

Allianz SE DB:ALV

FQ3 2018 Earnings Call Transcripts

Friday, November 09, 2018 1:00 PM GMT

S&P Global Market Intelligence Estimates

	-FQ3 2018-			-FQ4 2018-	-FY 2018-		
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	GUIDANCE	
EPS (GAAP)	4.58	4.54	▲ (0.87 %)	4.72	17.75	16.90	
Revenue (mm)	29941.01	30483.00	▲ 1.81	31380.03	128597.85	-	

Currency: EUR

Consensus as of Nov-09-2018 9:43 AM GMT

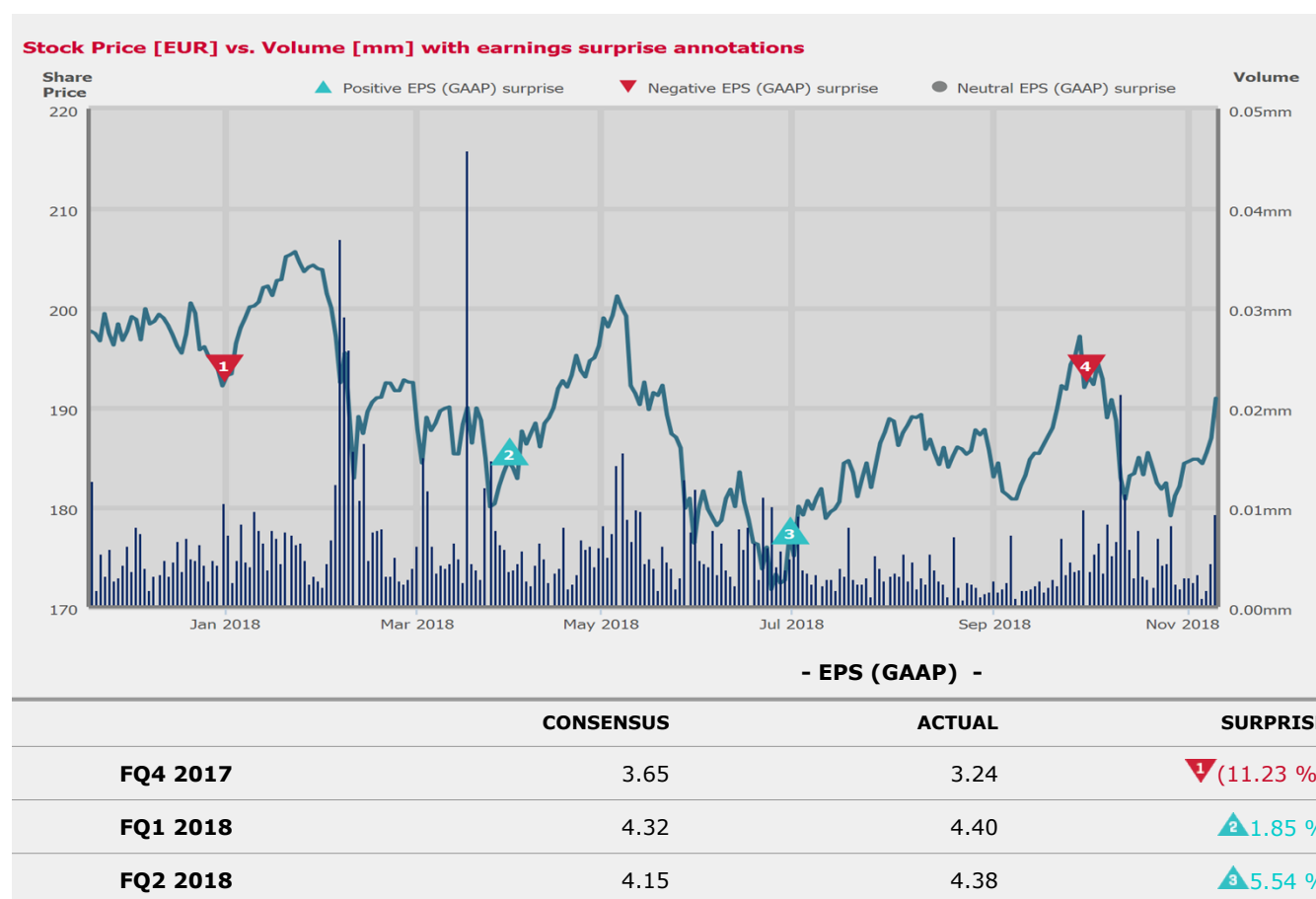


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Presentation

Operator

Ladies and gentlemen, welcome to the Allianz conference call on the financial results of the third quarter 2018. For your information, this conference call is being streamed live on allianz.com and YouTube, and the recording will be made available shortly after the call.

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, Stephanie. Yes, good afternoon from my side as well, and welcome to our conference call.

There's nothing specific I would like to add right now, so I hand over directly to Giulio.

Giulio Terzariol

CFO & Member of the Board of Management

Hi. Good afternoon, and good morning to everybody. I'm pleased to present to you the numbers for the third quarter. But before we go into the third quarter numbers, we can take a look at the picture as of September 2018, and we can go to Page #3.

As you see, we have very strong results for the first 9 months across the board. That -- when you look at the revenue, we have been able to grow revenue on an internal basis by about 7%, and the growth is driven by all segments. Especially, it's very nice to see the growth rate in P&C, which is close to 6%.

On the operating profit, we are up EUR 400 million compared to the level of last year. This is driven especially by property and casualty, and you can see also a nice contribution coming from Asset Management. On the life side, we are slightly down compared to the last year, but we need to consider that last year was kind of elevated because the volatility in the United States was particularly low. And even more important, with EUR 3.2 billion of operating profit, we are very much in line with our outlook for the year of EUR 4.2 billion.

When you look at the operational KPIs like combined ratio, new business margin, cost-income ratio, they are all heading in the right direction. Especially, you can see a nice improvement in the combined ratio, which is now, for the 9 months, 94%, which is also the level that we are targeting for the full year based on our Renewal Agenda target. The new business margin has slightly improved. And combined with increased revenue, this is leading to a nice growth in VNB of about 9%.

The flows year-to-date are at about EUR 30 billion, so that's also a nice picture. And then when you look at the bottom line, so when you look at the net income, we are up 7% compared to the prior period. This is driven once by the improvement in operating profit. On the other side, we have also a better tax ratio, which is mostly explained by the tax reform in the United States.

So all in all, when you look at this page, I think the picture is really compelling. We have good growth in revenue. We have operational KPIs moving in the right direction. And the net income and the earnings per share are growing very nicely.

If we move to Page 5, we can now go into the third quarter numbers. And also, the third quarter, on a stand-alone basis, is very strong. On the revenue side, you can see, always on an internal basis, that we have a growth rate which is almost 10%. This is driven by all segments. So we have a nice growth rate in property and casualty, which is consistent with the growth rates that we saw also in the prior quarters. We have a nice growth rate in Life/Health, even better than what we saw in the prior quarter, and we see a nice stability in the growth in revenue in Asset Management.

