Q1 2021 Earnings Call

Company Participants

- Giulio Terzariol, Member of the Board of Management, Finance, Controlling, Risk, Chief Financial Officer
- Oliver Schmidt, Head of Investor Relations

Other Participants

- Ashik Musaddi, Analyst
- Dominic O'Mahony, Analyst
- Farooq Hanif, Analyst
- James Shuck, Analyst
- Michael Haid, Analyst
- Michael Huttner, Analyst
- Peter Eliot, Analyst
- Vinit Malhotra, Analyst
- William Hawkins, Analyst

Presentation

Operator

Ladies and gentlemen, welcome to the Allianz Conference Call on the Financial Results of the First Quarter 2021. For your information, this conference call is being streamed live on allianz.com and YouTube. A recording will be made available shortly after the call.

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

Oliver Schmidt {BIO 2473131 <GO>}

Thank you, Madison. Yeah. Good afternoon from my side as well and welcome to our conference call. There is nothing specific to be added from my side today, so I hand over directly to Giulio.

Giulio Terzariol {BIO 17125489 <GO>}

Hi. Good morning, good afternoon to everybody. And I am going to go as quickly as possible through the presentation. Then I'm happy to take your questions.

As usual, if we go to page three of the presentation, you can see that we had a very good start into 2021. When we look at the revenue, the revenue are flat. This is mostly explained by Property-Casualty and Life/Health. In Asset Management, we see a nice development. On the operating profit, we have an operating profit of EUR3.3 billion, which is clearly above the prior period, but that was fairly easy. The point is that EUR3.3 billion is also above the run rate of our outlook of EUR12 billion for the full year. And also what is a good part of the story, all segments have contributed to these results. When we look at the combined ratio in P&C, we are at our target level of 93%. When we look at the new business margin in Life, we are basically also at our target level of about 3%. And then the cost-income ratio in property -- in Asset Management is below 60% and you see also that we had very nice inflows that we are going to see in a second. This is not just PIMCO, it's also AGI. The net income is EUR2.6 billion. Clearly, the net income is benefiting from the strong operating performance, but also there was basically no impairment in the course of the first quarter. So, overall, a good start into the year, which is also clearly encouraging as we think about the remainder of 2021.

And with that, I will go to page five. The solvency ratio has improved by 3 percentage points. If you adjust for the core or the RT1, in reality, the improvement on a pro forma basis is more like 7 percentage point. And the sensitivity as you might see on the right hand side are -- basically the sensitivity downwards are basically very close to what we had at the beginning of the year. So, strong capitalization sensitivities, which are broadly unchanged.

When we go to page seven, you can see the driver, the development of the Solvency II ratio. And I would say what is definitely positive is the development of the organic generation, it's plus 9%. This number is before dividend, before taxes. If you adjust for dividend and taxes, you have -- we have an improvement of 4 percentage point. The market has been also favorable, especially the interest rates went up. So, this leads to an improvement pretax of 8 percentage point. And then on the capital management/management action, we have especially the impact coming from the accrual or the dividend and also we had impact coming from having called the RT1. So, again, 210% is a good level of solvency ratio. And I would say also the fact that one driver of the improvement was the strong organic capital generation, it's definitely positive.

And now we go to page nine, that's about our Property-Casualty segment, and that's about the growth rates. Overall, the growth rate adjusted for consolidation and FX was minus 1.6%. If we also remove for second Allianz partners from the equation reality, the growth rate is minus 0.5%. So, very, very close to the flat growth rate. Clearly, this is not a growth rate that we would like to see, but here we are. Definitely, the impact coming from also the COVID situation. And on top of that, we are taking also measure to -- in our commercial lines business in order to increase the profitability. And we are very confident that as we go out of the COVID situation, we're going to see again our normal growth rates in Property-Casualty. The rate momentum is overall stable. There is an just an exception, which is Italy, but that's also the country where we had a very strong situation from a profitability point of view. So, we have definitely a good starting point there. And then just one comment on AGCS, the rate increases are still very, very strong. So, when we say stable, we mean that we see stable rate increases. They might be slightly below what we saw last year, but we are still speaking of double-digit rate increases in the industrial business.

So, if we now move to page 11. The operating profit is clearly much better compared to the one of last year. So, overall, we have an improvement of EUR500 million. The driver improvement is the combined ratio. And I would say that accident year loss ratio has improved by about 6 percentage point. Thereof, 2.5 percentage point of improvement is coming from COVID, 2 percentage point plus is coming from the better development of the natural catastrophe and a good 1 percentage point of improvement is coming from underlying performance. The main driver of this improvement is indeed the development at AGCS. When we look at the expense ratio, it's also improved. So, the -- so, again, a quarter where we are showing an improvement compared to the expense ratio in the prior period. And then the run-off results, it's lower compared to the last year. Here, I can tell you that we are just taking conservative stance. I think our results, as you see, how good they are, are at the level, the target we gave ourselves and we can also, say, take a conservative stand on our results. So, the quality of 93% combined ratio is, in my opinion, very, very good.

Moving now to page 13, we have the exhibit by OEs. And you can see a lot of our subsidiaries have good combined ratio. So, Germany with 91% or United Kingdom is even below 90%, the same applies to Eastern Europe, Italy, Spain. In Australia, we have a combined ratio, which is higher than our expectation and that's because of the natural catastrophe in Australia, especially I think in the month of January. Otherwise, you can see that AGCS has a combined ratio of 98%. This is in line with the expectation that we set at the beginning of the year. And here, I can also tell you there is a COVID impact negative of about 3 percentage points. So, in reality if you adjust for that, one could say that the underlying performance is already better than the 98% that you see on this page. And then Euler Hermes with a combined ratio below 80%, it's clear -- is a clear indication that at the moment there is no pressure on claims and we have been also fairly conservative in the choice of the loss peak.

And with that, let's move to page 15. The investment result is -- for P&C is up 3%. And here what we see is that we got indeed a lot of support coming from the equity. We got dividends. There was not a drop in dividend like we might have seen a little bit in the prior year. And also, we got some additional profit from our equity participation on the other side, and this was expected. We see that the current yield is going down, but this was already considered if you want in our thinking about the outlook. In reality, I would say that what we see right now is that we are running a little bit better compared to what we had anticipated in our outlook of EUR5.6 billion for the operating profit of Property-Casualty. So, this might be an area, where we're going to have a little bit of an uplift compared to what we told you a few months ago.

