S&P Capital IQ

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Allianz SE DB:ALV

FQ1 2015 Earnings Call Transcripts

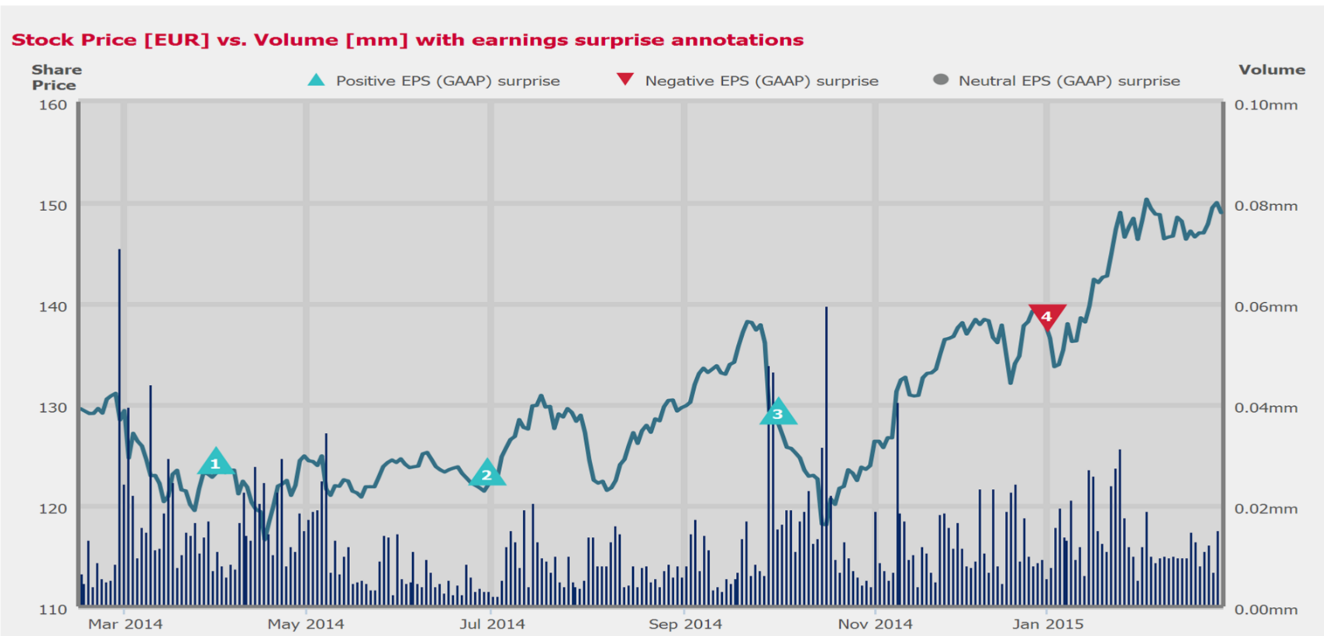
Tuesday, May 12, 2015 12:00 PM GMT

S&P Capital IQ Estimates

	-FQ1 2015-			-FY 2015-	-FY 2016-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS
EPS (GAAP)	3.70	4.00	▲8.11	14.14	14.56
Revenue (mm)	35400.00	37800.00	▲6.78	125859.00	125228.70

Currency: EUR

Consensus as of May-12-2015 12:45 PM GMT



- EPS (GAAP) -

	CONSENSUS	ACTUAL	SURPRISE
FQ1 2014	3.28	3.55	▲1 8.23 %
FQ2 2014	3.37	3.84	▲2 13.95 %
FQ3 2014	3.34	3.52	▲3 5.39 %
FQ4 2014	3.22	2.67	▼4 (17.08 %)

Call Participants

EXECUTIVES

Dieter F. Wemmer
CFO & Member of Management Board

Oliver Schmidt
Head of Investor Relations

ANALYSTS

Andrew James Ritchie
Autonomous Research LLP

Farooq Hanif
Citigroup Inc, Research Division

James Austin Shuck
UBS Investment Bank, Research Division

Jonathan Michael Hocking
Morgan Stanley, Research Division

Michael Hermann Haid
MainFirst Bank AG, Research Division

Michael Igor Huttner
JP Morgan Chase & Co, Research Division

Nick Holmes
Societe Generale Cross Asset Research

Paul De'Ath
RBC Capital Markets, LLC, Research Division

Thomas Jacquet
Exane BNP Paribas, Research Division

Thomas Seidl
Sanford C. Bernstein & Co., LLC., Research Division

Presentation

Operator

Ladies and gentlemen, welcome to the Allianz conference call on the financial results for the first quarter 2015. 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
Head of Investor Relations

Thank you, Chrissy. Yes, good afternoon from my side as well, and welcome to our conference call about the results of the first quarter 2015. I think I can keep it brief. We have published key numbers already last week. You have seen our analyst presentation this morning and all the details, you will now get from Dieter.

Dieter F. Wemmer
CFO & Member of Management Board

Thanks so much, Oliver, and good afternoon also from my side, and good morning to the one dialing in from the States. I'm using the analyst presentation as usually and mention from time to time the page numbers in case you get lost.

So I start on Page 3, the business highlights. I think it's good -- easy-to-read. Let me just highlight that in our joint venture with UniCredito, we have restarted on the motor side selling and that a rollout in a large branch network, 15,000 policies in one quarter is a very good start. But also, we have agreed on a new business plan for unit-linked products and there, we had a substantial increase in volume written through the bank channel but also through our financial adviser networks, so unit-linked sales in Italy substantially up.

Asset Management. PIMCO continues to contribute strong investment outperformance. Allianz Global Investors, good inflows, we will talk about later. On our real investments, the largest investment of the quarter was Colchester Garrison facilities in the U.K., where we are now the new landlord for the British Army. And the Fireman's Fund transaction, the sale of the personal lines business, got closed on April 1. That means the proceeds are in Q2 and not Q1. And with this one, I would move on to the numbers.

So let's start with a high-level overview of the operating results. Headline figure, EUR 2.855 billion, so 5% up compared to last year. But admittingly, there are 3 one-offs included in the numbers: in P&C, minus EUR 100 million restructuring for the commercial part of Fireman's Fund. In Life, I would say, EUR 200 million unusual realized gains, and I'll come to this later. And maybe EUR 100 million net in the Corporate segment out of changes of our own pension schemes in Germany. So the net one-off I see at EUR 200 million for the quarter, that means the quarter had started with EUR 2.655 billion. I think we can -- when we can stick to this for the rest of the year, that is probably a very good number, plus the EUR 200 million outperformance in Q1 even if it was one-off old accounts [ph] for the full year result.