The operating profit has increased substantially compared to the prior period. You can see there is a swing of EUR 500 million. Clearly, in the prior period, especially on the P&C side, we had the impact of the natural catastrophe, but it remains that with EUR 3 billion operating profit for the quarter, we are at a very good level. And again, the net income has improved significantly compared to the prior period, and this is driven by -- especially by the increase in the operating profit of 20%-plus. So good picture also for the quarter, which is confirmed in the numbers that we saw also in the first half and especially in the second quarter 2018.

We can move now to Page 7, where we see the development of the shareholder equity and on the Solvency II. I'm going to focus more on the Solvency II capital quote, which is about 229%. It's very stable compared to the solvency ratio that we had in the end of last year and also the end of June. I'm going to come back in 1 second to describe the different drivers for the movement of the solvency ratio.

When you look at the sensitivities, pretty much unchanged compared to the sensitivities that we had as of June 2018. The only exception is the sensitivity to interest rates, which is now minus 7%, if you remember, the sensitivity was more like minus 10% in Q2, and the sensitivity was minus 7% in Q1. So we are going back to the level that we had at the beginning of the year. And that's because, as you're going to see later, we have a little bit longer duration on the asset side compared to the duration of liabilities, so we have a little bit of a higher duration gap.

If you move to Page 9, you can see what are the drivers of the development of the solvency ratio. First, we had a small change, impact due to the tax reform in the United States. And that's because, with the changes in tax reform in the United States, when you run the calculation, the RBC capital, we have less of a tax offset, if you want, in the capital charges, and this is increasing the capital charges. So that's about 1%, and this was also expected.

On the operating earnings, you can see on a pretax, pre-dividend basis, we have an improvement of the solvency ratio of 9%, which is pretty much in line with what we saw also in the prior quarter. There is one thing I'd like to draw your attention to, is the business evolution, which is now plus 0.2 in the last quarter. If you take aside the second quarter, where, I think, we had 0.1, usually, we will see more a number of 0, it's now slightly negative. The reason why we see a plus now is twofold.

On the one side is the P&C is growing. So as we grow the P&C premium, we can see also there is an increase in capital associated to that business.

And then on the other side is also the growth in Allianz Life is picking up. And also we will not include in the business evolution, the Allianz Life, in the past because Allianz Life is on an equivalent basis, but now we are including also Allianz Life in the picture.

Market movements had been very minor, so no significant impact at all coming from the market movement. And then on the capital management, actually, you can see the impact of our dividend and the buyback of EUR 1 billion the we paid in the third quarter. And then the tax and other is mostly explained by the tax position.

So the bottom line is, if you were to adjust our solvency ratio for the buyback, the solvency ratio of 229% will be 232%. And that will be pretty much in line, if you want, with what we would expect in the absence of regulatory change in the United States. So nothing really exciting happening with the solvency ratio and again, a very strong solvency ratio.

If you go to Page 11, you can see the picture for selected OEs for the growth rate in Property-Casualty. Again, we had a very strong growth in P&C with 6%. Now one of the drivers for the growth compared to the past is Germany, which is growing very nicely at 4%. And Germany is growing in personal and also in -- sorry, retail business, and also commercial business is going more to property. So it's a nice growth rate across the board.

Also, Italy, you can see is now positive, more than 1% growth. That has not been the case in the past. In the last year, we were still negative. And then slowly, we have seen a recovery in our production in Italy. So now we are at 1.4% positive.

Then you have the usual suspect, like Australia, Eastern Europe and Spain. And the negative -- the only negative that you see on this slide is the United Kingdom. And this is somehow associated to the transfer of business between us and LV. And clearly, as we are transferring our personal line business to LV, there is a little bit of slowdown in production. When you look simply at the commercial business, which is the core business of Allianz U.K., then you can see a nice growth rate of 4% on that business, too.

Then, finally, just a couple of words on AGC&S (sic) [AGCS] and Euler Hermes. You can see a growth rate of 10% for both entities. There is some seasonality in the case of AGCS. It's associated to the ART business. In the case of Euler Hermes, it's more associated to the way the accounting can work. But if you adjust for the seasonality, the growth rate in AGCS and Euler Hermes is about 5%, which is a good growth rate and also something that we have not seen for Euler Hermes in the past, too. So across the board, I would say nice growth rate, nice movement and nice increase again in the top line.

Coming to Page 13. On the operating profit side, you can see a nice improvement. And as I was saying before, clearly, this has to do also with the swing in natural catastrophe from 4.5% last year to 2% this year, but this is not the only driver for the improvement. You can see that the expense ratios also improved compared to last year.

On the other side, the run-off has been lower compared to the high run-off that we had in the third quarter 2017. And then we have also this very important improvement of the attritional loss ratio. So at the end of the day, the bottom line is better productivity, lower natural catastrophe and underlying improvement of the attritional loss ratio pushing the combined ratio to a very good level of 93.1%.

As you remember, we are 94% as of the 9 months, so we feel very confident at this point in time that we're going to hit our 94%. I had to put, as usual, a disclaimer about natural catastrophe. But for the time being, in the first 6, 7 weeks of the quarter, we didn't see any particular activity affecting us in a way that could make our confidence in the 94% less.

Coming now to Page 15. You can see on the combined ratio -- when you just look at the delta in combined ratio compared to the prior period, you can see a lot of minus sign, if you want. You have an improvement in Germany that is driven by a better expense ratio and also especially by lower large losses and weather-related losses compared to the prior period. We have a nice improvement in Eastern Europe, where we are continuing to improve our underlying performance. And on top of that, we had also lower large losses. Spain is also improving, and then I will say also, in Latin America, you can see that we are constantly improving our position there. On the company with a plus sign: Italy, just because of a slightly lower run-off but we are speaking still of a very, very excellent, I would say, combined ratio.

And now as we see, AGCS, that's an improvement clearly. You can see we had lower natural catastrophe compared to the prior period, but improvement in the combined ratio is less than the lower amount in natural catastrophe. And the reason for that is the reality that we had large losses and also weather-related losses this year, which were in excess of the large losses and weather-related losses that we had last year. So the bottom line is that AGCS is still running at a high combined ratio.

So last year, the reason was natural catastrophe. And this year, we are affected by large losses and weather-related losses. And still, we have a nice load, let's put it this way, coming from the natural catastrophe. The bottom line is, when you look at the segment, 93.1% combined ratio, so I think, is a very, very good level. And combined with the growth rate of 6%, I believe both the technical SLAs on the combined ratio and our commercial ability to grow the premium, in my opinion, are clearly coming through the numbers.

Page 17, investment income, as you can see, is pretty resilient. Indeed, the investment income in the third quarter of '18 is just -- is less than EUR 20 million lower compared to the prior period. So from that point of view, we see resilience in our operating investment results. I don't know if you remember the second quarter number, but they were also pretty resilient. So overall, we see more resilience in the numbers compared to what we were expecting at the beginning of the year.

