Q3 2017 Earnings Call

Company Participants

- Dieter Wemmer, Chief Financial Officer
- Giulio Terzariol, Chief Financial Officer Elect
- Oliver Schmidt, Head-Investor Relations

Other Participants

- Andrew J. Ritchie, Analyst
- Arjan van Veen, Analyst
- Farooq Hanif, Analyst
- James A. Shuck, Analyst
- Michael Haid, Analyst
- Michael Huttner, Analyst
- Nick Holmes, Analyst
- Paul De'Ath, Analyst
- Peter D. Eliot, Analyst
- Thomas Seidl, Analyst
- Vinit Malhotra, Analyst
- William Hawkins, Analyst

MANAGEMENT DISCUSSION SECTION

Operator

Ladies and gentlemen, welcome to the Allianz Conference Call on the Financial Results of Third Quarter 2017. For your information, this conference is being recorded.

At this time, I would 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>}

Thank you, Paul. Yeah, good afternoon from my side as well and welcome to our quarterly conference call. Before I hand over to Dieter Wemmer and Giulio Terzariol, who will conduct today's call together, let me remind you that this will be Dieter's last conference call in his function as CFO of Allianz. At the beginning of next year, Giulio will take over as his successor.

Now, Dieter and I will be on the road in Frankfurt and then London and Dieter will join us for our Inside Allianz Series event at the end of November. So, most of you will have the opportunity for personal goodbyes later. That's why I want to keep it brief today and I don't want to spend too much time on farewells.

But allow me to quote just two numbers, when Dieter became CFO of Allianz at the beginning of 2013, our share price stood almost exactly at €100. Today, as you know, it stands almost exactly at €200. And not to forget, while we doubled our share price over those last five years, we paid some pretty decent dividends as well. In my view, Dieter, that is an achievement you can be really proud of.

All right, I promised to keep it brief. So, that's all from my side for now. Dieter?

Dieter Wemmer {BIO 4755450 <GO>}

Thank you very much, Oliver, and let's hope that after this call, the share price is still at €200. So, good afternoon to the colleagues here in Europe and good morning to the ones dialing in from the States.

I will start with the nine months page and then I hand over to Giulio and we will do the Q&A then together to warm up for this transition (02:16).

Okay, nine-month figures, our net income is 5% up and that's where the third quarter did at less than the previous two quarters. Actually, I could finalize (02:30) the third quarter pretty easily. It is like Q2 minus the hurricanes and earthquakes. That is, I think, from a story-telling (02:42) summary and we will then go through all details [Technical Difficulty] (02:46).

The growth in all segments is actually holding up very nicely. Overall, nine months' growth 3.5%, before FX and on actual terms, 2.2%, clearly continued to be driven by Life and Health and Asset Management, which has the stellar fee income growth story. Operating profit, €8.4 million, contributed €2.5 million in the quarter. And again, Life and Health, Asset Management, clearly is a driver, Property/Casualty affected that's by the hurricanes of the third quarter.

And with this one, I would hand over to Giulio to dive into Q3.

Giulio Terzariol {BIO 17125489 <GO>}

Thank you, Dieter, and good afternoon and good morning to everybody. I'm marvelously pleased to be here to report on our third-quarter results. If we move to page 5, the main messages here are twofold. First of all, we had a strong internal growth of 5.5% with contribution coming from all segments, but especially coming from the Life segment and this combined also with the increasing new business margin is leading (04:11) as we will see afterwards to a growth in value of new business of 29%.

And then, on the operating profit, the €2.5 billion of operating profit is a good performance, especially under consideration of the intense cat activity that we had in the quarter. And as you can see in the waterfall, NatCat (04:33) end of the day, the impact on our operating performance in P&C was about €400 million.

On the Life/Health results, you see a little bit of a normalization, but one plus €1 billion (04:45) is really (04:52). So, it's again a very good quarter. In Asset Management, the underlying performance is very good with some dampening coming due to the FX effect. So, all-in-all, I think €2.5 billion that Dieter was also referring before is a very good performance.

Just another thing is if you look at the development of the net income, it's exactly in line with the development of the operating profit. This is a kind of unique coincidence, but the message here is there was not really major happening below the line.

If we move to page 7, speaking of our capital position, both the shareholder equity and the solvency ratio are up. And notably, the solvency ratio is up by 8 percentage point. This is before we do any deduction for the announced €2 billion buyback. After deducting for the €2 billion buyback, the solvency ratio will be 222%.

On the sensitivity, they are very stable compared to the sensitivity that we disclosed in the previous quarter. So, the message here is we have continuity and the resilience of our solvency ratio and also we are increasing our solvency ratio.

If we go to page 9, I can give you a little bit more insight about the drivers or the improvement in the solvency ratio. Part of the improvement – I will say half of the improvement is coming from the operating generation. And this is reflected in the slides with 8% improvement, but this is before taxes and before accounting for dividend. Once we account for taxes and dividend, we have a 4% improvement.

The second driver is driven (06:33) by the market development. And in this quarter, both the interest rates went up, the equity went up and also the credit spread narrowed. So, the (06:47) going into a direction led to an improvement of our solvency ratio of about 4%.

There is one thing that I like to highlight. On the business evolution, you see there is negative number, which means we are releasing capital as we approach a new business and we are releasing the in-force business. And this is a consequence of the action that we undertook over the last quarters or the last years, I will say, to change the business mix. And now, we see how the change in business mix is also coming through the evolution of our solvency requirement.

Now, if we go to the segment, moving to page 11, we can see that we had a growth rate of 2.2%. About 40% of this growth rate is driven by price and 60% of the growth rates of 2.2% is driven by volume. When we look at the different entities, clearly Allianz partners is standing out with a growth rate of 12% and this is driven both by travel and also by international health.

Otherwise, you can see a lot of positive signs on these slides with two exception, one is Turkey, and this is the reflection of the change in regulation, we have touched upon those changes already in the last quarter, and the other one is Italy, this is a reflection of the contraction in motor TPL. We see anyway in Italy some signs of stability that are coming through. So, most likely, the number – that sign is going to change as we go into 2018.

If you move to page 13, we come here to the driver of our operating performance. And as I was saying before, the main issue in the third quarter has been the cat loss coming from the hurricanes in the U.S., in the Caribbean. On top of that, we had also two earthquakes, especially major earthquake in Mexico. And we had also some storms here in Germany and in Austria.

The cat loss for the quarter was €530 million. This is in comparison to only €30 million in the previous quarter. So, the swing is about €500 million. On the other side, you can see that the runoff is a little bit higher compared to what we usually expect on a quarter, but the important thing to note here is when you look at the runoff on a year-to-date basis, it's very much in line with our past experience.

On the expense ratio, you can see there is an uptick of 40 basis points. This is mostly driven by the loss of the crop business in the U.S. So, if you adjust for that, in reality, the expense ratio is relatively stable over the prior-year level.