Now we can move to page 17 on the Life side. Overall, you see that the production is up about 8%. So, overall, remember that we're always concerned about what could happen to production as we do all the product changes. And I would say that the production is already pretty nicely. We see also very nice development in Italy. We see a nice development in Asia. And USA, if you adjust for the FX, we see a growth rate of 8%. On the same time, the new business margin is going up by -- to be very specific by 10 basis point, although it looks like 20. And the improvement is coming from professionals. And that's because of actions we have taken, especially in France to improve the profitability of that business. But in my opinion what is very telling is the fact that in the capital-efficient products, although the environment is very different compared to what we had last year, the drop in new business margin is only 20 basis points and the actions we are taking, they are going clearly to have an effect in the course of the year. Indeed, also, as you know, we are calculating this new business margin based on the beginning of the period interest rate with exception for the US, but for the rest of the business we do that. So, as of now, even doing that, we are already above the 3% level. So, overall, good level of production, also new business margin which are going up and holding very nicely.

And with that, page 19, we speak about the in-force portfolio performance. Overall, nice increase compared to the prior year period. That was also easy, if you want, because in 2020 we had a lot of negative impact due to the volatility, but we have also to recognize that EUR1.2 billion is above the EUR1.1 billion of run rate operating profit and also it is nice to see all segments, if you want, all lines of business are contributing to this improvement. Clearly, the development in the USA has played a major role in getting to this kind of result increase. But I tell you we see also a nice development in Asia and also Italy, and the unit-linked business is also doing pretty, pretty nicely.

So, with that, page 21. We show the new business margin and operating profit by entity. Overall, I would say the new business margin is holding pretty nicely, and I will say in the USA you can see that we had a substantial increase compared to last year. In Asia Pacific, we see the new business margin of 6%. And also I would highlight in Central and Eastern Europe, although the margin is a little bit down, it's still at a good level of 4%. So, the only area where we need to put some additional work is France, but also there you see at least that we were able to improve compared to last year. And the operating profit, again, you see a nice recovery compared to last year. And I think now we are -- we have a sort of competition between Germany Life and USA. For the quarter, we have the exact same number of operating profit, so we're going to see who is going to do better in Q2. And clearly since I was in the USA, I'm always a little bit a fan of Allianz Life.

And with that, let's move to page 23 on the investment margin. We have an investment margin of the more than EUR1 billion. And when you look at the investment margin in relation to the policy reserve, it's about 21 basis points, which is higher compared to our expectation. If you annualize that of 70 to 75 basis points, I would say the following. Clearly, in this quarter, we didn't see any impairment. Basically, there were really no impairments, so this has supported also the net harvesting. And this leads also to this level of investment margin. As we've seen throughout the year, clearly we don't expect to have this 20 basis point recurring, unless the situation remains like that. But I think most likely, we're going to end up anyway at least at the upper end of the range of the 70 to 75 basis point that we provided you at the end of this year. So, overall, a good result. I would like also to highlight anyway that our Life profit are not just a function of the investment margin and, indeed, we get about 66% of our revenue, two-third of our revenue from loadings and technical margin. So, that's also something which is important to keep in mind.

And with that, page 25. On the Asset Management segment, I can say results are really good. We have achieved a level of EUR2.4 trillion of assets under management. That's the highest record -- highest level for Allianz. And also what you see both AGI and PIMCO contributing to this development. And when you look at the asset classes, you can see growth in all asset classes. When you look at the regions, you can see growth in all regions. I'd like also to highlight that in Asia Pacific, we have more than EUR200 billion of assets under management, so it's not just Europe and America where clearly we are very large, but we have also sizable now presence in Asia Pacific.

So, if you go to page 27 on the development of the third-party assets under management, you can see that the flows in the quarter had been strong with about EUR40 billion of flows. Thereof, EUR12 billion coming from AGI, that's the highest level for AGI. And if you remember, we saw also a nice trajectory at the end of 2020. In the case of PIMCO, we have been used to see this EUR20 billion plus now for a few quarters. And when you look then at the composition of these flows by asset classes and regions, you can see that overall there was a pickup in flows across the board. Then, as usual, we had the impact coming from market development from FX. And when you combine the two, you see that at least for the quarter the impact coming from these economic drivers was positive. So, we are starting with an asset base of about EUR1.8 billion of assets under management, so that's a good starting point as we think about also the second quarter and the remainder of the year.

Page 29, the revenue are up about 9% and we see a very nice growth in the revenue at AGI. If you adjust for FX effects, it's about 15%. PIMCO is a little bit lower, 6%, but PIMCO, we had also a special effect which is having impact also on the fee margin. We launched a closing fund in the first quarter. And when you launch these kind of closing funds, you have underwriting fees and you cannot defer the underwriting fees. So, if we adjust for that effect, fee margin will be a couple of basis point higher. And also I think the impact of that underwriting fees on our revenue compared to the prior period was about 5 percentage points. So, once you start adjusting the numbers of PIMCO for this effect, you get to a different picture. And clearly, that's a good thing, the launch of this closed-end fund because we're going to get revenue and profit moving forward.

At page 31, the operating profit of the Asset Management segment is up double-digit, 10%. If you adjust for the FX effect, it's up 16%. PIMCO is flat, but that's a consequence of the FX impacts. And in the case of AGI, we have a very nice development of the operating profit with about EUR200 million of results. And clearly here you see the impact of growing revenue on a double-digit level and the expenses are down about 7%. You remember, we did a restructuring last year, so now we see the benefit of this restructuring. And the cost/income ratio is 61%, it's the lowest cost/income ratio we have seen at AGI.

Corporate, page 33, is improved compared to last year. Here, we have always some volatility. We had some FX effect changes, so they were slightly negative last year, they are slightly positive this year. We have an improvement in the operating profit of our Allianz technology and also there is some seasonality in the expense line item. You might also remember that last year, we had here the impacts of the solidarity charge for COVID in

France. Overall, I would say, we are a little bit better than our expectation, but there is also some just seasonality in the numbers.