And with that, I will go into the life segment. As you know, we have 3 targets -- Page 19. For the Life segment, we have given us 3 targets. One target is we like to have a new business margin which is above

3%. As you see, this is the case with 3.5%. And we have been kind of moving at this level for a while right now. The second target is that we want to have more than 80% of production in the so-called preferred products. And as you see, in the third quarter, we are at 84%. So this is confirming a trend that you already saw in the last quarters.

The third one also is we like to grow the revenue. And when you look at the present value in the business premium on the right-hand side in the table below, you can see there is an increase of about 12% compared to the prior period. So we also see a nice growth kicking in. This is explained by Germany, and this is not unknown. Germany has been growing now for a while, but we also see growth in Italy, which has not been the case in the first half of the year. And we see also nice growth in the United States, where we had a sales promotion on the fixed-indexed annuity side. So overall, I would say very compelling case from a margin point of view and mix point of view and also growth of revenue point of view.

If you move to Page 21, here, we showed the development of the operating profit, which is kind of stable compared to what we had last year. If you look at the waterfall, you can see the investment margin is slightly lower compared to the level last year. I'm going to come back in one second on this number. Otherwise, the expenses are higher, but that's just the consequence of higher production. And these are expenses -- we are not DAC-ing the expenses yet. The DAC calculation comes later. So clearly, as we see more production, we are going to have higher level of expenses. On the other side, loadings and fees and technical margin are both positive. So all in all, when you add up all the different components of the waterfall, you get to an operating profit which is relatively stable and especially with EUR 1,050,000,000 is exactly the outlook divided by 4.

I'd like to draw also your attention when you look at the Protection and Health, you can see that the operating profit went down by about EUR 40 million. And this is pretty much explained by a small loss recognition in the LTC business in the United States. I'm sure you're going to have a few questions later, so I'll leave this for the question. But at the end of the day, it's a very small amount of loss recognition in the long-term care business.

Page 23, you can see that the value of new business is accelerating to 16%, and that's clearly the consequence of -- to a certain degree, also of an increased margin, but in reality, it's mostly driven by the 12% present value of new business growth that you saw before. Overall, it's a very compelling picture from value of new business growth, I would say, across the board.

Now when you look at the operating profit just focusing on the 2 major OEs, Germany life and United States, you can see they are slight -- they are down compared to the prior period. But in reality, that's more of the normalization, if you want. If you compare those -- the numbers in operating profit for Germany life and U.S.A. to our plan, they are very much in line, I will say, or just slightly below what we would expect for the quarter.

So just to give you an idea, in the case of the United States, last year, the volatility was very low. This year, it's more normal. Then, we had the LTC impact. But still, at EUR 220 million operating profit, this is not far from what we would expect for a quarter for Allianz Life. So this tells you about also the resilience that we have in our operation.

And now coming to Page 25, that's the investment margin picture. As you see, the investment margin expressed in basis points is reduced by 2 basis points. And if you do the annualization, the 21 basis points, you get to 84 basis points, which is below the 90 basis points -- or 90 to 95 basis point guidance that we gave to you. And this is not the first quarter, it happened also, I believe, in the other quarter.

One of the reason -- the main reason why this is happening right now is because of the net harvesting and other, as you see, is now negative 3 basis points. And the reason for that is twofold. First of all, last year, there was a benefit because of the low cost in -- of the hedging. But the other reason is, in our investment portfolio in Europe, we also have U.S. dollar bonds, and we do hedging clearly for the FX exposure. And the hedging costs are going up. So this is dragging right now a little bit the investment margin.

Now on the other side, the aggregate policy reserves is going up by 5%, so the margin is coming down a little bit but the basis is going up. So when you look at the absolute reduction in investment margin,

in reality, it's pretty small. And again, we have other source of [program] which are picking up, like technical margin or loadings and fees. So the bottom line is that we are comfortably making our EUR 1 billion plus of operating profit per annum.

And with that, I'd like to come now to Asset Management. First of all, we had achieved the threshold of EUR 2 trillion of total asset under management. This includes also the assets managed for our operation. So I think that's more of a statistical information, but it tells you a little bit about the scale and size of our operations. And as you know, scale counts in Asset Management. It counts in every business but definitely counts in Asset Management. So that's a nice number to have and speaks also really for the quality of the franchises that we have built over the last years.

When we are focusing only on the third-party assets under management, you can see that there was a slight increase compared to the level of June. But especially, it's nice to see that we had positive flows at both PIMCO and AGI of about EUR 15 billion in aggregate. And so if you remember the second quarter, we had some negative flows, the first quarter was pretty strong. So you can see that, a little bit depending on the market volatility, we go from having positive to having negative flows. But in general, we feel very, very good about the resilience of our operation in a market which is not always easy.

Another question that's going to come: What is happening to the flows now that we're -- activity is picking up in the fourth quarter? We, in the month of October -- or let's say, quarter-to-date, flows -- net flows are down EUR 10 billion, which is not unexpected when you have this kind of volatility. We still believe, first of all, it's not really that significant, if you want, for the operating performance of our operation, considering the size that we have. And I personally still believe that increasing interest rates are a long-term positive. You might get some volatility in the short term, but eventually, when the volatility reduced, we are going to be even in better shape than we are now, and we are in pretty good shape right now. So I think it's just weathering the volatility for a few quarters.

Also, another information because I know you're always very sensitive on this topic. On the 3 and 5-year performance -- benchmark performance, PIMCO is over 90% -- 90% of the funds of PIMCO -- more than 90% of the funds of PIMCO are beating the benchmark. So when you have this kind of numbers, I'd say the quarterly volatility on flows shouldn't be of any concern.

Now moving to Page 29. Here, we have a very nice development, especially when you look on a quarter-over-quarter basis, of the revenue. It's about 10%. It's also driven, if you want, from the performance fees at AGI. But even if you adjust for the performance fees at AGI, the increase in basis fee is still pretty compelling. And now also important, as you see, our third-party assets under management margin is going up both at PIMCO and AGI. It's been relatively stable in reality over the last quarter. And as you can see, we don't see it's also squeezing margin because of all the things that you might be aware of already in the publication. So from -- in our case, we are still capable to keep new business margin stable or indeed, even to increase the new business -- sorry, the margin fee compared to what we had in the last year.

Moving to Page 31. The growth in profit is double-digit when you also consider for a little bit of a push coming from the FX effect. So it's nice growth in operating profit. If you look at the cost-income ratio, this is going up 60 basis points, but that's also because of the consolidation, if you want to call it that way, of ACP in our Asset Management. ACP, just in the case you don't remember that, is our -- is a company which is managing assets for Allianz and now is part of AGI.

If you adjust for the consolidation of ACP, then the cost-income ratio will be, for the quarter, flat compared to the level of the quarter 2017. You might be surprised it's flat. That's just because we have some one-off expenses at PIMCO, and then also, we are investing. So the point is we are investing at PIMCO in technology -- and also AGI in technology and marketing expenses. So we are also not only growing our profit, but we are also setting the foundation for further growth moving forward. So bottom line is EUR 650 million of operating profit is very good profit for the quarter with a very nice increase compared to the level last year.