Net income, 11% up. We have a slightly lower tax rate. I explained this in more detail, and I have not forgotten to talk about the revenues. They are 11% up where we have to split it between the various effects: that's 3.7% internal growth in total, foreign currency makes good 5%, and then we have the first-time consolidation of the Unipol acquisition and also the smaller acquisition of -- in Australia, Northern Territory.

And with this one, I would move on to the balance sheet. I think it also a very good quarter for shareholders' equity, EUR 68.4 billion is a huge jump forward, not really surprising. There's on one hand almost EUR 2 billion of additional retained earnings. There is the FX impact: the euro got weaker against most major currencies. And what, of course, has the biggest impact is the U.S. dollar, but we should also not forget the Swiss franc and also British pounds, Australian dollar, et cetera, so broad positive impact. And then all asset values went up substantially.

On a gross basis before policyholder shareholder split and taxes, our unrealized gains are now almost EUR 90 billion. That is a huge jump in unrealized gains and part of it, of course, goes also into the net asset value. Conglomerate solvency, the old, still-relevant measurement for 2015, is also benefiting from the increase in shareholders' equity. Additionally, we issued a hybrid bond in March of EUR 1.5 billion, which is adding 4 points to Solvency I, and also 4 points to Solvency II. And I have seen that you were partially surprised that our solvency ratio is sticking pretty closely to the year-end number. When I take all market movement, we lost through straight market movements, 16 points; and then there was 3 additional points who, I think calculation and updates from year-end. So that would be 19 points drop, and we countered it with 20 points on action and including the hybrid, which made also here roughly 4 points. It's quite a long list of activities that is derisking on pension schemes that is lengthening duration through a whole list of increments. We have really looked in each Life unit how we can reduce sensitivity and also improve the situation and still keeping enough money at risk. Because I think it is easy to close out now the volatility, but it is more important that we keep enough capital at risk that we can benefit from positive developments going forward. What certainly has helped us is also our equity exposure. We have sold and reduced some equities, but in market value, our equity holdings still increased by almost EUR 6 billion to EUR 47 billion. And also, this increase, of course, supported -- the development of the balance sheet, as I said, but it is also, I think, a good support in the risk return, which we are taking.

So overall, a quite positive development, and actually S&P rating unchanged. And when I look at the S&P Q1 numbers, actually, we are very solid above the AA level.

So now moving to Page 9, the P&C growth. I think that is one of my favorite pages of this quarter. We continue to grow on a very broad scale. 3.5% internal growth adjusted for currencies is really a good number. You see here total growth, including currency and, as already mentioned, acquisition, 14 points. That is, of course -- that would be really great when we would have 14% without the currency movements, but 3.5% is actually nicely ahead of our 3% average ambition level. And also, you can see that the price effects were positive, and it is actually reconfirming what we said at year-end that we expect positive impact from price increases, Germany and France, but also U.K., Australia continue to contribute to this.

So how does this translate, then, in the combined ratio development? First of all, you can say, yes, all the positive news, but operating profits, EUR 200 million down. EUR 100 million is under Other. That is a restructuring charge for the integration of Fireman's Fund commercial business. We had actually planned it as a second quarter event, but I think the integration is so well advancing that we booked it in Q1. And then we have a weaker underwriting result mainly driven by catastrophe events, and that is Germany. We had EUR 150 million of winter and spring storms in the quarter, so 1.9 percentage point cat loss compared to 0.5% last year. 1.9% is still light, but when I take all weather-related events, then we are at 2.8% in the quarter, and that is roughly our normalized expectation for a quarter. So the quarter was on a normal level, but it was not excitingly positive. In particular, the personal lines business of Fireman's Fund is actually leaving the group with a very poor quarter, and that has been driven by the long and hard winter season in the U.S., where we had quite a substantial list of homeowners' losses in our personal lines portfolio. So that will certainly -- that has certainly stopped on April 1. Runoff results, 3.2%, a bit higher than last year, but 3.2% is actually our long-term average in runoff results. And we have here actually a positive contribution in runoff from many countries, so there is no concentration in one unit. It is very broadly supported as in most of the last series of quarters.

When you go to Page 13 and look at the overall operating profit combined ratio contribution, I think also continued to have a strong contribution from many markets. So how is Russia and Brazil doing? And actually, I should have mentioned this. The attritional loss ratio first quarter '15 looks 1.2 percentage points weaker than 2014. And I think in the first quarter of 2014, we did not yet fully recognize that the situation in Russia, Brazil and also, Fireman's Fund was as bad as it is. I think the full run rate attritional loss of these 3 markets is better reflected in the Q4 numbers. And compared to Q4, I think we see a slight improvement, and that is also visible in the Brazilian results, yes, still a combined ratio of 111, but an operating loss only of EUR 8 million in the quarter. And remember, in Q4, Brazil contributed almost EUR

200 million loss, operating loss in the quarter. Russia also is a driver for the decline in premium in Central and Eastern Europe. So the Russian business is shrinking as planned, and we are fully on track with the closing of the retail business. And Fireman's Fund, as I said, personal lines business had a poor farewell quarter and the commercial business is, in volume terms, I think, picking up nicely. The broker market in the U.S. clearly supports and encourage us with our One Allianz strategy and acceptance rate of the change is a very high. And that was a main focus of our change that we get back on track with the broker market.

When we move on Page 15 to the investment result. Operating investment results EUR 50 million higher. That is probably slightly distorted also by foreign currency changes. All numbers look in euro absolutely stronger, but also, we have to see that the negative net harvesting results was driven by foreign-currency losses, so where we held emerging market bonds mainly in euro balance sheet. And this year, the same bonds had a positive FX impact, so it is more actually is a turn of the negative harvesting results. And both added, makes EUR 50 million more investment income. Reinvestment yield actually substantially holding up with 2.1%, but I think that is driven by 3 effects: On one hand, we invested mainly right at the beginning of the quarter, then we increased duration slightly. And we had also from the mix of investments, there were maybe more investments outside the Eurozone than inside, and we increased also our holdings in corporate bond. So all helped with the 2.1%, but I would expect that this number is hard to keep for the rest of the year.