And at page 35, net income is significantly up compared to last year, EUR2.6 billion. Clearly, we are benefiting from the strong operating performance. And then as you see, the impairments are basically very close to zero, so there were no impairment during the course of Q1. And the tax rate is 23%, it's a little bit higher than last year, but somehow lower than our normal tax rate. That's because of the one-off positive impact. But all-in-all, I would say strong operating performance combined with the benign capital markets have contributed to these very strong results in our net income.

So, in conclusion, page 37, I would say very strong quarter. It's not just about the EUR3.3 billion of operating profit or the EUR2.6 billion net income, it's also about the underlying 93% combined ratio in Property-Casualty, with quality, a decrease or the expense ratio in Asset Management. Life, you see that our new business margin, as we speak, is already 3% and we're getting premium. And you can also see the operating profit is very, very stable. And in Asset Management, we have a record level of asset management flows. We have also, I will say, very strong cost/income ratio at AGI. We are starting with an asset base, which is a very good starting point as we think about the remainder of the year. So, there is a lot of strength in the underlying of the business and that's across the segments. On top of that is Solvency ratio II, 210%, it's very far away from 180%. So, we feel pretty good about the start of the year and also about how we are positioned to go into the remainder of the year.

And with that, I would like to take your questions.

Questions And Answers

Operator

Okay. (Operator Instructions) We'll go ahead and take our first question from Peter Eliot with Kepler Cheuvreux. Peter, please go ahead.

Q - Peter Eliot {BIO 7556214 <GO>}

Thank you very much. Good afternoon all and great results. I have three questions, please. Firstly on that cost/income ratio of AGI that you just mentioned, Giulio. Could you say how sustainable that is? And obviously a very good figure, I'm just wondering if -- I mean, probably too good to hope for that that can continue, but I'd be grateful for your comments. Secondly on PIMCO, it looks to me like you've been making a higher margin on internal assets for the last couple of quarters, just backing out the third-party funds. Just is that right, is there anything that sort of happened on the pricing structure or -- yeah, are you able to comment there? And thirdly on Euler Hermes. I mean, I guess, given that half the business presumably is still at sort of 100% combined ratio, the other half is really very, very low indeed. And I'm just wondering about your thoughts for the outlook there. I mean, should we expect the same pattern in Q2? What about as the economies sort of open up? And -- yeah -- I mean, I guess, when you think about the sort of state scheme now, I mean, with hindsight, obviously, that was a bad deal for you because you've given away a lot of profit. I'm just wondering, what the sort of outlook or discussions are on that? Anything you can add would be very helpful. Thank you very much.

A - Giulio Terzariol {BIO 17125489 <GO>}

Okay. Yeah. Thank you, Peter. So, starting from AGI cost/income ratio. I would now assume that we're going to be at 61% cost/income ratio as a new normal. But definitely, if you remember, the idea was we want to be at 67% cost/income ratio. And I think this target is very easily achievable. As we go through the remainder of the year and also as we think about the future, we need to consider also how much we want to invest in the business. So, I think we're starting from a very good point. And so, now, I will say that we are definitely in control of our cost/income ratio, so that's a good place to be. So, I would expect that clearly we're going to set us a goal, which is better than the 67% cost/income ratio and the conversation is going to be more about how much we want to invest in the business. But I think the progress at AGI has been really phenomenal. And I would say the statutory spaces initiative that we did last year are clearly paying off. You can see this in this number. There is -- that's important also. In this number 61%, there is no one-off, nothing. So, it's a pure number. So, from that point of view, one could also argue, okay, that's the starting point. But, again, I think we always need to consider about how much we want also to invest in the business, but again very good situation to have.

On the question about PIMCO and the internal assets, no, we didn't change anything. So, from that point of view, I don't know, so how you derive your numbers, but there is nothing really going on from the point of view of the profitability that PIMCO is getting out of the management of the Allianz France. The only case might be is ARE, Allianz Real Estate. Because as you know last year, we put Allianz Real Estate into PIMCO. So, you might see an increase clearly of fees due to that and also some increase in profit. But fundamentally, there is no change, otherwise, in the charges that PIMCO is taking on the managing -- on the management of the fixed income portfolio.

Then Euler Hermes, on your question about the expectation for the combined ratio. And I would say that the -- in reality, the combined ratio, the underlying combined ratio is even better compared to the one that we have showed in the slides because we are not seeing necessarily claims activity at this point in time. I believe we are going to be in this situation definitely also as we go into the remainder of 2021. And I would expect even to see stability in 2022. And then maybe by 2023, 2024, we might see a little bit of a different dynamic regarding solvency. The point regard with Euler Hermes is we are not like a bank, right, we're not extending credit for 20 years, so we can always adjust our exposure basically on a daily basis. So, definitely, the situation looks very good, very strong. With hindsight, I would be a billionaire. So, from that point of view, I would say at that time, the decision in my opinion was the right decision. We definitely gave some profit away, but think about how people were feeling one year ago, right. So, there is no regret or no complaints here. And we are -- actually if you ask me, we are happy anyway that we are having this kind of conversation now instead of being happy that maybe we are ceding some losses to the state, I think we are in a better situation this way.

Q - Peter Eliot {BIO 7556214 <GO>}

Yeah. Absolutely. Couldn't agree more. Many thanks.

A - Giulio Terzariol {BIO 17125489 <GO>}

Welcome.

Operator

(Operator Instructions) We'll go ahead and take our next question from Michael Huttner with Berenberg. Please go ahead.

Q - Michael Huttner {BIO 21454754 <GO>}

Hi. Fantastic. Thank you so much. Yeah. I think I'd just repeat as you said these amazing numbers. I think a three-point question. One, which is what's the previous -- your kind of competitor who just reported kind of said, the -- I think they've made it -- they didn't say quite like that. But that -- I think they said, they kind of implied they've never seen it so good. So, in other words, taxes fees for them was paid fully by rate rises. Is that the feeling you have for the business as a whole? And here, my specific question, because this sounds very, very vague, is why didn't you see -- if you're so confident, why didn't you change guidance? EUR11 billion to EUR13 billion is so big, it's like -- and then the second question also on guidance. So, you have raised it in operating profit from a range of EUR7 million to EUR8 million to now, I think, EUR10 million or maybe even over EUR10 million, I don't know. And I just wondered, what the moving parts are to this? And then my final question would be a really simple one. Your competitors are looking at back book deals. Is that something you were thinking about as well in Life? Thank you.