Page 33, it's very exciting, so I'm sure I'm going to get a lot of questions on this page. And with that, I will move to Page 35. And here, you can see just the development below the line. In reality, there's

a little bit of noise in these numbers because of the impact coming from ASPI, which is Autostrade per l'Italia. The point, if you look at impairment, they look pretty high compared to the last year. This is mostly driven by the impairment on Allianz -- on Autostrade per l'Italia. But if you look down, you can see the noncontrolling interests are positive. And the reason is the majority of the impairment that we are showing here in reality goes to minority.

The bottom line is there is noise around the number. If you remove for the noise, clearly, the calculation would look -- the number, there is really not much happening below the line. And so from that point of view, when you look at the net income, you can see the net income is up more or less consistent with the development in operating profit after you take into account for taxes.

And with that, I come to the last page, 37. As you see and as I was saying at the beginning of the presentation, we are very good underway. And especially when you look at the KPIs that we are most focusing on, which is earnings per share growth, RoE, combined ratio in P&C, also our ability to get to a good RoE in Life/Health and new business margin, they are all going in the right direction. So we are pretty pleased with the performance that we have to date, and we are also confident for the remainder of the year.

And with that, I would like to open up to your questions.

Question and Answer

Operator

[Operator Instructions] We will take now our first question from Thomas Seidl from Bernstein.

Thomas Seidl

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

First question on German P&C where you have the strong growth and also amazing improvement in currency loss ratio, which I suspect is mainly [PFID] rather than pricing driven. My question is -- I'm hearing a lot that the German motor market, in particular, is more competitive. And so first question is, what is the outlook on Germany? Is it getting more competitive? Should we expect less growth and also some margin compression, especially in the motor space? Secondly, on life, I mean, when I look at the life operating results, there are 3 unexpected things: the hedging cost, the low level of realized gains and the low policyholder share. So maybe you can give some color on what is the normalized rate of this and also, how long should we expect this FX hedging cost to be at this level? And finally, I wondered -- I mean, you showed us the 9-month picture, and it looks nice, as you say. What would be the 10-month picture, including October? So how have investments of Allianz fared in the term and in October?

Giulio Terzariol

CFO & Member of the Board of Management

I'm not sure I understood the last one.

Thomas Seidl

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

Okay. The last one is simply October, the capital market volatility, how are...

Giulio Terzariol

CFO & Member of the Board of Management

Yes. So I'm starting from the German P&C market and the motor development and so on. What I can tell you is the combined ratio in motor for Allianz Germany improved and didn't deteriorate as of 9 months and also looking at the quarter. So at the end of the day, based on our numbers, I can tell you that the growth rate that we are seeing is not coming from compromising on profitability. So we've seen that we are in a good track, and now we're going to see what happens during the renewal rates. But the facts are that our combined ratio in motor in Germany is not deteriorating. This is getting a little bit better.

On the investment margin issue, I will say that the issue with the high hedging cost is going to stay for a while clearly. First of all, if you have higher volatility in the capital market, this is going to affect the -- for example, it will be the United States. And also, the hedging cost on the U.S. dollar portfolio that you want to hedge back in euro are going to be elevated. But the point is, in this kind of environment, we are able to do our EUR 1,050,000,000 operating profit. So I would say that this is what counts, and we feel pretty good about our ability to get to this number. And then, clearly, we are also going to look at whether we need to deploy different strategy if this kind of hedging cost, especially on the U.S. dollar bond portfolio that we are hedging back, is available performance that we would deem as not adequate. But we feel pretty good overall about the resilience of our profit in life. So I'm not concerned at all about what is happening there.

The third question was how October looks like. Maybe you are referring to whether we had some major natural catastrophe or this kind of things. No, I will say that -- I would even tell you that I believe we are running slightly below the budget. So from that point of view, there is nothing that will particularly be -- there is nothing right now. Now as you know, December can always be kind of interesting, especially in Germany and also in Europe, but for the time being is -- yes, it's very, very calm. On the investment performance, because Oliver is telling me this was your question, I wouldn't say there was anything special in October compared to what we have been seeing in the last months.

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

And on German P&C, my question was also more on the outlook. You said the renewal phase is coming. Should we expect more competition? Or what is the outlook for Germany?

Giulio Terzariol*CFO & Member of the Board of Management*

I will say I believe the motor market is always competitive. So I don't think there is -- that competition is -- if the core capital is growing, that's totally welcome, yes.

Operator

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

Michael Igor Huttner*JP Morgan Chase & Co, Research Division*

Three questions. One is what would solvency be now? And the second is, the -- if I look at the bigger picture, you have these big budgets for digital and maybe IFRS 17. I just wondered as you see those developing whether they would put your nice trend of falling costs under pressure. And the third question, you explained at PIMCO that rising interest rates ultimately is positive. Can you maybe shed some light and say what would be a kind of crossover point? How have you defined it, short term pressure versus long term?

Giulio Terzariol*CFO & Member of the Board of Management*

So if I got your first question was about what is the Solvency II now. That was the first question? So like -- I would say, as of October, I would explain Solvency II, from a market movement point of view, to be unchanged. And then, clearly, we had the business evolution kicking in. The point is there was a widening of the credit spreads in Italy, so they will be, if you want, negative. But we are underweight at Italy compared to the EIOPA portfolio. So from that point of view, since we have like a basis issue between -- or advantage between what happens to the EIOPA reference portfolio, credit spread widening in Italy doesn't affect us so much. And on top of it, right now, if the spreads are staying at the level they are, the country VA will be triggered. So in reality, we might even have a positive impact as of now from the change in credit spread. But if you ask me, I will say let's call it a neutral impact, so no kind of issue now with Solvency II because of the credit spread widening. And also, very important for you to know, at the end of the day, when we are 20 -- 230% solvency ratio, a couple of percentage points more or less in the solvency ratio doesn't really make a big difference. But solvency is very strong, and we don't see anything affecting that in a substantial way because of the market movement as of now.

The other question was about IFRS 17, and you're asking me whether this is going to have a cost impact on our group. Clearly, we are paying this money. But we are a huge organization, and if we are not capable to absorb the cost of implementing IFRS 17 and 9, I will be very surprised. So from that point of view, sure, we need to also set priorities. If we are implementing IFRS 17, we are not maybe going to do other things that we would do also because of the resource issue, motor and other cost issue. But this is definitely not something which is changing our -- can have any kind of impact on our profitability. So that's not an issue at all.