And then, I would like to make a final comment, when we had these kinds of cat activity in a quarter, usually you should assume that we have also additional small weather-related events. So, at the end of the day, the number we have mentioned here with respect to the cat loss doesn't include other events, which are anyway impacting our performance in this quarter and this is totally larger than when we had this kind of cat activity. We are going to have also other minor events.

The bottom line is when we try to normalize our results to get to the underlying performance, we end up with a combined ratio, which is below 95%, and this give us confidence that we are going to hit our 94% combined ratio in 2018.

At page 15, you can see the impact of the natural catastrophe through the various entity and obviously, when you look at AGCS, you can see that, that entity has been particularly affected by the impact of the cat losses. The other entity that was affected by cat losses was France and that's because of the business they had in the old colonies in the Caribbean.

And then, just look at Germany, you can see the combined ratio deteriorated by about 5 percentage points, 1.6 percentage point is due to cat losses, but as I was referring before, there are also weather-related impacts and this was the primary driver in reality for the deterioration of the combined ratio in Germany.

So, all-and-all, I would say when you adjust for cat losses and for weather-related events, the picture is again very consistent with the performance that we saw in the prior quarters.

Moving to page 17. We see that our investment income is overall resilient. And especially when you look in the quarter to the interest and similar income, you can see that the number is really flat, indeed even slightly increasing. On a year-to-date basis, also the operating investment results is very consistent and is flat. And the point is, we see more resilience that we were indeed expecting in our operating investments results. On the current yield, you see that it is 2 basis points lower compared to what we had in the third quarter 2016. But the current yield is indeed even 1 basis point higher compared to what we had in the second quarter of 2017, and in the first quarter of this year. So, that's, again, a proof of some resiliency that we are seeing by now on the investment results.

Now, moving to page 19 and speaking about our Life results. The present value of the business premium is up 5%. If I remove FX effect related to the U.S., the number would be even north of 6%. And in general, we see strong growth in most entities. There is one exception or one notable exception, which is the U.S., where we are preserving profitability over volume. Now, if we adjust our growth rates for the U.S., the growth rate is 11%. This tells you a lot about the strength of the growth that we are recording in most markets. The new business margin has improved by 50 basis point (13:34), and this is pretty much widespread across all the lines of business with the exception of unit-linked, but this is due just to a geographic mix because Taiwan is getting more premium this year. And in Taiwan, the new business margin is lower than the average new business margin for the segment.

If you combine this nice picture to the fact that we have 77% of the business in what we call Preferred product, I think you get really a strong picture about the value and the quality of the business that we are generating on the Life side right now. Moving to page 21, and speaking of the operating profit. As I said before, the operating profit remains strong at almost €1.1 billion. And this is, again, another quarter with a very strong performance and also is above the outlook if you consider the outlook of €4 billion divided by four. The investment margin is lower compared to the prior period by about €125 million, and this is driven by lower harvesting especially in Germany. And last year, we had the derisking, and so we were selling BTP (14:54), and this was automatically creating realized gains.

And also we had some harvesting, if you want, in our French operations. That's just a little bit of a normalization. Again, results are extremely strong. If we move to page 23, the value of new business is up 29%, and you see an improvement basically in all operation, I would say. And I would like to come back to the U.S. As you see in the U.S.A., the value of new business is up 137%. That's again the point we are looking profitability. We are not looking at volume. The premium might go down but the value of new business growth, which is what counts. This is going up significantly compared to what we had one year ago. So, I believe this slide is, again, a proof (15:45) to the quality of the result and especially when you see so many plus signs and/or the magnitude that we see, this gives you an idea about the level of effort that we put to increase our new business margin over time.

Going to page 25, you can see here the breakdown of the investment margin. And here you can see a reduction of the net harvesting by 20 basis points. Indeed, the net harvesting for the quarter is only 4 basis points. And so, this means that the investment margin that you see below of 23 basis points is pretty much the level, which you could expect as totally normalized. One point to note here, the reduction in net harvesting is about 20 basis point, but this is largely cushioned by the profit sharing under IFRS. So, you get a little bit of a sense that there is a lot of cushion even when the net harvesting is coming down. And our investment margin of 23 basis points is the normalized level. This produced an investment margin of about €1 billion.

And as you saw before, this leads to an operating profits of €1 billion-plus. So, this gives you an idea about the resilience and the underlying performance that we might see on the Life side. Now, at page 27, we go into the Asset Management segment. We had in 2017 over €100 billion of inflows, which is a huge achievement, especially considering all the noise about (17:28). And when you look at the third quarter, also the third quarter got its fair share of this €100 billion with €30 billion-plus of net inflows. And this is PIMCO, but I would like to highlight that also AGI had another quarter with positive inflows. The market development has been positive, but on the other side, the FX effects have dampened the growth in assets under management. The fact is the underlying performance, the net inflows remains very strong also in the third quarter.

Moving to page 29, and look at the revenue development in asset management. The internal growth of the revenue was 5%. And when we adjust for the seasonality, volatility of the performance fees, the underlying revenue base is up 9%, which is a very good result. On the fee margin, you can see that PIMCO is very much stable. In the case of AGI, you see additional 1 basis point, but about half of it is driven by the technical factors associated to the sale of Korea. So, if you adjust for that, the fee margin in AGI is 47.5% and this is just slightly reduced compared to the levels that we had last year. And this, indeed, flat compared to what we saw in the other quarters.

Moving to page 31, on the operating profit development. As you see the operating profit is slightly down compared to the quarter a year ago. But if you adjust just for the FX effect, you get to a growth of 1.4%. If you also adjust for the volatility of the performance fees, then you get to a growth in operating profit, which is well in excess of 5%. A final comment on the cost/income ratio, which is up 1 percentage point. We had some one-offs, a small one-offs in the quarter. The point is when you look at the nine months development, the cost-to-income ratio, as data was shown in the first slide, is down 1.6 percentage point and this is more a reflection of the underlying improvement happening in our Asset Management segment.

At page 33, I'm going to be very quick because I'll just skip it. And then well go to page 35 where we can see the non-operating items. As I was saying before, there is really not much happening below the line. Maybe the only thing could be the effective tax rate. As you see its 28%. (20:24) 30% the prior quarter, which is also more or less what could be an expectation. The reason for the 2-percentage-point improvement is twofold. On the one side, we had a small release of a provision. This makes for 1% of the improvement, and the other 1% of the improvement is just related to the composition between taxable and tax exempt income.

And with this, I will turn it over to Dieter for his final remarks.

Dieter Wemmer {BIO 4755450 <GO>}

Okay. Thanks so much, Giulio. And then let me summarize on page 37, where do we stand and how are we doing with respect to our Ambition 2018. I think EPS growth is on a good track. Our ROE is still below our 13% target, but I think we have less of an earnings problem because I think the earnings have developed since we put up the target well above, but our equity did even better. So, our €2 billion share buyback program, which we announced on top to our Q3 results and we have not yet mentioned today. It's certainly, also helping to get our ROE in the right perspective, that's ratio between strong earnings and adequate equity results into the right number. The combined ratio is 94% after nine months but with a very difficult quarter as the industry and most of our peers have shown.