Moving on now to the Life business. Life business, internal growth, 5%. As I said, strong growth in Italy. This is 2 unit-linked business without any bells and whistles. So we have actually 108% growth in unit-linked only, and the other business shrunk by 5% in Italy. In France, we carved out international health business, which is now shown under AWP. That explains part of the negative numbers, but also, we have reduced our single premium business in this market environment. In Asia-Pacific, it's -- Taiwan contributes with strong growth that is almost all unit-linked business, so very positive. And in the U.S., we have seen a little reduction in volumes. Well, first of all, we had a really strong quarter a year ago. But also with the repricing to keep the profit margin up in this falling interest rate environment, we lost some volume, so that was well directed and not surprisingly.

So let's move to the Life operating profit. I mentioned already in the beginning that maybe of the investment margin, you have to apply a EUR 200 million haircut to get to a longer-term average number, but also a EUR 900 million operating profit is a very strong number, driven by the volume increases of last year. Then also here, our U.S. operation has a bigger share in the overall pie with a stronger dollar. And so what drives this EUR 200 million one-off in the investment margin? Well, that is quite a composition of events. On one hand, there are the trading results from our derivatives. There are the derivatives to protect against falling interest rates, so they had obviously a fantastic quarter in Europe. Then there are trading results from equities, and also some trading results from foreign currency exposures, emerging-market bonds, as I also mentioned on the P&C segment. And then we turned over some of the public equity, and also, we lengthened duration on our fixed-income portfolio in some OEs. And when you sell at the moment in any investments, you always realize a gain because I think we have almost none investment left with an unrealized loss. Everything is -- have a strong realized gain. So the big swing in loadings and fees, I think that is more a technical change based on quite a number of foreign currency impact. So in the operating profit, it has net -- -- less visible impact. There is some -- Taiwan is growing nicely and has products with high loadings, then also Taiwan dollars is higher against the euro. And then also, the U.S. and then also some other market that is less of a change in the overall profit line.

Then I would move on to the value of new business. New business margin, 1.5% is a drop of 1 percentage point. And I have to make here an additional explanation. We are moving forward fairly radically and with full consequence to the Solvency II world and, therefore, we have also adjusted our new business margin calculation. So what does this mean? Under the Solvency II world, the contract boundaries are quite different. So you cannot assume that a 12-month contract is renewed with a certain probability, which was the old actuarial calculation. So for example, our French group business, which were all 12-month contract, most of them are being renewed after 12 months. But in the Solvency II world, you account for them as a 12-month contract. That means also the new business margin calculation for this business is then more or less being reduced to calculating a combined ratio. Make it very simple, that is actually also notice [ph] that some things are getting simpler in Life actuarial terms. But that has, as a consequence, that new business margin might look slightly different, and I'll come to this point later. And you have much more recurrent premium new business in your books. And when you go to our -- in our appendix, you will see that actually, that the French business shows a huge increase in new business with current premium, and that is a contract boundary effect.

So now what would have happened to last year's new business margin with the new contract boundary? It is, plus/minus few basis points, so same 2.5 percentage points we have shown last year. There are pluses and minuses. The statement is not to -- for each OE, but for the overall portfolio and, therefore, we didn't make a big restatement page and started to go through all the analysis, because the number variation, in total, was so small, but I think for the analysis of the profitability, it really doesn't change the picture. But internally, it makes the calculation much easier because now the market-consistent balance sheet of Solvency II, and everything we do for the Life business profitability calculation is now all integrated into one calculation and, therefore, there is also no different assumption setting, which makes everything in the long run easier for everybody.

And now let's move to the investment margin. There are 2 things I would like to draw your attention to. Current yield, first line, that is IFRS current yield dropped by 11 basis points without deeper looking at it. When you see how strongly the market value of the assets moved -- so the average market value of the assets moved from EUR 414 billion to EUR 494 billion, where the policyholder reserves only moved EUR 40 billion, the difference in the movement is the market appreciation of all the assets. That means also, when the same asset pool, when you calculate the average yield, the yield is already a bit suppressed because of the higher market values. Also, you have the same bonds and the same coupons as before. And when you split the effect, then it is roughly half-and-half. I would say 5.5 basis points is too [ph] drop in yields, and 5.5 base point is the drop to asset appreciation. And that shows you actually more how slowly the yield is dropping. Also, it shows that, based on policyholder reserves, we have a much higher, nicer yield as we only pay the yield to the aggregate policyholder reserves and not to the market value of assets.

And then comes the big item is the net harvesting and another. That was at 0.7%, which I explained with some realization, the duration lengthening and also trading result. But in this calculation, most of it goes to profit-sharing, to policyholder, so that the net margin moved from 19 basis points last year to 25 basis points this year. 25 basis points is, as I said, still too high for an average quarter, so probably more around 20 basis points is more reasonable, and that is equivalent to my EUR 200 million less investment margin.

So with this one, I move to Asset Management. I think you all know the whole discussion and story about -- around the PIMCO outflows. Again, market and foreign currency helped us a lot because at first glance, third-party assets are actually up to EUR 1.4 trillion. I think the movement chart on the right-hand side of Page 25 shows you that FX is a big driver of it, and the outflows of PIMCO were at EUR 68 billion. It is actually half of the number we had in the fourth quarter. And the vast majority of the outflows is in the traditional business and only a smaller number in the nontraditional. Before we forget it, Allianz Global Investors actually with EUR 6 billion inflows for the quarter, a very strong number, and that is now the ninth quarter with net inflows and EUR 6 billion is so far our biggest number. Market appreciation also supported strongly the development at Allianz Global Investor, and that is then also in the assets under management included.

When we move to the revenue page. Also, revenues are slightly up in the overall Asset Management business, where PIMCO is 3% down in euro terms. In internal numbers, that means, excluding FX, it's 20% down in revenues, and Allianz Global Investors is strongly up in all measurements, driven by market inflows.

And that results then on Page 29. In an operating profit development, which is in euros, 14% down. And excluding the dollar, we would lose another 12%. And here, it is the volume decrease has a big effect, but expenses stay more or less stable in euros and are not falling. And that is certainly in U.S. dollars -- sorry, the expense stays stable in U.S. dollars and, therefore, the cost income ratio in PIMCO is deteriorating by 10 percentage points. We have not reduced our staff, and we have additionally some one-off expenses. There is the higher retention [ph] package, which we started in October. There are additional marketing expenses, there are some provisioning for the legal actions, defend costs. And there is an also additional one-off proxy fees for some of the major funds because the lead manager is changing, and then we have to redo old prospectus and everything. So I would say in the PIMCO, our cost [ph] income ratio there might be good; 2 percentage points of one-off costs in Q1. And please also remember that we said with our February outlook that we expect still a substantial amount of performance fees out of private funds maturing in the fourth quarter. So the whole annual results for PIMCO will be very much back-end loaded.