A - Giulio Terzariol {BIO 17125489 <GO>}

Yeah. I think I got two out of the three question, maybe first I answer the two and then ask you -- maybe I tell you what and then --

Q - Michael Huttner {BIO 21454754 <GO>}

(Multiple Speakers)

A - Giulio Terzariol {BIO 17125489 <GO>}

-- and then we -- okay. So, on the first one about changing the guidance, it's almost philosophical that we're not going to change the guidance in Q1, it's after three months. But clearly when you look at the underlying performance, we are doing fine. And to a certain degree, clearly we expect also this underlying performance to stay. So, I wouldn't take the EUR3.3 billion times 4, but I could also tell you that, yeah, most likely the EUR3 billion per quarter, we are going to be able to exceed that. But in the first quarter, we are not going to change guidance. It's -- I would say, it's really a matter of principle, almost philosophical. In the second quarter, we see where we are and that's the time when clearly we might consider to change guidance. So, there is no -- let's say nothing to read behind the fact that we are keeping this EUR12 billion plus/minus EUR1 billion, it's just a philosophical position if you ask me.

On the back book, because I didn't get necessarily the second question, yes, we also look at back book.

Q - Michael Huttner {BIO 21454754 <GO>}

(Multiple Speakers)

A - Giulio Terzariol {BIO 17125489 <GO>}

Yeah. The back book is -- okay. The back book, yeah, you also just said there was very -- it's very small transaction, but basically we closed the back book transaction in Benelux. We are looking at other back books in Europe. We might consider also back books in the United States, where it's a little bit even easier to get things done pretty quickly. So, we are definitely also looking into this kind of a tool in order to make sure that the capital allocation can be optimal capital allocation from a return to the shareholders. So, we are definitely working on this dimension too. It can take time. As I said, it's -- you need a lot of education, sometimes you need to educate regulator -- regulators because they are not used to it. And sometimes policyholder consideration that you need to be aware of, there can be tax consideration that you need to be aware of. That's the reason why it can take time. We concluded a transaction about our Spanish back book that was about EUR1 billion last year, it took us basically over two years to get from basically where we had the clear plan of what we wanted to do to get the final approval. So, two years from once we are ready to move to getting the final approval. But I believe that you're going to see some activities in the next quarters from our side.

Q - Michael Huttner {BIO 21454754 <GO>}

And may I ask this is on buybacks?

A - Giulio Terzariol {BIO 17125489 <GO>}

Sorry?

Q - Michael Huttner {BIO 21454754 <GO>}

On buybacks?

A - Giulio Terzariol {BIO 17125489 <GO>}

(Multiple Speakers) Buybacks, at the moment is still where -- here at least in Germany, we are a little bit behind with our corona situation. So, we still have some lockdowns. I believe that after the summer break, the situation is going to be back to normal also here. At that time, I believe that also from a regulatory point of view the sentiment is going to be different. And as we clearly go into the second part of the year, we are going to potentially consider buyback. I would say on the buyback, I would say -- and that's more a general statement is our -- definitely our intention over time to -- and that's what we did in the past, to have a very disciplined approach where we do buyback and also we can take the opportunity to do M&A. So, we are -- that's the philosophy that we are going to use, and that's the way we want to run the company moving forward. Now, clearly, you cannot do this on a quarterly basis, on a yearly basis, half and half, right. So, there can be situation where you might see more M&A coming through and then you might owe buyback and the other way around. But on a rolling basis, I can tell you that the philosophy that we are going to have is to have this healthy combination between M&A activity and buybacks.

Q - Michael Huttner {BIO 21454754 <GO>}

Brilliant. Thank you so much.

A - Giulio Terzariol {BIO 17125489 <GO>}

Welcome.

Operator

All right. We'll go ahead and take our next question from James Shuck with Citi. Please go ahead, James.

Q - James Shuck {BIO 3680082 <GO>}

Thank you. Good afternoon, good morning, everybody. So, two questions from me. So, on the premium growth in P&C, Giulio, so down 1.6% in Q1. The annual report recently you published, it was published in March and you have 2021 targets in those numbers and those targets will go up with -- we're talking about COVID and the impacts of COVID, but expecting P&C premium to rebound pretty strongly, 5% to 6% is the number that we've targeted for 2021. What happened in the phase of two to three months with -- we're missing by that amount? That's my first question.

Secondly on P&C operating profit, you've got the guidance for EUR5.6 billion plus or minus 10% in 2021. But the three-year plan is actually calling for a number actually growing at a 5% CAGR. So, we're looking at more like over EUR6.3 billion from that three-year plan. I appreciate interest rates are lower, so there's some real pressure and clearly the volumes are actually low as well. But can you just help me understand the delta versus that EUR6.3 billion, even if we are coming in at the top end as you said earlier? Thank you.

A - Giulio Terzariol {BIO 17125489 <GO>}

We cannot understand you properly, the line is very broken. So, we got the first question, but the second one, I couldn't get you. The line is very --

Q - James Shuck {BIO 3680082 <GO>}

(Multiple Speakers) I'll just touch on that quickly. Sure. So, the 2021 profit target that you have for P&C is EUR5.6 billion plus or minus 10%, but in the three-year plan that was given in 2018 that called for 5% CAGR getting to at least EUR6.3 billion in 2021. Appreciate that EUR5.6 billion you're now saying it can be top end of that, so maybe closer to EUR6 billion, but I'm just keen to understand what the difference is between the three-year plan and where you're guiding to at the moment. I presume it's sort of volume growth and some of the investment in your pressure, but if you could just help me understand some of those moving pieces. Thank you.

A - Giulio Terzariol {BIO 17125489 <GO>}

Yeah. Perfect. So, coming on the -- the first question was about the premium and premium growth. Okay. I know in the annual report, there was the statement about growth in P&C. This came a little bit from our economic reserves. We've been always very clear in our conversation that our expectation, especially for the beginning of 2021, was to have a flat revenue growth, what we saw. So, I think the statement was a little bit more forward-looking, but our expectation have always been that in reality in 2021 the growth is going to be muted. And that's also the way we have been talking in our meetings.