So, we are – feel comfortable about our next year's target. Our Life OEs, as they're making the 10% ROE, we are convinced that we are getting it to a very strong number, maybe not 100.0% but already in the direction of 100%. Life new business margin we talked about, we are on target. PIMCO cost income ratio, interest rate sensitivity, we are pretty much on target and also IMIX is actually a latest measurement of our asking our employees on (22:55) and engagement in 72% is a very recent number where our NPS measurement is already sometime old and will be updated then with the next round of market surveys.

So, with this one, I think I would move to the Q&A and happy to learn what really interest you (23:25) already.

Q&A

Operator

Thank you. We will now take our first question from Peter Eliot of Kepler Cheuvreux. Please go ahead.

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

Thank you very much. I guess, the first one was on that buyback. Thank you very much, Dieter, for the – your farewell present. I guess, net of that buyback, I thought you're at 222% solvency, so still above the top of the range. And I guess, by midyear, barring unforeseen circumstances, we should be again well above. I was just – I mean, obviously, you might have M&A opportunities. You could have adverse market development. But taking those out, I'm just wondering if you could share your thoughts on whether there's anything that would – prevent you continually repeating the buyback and just – is there anything in the sort of quality of solvency capital? Anything anywhere that might limit your thinking there?

The secondary area of question was on the Asset Management division, some really strong inflows. I note your comments that October has done very well as well. Are there any large mandates in there or is there any reason we shouldn't sort of think about it's actually a pretty sustainable level? And I guess also in the past, you've given some guidance on performance fees in the pipeline. Are you able to – and obviously, they were low this quarter – are you able to hint at what we might expect (25:11) going forward? Thank you very much.

A - Dieter Wemmer {BIO 4755450 <GO>}

Okay. Peter, thank you. I think the first question and including the Asset Management, so share buyback, I think it is – your calculation is pretty correct. I have also on my end result 222% post share buyback. So, there is nothing which would stop us to do – to continue our solvency management. However, I would not make now this to be a quarterly or half-year event. I think that it could be also other business opportunities we could look at and the group will look at. But it is – we promise more dynamic in our capital management, and that is what we continue to do. And the liquidity comes along with the capital generation, as I mentioned already several times on various road shows. So, we feel very comfortable that we can handle this.

The inflows continue to be at PIMCO very broad. In particular, what is really nice when you look at the geographical diversification, it is really a global inflow, which makes it, I think, a very strong inflow. And, therefore, we have not any lumpy one-offs in it. It's not that part of the €18 billion, €17 billion as one cash pool (27:03). So, it is really broad and mainly retail funds. The performance fees, yes. They are quite – where it, you have to remember and, therefore, it's a bit different with previous years, we had strong performance fees in prior years from carried interest from Bravo I. That fund has to be paid back completely. So, therefore, we didn't have – almost no performance fees in the PIMCO calculation in Q3.

And the next carried interest, which will come due I think is starting in 2019, 2018 as – maybe at the end of 2018 but probably more 2019 is then Bravo II to be harvested. That means the PIMCO performance fees are all out of normal mandates, so segregate account, hedge funds, et cetera, and Q3 is not a performance quarter to be calculated. So, there is in Q4 coming, and that is linked to their capability to produce Alpha. So, based on what they did so far in the nine months on delivering Alpha, that is certainly a positive indication. But as you know, Alpha can also be a very volatile guest. So, we have to wait until we complete the calculation in December and then we know how much performance fees we will see into the fourth quarter 2017. Did this answer your question, Peter?

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

It did. It did in great detail. Thank you very much.

Operator

Our next question comes from James Shuck of Citi.

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

Hi there, Dieter. It's James Shuck from Citi here. I had three questions, if I may. The first one is around the capital generation in the quarter. So, this is the third quarter we've seen 4 points of capital generation net of dividend third quarter in a row. So, we're kind of annualizing it around the 16-point level. I think previously your guidance had been 8 to 10 points net of dividend. So, just thinking, are we seeing a step change in that number? Are there any one-offs we should be thinking about? The second question is around the P/C combined ratio. So, I think – I mean, my numbers were normalizing around 95%, maybe there's a bit of kind of large losses and weather type things there that mean you're a little below that, I think based on the comments you made.

You previously indicated that this is the division that potentially could surprise the greatest, positively, I think. And I kind of just keen (30:07) to understand where you think you are with the plan because the 94% by 2018, what kind of starting point, is it a normalized level of 95%, obviously some headwinds here and there. So, I just kind of – are you running ahead of plan? Is it still the division that excites you the most because when we look at the sources of the beat (30:27) so far, it seems to be coming from Asset Management and Life and Health rather than P/C? And then just my final question was actually on Life and Health profitability. I'm kind of looking for a bit of help here because 2016 vantage (30:42) is from a high level of harvesting the boosted the investment margin.

I think you've indicated the underlying investment margin was around 95 basis points. Where do you see that margin kind of going to because I think it's around 80 basis points annualizing at the moment year-to-date? And I get lost a bit around the potential profit signature from the U.S. because lot of the geographical improvement in Life and Health has come from the U.S. And obviously, you've seen very strong sales of fixed index annuities there in recent years. And I suspect the profit signature is quite front-end loaded. So, as that falls away, I'm just interested to get some insight into the sustainability particularly in the U.S. please? Thank you very much.

A - Dieter Wemmer {BIO 4755450 <GO>}

Okay, James. I start with capital generation. Indeed, I think our – in particular, when you look at our chart, the solvency waterfall, it's a business evolution. That means that it's a – the difference between the released capital and new consumed capital is probably a little bit stronger than we expected. We are also watching whether this is stable development over the quarters and look, our additionally announced share buyback and that we do it now after Q3 is also an expression of our confidence that we see the quarterly development of our solvency ratio into good shape. So, I'm not sure that we are already ready to change the guidance. We – give us more quarter to learn, because you have also remember that we are just in quarter seven of the (32:47). It just started 1/1/2016, so it is not yet a long learning. And also, our Life books are still complicated beasts, which when you translate it into Solvency II terminology. So, our comfort and confidence is high, but we are not yet changing the guidance. Let's put it this way and leave some work to do for Giulio.

A - Giulio Terzariol {BIO 17125489 <GO>}

Yeah. I can pick up the two questions. The one on the combined ratio for P/C and also the one on the Life profitability. The combined ratio for P/C, there are two ways we can look at these numbers. First, if you take the combined ratio of the third quarter of 96.9%. As you see, we had a cat loss (33:45), which was definitely more than what we usually expect. So, you can definitely normalize the number by 2.2 percentage point. Then, on the other side, the run-off is a little bit higher. So, you can normalize also the number by 1.1 percentage point. So, you end up somehow below the 96%. And then, as I said before, there is a lot of weather-related activities going on in the quarter. So, when you also normalize for that, you get to a combined ratio, which is definitely below 95%, and that's the reason why we are very profitable that we are going to get to the 94%.