The final point was on the PIMCO. Now your question about the crossover, I cannot clearly answer you in a -- give you a number. But at the end of the day, it's very simple. When rates go up, clearly you can see a drying up of the flows. Just to give you an idea. If you had EUR 10 billion less of flows, for example, on a run rate, assuming you do nothing, that would be mean EUR 20 million less profit for -- run rate for annual profit. Then you might see a little bit of -- clearly, when you see an increase in the insurance rate, the asset basis can go down. So you can -- if you want to look at it that way, you could also say that an increase of 50 basis points, considering lower flows and a change in asset base, can make about EUR 50 million less operating profit on an annual basis, assuming you do nothing. And I will say this is very easy

to recapture once the situation stabilizes because you get the flows back very quickly and assets under management are getting higher crediting. That's the reason why I strongly believe that the short-term reduction in operating profit, assuming you do nothing, by the way, can be easily compensated on present value terms but expectation that the business is becoming more appealing once the rates are up. And those accruals that you have on the assets under management, and thinking about the amount of assets under management we have, is going to be stronger. So for me, it's a clear positive once rates go up, but clearly, first, you need to go through some sort of volatility.

Operator

And now our next question is from Peter Eliot from Kepler Cheuvreux.

Peter Eliot

Kepler Cheuvreux, Research Division

Three questions, please. The first one, just on expenses again. I mean, Michael was asking about future costs. But if I look at your current ratio, which is obviously very good again this quarter, you'd said at Q2, I think, that we might get a bit of sort of relaxing of discipline since the target was sort of in the bag, but we've seen quite the opposite. I'm just wondering if you could sort of say -- to what extent do you think this is a sort of normal level? Are there any one-offs in the short term? Is there any reason that this should or shouldn't continue? Then second question on life. I mean, since you invited the questions on long-term care, I would give you the opportunity to talk about that. And perhaps any comfort -- I mean, it doesn't seem a very big number, as you say, but is there any comfort you can give us that that's fully put to bed? And then maybe finally, just on your investment strategy in general. I'm just wondering if there's sort of any change in view at all, even at the margin, in terms of where you like to put your money? I mean, obviously, alternative investments in infrastructure being a big focus. I guess, we had one unfortunate event over the summer. But just generally, whether there's any sort of change in strategy there at all.

Giulio Terzariol

CFO & Member of the Board of Management

So very good. So let's start from the expenses. I mean, what I meant in the second quarter was not that discipline is going to reduce. We are totally focused on expense productivity, expense management. So this is going to stay, and this is going to stay for a long time. The point I was making, usually, especially towards the end of the year, in the last quarter, you might have the accrual kicking in because as much as you try to do accrual over the year, you have accrual kicking in overproportionately, if you want, at the end of the year. And also, a lot of marketing activities can take place at the end of the year. So there's no -- and also, clearly, when you have such a focus on expense ratio, companies are going to be -- they want to be very sure that they can meet their target. But I wouldn't interpret that as we are disciplined, then we take the discipline out. It's more sort of natural development that you might see. So the discipline is going to stay.

I can give you an idea. By the end of the year, I believe we have a target of 28.4. I'm pretty confident at this point in time that we are going to beat the 28.4. If I shall give you a guidance, I will say, at this point in time, it may be even 28.2. But I don't want -- it's very difficult to predict a number to the 10 basis point. But we feel that we should be able to beat our target significantly. And then, clearly, we want to get better as we move into 2019 and 2020. So the idea, as we discussed several times, is to get a productivity improvement year after year and not to have just a big one shot and then we go back maybe the year after in the other direction. So that's the way we look at productivity improvement over time.

The other point was about the LTC business. Okay. First of all, I will give you some numbers so that you have a little bit of an idea what we are talking about. On a gross basis, we have about EUR 4.5 billion of reserves. When you look, in reality, at what is the net, so what is our retention, if you want, because we have a huge reinsurance program, we have about EUR 1.3 billion which is retained. This is also very important. The part which is reinsured is a business before 2002, so -- which is indeed a business which was more challenging because it was a time -- a point in time where the market realized that LTC was not pricing properly. So all the business which is before 2002, in reality, is completely reinsured. The business

after 2002, which is not necessarily profitable but is definitely way better compared to the business before 2002, in this case, we have -- on that business, we have a reinsurance which is about 20%. So it's mostly all retail. So what we do -- in reality, we do this every year.

We go through a review of the assumption. So we review the morbidity, mortality assumption. We also review what is improvement that -- or deterioration that we assume in this assumption. And this year based on the statistics and analysis that we got, we determined that we had to change the gross premium valuation -- or the gross premium valuation change to a level because that was changed also in the past, but now we change to a level that this trigger loss recognition, which is about a little bit below EUR 40 million. One thing to keep in mind, we have the ability in the United States to increase tariff. So as we're going to look at what happens in the future, and we might also see deterioration in morbidity and mortality in the future, we have also some ability to compensate future deterioration through rate changes. So at the end of the day, based on the analysis, we determine that there was a necessity to increase, if you want, reserve by about -- a little bit more than EUR 30 million. And I would tell you it's, from my standpoint, is a very small amount and I was hinting to that before. So the operating profit of Allianz Life for the quarter has been pretty much in line with plan. So this tells you that even at Allianz Life level, the ability to sustain such kind of impact very easily from Allianz group point of view, honestly speaking, this is a very -- think about a big claim in P&C can be -- easily be EUR 40 million. So I will say, for me, this is really nothing to be concerned about. There was another question? The investments, sorry. The last question, investments -- no, we're not really changing our strategy. As you know, we have a strategy anyway to increase the allocation to alternatives, which was about EUR 110 billion in 2017. We want to go all the way up to EUR 150 billion. So we are continuing in the next few years. So we are continuing with this strategy. Otherwise, from asset allocation in a sense of how much equity we have, fixed income, we are pretty much staying in the core. So there is no -- we are not going to change our strategy based on some volatility we might have at a certain point in time in the market. Because clearly, we always take a longer-term view, and especially we position our portfolio based on the level of what kind of level Solvency II we have, what kind of sensitivity in Solvency II, this is what is driving our strategic asset allocation. Clearly, we can always say some tactical adjustment, but this tactical adjustment are not necessarily changing the big picture.

Operator

And now we will take a question from William Hawkins from KBW.

William Hawkins

Keefe, Bruyette & Woods Limited, Research Division

I'd like to come back to Thomas Seidl's question about the investment margin on Slide 25. In the past 18 months, the shareholder share of the gross margin has risen quite significantly. Prior to that it had been stable in about the mid-30s. And now it's in the high 40s. Can you just remind us why that's happened? And what does it mean for the future? Do we expect the current level to stay? Or could it be rising or falling? And then also, your published remarks in the slide presentation implied the investment margin could be improving in the fourth quarter to hit your 90 basis point target. But when you're answering Thomas, you sounded appropriately more cautious about the ongoing hedging costs. So I'm just wondering is there another positive that offsets that, that makes you optimistic in the slide comment? Or should we treat that with caution? And then secondly, can you help me on the growth on P&C? It's very clear that you're proud of the 6% growth, and that's very good. But I spent a lot of time learning that growth in non-life can be the #1 warning signal for the outlook for profitability. I know the current combined ratio is great. So what would you recommend that I look at on a forward-looking basis to say, "Yes, this growth is good-quality growth," rather than you're storing up problems for the future?