With regards to the Property-Casualty operating profit, yes, the point is clearly the investment income is different compared to what we might have assumed at that time. If you look at the combined ratio, it's 93%, it's the same. So, from that point of view, the 93% has not changed. Then there is clearly the fact that rates went down compared to what we had in 2018. Also, consider that I said before, we might have been conservative in the estimates of our investment income for 2021. So, we might see an uplift compared to the EUR5.6 billion that we gave you. And then also the revenue growth in general is a little bit lower. I think also that just because of partners and Euler Hermes, we are basically losing EUR200 million, EUR250 million of operating profit. So, if you start just adjusting for that, which is probably -- which is going to come back once we get to the normal revenue basis, if you also adjust for the investment income, then you see that in reality the numbers are the one we said. And think about the fact that the combined ratio of 93% is what we are planning to hit and we feel very comfortable about that. The expense ratio is better compared to what we said at the time, so it's driven partially by Euler Hermes and partners. And partially, it's also -- clearly, there is a little bit less investment income compared to the assumption of 2018.

Q - James Shuck {BIO 3680082 <GO>}

Thank you, Giulio. The second part is clear, but the premium growth one, I just -- the annual report, which was published only a couple of months ago is talking about 5% or 6% revenue growth in P&C premium. And now, we're kind of looking at minus 1.6% on a gross written basis. So, just my question is more about what's happened to that expected growth --?

A - Giulio Terzariol {BIO 17125489 <GO>}

Nothing happened to that. I think the 5% to 6% of premium indicated there was sort of think on a normalized basis as we go. I think it was about what a total market can do, but that's not the number that we have really considered in our thinking. That's also not the number that we've been using in the conversation that we had. We always have highlighted that we expect premium P&C to be flat, so I will not take that as the number that we have been discussing in our conversation.

Q - James Shuck {BIO 3680082 <GO>}

Okay. Thank you very much.

A - Giulio Terzariol {BIO 17125489 <GO>}

Welcome.

Operator

All right. We'll go ahead and take our next question from Vinit Malhotra with Mediobanca. Vinit, please go ahead.

Q - Vinit Malhotra {BIO 16184491 <GO>}

Yes. Good afternoon. Thank you very much. Just if I can ask one more on AGCS. I mean -- so, obviously, some very good numbers in this quarter already. I mean, I was I think surprised because I was thinking 98% would be somewhere towards later part of the year, but you already got 98%. Is there some hope that AGCS can even do more? And because the pricing, 22%, is rated somewhere will obviously come in, will be earned through the year. And I just wanted to understand how you think about AGCS. If I can ask about PIMCO. So, obviously, very strong net growth, but the perception in the market, how should we -- or how do you propose to that change and challenge that perception that, hey, when the US treasury yield goes up, there will be a deluge of outflows of -- at PIMCO? I mean, that's why -- is there some more data you can provide to the market to say, hey, this is the kind of revenue per strategy or -- obviously, there is evidence of inflows coming in, but I was just wondering if you could comment on that? And lastly, if I may ask, there has been some -- if I could just ask for an update on the M&A strategy, please, given there's been an asset in the US where there's a lot of chat about yourself as well. Could you just comment -- what kind of -- I mean, is there a change or should we just continue to believe that the old bolt-on approach was what Allianz was most comfortable in? Thank you.

A - Giulio Terzariol {BIO 17125489 <GO>}

Okay. Thank you, Vinit. On AGCS, I will say that, yes, we should over time see an improvement. As I was also saying before, the 98% includes 3 percentage point of COVID impact. And also if you look at the natural catastrophe, they were not excessively high for AGCS, but they were also not low. So, I would say, there was no benefit, let's put this way for natural catastrophe that in the sense that we had a low loss from that. So, I would say the 98% is a number that if you look at the underlying, it's even better. We see rate increases. So, from that point of view, yes, the expectations that we're going to see over time better performance at AGCS. Indeed, I was also discussing the situation with them the other day. And we are at a point where we also believe that on a selective basis, clearly, with a lot of discipline, we can also start thinking about growth again. We wanted to be very sure that the underlying performance is strong. We did the analytics clearly at the beginning of the year as we had all the information collected by year-end and we got good response that we are on a good track. So, from that point of view, I will say that the 98% is not the end of the story, but that should be the beginning of a different chapter for AGCS. And the market is also helping, let's be serious. There is a lot of good stuff that we did and the market is definitely also supporting this direction.

On PIMCO and the net flows, on the yield and treasury rates going up, I would always say that, yes, clearly, if you have rates going up, first, you might see investors going on the sideline because, clearly, they are not going to invest in a fixed income if there is expectation that rates are going up. I would also differentiate there are a lot of investors that are just investing in fixed income, no matter what, but you might have the, call it, smart money might clearly wait, but then you get the flows six months later because then their money eventually is going to flow. So, I would always separate what can be the volatility that you might see in a quarter, two quarters. So, three quarters compared to what you have to expect on long-term. And I would even say that higher rates would not be a negative for PIMCO, I will say they will be on a present value basis, rather a positive. So, from that point of view, I would say that it's something that can be manageable.

Also, I will say, think about how diversified we are. So, at the end of the day, when you look at the diversification that we have, also by strategy, I think there is a lot of resilience. And I'm also sure that PIMCO will be capable to come up with some strategy also to manage maybe the situation in the short-term. So, yes, there will be definitely an impact. If rates go up, it might be more significant or less significant, but I will not be concerned about the fact that the franchise of PIMCO is going to be very strong. In reality, we're going to benefit out of that. So, I'm not concerned about rates going up. I might have maybe to explain to you this quarter flows were negative. And then two quarter later, I'm going to explain to you why the net flows were so great and everything is going to be fine.

On the question whether we can give you a revenue or margin by strategy, the answer is no. We cannot do that, but you can imagine. Right? If it's a commodity fixed income, it's going to be lower fees. If it's some alternative asset, it's going to be higher fees, i.e., I think that if you do some normal market research, you're going to find out that what could be the revenue strength by asset classes. I can tell you that due to the quality of our franchise, usually, we can get fees which are at least at the market level, let's put this way. But I cannot give you numbers, internal numbers by revenue, but there is no major secret.