If you go to the page 14 by the way, you're going to see there is a table where there is a nine-month results. On that table, when you look at the 95.4% combined ratio, that somehow almost implying the normalized level NatCats and the run-off that's usually we would expect. So, 95.4% on a nine months basis. And then, again, we had the issue that we have more weather-related losses and also large losses. So, again, it doesn't take long to go below the 95% level. That's the reason why we feel we are really on track to get to the 94%. If you ask me, are we ahead of schedule or behind schedule, I would say, this is a German company, so, yeah, it's scheduled. And that's my view on the combined ratio for 2017 and what this means for 2018.

On the Life results. Our investment margin for the quarter is 23 basis points, and this is pretty much a normalized level that you would expect. (35:36) should be about 95 basis point on a full-year level. So, if you said the 23 basis point times four you get pretty much there. When you look at the investment margin in the previous quarter, they were higher than the 23 basis points. So, I will say, what you see right now it's a sort of good indication of a normalized level. And from that point of view, you should expect this kind of performance also with some plus and minuses to come through in the future. On the U.S. business, I'm not fully sure I share your view on the front-end loaded profit in Allianz Life. I was the CFO there for many years, I wouldn't say that.

Their Property margins is just smooth across the duration of the policy. What is our expectation for Allianz Life, we expect to have an underlying performance, which is still growing. Even if premiums are coming down, the book is growing. The only thing to consider, this year the profitability of Allianz Life is very strong also because the volatility is very low. And when you have such low volatility, then you get really too (36:51) good performance also on the VA business, which is not a major business for Allianz Life. But we shouldn't forget we have €30 billion of liability, and those €30 billion liability are performing very nicely in this kind of environment. So, the bottom line is the underlying performance is for Allianz Life is going to go up, and then there is always some plus or minus associated to some volatility. Does this answer your question?

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

Yes. No, absolutely. Thank you very much for that.

A - Giulio Terzariol {BIO 17125489 <GO>}

Thank you.

Operator

Our next question comes from Michael Huttner of JPMorgan.

Q - Michael Huttner {BIO 1556863 <GO>}

Hi. I was tempted to ask just one but now it's too tempting to ask more. But the main question is really what's your view, both Dieter and Giulio, what's your view on disclosure? Are you happy to continue with this, what I think is a very nice quarter (37:53)? Or would you move to like (37:55). That would be my one question. The...

Q - Oliver Schmidt {BIO 2473131 <GO>}

Sorry, Michael. Michael?

Q - Michael Huttner {BIO 1556863 <GO>}

Yeah.

Q - Oliver Schmidt {BIO 2473131 <GO>}

The line was – is relatively poor. Could you please repeat the question? Thank you.

Q - Michael Huttner {BIO 1556863 <GO>}

Sorry, just what is your view on the topic of disclosure and on quarterly disclosure and whether you're happy to continue with what you have now or whether you'd be looking to reduce it like some of your peers have done? The second question is your – I know you're saying, you can still improve. Can you actually say where you can improve? I can't see any significant areas of improvements. There's small, like maybe Brazil can improve. I don't know maybe, you said the weather relating might be normalized, I don't know. But I can't see where you can improve anymore. There's no pockets of underperformance, and I just wondered if you can say where there's – where you see any variances going forward? And then last question, is a kind of phishing (38:54) question. Inflation is picking up. I don't know how you see that, but my feeling is that the reserve releases – a very nice level of reserve leases we've seen. It might start coming down, and I just wondered what your thoughts on that? Thank you.

A - Dieter Wemmer {BIO 4755450 <GO>}

On the disclosure?

A - Giulio Terzariol {BIO 17125489 <GO>}

Yeah. That's your call.

A - Dieter Wemmer {BIO 4755450 <GO>}

I am – I have done my Q3.

A - Giulio Terzariol {BIO 17125489 <GO>}

How we see that? We had some conversation here internally about whether we want to continue to do full disclosure for Q1 and Q3 or not. And at the end of the day, the decision has been that we're going to continue to do disclosure in Q1 and Q3. And to be perfectly blunt with you, one of the reason why we decided to do that is also because you don't want to maybe decrease the level of disclosure just right when you have a new CFO coming up. The point is, we should also get some sort of recognition if you continue to do this – the kind of disclosure that we are doing now when all other competitors are getting too much less disclosure.

So, if we're going to see that, this is going to be appreciated by you or by the investors, we are going to be very happy to continue to provide quality information. But if we see that this is not the case, then clearly, we are business people here and we are going to make a cost benefit analysis and potentially change how we do things. But the idea, we're going to continue to do it and we believe that providing quality information to the rest of community can be a value add, but we're going to see what the numbers are going to say. So, that's on the disclosure. On the combined ratio, yes. Indeed, we are doing very good, and I will say there is maybe not a huge amount of improvement, but this is certainly the point.

We just need a little bit to get to the 94%. Anyway, we have definitely pockets where we can better. So, just think about Latin America. There is still room for improvement. When we look at the different portfolios that we have in the different OEs, there are portfolios where we can get better. And the third lever would be to work on the expense ratio. So, when you start improving on some regions, when you start improving on some portfolio, when you get productivity improvement, and potentially you might see also rate increases for doing (41:35) the cat activity that we saw this quarter, I believe that we should be well-positioned to get some additional improvement. And the last question was?

Q - Michael Huttner {BIO 1556863 <GO>}

Reserve releases.

A - Giulio Terzariol {BIO 17125489 <GO>}

The reserve release. I – one of the good things – one of the many good things that Dieter did is also to leave a very strong balance sheet. So, I'm not concerned about our ability to have also a healthy support from our balance sheet in the future. Maybe, Dieter, you want to say something (42:10).

A - Dieter Wemmer {BIO 4755450 <GO>}

Yeah. Well, actually, the – Michael, we – I think it's quarter number 54 of reserve releases. That is a pretty long track record. And I think we have managed over this time our reserves very well, and I think I can also say, without giving business secrets away, the balance sheet and reserves strength is, as of today, higher than the day when I started.

Q - Michael Huttner {BIO 1556863 <GO>}

Well, no, thank you.

A - Dieter Wemmer {BIO 4755450 <GO>}

That is – and that is not going away into next (42:55), I can tell you.

Q - Michael Huttner {BIO 1556863 <GO>}

Good. Lovely. (42:59). Thank you so much.

A - Dieter Wemmer {BIO 4755450 <GO>}

On P/C, I would make one remark. We are not going to give individual countries and OEs, but I just discussed yesterday with my colleague, Axel Theis, who is responsible for the global P/C besides his geographical hold. He discussed with me a list of more than 100 larger and smaller portfolios where we have, behind each portfolio, action items and that is the way how we manage our segment base combined ratio performance. So, therefore, I think we are well on track with our promises.

Q - Michael Huttner {BIO 1556863 <GO>}

Lovely. Thank you very much, indeed.