Finally, the Corporate segment, a small EUR 100 million loss, including EUR 100 million one-off net because there were actually 2 one-offs, EUR 150 million from a pension provision but also some write-downs on software. So I would say the net one-off is EUR 100 million. And that is coming from still restructuring or I should say, bundling of the German pension schemes from local subsidiaries to the holding company. And additionally, we will, in the second quarter, also do some derisking of this pension schemes in Germany, but also in other markets, also to continue to manage our solvency ratio.

And I now move to the last page with numbers, only to mention that the tax rate is 2 percentage points lower. But from my perspective, it is lower for the wrong reasons. The reason for the lowering is the mix of pretax profit. PIMCO has a 38% tax rate, which is above the average. That means reduced PIMCO operating profit creates then also a lower effective tax rate, and that is, for me, the wrong reason to get the tax rate down.

And now let me come to the summary. In euro terms, revenues growing double digits; profit, 5%; and shareholders' net income, up 11%. Overall, I think we are reconfirming our strong capital and balance sheet basis in all measures: IFRS, Solvency I, Solvency II and S&P rating. And I think also in the Q1, we are showing really substantial progress on all the promises we made beginning of the year. And the promises starting with -- that we manage our Solvency II ratio actively, finding a right balance between risk taking and risk avoidance because we want to benefit from the changes in the financial market. We -- I think on track to correct the developments in Brazil, closing in Russia, integration of Fireman's Fund. And also, the outflows at PIMCO are in line with our expectation for the first quarter. So I think that is a successful start in executing plan 2015 at Allianz.
And with this one, I open the questions.

Question and Answer

Operator

[Operator Instructions] We will now take our first question from James Shuck from UBS.

James Austin Shuck
UBS Investment Bank, Research Division

I had 3 questions, please. Firstly, on economic capital. I mean, obviously, you've managed the development since year-end to Q1 to be broadly flat. There's a number of moving parts in there. There's a certain amount of subjectivity around the calibration of economic capital. And I think in the past, you targeted 160% plus the 30% buffer on top of that. And what's clear is that you have a certain degree of subjectivity around how you calibrate it. So my question is, what is the kind of additional buffer that you have to play with, with regards to how you actually calibrate the economic capital model? You've made some changes around policyholder participation, rate assumptions, for example, I understand those are still above statutory minimums. But I just want to get a feel for kind of what scope you've got to actually manage that number, if possible?

Secondly, on economic capital sensitivities on Slide 42. I was just a bit surprised to see that you're still fairly positively exposed to a higher yield environment. So plus 50 basis points, adds about 9 points to Solvency II. I was surprised to see that given the closing of the duration gap on the Life business. So you could just explain where that's coming from, please?

And then finally, on the MCEV disclosure on Slide 67, could you just talk through some of the movements here? I'm particularly interested in the asymmetric nature of the differences between the German-speaking countries and the Western and Southern Europe part of that. So for example, the interest rate being positive for Western Europe but negative for Germany, obviously, the German speaking is clear, but the volatility differences and the equity differences. And I suppose as a subset within that, could you just talk about the negative experience variance you had on Alliance Life U.S. following the very strong growth there, please?

Dieter F. Wemmer
CFO & Member of Management Board

Okay, James. Thank you very much. I must say I have to reject the statement about subjectivity in the economic model. If this would be our own internal model, yes, there would be subjectivity. But this is the model we are going to file over the next few weeks with the regulator as part of the official IMAP process. So -- and that model is being accompanied by more than 60,000 pages of documentation, and that is now after 3 years of intense discussions with many regulators in Europe, which are bundled under the supervisory college who deals with Allianz internal model application. So that reduces subjectivity actually quite a lot.

What, of course, is still a management decision is how long you keep a certain crediting rate for a policyholder up depending on future interest rate scenarios. And that we -- in this environment are actually more careful in crediting rates that are management decision if you want to call this subjective, I think that is more a careful reflection on what you see in the interest rate development in Europe all together. But that is a small impact in the overall calculation in Q1 and is much more the active changes we have done to the asset portfolio, but also, we are certainly also reviewing in force business where we can adjust some conditions on group contract. I think we are careful acting here in the interest of our customers, but also keeping a balance to the shareholders.

The interest rate sensitivity, that is a complex thing. And I think the better calculation, which gives the deeper insight, is the full economic solvency interest rate sensitivity, because here we are modeled through the whole impact: a duration calculation that's in the end, a simplified calculation, in the end, linear rising curve, which is actually convex. And this effects, therefore, showed different numbers. So even if the duration would be completely showing the same number, you are still not getting out of the interest rate sensitivity because our liabilities are convex. That means when interest rates are falling, the liability duration gets longer. And that is better reflected in the interest rate sensitivity of the full calculations than just the shortened duration calculation.

On the sensitivities in the MCEV, Page 67, that's different under the column German-speaking versus Western and Southern Europe. I think the totals are correct. I think there is some messing around with the individual numbers because you are picking here a good point, that the signs look to me also difficult to interpret. I think we will look at this Page 67 and maybe send out an updated version of it. We are, at this quarter, a bit short in time, and I think some of the checks probably missed this. Sorry about that.

James Austin Shuck
UBS Investment Bank, Research Division

No, that's fine. Could you just clarify on the experience variance on the U.S. business, please?

Dieter F. Wemmer
CFO & Member of Management Board

I think that is probably just a trading results out of the hedging, which are not always perfect as we take also some small base risk here. And that is being updated in the changes, but that is very small. That is driven by changes in interest rates that is coming from mismatches in the hedging product.

James Austin Shuck
UBS Investment Bank, Research Division

I guess my point is on the U.S., we've seen very strong growth coming from Allianz Life. And I just want to be sure that, that business is behaving as you thought it would do when you sold it.

Dieter F. Wemmer
CFO & Member of Management Board

Absolutely. And by the way, it is a positive number.

James Austin Shuck
UBS Investment Bank, Research Division

It's a negative number, isn't it, minus EUR 386 million?

Dieter F. Wemmer
CFO & Member of Management Board

Then I'm on the wrong page. I'm on Page 67, and look at the EUR 61 million.

James Austin Shuck
UBS Investment Bank, Research Division

In -- minus EUR 386 million in point number 2.