And then on M&A strategy, no, there is no change compared to what we had done so far. And also, if you look basically at the latest transaction, they are no different. They might be a little bit larger in size because clearly the Aviva Poland transaction was larger. But from a philosophy point of view, it's clearly trying to strengthen our franchise in countries where we tend to have a presence where we can create some synergies. So, there is no change to the M&A strategy. And as I was saying before, there is also no change to this idea that we want to combine buyback and M&A. As I was saying before, we can now do this on a quarterly or yearly basis. But on a rolling basis, definitely, you're going to see this balance coming through.

Q - Vinit Malhotra {BIO 16184491 <GO>}

And just if I can follow-up please. On COVID, there seems to be, I'd say, very low impact in 1Q. If -- I mean, do you have an outlook update for 2021 and if it is going to affect your '21 target?

A - Giulio Terzariol {BIO 17125489 <GO>}

So, on COVID, I can tell you the impact in Q1 was indeed neutral. So, we had some -- we still had some business interruption losses also as I was saying before, there was an impact of about 3 percentage point at AGCS. But on the other side, we have the frequency motor, which is lower. So, as I look to the remainder of the year, I will say that I would not expect an impact from -- a negative impact from COVID. We might see in some legislation still some development on business interruption. On the other side, we also know that the frequency in motor is going eventually to normalize, but as of how, it's still lower than normal. So, I would say that COVID situation is not going to have an impact on our numbers. I would also expect that as travel is coming back that we're going to see a lift in revenue and profitability at Allianz Partners. And also we are going out of the state scheme in July here in Germany, so you -- we should also see some more profit coming from credit insurance. So, overall, I will say that COVID should be neutral and, in reality, I think we might still take the opportunity to even add to the quality of our balance sheet as we are doing right now.

Q - Vinit Malhotra {BIO 16184491 <GO>}

Thank you.

A - Giulio Terzariol {BIO 17125489 <GO>}

Welcome.

Operator

All right. We'll go ahead and take our next question from Farooq Hanif with Credit Suisse. Please go ahead.

Q - Farooq Hanif {BIO 4780978 <GO>}

Hi everybody. Good afternoon. On reserve releases, when do you think the conservatism and visibility on some of the IBNR clears up and then you move back to the more normal range? That's question one. Question two, you painted obviously a very bullish picture for AGCS, but on the reverse side there, did you think there's potential risk of liability claims inflation coming back as the economy opens? And then lastly on illiquids, are you still at close to the sort of 21% level or do you think now, particularly as we go into new IFRS, do you think now there's an opportunity to even further increase exposure to illiquids? Thank you.

A - Giulio Terzariol {BIO 17125489 <GO>}

Okay. So, the first question on the run-off, I would say that we might change approach as we go into 2022. And for this year, I think we are going more or less to follow this approach. So, next year, 2022, '23, '24. You are raising by the way a question of inflation. We're not concerned, honestly speaking, about a big spike in inflation or we might see some inflation happening here and there. General inflation is not necessarily the claims inflation, but this is something anyway that we -- at least we need to consider. So, having a stronger reserve base is might be anyway also a solution in the case -- or an offset in the case indeed, inflation is backing up and is impacting the claims inflation. So, for the time being, we are doing analysis definitely, but we are not seeing, I'll tell you, right now that there is an increase in claims inflation or at least, let me say, we don't see this across the board. You might see in some specific country, but we don't see a trend now generalized about an increase in claims inflation.

And now on the illiquids investment and IFRS 17, I don't think necessarily that IFRS 17 is going to have an impact on the amount of illiquid that we are holding because, at least on the debt side, okay, we need to consider what the classification might be. So, if we end up having a classification of some illiquid that we need to use fair value, we might reconsider the exposure to those illiquids. But I would assume that there are plenty of opportunities to find illiquid, which are going to be treated from an accounting point of view the same way that we are accounting now. So, I think that, in general, on the portfolio, you might see some movement, but it's not going to change our approach and our appetite for illiquid assets.

Q - Farooq Hanif {BIO 4780978 <GO>}

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

A - Giulio Terzariol {BIO 17125489 <GO>}

Welcome.

Operator

All right. We will go ahead and take our next question from Ashik Musaddi with JP Morgan. Please go ahead.

Q - Ashik Musaddi {BIO 15847584 <GO>}

Yeah. Thank you and good afternoon, Giulio. Just one question I have with respect to, again, going back to Farooq's question on runoff. I mean, runoff in this quarter was quite low, I think 1 point something versus, say, 2%, 2.5% normal run rate. And at the same time, obviously, CAT was a bit lower as well. But even if I normalize both of them to your historical levels, it looks like you could be hitting 98% -- or 92.5% of combined ratio. That's what I'm kind of getting a bit more cleaner number, which is better than your 93% ratio. Now, typically, I don't want to go into decimal places, but because 0.5% or 1% is still relevant combined ratio, I just want to get a bit more color. Is this the right way of thinking about it? Because you also mentioned that travel is coming back, the state scheme will give you higher profits, which will offset any motor. So, there is no negative drag from there. So, any thoughts on that would be helpful.

A - Giulio Terzariol {BIO 17125489 <GO>}

So, I would say that, okay, the only thing I can tell you, the quality of the 93% combined ratio is good. So, clearly, then, if I say this statement, one can also derive the conclusion that the 93% can be lower than that. I would really not go into this kind of consideration on a quarterly basis. The only thing I can tell you, the quality is good. And also as we are thinking about the future, we might think about definitely bringing this combined ratio, 93%, as an indication below that level. And it might be that we are already positioned well to do that, but I will not really over-analyze a quarter. So, the only message I can give to you is that we have our 93% combined ratio, we feel good about the quality of the 93% combined ratio.

Q - Ashik Musaddi {BIO 15847584 <GO>}

Okay. That's very clear. Thank you.

A - Giulio Terzariol {BIO 17125489 <GO>}

Welcome.