Operator

Our next question comes from Arjan van Veen from UBS.

Q - Arjan van Veen {BIO 5197778 <GO>}

Thank you, gentlemen. Two questions, if I may. Firstly, on capital generation. Can you give a bit more color around the profile of the Life book in terms of the shift mix? All of a sudden, new business is shifting more to lower capital intensive products, you're releasing therefore on the back book and whether that can accelerate, and particularly when you look at (44:22) the two cap-gen disclosure where your Life capital generation is running quite a bit ahead of the IFRS profit and whether we can kind of expect that to continue? And then just kind of a question on that point, it's coming through the own funds developments rather than FCR (44:39). So, maybe just if you could explain that why we shouldn't be seeing FCR (44:45) releases given that mix shift? And then, the final question, just on the UK adverse large loss development, I think one of your peers saw something similar, so just curious as to what that is and the actions taken?

A - Dieter Wemmer {BIO 4755450 <GO>}

Sorry. I didn't get the last question. What was it?

Q - Arjan van Veen {BIO 5197778 <GO>}

The UK large loss development.

A - Dieter Wemmer {BIO 4755450 <GO>}

Okay. Yeah.

A - Giulio Terzariol {BIO 17125489 <GO>}

Okay. Maybe I can pick it up on the capital generation. Indeed, what you were referring to which is the release of capital coming from (45:26) and capital Life business compared to the capital intensive business we had in the past is coming through the ACR. So, if you go to page 9, you can see there is a minus €0.2 billion of business evolution, which is exactly what you were referring to. So, it's coming through the capital generation. Now, I can give you a little bit an idea what we are talking about. We had this quarter €12 billion of present value of new business premium, and I would tell you this €12 billion of present value of new business premium is more or less in line with the release of reserves that we had broadly speaking.

So, it means if you take €200 million divided by €12 billion, you get to about 1.5 percentage plus. And you can say this 1.5 percentage plus is the difference between the capital consumption on the old business and the capital consumption that we have on the new business. And so that gives you a little bit of the idea of what we see. Do we expect to see this also in the future? I will say yes. Indeed, we had this business evolution also in the second quarter. So, fundamentally, we should see this also playing a role moving forward. Obviously, I always put a caveat there is – they are complicating model.

There is always potentially some noise. And also one thing to consider, the third quarter is a weaker quarter from a premium point of view compared to other quarters. So, you might see depending on the premium (46:59), depending on the quarter, you might see a little bit more of a positive business evolution or a little bit less. But fundamentally, this is the trend. On the UK, yes, we saw large losses in the UK this quarter. So, that's definitely something that has affected the performance, but we see also that especially on our property business, there are some challenges. And as Dieter was referring to this, it would also be part around the portfolio where we're taking action so that we can have a better results as we go into next year.

Q - Arjan van Veen {BIO 5197778 <GO>}

Okay. Great. Thank you.

Operator

Our next question comes from Thomas Seidl of Bernstein.

Q - Thomas Seidl {BIO 17755912 <GO>}

Yeah. Thank you. Good afternoon. First question on the ROE target, 12.4% it is now. My question is what does it take you to get through the 13%? Is the €2 billion buyback plus the earnings closure you're planning for next year already sufficient to get you to the 13% or is there anything else you're going to do capital-wise to get to the 13%? Second question on Life, I mean, year-to-date operating profit at 84% versus midpoint full-year guidance, Dieter. So, what has surprised you over the last nine months to have such a strong outperformance? Is there anything structural we should consider going forward? And the third question is on the P/C investment income side, asset under management down, re-investment rates below (48:46) regular investment income even slightly up, different from the Life side by the way. So, what's going on? How is it possible to produce slightly increasing regular interest income in the P/C side with a falling asset base?

A - Dieter Wemmer {BIO 4755450 <GO>}

Okay, Thomas, I take the first two questions and then Giulio will talk about the P/C investment income. The first question, how to get to the 13%? I will probably not answer to the detail you would like to hear, because we are not doing now a forecast of our 2018 net income. I think you have to wait some time before we get there. And I only said that the share buyback, is certainly a measurement, which supports a stronger ROE, that is the only point I made, and I hope that the sentence is correct, actually. If my math is right, €2 billion makes about 20, 25 basis points in our (50:06).

So on operating profits, we are – I think we had a very strong first nine months, whereas the first six months contributed even stronger. I think €2.5 billion in Q3 is, in pure comparison, a very good number, maybe even stronger than our previous numbers in distance. But as a absolutely number, of course, smaller, what did surprise ourselves. I think the stability of the Life results – and we had just a second ago a lot of debate about investment margin and if it's moving up or down. I think that €1,070 (51:03) operating profit for a quarter was really de minimis realized gains and actually a weaker dollar because although Giulio is coming from there but he's always thinking in dollar. Actually, the average investment margin drops when the dollar gets weaker because we have the highest investment margin in the U.S. And it is a strong contributor.

That means, the average investment margin for the portfolio is as a number shrinking when the dollar is coming in weaker. So, I think, all this included, the third quarter Life result is to me a real evidence that we have turned the Life business into a very positive direction. And the other surprise in the operating profit is, obviously, the stunning development at the PIMCO inflows and AGI also nicely holding up. I think even optimistic guys and I was always very positive about PIMCO's capability but to assume that such big numbers that was certainly out of expectation naturally. I think what were fully aware is that the group is very robust with its three segments and play very well together as a team, and that is being shown in the numbers.

A - Giulio Terzariol {BIO 17125489 <GO>}

Yeah. On the operating investment results and the stability that we see. Clearly, when you look at the current yield, this is coming down a little bit. There was 2 basis points. If you translate that into an operating profit for the quarter, there will be something about €20 million. But on the other side, we're getting more yield from real assets especially from equities. So, that's the point where we are able to compensate the decrease in the interest income through other sources of regular income like kind of regular income dividend. And in general, we are pushing more the alternative assets where we can get a yield pickup. That's the reason why you see the stability on the interest and similar income. You don't see much of a drop in operating profit performance from an investment point of view.

Q - Thomas Seidl {BIO 17755912 <GO>}

May I follow up on the capital side? So, I appreciate, of course, you don't want to do – discuss next year's earnings, but why €2 billion buy because I think in the past, you often discussed that you need to deploy more than €2 billion capital management to get to the 13%. Now you're doing €2 billion. Why €2 billion?

A - Dieter Wemmer {BIO 4755450 <GO>}

Why €2 billion? First of all, I would say we are just in the final completion of the €3 billion share buyback, which we announced in February. So, as this on an automatic buying program with one of the large banks, I think it is being finished mid-December. So obviously, you don't start a new share buyback program in a week (54:42) before Christmas. That is a pretty useless time of the year for share buyback programs. So, it is a 2018 event. I think the €2 billion is a strong signal that we can do more in the year than the €3 billion, but as I said before, we are not putting it on some evergreen automatic formula that you can calculate at once what the announcement will be. I think capital management will always take into account where the company is standing, what are the opportunities in the market and what is the specific situation how these (55:34) foreseeable future developing. All this comes together and that it leads to our decision of the €2 billion.