Dieter F. Wemmer
CFO & Member of Management Board

Sorry, you are on Table 2.

James Austin Shuck
UBS Investment Bank, Research Division

Yes.

Dieter F. Wemmer
CFO & Member of Management Board

I was on Table 3. Sorry, yes. I think that is -- we need to follow up on this number. I think the operating profit margins are still all holding up.

Operator

We will now take our next question from Paul De'Ath from RBC.

Paul De'Ath
RBC Capital Markets, LLC, Research Division

Couple of questions please. Firstly on the duration management that you've been doing during the quarter and obviously now. As you mentioned, the duration gap on the Life side is practically 0. Is it -- should we now think that you're -- potentially you're linked in the duration as much as you would like to? Or should we expect any more of these kind of actions going through the year? Just a viewpoint on that [indiscernible] also impacted the earnings.

And the second point is just a bit clarification really on the negative new business margin in France. Obviously, you mention this due to the change in the contract boundaries, and that this turns negative. Should we just be factoring in negative new business margin France going forward here? Is this the new normal and kind of under the real situation, it will turn out fine? But under new MCEV guidelines, you'll be reporting negative margins here?

Dieter F. Wemmer
CFO & Member of Management Board

Paul, I think the duration management's done for the year. I would not say we continue to look at each OE, and we'll continue to very proactively manage our solvency ratio. But certainly, as of today, as you have probably all noticed, that 20-year euro spot curve at the end of March was 79 basis points. And the 20-year is more important point in the interest curve for the solvency calculations than the others. And now, last Friday, we were at 110 basis points. So it's 31 basis points up. That has certainly a positive impact on the overall solvency calculation, but we will continue to watch it. And as I said, derisking of the pension liabilities will continue, also matching of our pension liabilities because the duration gap. And our pension liability is actually certainly bigger than in our customer portfolio. So that is also part of the interest rate volatility. So we will continue to work on this. And then the French margin -- no, actually, I think, the new measurement is probably giving a better transparent view on the tools [ph]. We have 2 major lines of business in France. On one hand, it is the group health business, which has, in combined ratio terms, has a combined ratio above 100. Therefore, the new business margin is negative. And the normal standard capitalization product in France due to the interest rate difference between what we credit to the customers and your new investment rates you can achieve in some markets is also slightly negative. And we have because you have to pay in between expenses, and we have to work on to reprice both products to turn positive. So therefore, I think it is not due to the change in rules, it is a very transparent weakness.

Operator

We will now take our next question from Farooq Hanif from Citigroup.

Farooq Hanif
Citigroup Inc, Research Division

I was wondering if you could quantify what would happen if you moved your U.S. business to -- now to 2x the level of capital that you're assuming. And also if you could comment on what BaFin thinks of your U.S. capital assumption that you're making in the equivalents calculation. That's question one. Could you comment on -- maybe you said this already, but could you comment on the actual method you used to increase duration? So how much of it was in sort of physical assets and how much was hedging overlay? And could you also, lastly, just talk about what you think the regular growth rate in your reserves is in the Life business, if you exclude FX? So it was obviously up, on an average basis, 11%. But it seems to me that your net flows are also quite positive. Your interest rates are, on a normalized basis, holding up. So do you think you could yet achieve roughly 4% or 5% growth a year on your reserves? Could you possibly quantify that? That would be really helpful.

Dieter F. Wemmer

CFO & Member of Management Board

I think if I remember correctly, from end of 2014, we had roughly 8% net growth in the reserves, and half was inflow and half was accrued interest. And 3 months later, the situation has not changed a lot because of a lot of the inflows were from the second half of 2014 and, certainly, further supported by inflows in 2015. So I would say 7% to 8% is probably the gross effect of [indiscernible]. I think that's actually -- in our year-end call [ph] there was certainly a disclosure for this. I don't know what BaFin thinks, but certainly, we are filing the model as we explained it and as it is here currently stated. I'm also positive that the EU Parliament will grant the U.S. equivalents. And the whole discussion about what is the right percentage of co [ph] is a very complicated one. I think you should start talking to your U.S. colleagues and look at the comparability of local solvency ratios. For U.S. to be a business, the U.S. regulator has actually adopted a total assets concept, and that means you can either increase reserves or you can have a higher capital charge. And the U.S. regulator looks at the sum of reserves and capital charge. That means to the extreme, if you want -- if you assume you're a pure VA player, you could have EUR 10 million capital charge and to have in your balance sheet EUR 100 million capital, and you would show 1,000% ratio. Or you show the whole EUR 100 million as capital and not as a reserve charge, then your solvency ratio would be 100%, but it is the same balance sheet. And this little refinement has to be considered quite a lot before debating what multiple you want to apply to what numbers. Therefore, I'm staying away from all this speculation, whether it's factor 1, 2, 3, 4 or, 5 because I think that all debate's based on an uneducated view on U.S. statutory requirements.

Farooq Hanif
Citigroup Inc, Research Division

Actually, my question was probably a little bit more benign. What I meant was, obviously, you must have -- I mean, BaFin are not going to be completely surprised when you input this model to them because they will have seen it before. Is that correct?

Dieter F. Wemmer
CFO & Member of Management Board

Well, as I've said, we are discussing with them all details since more than 3 years with the same team. And actually, when the -- I also said in the February call, when we changed to U.S. equivalents, of course, we had a consultation discussion with BaFin. And we are not hip-shooting.

Farooq Hanif
Citigroup Inc, Research Division

And is it a big effect if you changed your assumption?

Dieter F. Wemmer
CFO & Member of Management Board

Well, that is -- in the end, that is -- that would go a few points down. And actually, probably the gap between internal model and equivalents, as we speak, is smaller than at the beginning of the year. I did not do the test, but U.S. interest rates are on the rise again. Credit spreads came down. So, Paul, the end of April number, the difference between the 2 is certainly smaller than January 1, but it's not relevant as we will file now with U.S. equivalents.

Operator

We will now take our next question from Thomas Jacquet from Exane.

Thomas Jacquet
Exane BNP Paribas, Research Division

So my first question is on the Italian Life new business margin. I'm quite surprised to see such a decline in new business profitability given the fact that you have a lot of unit links. So do you plan to take actions to restore profitability? Or is it something linked to the calculation methodology? And my other question is regarding your -- the management actions you've taken to save the solvency. Can you give an order of magnitude of the different things you've done? And can you specify whether you use some hedging techniques and some -- buying some swaptions, for example?