Giulio Terzariol

CFO & Member of the Board of Management

Okay. So the first question was about the margin, right? So we don't necessarily see the trend that you are describing. But maybe -- because when we do our calculation now what is the policyholder sharing, we at the minimum guarantee the profit share and divide it by the total yield. And when we do this current calculation, we don't see necessarily the trend. I understand based on what you said, maybe you're

doing the calculation profit sharing over gross investment margin. If you do that kind of calculation, then, clearly, you're going to see a little bit of different trends, because -- but that's almost mathematical issue. So the way we do the calculation, we look at the total yield, and then we sum up minimum guarantee and profit share. And I think that's the best way to look at. If you look your way, by definition, as there is some compression between current yield and guarantee, once you keep the total participation cost, then automatically you're going to have, based on the calculation, you do a little bit of a compression. But it's just a matter how you do the math. When we do the math in the sense of, that's the total yield and this is how much we're giving to the policyholder from a guarantee plus profit sharing, this number is pretty consistent. And I will say that's also the way I would look at the number. But the implication is, yes, you are somehow giving less profit sharing to the policyholder, if you want. But you're not giving less of the pie in total. You got my point?

William Hawkins

Keefe, Bruyette & Woods Limited, Research Division

I think so. I might come back offline.

Giulio Terzariol

CFO & Member of the Board of Management

So that's one. On the other one -- the 90 basis points. I will be a little bit cautious on that point of view because I don't think that we're going to necessarily reverse the trend in the fourth quarter. This said, I -- the point is, how do we feel about so getting to our EUR 4.2 billion outlook? We feel pretty good about that. But from a pure investment margin point of view, yes, I will be a likely kind of cautious for the fourth quarter. That's also important to me. That's not really our target. Because honestly speaking, if there will be a target, we can get to the number, that's more a guidance. That's how we try to explain how our numbers are coming up together, but I wouldn't define that as a target. Because if we start defining that as a target, we can make the number. But then we go into the conversation about how we are treating the policyholder, all this kind of things. So I would say it's a guidance as opposed to be a target. It's more explanatory number as opposed to be a target. And in the other point was on the growth in P&C. I think I have good answer for the first part and less for the second. I don't know what to give you to look up from your standpoint to whether the growth is good or not. We, clearly, internally, we are very aware that if you're chasing the wrong customer, this can be very costly. So we are very much focused on looking at what kind of business that we're taking in. We can definitely look at the accident year performance. We do analysis also with our trial team in muni. So we internally we have a good view on the kind of growth we are getting. And clearly, we are always very cautious about looking at this number. What I can give to you to look at that, I will say, I -- unless I start sharing with you our internal information, that will be very, very difficult, yes.

Operator

And we will now take a question from Andrew Ritchie from Autonomous.

Andrew James Ritchie

Autonomous Research LLP

Just first of all on P&C. I'm not entirely clear, was the man-made large loss experienced in the discrete Q3 above expectations or -- above long-term expectations or about in line? And just related to large losses, there were quite a lot of large losses man-made in the market, but it doesn't seem to have a particularly affected your result. I understand you have very low per-risk retention. Is there additional man-made aggregate protection in place? Or some other additional protection on man-made losses? Second question, on Italy. I appreciate the impact of spread widening is minimal at the group level, but clearly, it won't be at the Italia -- Allianz Italia. That business has paid pretty decent dividends to the group in recent years. At what point would there be an issue, do you think, about continuing to withdraw a decent dividend?

Giulio Terzariol

CFO & Member of the Board of Management

Yes. So starting from the large losses. I will say our experience in the third quarter was a -- and we have also commented somehow, was slightly above what we would expect normally, but I'm not speaking of a huge deviation, but there was, I would say, some kind of deviation. In the sense of what we do from reinsurance point of view, I wouldn't say that we have a particular program, but we have a EUR 150 million reinsurance protection excess of EUR 150 million, and that's what we're doing. But I wouldn't say that we have a particular protection that we buy on man-made from a reinsurance point of view. So I think it has more to do with the underwriting discipline. And maybe the retention that we have really at the -- because what I'm referring to is a sort of reinsurance program group level. And then clearly, you have a kind of retention you take at the local level on single risk that you are underwriting. So from that point of view I'm sure...

Andrew James Ritchie
Autonomous Research LLP

You mean gross retention so there is 2 levels of protection, one is the reinsurance where you're taking a relatively small lines, it sounds like.

Giulio Terzariol
CFO & Member of the Board of Management

Yes, that's the point. Yes, that's it.

Andrew James Ritchie
Autonomous Research LLP

So the variable or the experience was average, more or less?

Giulio Terzariol
CFO & Member of the Board of Management

Slightly above what you would expect. But -- I would say close to average or slightly above what we expect in a quarter, but nothing substantial more than that, yes. The other question was about Italy and the dividend, right? So clearly, as you have increase in spread, it's going to have an impact on the Solvency II level. But from a dividend point of view, we see also when we put the plan together, the dividend plan is not affected by that. If you have then -- and that's assuming there is no change in a country VA. Clearly, there is a reduction in excess capital. So from that point of view, if you have some nice idea about excess capital upstreaming, that can be a little bit reduced, but the dividend is a different, different story. Now that's the beauty when rates are going up, there is a point where you get in reality the country VA. And this would even create excess capital. So from that point of view, it depends on where you are. It might be a little bit of dampening on excess capital repatriation. Or it can also be that this dampening on excess capital repatriation is removed. From a stable dividend point of view, I will say at a point where we are right now we don't see any impacts on the expected amount of dividend. So there is a little bit of a hedging, if you want, because of the VA -- country VA.

Operator

[Operator Instructions] We now take a question from Nick Holmes from Societe Generale.

Nick Holmes
Societe Generale Cross Asset Research

I wanted to ask, with U.S. Life, how comfortable are you with the very high growth in fixed index annuity products in the U.S.? I ask because these aren't really capital-light are they? Or you do you disagree with that? And then secondly, another one on U.S. Life. Do you have any thoughts about the new FASB changes to U.S. GAAP? Will they make U.S. Life reporting more volatile, do you think?