Q - Thomas Seidl {BIO 17755912 <GO>}

All right. Thank you very much, Dieter.

Operator

Our next question comes from Paul De'Ath of RBC Capital Markets.

Q - Paul De'Ath

Hi there. And couple of questions, please, on P&C. So, the expense ratio, you've have mentioned needs some improvement still and it's been a couple of quarters. Now that you've been talking about – you're slightly disappointed with – and what actions are you actually taking to improve that? And where do you think we (56:22) can see that benefit coming through, will it be kind of towards the end of next year or sooner than that?

And, secondly, on the hurricanes and there's also the ongoing impact from that, so have you seen any sort of change in the pricing environment for AGCS? And linked to that, what's your view on reinsurance and prices going up there to reduce your reinsurance cover if prices increase significantly? Thanks.

A - Giulio Terzariol {BIO 17125489 <GO>}

Okay. So, P&C expense ratio, first of all, yes, there is no doubt that we need to do better on that. We have started taking action already this year. For example, I'm not sure or remember the first quarter where we had restructuring cost at AGCS and we also look in other entities what we can do to get to a better expense ratio.

So, we are putting strong focus in the current planning around into the topics specifically of expenses and this is also going to be something, which is on my personal agenda as we move into 2018. So, there is definitely a big portion. We want to see the expense ratio to move downwards and I don't think we're going to be happy if we see in the future a continuation of what we had in the last year.

On the hurricanes, I will say, it's too early now to see that we see anything on the pricing side. We can't speculate about what is going to happen and this morning, Dieter was very clear anyway on the reinsurance side, we didn't have a lot of retrocession to reinsurance companies. So, we would not expect any way to get rate increases coming to us.

What is going to happen to primary markets, it's a little bit too early to speculate on that. In theory, one should expect rather increases, they're not something different, but again we need to wait to see how the whole thing is going to play out.

Q - Paul De'Ath

Okay. Thanks.

Operator

Our next question comes from Andrew Ritchie of Autonomous.

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

Hi there. Just question on the capital efficient life products profitability. I'm assuming – but it seems to be the case, if I look at the U.S. Life profit and capital-efficient profit. That the capital-efficient products outside the U.S. is still loss-making, I guess, because of new business strain. Can you update us on when you think those products will start to be breakeven and start to (59:23) profit? So that's capital efficient outside the U.S.

Second question, Italy, Italy Life is making 7% ROE. You make a statement in the comments that you're still confident that'll be a 10% ROE in 2018. Is that driven by the numerator or the denominator? And (59:45) believe this is the moment where AGCS switches from a soft market strategy to a hard market strategy or is that possibly the case? And obviously, you have been cautious in that division. It doesn't sound like you're thinking the market may change to give you lot of new opportunities there? Thanks.

A - Giulio Terzariol {BIO 17125489 <GO>}

Okay. So, starting from the capital life products, your question is pretty much referring to Germany. And I will say that right now, depending on the level of production, we are kind of sometimes get into the positive, sometimes it can still be a small negative. So, I believe fundamentally we are very closed to get to a stable breakeven. So, it really depends on the strength of the production, because, as you said, there is a sort of strain that we get into our IFRS numbers. So, that's on the...

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

Would you expect it to be profitable next year?

A - Giulio Terzariol {BIO 17125489 <GO>}

I will say, next year could still be swinging depending on the quarter between plus and minus, but then I will expect this to become profitable starting 2019. But then, it could still be in between depending on the level of production.

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

And could you clarify what the loss is at the minute (01:01:03)?

A - Giulio Terzariol {BIO 17125489 <GO>}

What the loss is, it's called – is it the capital life...

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

The loss, the amount of loss...

A - Operator

It's very minor, but...

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

Right.

A - Dieter Wemmer {BIO 4755450 <GO>}

Of course, we are in the (01:01:16).

A - Giulio Terzariol {BIO 17125489 <GO>}

It's €13 million.

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

Okay.

A - Giulio Terzariol {BIO 17125489 <GO>}

So, it's very minor.

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

Okay.

A - Giulio Terzariol {BIO 17125489 <GO>}

That is, as I told you, swinging from plus to minus.

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

Yeah.

A - Dieter Wemmer {BIO 4755450 <GO>}

By the way (01:01:27), for Italy, it's both. It's both the denominator, it's both the numerator (01:01:32). So, when you look at the ROE of Italy, which is about 7.5%, consider this is annualized and this includes also the – we got a hit on (01:01:45) in the first part of the year. So, if you normalize for that, the ROE would be automatically normalized 9%.

Then you would expect, anyway, some improvement. And then, we are also going to work on the capital of the company, but, again, read the number, right now more is 9% (01:01:59) when you adjust for the one-off and there you're very close to get to 10%.

And the last question (01:02:07), so you need to repeat the last question, (01:02:12).

(01:02:10)

A - Giulio Terzariol {BIO 17125489 <GO>}

Look, I think all these pricing changes, in the fourth term, we will certainly see that people, who urgently needs cover or need to replenish a reinsurance coverage, they probably pay more. What is really the midterm pricing change, we will see in which areas, which customer groups and how broadly will it affect the market. If you all believe that we are too conservative here, then it is an additional upside for our business.

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

Okay. That's even. Thanks.

Operator

Our next question comes from Nick Holmes of Société Générale.

Q - Nick Holmes {BIO 3387435 <GO>}

Hi, guys. Thank you very much. First question is on U.S. Life. Wanted to ask, is your hybrid variable annuity basically taking over from the fixed index annuity, if you can basically remind us of your strategy there and also your view to DOL?

Second question is on unit-linked growth and how sustainable do you think this is? And the third question is on Italian P&C (01:03:33), say the runoff is extraordinarily high. I wondered, do you think next year, we should see a correction to this? Thank you very much.

A - Giulio Terzariol {BIO 17125489 <GO>}

Okay. So, starting from the Life business and starting from the hybrid VA versus the FIA, now (01:03:55) not taken away, because the hybrid VA goes through the security channel and the regular FIA goes also through the security channel, which is mostly on the agency channel if you want. So, I would not say that there is a cannibalization between the two.

On the – DOL has been delayed until 2019. So, I would tell you the DOL has been somehow impacting us in the first part of the year, also because we had to do all the preparation to get there instead of maybe doing other things, but right now, the DOL is not having a major impact on what we are doing.

On the unit-linked and the growth in unit-linked, I would say fundamentally, yes, the trend line is sustainable, but clearly, depending on the market condition, you might have some volatility. So, I think we have the distribution. We have all what it takes to have a story, continued story on the unit-linked business absolutely. If we have a big shock (01:04:59) in the market, you're going to see volatility. There is no doubt about that.