Operator

We'll go ahead and take our next question from Michael Haid with Commerzbank. Please go ahead, Michael.

Q - Michael Haid {BIO 1971310 <GO>}

Thank you very much, and good afternoon to everyone. Two questions. First on life insurance. The new business margin you mentioned in France is clearly insufficient and you said that you need to do additional work there. Can you elaborate a little bit on what you want to do in France? Second question on Allianz Direct. The gross premium development in the first quarter was fairly low in my view, looks a bit disappointing. I would have expected in times of corona that Allianz Direct would grow more. Instead, you shrunk. Is that -- is Allianz Direct below your expectations? Internal growth there was minus 11%. What is going wrong at Allianz Direct?

A - Giulio Terzariol {BIO 17125489 <GO>}

Okay. Well, thank you for your question, Michael. So, starting from France. The point in France, the new business margin, we are taking actions and indeed no product that we launched has a new business margin. You need to do some economic calculation. We're not going to go into the details, but let's say the new business margin of the product is more about 1.5% to 2%. So, over time, you're going to see that flowing -- flow, but we need to clearly build up that business more over time. We need to get to a better performance in our protection business and then potentially we need to try and see how we can push more pure unit-linked business.

So, I wouldn't say that we are not taking action. So, we have been taking action. You see there is already at least an improvement compared to the Q1 of last year. We think that by the end of the year, you're going to see an improvement compared to the full year 2020, but that's an area where we need to push a little bit harder on the mix and we need to see whether the new hybrid product that we have been launched is going to be enough to position the company the way we like or whether we need to have even a stronger change in the mix and think more about unit-linked solution the same way we did in Italy, where the reposition has been extremely strong. And I want to also highlight the 1.5% of new business margin in Italy in reality is very good because you are talking about unit-linked with very high efficiencies, also short-term unit-linked. So, sometimes, it's also important to understand that the new business margin is not -- is a KPI that one has to really look into to appreciate the quality of the KPI. So, in France, we are taking action. We are not there where we want to be. But if we need to take strong action on the mix, we are going to do that. So, I think we're going to have the response in the course of 2021.

On Direct, the reason why premiums are down compared to the prior period is that we basically decided to go out of the aggregator. There was a decision in Germany. And the reason was that the profitability was very, very poor. So, we basically canceled that business. Also in Italy, we are still in the aggregator, but we decided to follow a sort of hard line on profitability. So, from that point of view, yes, you see premium going down, but that's almost adjusting the baseline. So, we have basically created no IT platform, we have created no business model. And also, we have a different view on what we think is good and profitable and what we think is not really good and profitable. And this explains, I think, also about that if you had this aggregator business, which was not very profitable and this was part of the gigantic Allianz physique, the impact was relatively minor. When you put this on a smaller scale, then you see things that you don't like. And so, I will say that from a discipline point of view, that's a positive because, clearly, what was maybe just a very minor issue in a bigger portfolio, this becomes a little bit of a more visible issue in a smaller portfolio. And we didn't like it and we made changes.

Other point to say on Direct, I will not measure the success of Direct in quarters. Strategic decision of this relevance, they get -- they have to be measured over a time horizon of years. So, from that point of view, I think we have now created the platform. We have created the -- or from the portfolio whether we think it makes sense and then let's see what happens in the next two, three years and then we're going to judge the success of this initiative.

Q - Michael Haid {BIO 1971310 <GO>}

Thank you very much. Excellent.

A - Giulio Terzariol {BIO 17125489 <GO>}

Welcome.

Operator

All right. We'll go ahead and take our next question from Dominic O'Mahony with Exane BNP Paribas. Please go ahead, Dominic.

Q - Dominic O'Mahony

Hello. Three questions from me, if that's all right. Firstly, I think you've extended the duration of your assets to be on the length of your liabilities in Life in addition to P&C now. Just curious to understand the rationale for that. Is this to control the rate sensitivity in a solvency position or is it something else? Second question, just on AGI, very strong flows. Can you just remind us sort of of the changes there? Familiar with the costs and sort of efficiency changes, but could you just remind us maybe on the product side if there's anything driving the very strong flows there? And then thirdly, in April, EIOPA announced a review of value for money in unit-linked and hybrid savings products. Can you just comment on any expectations, any potential risks you see from that review? Thank you.

A - Giulio Terzariol {BIO 17125489 <GO>}

Yeah. So, I couldn't get the first question anyway, asset duration standards. Why? Okay. On the asset duration, sometimes this happens, we need to make -- we expand the asset duration because we might be short. So, we go longer, then rates go up and then you end up being on the other side of the spectrum. So, it's always a little bit of an adjustment that we do as we see the -- what is happening on the market, but we are always a little bit behind. So, that's the reason why sometimes we are under-shorting on the duration, sometimes we are over-shorting. Fundamentally, the idea is that we want to be duration-neutral. So, we are not going to run with the duration gap one way or the other for -- on the Life side for an extended period. But, again, always keep in mind that rates are moving and we are always kind of following a little bit the rates movement.

On AGI and the flows, when you look at where the flows are coming basically from, I would say, from Asia Pacific, we see more flows that we saw in the past, so there's definitely something new and we have a very strong equity story, also, especially in Asia, but we also saw nice flows coming in Europe. So, from a distribution point of view, we are pretty strong in these two areas. From a production point of view, we are producing -- where we are producing the asset, this is coming also from the United States. So, we have, I think, a good combination of a strong manufacturing platform and then we are capable to place this solution in Europe. And right now, there is a lot of growth also coming from Asia Pacific. I think also the ESG topic is something that we are stressing and that can be helpful. And also, I will say, before we were trying to push a lot of different strategies. And maybe when you push too many strategies, then you lose focus and then maybe you are more confusing for the clients. When you are putting more focus and pushing just a few strategies, you might not have the same level of diversification, if you want, but if you are doing a good job, you might get better effectiveness. So, I think these are the changes that the new management team has done and they are playing pretty nicely. I would also not underestimate the new CEO, he was the head of distribution. So, I -- so if you put me in charge of AGI, you might see a different outcome. So, everybody has to do his job. And I think that might be also a reason why we see a different distribution effectiveness in AGI.