Giulio Terzariol
CFO & Member of the Board of Management

Maybe I'll start from the second one. In reality, we don't need to submit U.S. GAAP anymore because we have talked to the SEC, and we can per our filing and we have a special filing for some products. We can use statutory accounting. So from that point of view, that's not an issue for us. We have been working for many, many years. Indeed, I was still in Minneapolis when we tried to get the statutory accounting instead of the U.S. GAAP to be utilized. And now finally, we've been able to get this approval from the SEC. So U.S. GAAP is now going to be irrelevant, if you want for us. And by the way, even in the past since there was just the filing it was not really something we were using for performance measurement, and it's not relevant from solvency point of view. In reality, those numbers were not really impacting our decision-making. But anyway, right now, we don't try to submit any U.S. GAAP moving forward. On the business and the FIA business, I feel pretty comfortable, obviously, about what we're doing there on the FIA side. Your question whether they are light or not, I would differentiate. From an economic point of view, they are capital-light products. There is no doubt because the level of guarantee is so low that if you run an economic calculation, you can see that there is not much capital required. That tells you even more. That's something that we can see the modeling we are doing now. You can see -- we can see this even when I joined Allianz, I will say, 15 years ago, on an economic model, the kind of product is very light. From a statutory point of view, it's a little bit of a different story. Then from a statutory point of view, I'll say, yes, you have some capital intensity. On the other side, the business is so large now, and the in-force profitability is significant that you know there is enough capacity to produce profit on the in-force to also absorb what could be the impact on the requirement because of the growth in the business. And then I always like to say, as long as you price at an RoE which is above IRR, which is 13% unlevered, honestly speaking, I think is a good business to put in your book. So when I say it's economically capital light, from a statutory point of view, I wouldn't define this as capital-light, but we are pricing at a nice RoE. And so I think it's a good business.

Nick Holmes*Societe Generale Cross Asset Research*

That's very interesting. Can I follow up just with one quick question, which is could you remind us what the guarantee actually is in basic form? Because, I mean, they get quite complicated, don't they? I'm not quite sure where you are with your latest products.

Giulio Terzariol*CFO & Member of the Board of Management*

Okay. When you look at the crediting, that guarantee could be 20, 30 basis points. So it's really low. Now you can run a calculation where you can assume what happens to the -- you have the withdrawal payments and what happens to, in the case, no policyholders are going to lapse and you put a mortality assumption, that case you're going to get closer to, I will say guarantee, which is about 1.5%. But that what I will say could be an implied level of guarantee. In the case, you're assuming really there's no lapsation, nothing, and then you need to make an assumption about the mortality of people. And then you can say there will be the maximum level of guarantee.

Operator

We now take our next question from Vinit Malhotra from Mediobanca.

Vinit Malhotra*Mediobanca - Banca di credito finanziario S.p.A., Research Division*

Two questions, please. So firstly, just on the -- just focusing on the P&C growth, which is, of course, amazing number. What I noticed is that the Euler Hermes for example, after the minority buyout, there's been a really strong pickup in the Euler Hermes. Now what I'm trying to understand is that is this growth just because some of the competitors of yours are distracted either in global lines or with their regional markets? Or -- and you are in a stronger position so you can push, pull? Or do you think it's just that the business is -- the economy or some other effect, so just want to understand how much of the growth is because you seem to be in a stronger position. And the Euler Hermes for just an example, but if any comment would be great. Second thing is that on the Life side. Again, I'm just curious about one thing. The target of preferred products, for example, capital-efficient products, the target for new business is

being met, the 80% or so. But the operating profit of the capital-efficient product, as an example, is quite sort of stuck in a very -- like EUR 200 million range for several quarters now. What should we think about -- is it that the new business value growth of 16% is going to ultimately help the Life earnings in future? Or how should we think about this given the sort of stable capital-efficient product profits operating level?

Giulio Terzariol

CFO & Member of the Board of Management

From Euler Hermes. I'm going to make a joke now. The difference between now and before, before the company was listed. So management has to do a lot of conference calls, and now they can focus on running the business. That's just a joke. No. The reality is that the economy, definitely the economy is helping. The economy is pretty strong, and so from that point of view, this is helping definitely the business, also the franchise is pretty strong. But I wouldn't say that because of getting -- the rating has been upgraded that's also -- I think there was also an upgrade in rating as we did the transaction. So all these kind of things are helping, but clearly, the economy has been definitely also helping the performance on the top line of Euler Hermes. In the case of the capital-light products and the operating profit development is a fair comment, and the point is -- but you're going to see the number is going to pick up. In reality, what is happening right now on the capital-light products that we are writing in Allianz Germany, we're not getting a lot of profit. And if you want, this is also a -- it's part of a function how the accounting works and it's also part of the function how we do the allocation of profit between, if you want, the different segments. So from that point of view, I would even say that we are most likely a little bit understating what the amount of profit could be on that line of business. Over time, you're going definitely to see that the performance coming from Germany and the capital-light products is going to kick in, and then you're going to see more substantial numbers in that line of business. So just a matter of be patient. The numbers are going to come through -- they are going to become invisible.

Vinit Malhotra

Mediobanca - Banca di credito finanziario S.p.A., Research Division

And just on the broader topic of growth and competition, is there some element of you being able to push harder because you're in a stronger position than peers or something like that that you can see?

Giulio Terzariol

CFO & Member of the Board of Management

You mean, in general, or...

Vinit Malhotra

Mediobanca - Banca di credito finanziario S.p.A., Research Division

In P&C. So because the fact that your -- with your 5, you grow 6% or whatever, that kind of range, for 3 quarters now. So it's quite remarkable.

Giulio Terzariol

CFO & Member of the Board of Management

Yes. If you look in the past, we were -- and you were growing at 3%. So it's not that we're growing at 0. And now we are really a few companies who -- which are performing better compared to the past. So if you take Germany from 2% to 4%, this makes a difference. If we take Italy from negative to positive, this makes a difference. Also think, in general, the economy is somehow stronger. So there's also some lift that you get on the P&C side. So I will say it's a combination clearly of, in general, some more momentum. And then we are getting few companies to perform at the different level compared to how they were performing before. And then the other companies are also pushing a little bit stronger. So it's usually when you get combination of everything going in the same -- in the right direction that you get to this kind of growth rates.

Operator

And now we take a question from Farooq Hanif from Credit Suisse.

Farooq Hanif*Crédit Suisse AG, Research Division*

On German combined ratio, you had a 4-point improvement on the attritional loss ratio. You made the comment that it's kind of lower weather-related claims and losses. But I just kind of want to know what proportion of that 4 points is that? And how much of this is kind of the improvement of pricing? And how much of it is temporary? And then second question on capital generation. Solvency II, that's tracking better in the quarter, and I suspect it's helped by both P&C and by Life new business. I was wondering do you think third quarter is a good reflection of how it may continue? That's it really.

Giulio Terzariol*CFO & Member of the Board of Management*

Sorry. On the Solvency ratio question, was weather on the business...

Farooq Hanif*Crédit Suisse AG, Research Division*

Capital generation -- yes, was very strong.

Giulio Terzariol*CFO & Member of the Board of Management*

Yes. I would say -- yes, I will say, when you take the 9% and you remove dividend and taxes, we are at about 3%. So I will say, broadly, this could be also an expectation for the future. We know our guidance was about 10% per annum, so -- but now I will say this is somehow the guidance that I would still keep in mind. So it's about 2.5% per quarter, that could be the expectation that we have moving forward. So we're not really changing what we said at the beginning of the year. And that's the other question was on the German combined ratio, loss ratio. One quarter of improvement or the 4 percentage point improvement is driven by attritional. And I would say 3 quarters driven just by weather-related large losses.

Operator

And we now take a question from James Shuck from Citi.