Dieter F. Wemmer
CFO & Member of Management Board

Yes, well, the drop in Life new business margin is, I think, we have a good new business margin on the unit-linked business, but also the classical Italian general account business has a small negative new business margin. Why is that? Because the old fund that credits to the customer are higher interest rates than what you can achieve in investments. So therefore, you are, in the end, making a loss when you calculate it stand-alone. And that is what a new business margin should reflect. So therefore, it is not a surprise, and we have to do a repricing or changing of the traditional business to get the overall new business margin back to a good level. The unit-linked sales, stand-alone, are absolutely fine. So what did we do in ALM? I think, to a large extent, we just bought longer physical bonds, but then also we have extended our swaption programs. But I think the bigger part were actually futures, which we executed, and which we are using in hedge accounting. That means, let's say, they are not -- you are not seeing any derivative impacts in our P&L.

Operator

We will now take our next question from Jon Hocking from Morgan Stanley.

Jonathan Michael Hocking
Morgan Stanley, Research Division

I've got 3 questions, please. Firstly, could you go through the movements in the solvency ratio? You're talking faster than my ability to write, unfortunately. I think you said market movement of 16 points -- 20 points. So actually 4 points behind, but I think I missed something in the middle. That's the first question. The second question, on the duration gap narrowing. Has all of that been achieved on the asset side or have there been some changes to modeling on the liability side? I'm just wondering whether some of the currency [ph] rate adjustments you've put through have actually made the difference to the duration of liabilities. And then finally, just on the reinvestment yields for the Life business, just on, I think, Slide 23, you sort of break out a lower number due to the impact of derivatives. Just wondering if you can explain what the difference is between the gross number and that lower net number.

Dieter F. Wemmer
CFO & Member of Management Board

I think with the last question, you lost me. What is...

Jonathan Michael Hocking
Morgan Stanley, Research Division

Just on Slide 23, Dieter.

Dieter F. Wemmer
CFO & Member of Management Board

The new investments?

Jonathan Michael Hocking
Morgan Stanley, Research Division

[indiscernible] in brackets or in the bubble, actually. So you have the 2.2%, down from 300 (sic) [3.0%] the prior year, and there's a breakout bubble, so in the economic reinvestment yield, including derivatives.

Dieter F. Wemmer
CFO & Member of Management Board

Yes, and the duration extension on the new business, when I include also the forwards, and these are more the AAA government bonds, that reduces the average new investment yield.

Jonathan Michael Hocking
Morgan Stanley, Research Division

So the more -- the economic one, so we should be using the 1.7%, that's the number to compare going forward, is it?

Dieter F. Wemmer
CFO & Member of Management Board

Well, in accounting terms, in the next number of years, the 2.2% is what materializes because the 1.7%, if you buy a forward during the forward period in hedge accounting, there is 0 impact of this one that will only crystallize after the forward period. And so that was this question. Then the Solvency II movements, I think that was -- in total, the downward changes were 19%; and the upward changes, obviously, 20%. Otherwise, it's not moving plus 1%. And there is, I think, that we're -- mainly the management actions, and then of course, including the hybrid, which makes 4 points.

Jonathan Michael Hocking
Morgan Stanley, Research Division

Is it possible to break out a little bit the 19%?

Dieter F. Wemmer
CFO & Member of Management Board

Well, I think -- I thought actually more it was our results call, and now it's becoming a Solvency II seminar. I think you are only using the very detailed disclosure for Allianz to challenge the others. That is fine, but I'm actually not sure whether Allianz gets a lot of benefit out of the details. It seems that every detail creates only a myriad of further reviews of our model, and that is already being reviewed by the regulators. So the main driver is asset duration. There are some equity hedges in it. There is a better matching of our own pension liabilities and things like that. So it is, in each of our Life OEs, I would say it is a list between 5 and 20 smaller actions. And it is all adding up. I think it was a well-orchestrated activity across the group. And the group has demonstrated that they can live in a Solvency II world because Solvency II means active management, that is not a stable number, which you calculate once a year, and which is only changing every 5 years like Solvency I. And I think that is what you have to learn when interpreting it, and the companies has to learn to manage it.

Jonathan Michael Hocking
Morgan Stanley, Research Division

Okay. And then the duration gap closure, it was up principally on the asset side. Or was there any...

Dieter F. Wemmer
CFO & Member of Management Board

I think liabilities are naturally going also slightly up because we are in a convex world. And convex actually means that when your credited interest rates goes closer to the guarantee, you get closer to the pure naked duration calculation of the guarantee. As long as you pay high crediting rates, your liability duration appears shorter because the crediting of the profit-sharing reduces, so to speak, the average duration. That is the explanation for the convexity.

Operator

We will now take our next question from Andrew Ritchie from Autonomous.

Andrew James Ritchie
Autonomous Research LLP

I promise I won't ask about Solvency II. The first question, just on Non-Life, I noticed in the roll forward chart of the accident year loss ratio, you show a 1.8 effect of frequency and severity, excluding nat cat. I think from your comments, you would suggest a lot of that is sort of weather effect underneath the nat cat and maybe some large losses, but maybe just give us a sense if there are any underlying severity trends.

Dieter F. Wemmer
CFO & Member of Management Board

Yes, there is a bit of severity. But as I also said, in Q1 '14, we were still too optimistic on Brazil, on Fireman's Fund and also Russia. And the whole catch-up which happened during the quarter, during 2014 is, of course, now embedded also in Q1 '15. So that has certainly changed also in the numbers. So therefore, I think when you look on the same page on the comparison to Q4, you actually see, well, quite a lot of improvement to Q4 and Q1. It's, of course, always tricky because you, as a very experienced analyst, know that there are always seasonal effects in loss ratio and, therefore, we usually compare season by season. But Brazil and Russia, that was less of a seasonal effect that was a really operational deterioration. And that is...

Andrew James Ritchie
Autonomous Research LLP

I guess, I just observed in some of the commentary, you talk about severity in Italy and, I think, Turkey. I mean, is it -- is there-- what is severity running at Italy, for example?

Dieter F. Wemmer
CFO & Member of Management Board

Well, our claims average is slightly up. That is -- and in Turkey as well also on the motor side. But that is, I think in the -- that is probably not baking in a lot here in the numbers yet. Our attrition loss ratio also in Italy is slightly higher than a year ago, and that is not surprising as the whole market is reducing rates, and we can also not keep rate completely unchanged.