The last question, the hybrid and -- we always look internally at what is the value for money for our policyholder. We do this in Life. We do this also in Property-Casualty. But one of the reason why our growth in France in Property-Casualty was low this quarter is because we decided to dismiss some business because of -- we were not happy with the amount of commission versus the loss ratio. So, these are considerations that we always do. And so from that point of view, we should be positioned in a way that when the regulator is going to come out with any kind of specific guidance, we should be able to, either to be already there or to adjust to it very, very, very quickly, but customer value has been -- since years for us on the P&C side and even more, I would say, on the Life side has always been one of the indication that we -- the things that we look at. We have a framework here at Allianz, where we are rating our products in a different category, like AAA, AA, A, all this way, all these kind of an S&P ratings. And one of the criteria in order to be a AAA product is that there is customer value. Otherwise, if you don't take customer value, I think that's almost an entry point to have a conversation about the product.

Q - Dominic O'Mahony

Very helpful. Thank you

A - Giulio Terzariol {BIO 17125489 <GO>}

Welcome.

Operator

All right. We'll go ahead and take our next question again from Michael Huttner with Berenberg. Please go ahead.

Q - Michael Huttner {BIO 21454754 <GO>}

Thank you very much. I'm very lucky. Thank you. Can you say -- three things. One, a word about flows as you see them in current AGI. The second is, everything sounds so positive, I just wondered if you could give us a few risks as well and what -- profit consensus numbers might go very high. And then the last point, can you give us -- you've given us a few hints already for the next three-year plan, so lower combined ratio is one of them. Can you give us a couple of more hints, please?

A - Giulio Terzariol {BIO 17125489 <GO>}

Okay. So, on the flows, on asset management, and you can also then look at page 27, you can see where the flows are coming from. So, I can give you a little bit on -- idea because you're asking also maybe PIMCO versus AGI. When you look at the flows at page 27 from -- in fixed income, clearly, they are mostly coming from PIMCO. We are going to look at the equity side, they are coming from AGI. And I will say, when you look at multi-assets and alternative is fairly split between the two. So, basically, you see the strength of PIMCO playing in fixed income, you see the strength of AGI playing in equities. And then on the other two asset classes, both are contributing.

When you look at Asia Pacific, as I was saying before, clearly, there is also a nice contribution from PIMCO, but I will say the contribution from AGI is pretty strong and over-proportional. And then when you look at Europe, you can imagine that AGI is a little bit stronger. Then in America, PIMCO is definitely taking the lion's share. So, overall, I would say you see strength across the board in both entities. Clearly, one is playing some strengths more than other, but it's very well diversified, especially when you put the two entities together, you get to a very nice diversified flows revenue. And I think that's very important.

The other day -- or a couple of months ago, I was looking -- I don't know why, but I was looking how S&P is doing the rating of asset manager companies. There was a very interesting reading, that's a lot about the diversification of revenue, the diversification by geography, the diversification also you might have in your distribution channel. So, this is something that we are keeping in our mind how we can create as much as diversification as possible. And I think this picture tells you that definitely we are getting flows from different areas of our portfolio.

On the profit consensus, I do my job, you do your job. You -- somehow we'll get consensus and then when I -- we look at that, then we make our comments. And on the expectation for the future, I would say, we're talking in the Capital Market Day, that's where we can really talk about that. I can just tell you that based on where we are now, we think we are going to have a good set of numbers this year and then this is going to be a good starting point for the future.

Q - Michael Huttner {BIO 21454754 <GO>}

(Multiple Speakers) also thank you. Sorry? (Multiple Speakers) Yes, well, I'd love that. Can you say a word about flows in April and May?

A - Giulio Terzariol {BIO 17125489 <GO>}

Yeah. The flows, I can tell you the numbers of April, they were EUR8 billion flows, half and half between PIMCO and AGI.

Q - Michael Huttner {BIO 21454754 <GO>}

Thank you very, very much.

A - Giulio Terzariol {BIO 17125489 <GO>}

Welcome.

Operator

(Operator Instructions) We'll take our next question from William Hawkins with KBD [ph]. William, please go ahead.

Q - William Hawkins {BIO 1822411 <GO>}

Hi. It's still KBW as far as I know. Giulio, can you just tell me, so one question, why is the ratio of acquisition expenses to PVNBP so low in your Life division this quarter? Your disclosure says it's 6.8%, it's normally about 8%. And it's quite eye-catching that whilst your revenue has been strong, your acquisition expenses have gone down. And that's happened in all four of the parts of the Life and Health, so it doesn't seem to be a business mix issue.

A - Giulio Terzariol {BIO 17125489 <GO>}

No. I think it's a business mix issue at the end of the day. And -- because we did not really change the compensation strategy in a significant way. I can also give you an example, that's always easier for me to talk about Allianz Life. There, you see, for example, a reduction of the -- of this ratio and that's driven by the fact that we are selling more IVA versus fixed index annuity. And in IVA, the present value commission of the present level, the commission of the present value of new business premium is going to be lower. It's also shorter duration product, by the way. So, it's mostly mix related. And the case of Allianz (Technical Difficulty) so sometimes even within a company, you might see a reduction, but then you need to drill to dig deeper into the company and then you're going to see that change in business mix within the companies can make a difference. And think about the fact that we are changing business mix significantly. So, just to come back to the point of Allianz Life, right now, we are basically 50-50 between fixed index annuity and IVA. It was not -- so the IVA production is matching the fixed index annuity production. That was not the case last year. And there are other similar cases in other OEs. So, that's also a sign of the change in business mix that we are doing.

Q - William Hawkins {BIO 1822411 <GO>}

Okay, thanks. It's just strange because it seems to affect all major divisions because it's a very big change. (Inaudible) Thank you. Yeah. Welcome.

Operator

All right. It appears there are no further questions at this time. Mr. Schmidt, I'd like to turn the conference back to you for any additional or closing remarks.

A - Oliver Schmidt {BIO 2473131 <GO>}

All right. Thanks, Madison. Yeah, if there are no further questions, let me thank you for joining our conference call. And I wish all of you a pleasant remaining day. Goodbye from our side.

A - Giulio Terzariol {BIO 17125489 <GO>}

Thank you, guys. Have a good rest of the day. Bye.

Operator

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