And with respect to the runoff in Italy, yes, I think the run-off in Italy has been consistently very healthy. It's going to flatten down a little bit over time. I will say, yes, most likely, we're going to see less positive runoff (01:05:22) coming from Italy in the following years (01:05:25), but we still expect the performance of Italy to be very, very good and very healthy.

Q - Nick Holmes {BIO 3387435 <GO>}

Thank you very much. Can you quantify the Italian runoff? Can you give us any sort of sense of the size of the impact on your overall runoff?

A - Giulio Terzariol {BIO 17125489 <GO>}

I have memory losses right now. So, I don't think I can quantify that, no.

Q - Nick Holmes {BIO 3387435 <GO>}

Okay. Thank you very much.

Operator

Our next question comes from Vinit Malhotra from Mediobanca.

Q - Vinit Malhotra {BIO 16184491 <GO>}

Yes, yes, good afternoon. Thank you, Dieter and Giulio. Just one thing. One factual check please. The AGCS, which is – tend to be very volatile of course. If ex the NatCat, it's around 88% (01:06:12) combined just on slide 15. Is it just an assumption that a lot of this runoff comes from here? That's a quick fact check question.

The second question is on the – just how you view the emerging market as investment opportunities or what have you, because there's been a lot of volatility in the currencies of some of these markets, including areas where you are exposed to, just Turkey and Brazil? Do you intend to hedge or how do think about that?

And just last third question if I may, there's been a lot of chat around – in the asset management world around performance-based fees, so not performance fees, the performance-based fees. And have heard a story that AGI also has two or three funds being tested. How do you think of this trend also from a broader PIMCO and any other perspective that you can offer here? Thank you.

A - Giulio Terzariol {BIO 17125489 <GO>}

Well, maybe I start here. The AGCS is clearly a contributor for the runoff in the third quarter. And AGCS was always and also in past quarters and years a reliable contributor to runoff results. Investment opportunities in emerging markets, that is you mean buying businesses, you don't mean investing in bonds, Vinit?

Q - Vinit Malhotra {BIO 16184491 <GO>}

Well, at the moment, to be just safe, I do mean bonds and other exposures. Buying companies is something I don't want to talk today.

(01:08:05)

A - Dieter Wemmer {BIO 4755450 <GO>}

Okay, because you were a bit inked (01:08:10) on this one. We have, in total, at the moment €7.6 billion of emerging market bonds and that is a bit – in some – that is our exposure after hedging. So, on nominal, it would be a bit bigger. I think it is a long discussion, I think, as in all the (01:08:40) many other places. Do the additional coupon pay for the FX risk? That is – it's a $50,000 or $60,000 question to discuss. We had quarters where it didn't work out and other quarters (01:09:06). So, you have to a bit flexible and practical on this question. And we have this PIMCO, I think an experienced bond manager in this one, also PIMCO is not always getting it right and are also a different experience here. All together, we are not big in expanding the FX without hedging (01:09:37).

The asset management question on the performance-based fees, yes, you are right. Allianz Global Investors is testing it in some – couple of funds. I think it is more a more a pilot and assess (01:09:53). PIMCO, I think, is a trust valued (01:09:59) simple saying, we have a strong and long track record on alpha and when you want our funds, you pay for it.

And I think on income funds, maybe the track records are a bit more stable. The active equity managers have – also deal with this question, how they get along with it. The pressure from passive is in this category much bigger. I think if you are a good alpha producer, you should also get your fee for it and whether the performance-based fees are the answer to deal with the passive challenge, I personally do not believe it.

Q - Vinit Malhotra {BIO 16184491 <GO>}

All right, thank you, very clear. Thank you, Dieter. Thank you.

Operator

Our next question comes from Farooq Hanif of Credit Suisse.

Q - Farooq Hanif {BIO 4780978 <GO>}

Oh, hi there. Thank you very much, Dieter. Just on the EBITDA's (01:11:07) margin in the U.S., how much of the improvement has been macro-driven? You spoke about volatility being low. How much is kind of structural mix on the new hybrid VA product? And presumably, if long-term yields go up, that will improve the margin.

Secondly, going back to Italy, in non-Life, could you just clarify kind of what is driving the high reserve releases of the industry you have seen and kind of what is allow you to sort of run out (01:11:41)? And then on pricing, is it that motor is stable and even non-motor is positive or is it that you expect motor actually itself just start doing positive?

And lastly, going back to some of the questions on the attritional loss ratio, could you sort of quantify the level of kind of large losses versus what you'd expect to be a more normal level? Thank you very much.

A - Dieter Wemmer {BIO 4755450 <GO>}

Yeah, so maybe on the U.S.A., when you look at the developments quarter over last year quarter and there is an improvement of about 2%, I would say, a lot of that improvement was driven by the economic scenario. The point is Allianz Life is then keeping the pricing discipline through time. And so, that's where we see that other (01:12:27) narrowing.

They kind of (01:12:31) continue to price aggressively, where Allianz Life is always going to adjust the price. The point is in a new business value, you're going to see or in a new business margin, you'll see more the impact coming from the movement of interest rate, but under is a consideration, which is related to the case, spread (01:12:48) narrowing and widening and that's where this is more an IRR consideration and that's where Allianz Life is very diligent at keeping the pricing and sacrificing on volume. And this translates into the individual (01:13:07) business that you saw.

On the runoff for Italy and where is this coming from, again, I don't like to go too much into the details, of what is generating that runoff. The point is it's been relatively stable over the last years, but as I said before, eventually we're going – tend to see healthy (01:13:27) runoff from Italy, but it's not going to be as significant as (01:13:33).

On the pricing, we think that there is more stability coming in the price in Italy. So, the situation was definitely more challenging a few quarters ago. And now, we see that the situation is getting more manageable. Indeed also, when we see the performance of Allianz Italy compared to our plan, we see that, that performance is better than what we were anticipating. So, that is also a sign of stability.

And on the attritional loss ratio, we do our internal calculation, but the difference – the reason why we are now sharing with you those numbers, regarding the large losses or the weather-related loss is very simple. On the NatCat, that's pretty much of a, if you want, very clear definition. On the other one, it's a little bit of a local definition. So, the number, the quality of the number can be a little bit less compared to the very determination (01:14:37), the standard definition used at the group level for the NatCat.

That's the reason why we don't want to share those numbers, but I can tell you that the gaps (01:14:47) in what we see this quarter and what is a normalized level is significant enough that we can be very confident to tell you this has an impact on the numbers. I hope this is...

Q - Farooq Hanif {BIO 4780978 <GO>}

Thank you very much. Yes, very clear. Thank you very much.

Operator

Our next question comes from William Hawkins of KBW.

Q - William Hawkins {BIO 1822411 <GO>}

Hello, gentlemen. Thanks very much. Giulio, welcome to the frontline, hope you're enjoying yourself.

A - Giulio Terzariol {BIO 17125489 <GO>}

Thanks.