Andrew James Ritchie
Autonomous Research LLP

And frequency is no longer falling, presumably?

Dieter F. Wemmer
CFO & Member of Management Board

Frequency is actually slightly lower in Italy. It depends whether you look on MTPL alone or whether you look at other MOD. The total frequency in Italy for our book is still a little bit lower.

Andrew James Ritchie
Autonomous Research LLP

Okay. But other than...

Dieter F. Wemmer
CFO & Member of Management Board

MTPL is a little bit up.

Andrew James Ritchie
Autonomous Research LLP

Okay. Second question was just on the Life new business in the U.S. You mentioned in your comments -- I mean, you repriced it to maintain the margin. But the margin still fell quite a lot year-on-year. I guess, I'm just curious, why did the margin fall on a product that's not that interest rate-sensitive, the FIA product? And also I'm a bit surprised, sales fell as much as they did. I thought you still had exclusive use of the Barclays hedge, and that still meant that even though you're repricing, you would still see decent volume growth. So maybe just a bit more explanation on what happened to the U.S. would be useful.

Dieter F. Wemmer
CFO & Member of Management Board

Well, I think, first of all, the starting point last year is fairly high sales volume. There is also a little bit more competition coming in. And the product is, in falling interest rates, less attractive for the customer.

Therefore, it is not surprising when you increase your fee charges. That means that the total return for the customer is reduced that you have less sales. Our bigger step in repricing will kick in, in April. We did 2 smaller steps in repricing in the first quarter, and we did not maintain the full new business margin. But the new business margin is still above our 2% level. And it was, in the end, the local decisions, the trade-off between volume and margin, which is okay from a group perspective as long as the margin is above 2%.

Andrew James Ritchie
Autonomous Research LLP

So the repricing may affect volumes a bit more, but I guess, you hope you get a bit of margin back?

Dieter F. Wemmer
CFO & Member of Management Board

We get a bit of margin back in the second quarter, yes.

Operator

We will now take our next question from Michael Huttner from JPMorgan.

Michael Igor Huttner
JP Morgan Chase & Co, Research Division

I'm afraid I'm not going to merit any kind of beer, but I hope this is a light question. The -- on this Solvency, my understanding, and it's very, very high level, is effectively the big trade-off is that -- or the big management action involved futures. And as you described of them, they go through the balance sheet and the impact on earnings, therefore, is limited for however long the futures hold. Is that the right way of thinking about it? In other words, that in a way -- let me use my words carefully. The management actions that you took have no immediate impact in terms of -- or very little immediate impact in terms of earnings. The other question is the combined ratios -- so I was trying to guess what a sustainable level would be. I'm coming around because there's a bit of pricing improvements still coming through. Maybe the weather was a bit worse in Q1, I don't know. Is 94 the right level, or 93.5? Just trying to average all these things out, which you mentioned, given that it's a bit worse in Q1 '14. But the other, it seems a bit better than the rest of the year. I mean, the rest of the year seems to average just around 94 and a bit, 95. And then the last question is on the PIMCO. How much is the -- or can you give us a rough idea of how much performance fees has to come just to -- so know what figure to add? And yes, sorry, no beer.

Dieter F. Wemmer
CFO & Member of Management Board

I think that was indeed a light question on Solvency II. Maybe you get half a pint. So impact on earnings is very small through the actions. I think some of the shorter dated physical bonds we replaced by longer dated, that was probably more of -- well, economically it was partly positive. And in operating investment, in terms small change, I think the futures make maybe a sort of the whole lengthening program. It was a lot in physical bonds and there are also some additional swaptions, which we added. So it was a well-balanced package between all this. We're really looking at the individual situation. You have to remember that actually a lot of the balance sheet are split in segregated funds, and you have to take the right decision for each of the segregated accounts. There are individual policyholder, shareholder holds. There are accounting regimes, very different from country to country. So therefore, you cannot take one strategy to solve the problem. It is really a very detailed bottom-up work. On the combined ratio, I think for me, the more important statement was that we are on track with the turnaround cases. And we said that we will keep in the matured markets a combined ratio stable compared to last year. And I think that we are going to do because the small deterioration in Italy. And actually, Italy is holding better ups than I expected because I thought that the Unipol portfolio will have a more worse loss ratio than our portfolio. But in the end, it played out that we are a little bit worse than the Allianz average portfolio. So therefore, the average share combined loss ratio in Italy, and that is a 20% portfolio expansion in Italy, is actually looking very strong. That means supporting our underwriting results. France and Germany continues to have rate increases. So also support from there, [indiscernible] and oil are holding up. And the turnaround candidates, I think, are on the right track. Russia will just be diminished to [indiscernible] to almost nothing. Brazil is on a good way going forward. The personal lines business, Fireman's Fund, is sold, and the commercial business before we improve the loss ratios there. That is a longer-term work, but I think we see already some good first steps on the expenses. Certainly paid by restructuring charges, but the restructuring charges will also be offset by EUR 330 million that proceeds from ACE. So I think that is all balancing out quite well. PIMCO, you had a question on the performance fees. Well, in the end, when you take the midpoint outlook of our Asset Management segment, you can almost easily calculate how much performance fee has at least to come.

Operator

We will now take our next question from Thomas Seidl from Bernstein.

Thomas Seidl
Sanford C. Bernstein & Co., LLC., Research Division

Three questions, please. I'm also in for a beer. It's only on earnings, not on capital. The first question on is -- I'll come back to the U.S. Life and also maybe Italian Life. And the fact that you repriced the business from a management perspective, does this imply that the business you sold the last 1 or 2 years basically now looks not as good as you thought and, hence, the need to reprice? What triggered this need to reprice? And how should we think about the back book rather than the new business as you said right now? First question. Second question, you mentioned, of course, the obvious problem at PIMCO, the lowest scale driving up cost income ratio. So what are the plans here? Do you expect the asset situation to stabilize or improve from here? Or should we expect that you take material action to bring the cost in line with the lower scale? And the third question is on the P&C segment. We know that the price momentum seems to have stabilized right now after a number of quarters. We are now at 80 bps increase, which is not great, but it's still stabilized. My question here is, from here, is your expectation that we basically see a slight upward trend or when if I just look at the Page 59, overall, it seems to be maybe slightly going down going forward.

