life side goes down by, let's say, around 0.1 and, I think, that a steady pace. And we would not like to increase it by taking too much hidden reserves out of our portfolios.

Q - Nick Holmes {BIO 3387435 <GO>}

Thank you very much for that. Just a very, very quick follow-up. So, would it be right to say that your policy of extending durations is sort of still happening? It's not something that was an event that took place last year. It's still something that you're looking to do as appropriate.

A - Oliver Bäte

In general, we would like to have a mixed approach for the new business. You know that that is our overall target. But it doesn't mean that we close every time the duration. It's very much depending on the situation of the companies as such, and what are the risks from the duration gap. And it's also depending on our interest rates outlook. Therefore, I can't say or make a general judgment on that one.

Q - Nick Holmes {BIO 3387435 <GO>}

Okay. That's great. Thank you very much.

A - Dieter Wemmer {BIO 4755450 <GO>}

And, Nick, it's Dieter here. You have also to remember that we have also a lot of normal maturities in the Life portfolio, that means duration lengthening. You can also do with new investments. You don't need to sell all these old papers to achieve it. And the guidance I have given for the average investment margin is assuming a normalized flow of realized gains. That means also no special action that you would get more realized gains due to lengthening activities.

Q - Nick Holmes {BIO 3387435 <GO>}

Okay. That's very clear. Thank you very much.

Operator

We will take our next question from Micheal Haid of MainFirst Bank. Please go ahead. Your line is open.

Q - Michael Haid {BIO 1971310 <GO>}

Thank you very much. Micheal Haid, MainFirst Bank. Good afternoon to everybody. Three questions. First question, on the operating profit target 2016. As you mentioned, it includes some degree of prudence also owed to the low-interest rate environment. I wonder how much have the first six weeks of this year affected this operating profit target, the recent market turmoils?

Second question, on AGC&S, the combined ratio of 94%, in a very competitive environment, to what extent is that driven by reserve releases or abnormal reserve releases, and why can you perform so well in this competitive environment?

Last question on the fixed index annuity, you mentioned close to $1 billion of operating profit come from the fixed index annuity book that is very strong in my view. How resilient is this figure to lower sales? Not that I expect this, but I would like to get a feeling for the sensitivity of declining sales to this operating profit?

A - Dieter Wemmer {BIO 4755450 <GO>}

Well, Michael, let's start backwards. The profit in fixed index annuity we make on the reserves, so accumulated investments, and that is more than hundreds of billion dollar portfolio, mainly corporate bonds, BBB, that is maybe also an additional answer to the question why the unrealized gains on the portfolio that move because it's a 10-year bond. I would say, it's a very stable source of operating profit, only when the customer would all run away, then the profit falls apart. As long as the customers are staying, and we don't see any movements in surrender or lapse rates. So it looks to be a stable portfolio where we have more net inflows and then maturity, so it is still a growing number.

AGCS had indeed quite some run-off but we had the same run-off in previous years. So it is a very stable number. Why is it better than the competition? Well, I think we have maybe missed some growth opportunities and with the missed growth opportunity, we missed also chances for some higher man-made losses. So it is an underwriting and bottom line-focused approach And I think AGCS has delivered since it started a year-by-year improvement in its underwriting discipline. And it is certainly within the Allianz organization one of the leading organization, or the leading organization providing complex and commercial business.

Is our OP targets 2016 affected by the current volatility? Yes, for sure. We have increased the range around it because we feel that the year still might have more surprises than the first six months, when it's getting back to a more stable environment, then we have certainly plenty of time in the upcoming quarters to refine the outlook for the year.

Q - Michael Haid {BIO 1971310 <GO>}

But not the absolute level. It's more the volatility of the operating profit, which has been affected.

A - Dieter Wemmer {BIO 4755450 <GO>}

Well, I would say both. I think we have left the upper end stable.

Q - Michael Haid {BIO 1971310 <GO>}

Okay. Thank you very much.

Operator

We will take our next question from Johannes Reich of Metzler. Please go ahead. Your line is open.

Q - Johannes J. Reich {BIO 1808084 <GO>}

Thank you very much. Good afternoon. I have just one question on digitalization. Could you provide a figure for online distribution in your German operations in 2015 as well as the comparison with 2014? That's my question. Thank you.

A - Dieter Wemmer {BIO 4755450 <GO>}

I think Oliver will get up and then send it out because I think it takes a minute to find it. Correct? Yeah. We are digging it up. It will come to you in a few minutes.

Q - Johannes J. Reich {BIO 1808084 <GO>}

Okay. Thank you.

A - Oliver Bäte

Maybe it's a good time before we get to very much the fine details of the numbers that I'd like to give you a little bit of a top-down view reflecting on your very good questions and thank you for those. I think the question we just had on the outlook and the level and volatility is nicely summarizing really the questions that you may have looking at our disclosure. Maybe we could give you the following feedback.

Allianz had had a very strong year, and we're looking to capitalize on the number of strong years and a very strong balance sheet. We believe the volatility in the markets around us, as I said a little earlier, will create significant opportunities for us. And we would like, if I may say so, point out to the fact that we want to keep our powder dry for the opportunities that are coming. And if you are to interpret the way we are communicating today and the way the numbers have come out, please keep in mind that we are taking a measured approach to earnings per share growth that we want to make sure that nothing we are doing is threatening the stability and the strengths of our balance sheet. And we want to be able to move when the time is right.

Maybe that helps you in an environment that is increasingly getting nervous and concerned about where to put the money. Max have said it very nicely. If you can get zero for investing an abundant 5% minimum dividend yield in Allianz, I have my money here if that is of any consideration for you. That's the better investment.

A - Oliver Schmidt {BIO 2473131 <GO>}

All right. Thank you, Oliver. I think, with that, we should close the call. Thank you very much for your time and for your interest. We wish you a very nice remaining afternoon, and we hope that we will see you next week on one of our analyst meetings. Thank you.

A - Oliver Bäte

Thank you.

Operator

That will conclude today's conference call. Thank you for your participation, ladies and gentlemen. You may now disconnect