Q - William Hawkins {BIO 1822411 <GO>}

So, I'm following up slightly on some of the other questions. The Life 10% ROE target for the end of next year, can you just remind us briefly how you think you're going to get there? Because I know you said a bit about Italy (01:15:31), but from my count (01:15:34) pretty large operating entities, but is still below where you want it to be. So this isn't just one big market, there's a few big markets that need addressing.

And can you try and give us a bit of a balance between, again, 23 percentage points is quite a lot, how much of that is going to come from earnings? I assume, an aggregate, not very much notwithstanding what you said about Italy and how much (01:15:55) a question on that.

Could we have a big step forward at the end of this year, given that particularly capital management measures are sort of (01:16:02) full-year issues? And then, secondly, much of your programs so far, much of your successful earnings has been focusing very much on getting great margins. We've seen great combined ratios, great new business margins.

As we go into 2018 and 2019, is there any feeling that Allianz wanted to be rebalancing back a bit more towards volume growth and capitalizing on your superior margin performance? And then, lastly, to the extent of those are quite medium-term questions, very short term, there's been a bit of sort of cautious commentary coming out of Allianz about the weather and natural events in the fourth quarter as well, gentlemen, weather, wildfires (01:16:32) in the U.S. and that kind of thing.

How conservative should we be about the events that we've seen month-to-date, in terms of how they're affecting you – sorry, quarter-to-date? Thank you.

A - Giulio Terzariol {BIO 17125489 <GO>}

Okay. Maybe I'll start with the ROE of how we get to the 100%, because on the group level, on the segment level, we are already over the 10%. How we get to 100% or almost 100% of capital with a 10% ROE, if we adjusted third quarter numbers, if we adjust for Italy, we are already 90% and there we know there are couple of other entities like Switzerland, which is not at 10%, but we know they we're going to bring Switzerland up to 10%.

So, we feel very confident that we are going to get very close to 100%. It's not necessarily to be 100%, but it' going to be very close that adjust one carrier (01:17:30). Clearly, if next year we have a lot of volatility in the financial market, maybe in that year, we might miss the 10%, but on a sustainable level, we think that we are on good track and keep in mind that just adjusting for Italy, we are a 90% of capital with a 10% already.

On the new business margin, yes, you already have good points (01:17:56). We are not necessarily thinking to rebalancing from margin to volume, but we feel confident with the profitability and at this point in time, we are not going to push for higher new business margin or higher profitability. We would like to see volume come in the level of profitability that we have right now. But you have touched on the right point that this level of profitability is more about pushing the growth instead of pushing further in (01:18:24) new business margin.

On the fourth quarter or October event, yes, we had a wildfire in California. We had also few storms here in Germany. I can give you a little bit of sense about the wildfire in California. We expect that that number could be above €100 million. And also the cat losses in Germany, they could also grow in the €100 million direction.

So, the October month has been definitely challenging from that point of view and you can take this as information that you can use to do your projection, but that's also the reason why we said that we're going to be at the upper-end of the range and since we saw – this was in August and since we saw a lot of activity in the third quarter and we see also activity in the month of October, now we are saying that we're going to be in the upper half, but not at the upper-end of the range. This is part of our consideration. And so, this is for your reference.

And then, you had another question that I honestly speaking (01:19:39) was your second question, but I didn't get it.

A - Dieter Wemmer {BIO 4755450 <GO>}

I think we're good.

A - Giulio Terzariol {BIO 17125489 <GO>}

Okay. That was good.

Q - William Hawkins {BIO 1822411 <GO>}

Definitely good. Thank you.

A - Giulio Terzariol {BIO 17125489 <GO>}

Okay.

Operator

We will take our next question from Michael Haid from Commerzbank.

Q - Michael Haid {BIO 1971310 <GO>}

Thank you very much. Good afternoon. Two questions. One, again, on the SCR, the minus €0.2 billion (01:20:05) business evolution. My understanding is that all segments play a role here and could you provide kind of a breakdown. First of all, breakdown between P&C and Life and Health, how this minus €0.2 billion (01:20:22) comes as a result?

And then maybe also what is the gross and – the gross of capital changes with respect to traditional and products with currencies and to the capital efficient products? I understand that you don't want to make a forward statement. But just for this minus €0.2 billion (01:20:44)?

Second question with respect to retro, when I look at your losses from the hurricanes, then they are below – what you said, that the maximum loss which you could incur, does that – and I assume that you have mostly excess of loss in retro protection. Does this mean that you have no recovery from retro in the third quarter for the hurricanes?

A - Dieter Wemmer {BIO 4755450 <GO>}

Michael, it's Dieter, let me start with the business evolution. That is old Life, because our P&C growth has resulted more or less in a flat with development. So, that was a big number as a Life number and obviously asset management has no answer, almost nil. And P&C, it's also very flat.

I think so – our retro (01:21:53) number is really very low. We have let around (01:21:58) around €50 million of losses (01:22:05) and that is actually on our Caribbean cover to be in very much in detail.

That means also as a message. We have still full reinsurance cover if there is any further event coming up. So, we did – by no means we'll run out of coverage for the rest of the season (01:22:29). We are not paying any reinstatement premiums and we also don't need to knock at urgently at doors of the insurers and ask for new coverage, which is – step knocking is (01:22:44) at the moment a bit more expensive, but therefore we wait (01:22:50) very relaxed on the renewals. I think the cat covers are usually done April 1. So, let's see where the market is when we discuss April 1 renewals.

Coming back to the minus €0.2 billion (01:20:03) evolution, so, this is all basically Life and Health.

That is what I said, yeah.

Q - Michael Haid {BIO 1971310 <GO>}

It is the net figure?

A - Dieter Wemmer {BIO 4755450 <GO>}

It is a net – you want now to break it down and to risk (01:23:20) capital of the new business versus the lease capital (01:23:26).

Q - Michael Haid {BIO 1971310 <GO>}

Yes.

A - Dieter Wemmer {BIO 4755450 <GO>}

That is a bit more tricky. Yes. The in-force number is a bit bigger. The new business is, of course, in year one not so consuming, because the policies have first to grow with the size of a good investment income. Therefore, it is – yeah, I would say, it is maybe €100 million more of gross versus the net to make it very simple.

Q - Michael Haid {BIO 1971310 <GO>}

Perfect. Thank you very much.

A - Giulio Terzariol {BIO 17125489 <GO>}

Okay. We're almost through with our time. So, we have time to take one last question if there's any, please.

Operator

It seems there are no further questions. So, I'd like to turn over back to our hosts.

A - Giulio Terzariol {BIO 17125489 <GO>}

Thanks, Paul. Thanks, everybody, for joining the call. Thanks for your questions and we wish you nice and pleasant weekend.

A - Dieter Wemmer {BIO 4755450 <GO>}

And also for me, goodbye, and I will hope to see some of you in London or at other opportunities. Otherwise, I really want to thank you for 20 quarters of very interesting discussions at our quarterly result. And also, we are very grateful that you are all following our company and dialing in every quarter following our announcement. So, thank you and goodbye.

Operator

This concludes today's call. Thank you for your participation. You may now disconnect.