Dieter F. Wemmer
CFO & Member of Management Board

Okay, Thomas. The repricing in the U.S. is actually a very ongoing activity. And I think in 2014, we have repriced 8x our fixed index annuity business because we are selling the business, so to speak, in tranches. We look every 2 weeks how did the U.S. Treasury rate move? And depending on this, we recalibrate our expense charges, but also we take our investment income because we match the received premium risk and investments being done. So therefore, the old business is not affected by this one. It is an ongoing adjustment. And additionally, in case that there is something wrong, we can, on a yearly basis, but always with 1-year delay, adjust the fee charges for our fixed index annuity business in the U.S. And correct, therefore, I'm not concerned at all about the business in the past. In Italy, well, I think that the large difference between your old yields you have in the portfolio and your new money yield is creating a problem. And that is an inherent problem in most Europe -- Continental European countries for all this general account business. And that is simple. You can go to your bank, borrow EUR 1 million short, date it and invest it in a Life policy. And there are combinations in Europe possible that you can create a positive arbitrage out of it, and I think what we have to do to ensure that our products are not giving any opportunity to this type of arbitrage. And that is -- therefore, we introduce limits on the sizes of single premiums. In Germany, for example, you are in the first -- when you buy a single premium policy the first 5 years, you are not participating in the general account returns. You get a substantially reduced total return because the arbitrage guys are not patient to wait more than 5 years, and there are also steps you have to do when you have such anomaly in interest rates between existing yields and new money yields. I think the pricing increase of 18 basis points, I think that is for the overall portfolio, still a good number because we are still living largely in a flat claims inflation world. You can read every day how desperate ECP is trying to create inflation in Europe. Italian business, I answered. PIMCO, yes. Sure, lower scale is correct. Total Return Fund's smaller than before. I think with the expense actions, we are more prone to invest in the future and building up the next development phase of PIMCO instead of optimizing next quarter's earning. But certainly, the one-off expenses of Q1 should also be less. And as I said, maybe

62% is a too high cost income ratio, and slightly below 60% is a better cost income ratio for the year, not counting on performance fees. If you add them, then of course we are back to a very good cost income ratio.

Operator

We will now take our next question from Nick Holmes from Societe Generale.

Nick Holmes
Societe Generale Cross Asset Research

Dieter, I've got just one question. I'm afraid it's on Solvency II, but it's a nice Solvency II question. I've wanted to ask, looking positively at what Solvency II is doing to the industry, do you think that you will stop writing guarantees in Germany? And do you think the whole industry is going to change, that everybody's going to get out of the guarantee business and this could actually be a very good thing for the industry overall?

Dieter F. Wemmer
CFO & Member of Management Board

Yes, that is indeed a nice question on Solvency II. Well, maybe the industry would not consider it as a nice question. I don't think that we would stop writing any guarantees. I think when you look at our product perspective in Germany, that is exactly our answer to writing guarantees in the Solvency II world because that product has split the guarantees into 2 halves. And therefore, you end up with a duration liability which you can match with assets. The accumulation phase for people are 60 or 65, whatever they pick as retirement age. And then a new market adjusted guarantee from de-accumulation point starting. I think that is one of the potential answers to Solvency II. And also, our fixed index annuities in the U.S., which we sell also quite very well, actually, in Germany, also examples because these products are matched and you have more options to reprice and react faster to market movement. And certainly, the industry in Europe has still to become more flexible with the fast changes of the financial markets, that we are living at the moment in this total -- yes, extreme yield scenarios driven by quantitative easing exercises around the globe. I think that is something different. But even if this goes away, that interest rates will recover to 6% is very, very unlikely. And also, financial markets are, today, much more volatile than we were -- all used from previous periods. And this volatility is probably more the driver that this 40-year stable guarantees are very difficult to manage.

Nick Holmes
Societe Generale Cross Asset Research

Dieter, so just to clarify, are you actually selling at the moment open-ended guarantees in Germany, ones that can extend 20, 30, 40 years?

Dieter F. Wemmer
CFO & Member of Management Board

To a small extent as everybody else in the market, but I think we do this with a very large and highly capitalized balance sheet. And it is in our new business, I think, by far, the smallest share of old players.

Nick Holmes
Societe Generale Cross Asset Research

Right. And in 2016, would you actually stop altogether writing that type of business?

Dieter F. Wemmer
CFO & Member of Management Board

Look, as we are measuring internally already now for several years under the Solvency II regime, and we manage the company like in 2016, why would we act next year differently than this year? You cannot start acting under the Solvency II on January 1. That will be a bit late. It seems so that some people believe they can start next January, but I think that is a bit late.

Operator

[Operator Instructions] We will now take our next question from Michael Haid from MainFirst Bank.

Michael Hermann Haid
MainFirst Bank AG, Research Division

Michael Haid, MainFirst Bank. One question on Allianz Leben. Certainly, Allianz Leben is not amused by the current low interest rate environment. So my question is maybe a little bit broad, but aside of lengthening the duration of the asset side, what other measures do you take or you plan to take to improve the situation here? I guess, my question goes in the direction of how can you improve the mortality results or cost results? Or what other measures can you take or you have already taken?

Dieter F. Wemmer
CFO & Member of Management Board

Well, first of all, I actually read your study on the German life insurance industry. It was very well done and very interesting reading material, Michael. So what can we do in the ultra-low yield environment? I think we play here our scale and peer advantage. I think that it's the product design I mentioned already to reduce duration length. I think that is a deferral period we have on the single premium products. Then I think our cost advantage is probably around 80 basis points compared to the average market. And our asset strategy is probably also more exploited and more sophisticated. We have -- a part of the garrison I mentioned right at the beginning of my presentation, of course, is being held by the investment portfolio in Stuttgart in our Life balance sheet. And that is also a type of investment that is lengthening out our asset duration and gives still reasonable returns. I think it is really a combination of all of it and, I think, the scale advantage and the active asset management is probably the main positive. That does not mean that we are sitting idle on our old successes, we are constantly working on further changes and improvements.

Michael Hermann Haid
MainFirst Bank AG, Research Division

How easy would it be for you to improve the expense result? Which -- if it's negative, it has to be carried...

Dieter F. Wemmer
CFO & Member of Management Board

We have a positive expense result.

Operator

There are no further questions in the queue.

Dieter F. Wemmer
CFO & Member of Management Board

Great.

Oliver Schmidt
Head of Investor Relations

Great. Then thanks for joining the call. We say goodbye to everybody, and have a very nice remaining afternoon.

Dieter F. Wemmer
CFO & Member of Management Board

Yes, thanks so much, and see some of you in the next days. Thank you. Bye.

Operator

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