James Austin Shuck*Citigroup Inc, Research Division*

Three questions from my side, please. Firstly, just thinking about how you communicated around the outlook around expenses, because I think you've acknowledged that structurally expenses need to come down quite significantly, and particularly in P&C I'm really referring to. I guess I'm kind of just want to think about how you manage the kind of reduction in the overall combined ratio and balance that with the growth outlook. As we've talked about quite a lot on this call, you're growing closer to 6% you previously guided in most of your outlook statements for kind of 3% growth. So clearly, a step-up. I just wanted to get a feel for how you think about managing that combined ratio in the context of growth. So is the scope for the 94 still to be driven down and grow? Or how do you manage those 2 things? Second question, as you alluded to, there are some companies that are performing on a different level. Spain, CE, Germany, Italy, all looking very good and showing good signs of productivity gains, which is what you've been targeting. I guess, from here, what are the next lines of businesses and territories that we should keep an eye on? Which are closest to really delivering? Is it really about finding a key to each market? Or are you starting to leverage the scale of the group more effectively? And which are the areas we should keep an eye on? Final question, just around AGCS, really. I mean, strong organic growth in the period. I guess there's a lot happening in terms of specialty at the moment, some players are adopting more of an integration insurance, reinsurance, strategy. What would kind of a greater alternative capital capabilities and perhaps a bigger third-party reinsurance business, what would that actually bring to AGCS? Is this organic growth that we're, is it genuinely sustainable? Or is AGCS going to get left behind a little bit over the medium term?

Giulio Terzariol

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CFO & Member of the Board of Management

Okay. So starting from -- the question was about the expense ratio, our view with that and combining with growth and all this kind of consideration. First of all, clearly, we want to reduce the expense ratio. We don't want to reduce the expense ratio at the cost of investing in the business, if that was your question. Because I tell you, we can get to an expense ratio which is way lower, very quickly if we decide to compromise on building up the business for the future. So that's the challenge, if you want, is really reduce the expense ratio and still find ability to accommodate growth initiative. But we are setting as a goal that -- by doing both we still want the expense ratio to go down. But clearly, if we were to focus only on reducing the expense ratio without any consideration for invest in the business, then we could bring this number down very, very quickly. In the sense of how we are looking for -- to the combined ratios for the future, I would say, for that anyway we can -- I'm sure you're going to come to the capital market day, so on that one, we are going to provide guidance, but you can imagine that we will like to get better compared to where we are right now. But for more guidance come to in the capital market day where we're going to give you more specific input on this issue. And then the other one was on the P&C, how we look at performance and what we should be looking at. In reality, I would look at everything because -- I just give you an example. Even in Spain where we have a very good performance, and you were mentioning that, they are still getting better, and we still believe we can get better even on the expense ratio. And what we are doing right now, we are doing also a lot of benchmarking where we are moving from benchmarking as to the average of the market, and we are going for the so-called best in class. So when you do these kinds of things, you can get performance improvement almost in every organization. Clearly, depending on the quality of the organization, you might have more or less of a performance improvement, but I believe that there's the still a potential to get better. Also, as stated, there are some segments where our profitability has not been as good as other segments. I'll give you an example, mid-corp, where we are now putting a lot of effort to get a better profitability. And based on the plan that we are discussing right now, we see also better numbers for the future. So the franchise is very strong. This doesn't mean that we are perfect, right? So there's definitely always the possibility to get better results. And by the way, since you were mentioning AGCS, that's also definitely a company where we can get better than 100 for combined ratio, just to look at the numbers. So think about that we had this quarter a 93.1 combined ratio for the group, even if AGCS was a 104. And you can imagine what would be if AGCS would have had a combined ratio of 96, just to put a number there. So there is room for improvement. On your question about the alternative capital this kind of thing, I'm personally not a big fan. Every time I'm thinking about alternative capital, Bermuda, I see low RoE, volatility, interest payments kind of financial engineering. So from that point of view, it's not necessarily the kind of business that is -- will be on top of my list as I think about opportunity. This said I will never say never because there can be exception. But if we are just looking big picture, I'm not waking up in the morning thinking we need to do some alternative capital in Bermuda.

James Austin Shuck*Citigroup Inc, Research Division*

And likewise, kind of no real plans to accelerate the growth of third-party reinsurance and folding that within AGCS?

Giulio Terzariol*CFO & Member of the Board of Management*

Not really. So we'll do some third-party reinsurance definitely, and also profitable, but we don't have a place now to do substantial more compared to what we are doing now. So we'll continue with the strategy that we had in place, so we do it, but not big plans to make big changes there.

Operator

[Operator Instructions] We now take a question from Michael Huttner from JPMorgan.

Michael Igor Huttner*JP Morgan Chase & Co, Research Division*

It was really a very, very lightweight question. What -- you were talking about guarantees and stuff, and I just wondered whether you can say what the average guarantee is now for your life book and what it was before to give a feeling for it? I'd like to think of other question but I have nothing.

Giulio Terzariol

CFO & Member of the Board of Management

So maybe the way to answer the question, if you -- when you look at the 49 basis points, and then you can pretty much annualize that, that will be potentially, from an IFRS point of view, the kind of average guarantee. This is not necessarily economic. So this is not necessarily economic guarantee, to be perfectly frank. But from an IFRS point of view you could say this is the kind of guarantee that is embedded in the calculation. And so it's about 2%.

Michael Igor Huttner

JP Morgan Chase & Co, Research Division

About 2%. And how much is this down -- or how quickly is this coming down?

Giulio Terzariol

CFO & Member of the Board of Management

You see, for example, a few years ago, just 3, 4 years ago, it was about 2.5%. So it's coming down consistently. If I look at it -- because sometimes it's easier when you look at the book by book, when I look at Allianz Leben book, the number is coming down, I believe, 20 basis points per annum. So then you need to also consider different kind of mix that you might have as different countries come in. But when you look at the development in Allianz Leben, for example, you can see that the guarantees are up significantly every year.

Operator

And our next question from Michael van Wegen from Bank of America Merrill Lynch.

Michael van Wegen

BofA Merrill Lynch, Research Division

One quick question. On the long-term care book, the assumption change that you've made, are you still assuming morbidity improvement? Or has this now been changed to a stable level? Reason why I'm asking is that a number of the U.S. players have made this adjustment as the NAIC is looking into this. So just wondering whether that is already part of the EUR 36 million or might still be coming?

Giulio Terzariol

CFO & Member of the Board of Management

We have also looked at that, and we also made change to that. So we have changed the assumption that we see right now based on the experience that we see right now, but we have also changed somehow what could be the morbidity improvements implied for the future. So we looked at both and we made a change to both. And so now we're going to do anyway, and we have been done this every year, and we're going to continue to look at what kind of information we get. And again, as I was saying before, we have the ability to increase rates. And then we need to see how these 2 things are going to play out as we go through the next years. But we are looking at all assumption. We've been changing all assumptions. So we have to experience...

Michael van Wegen

BofA Merrill Lynch, Research Division

Sorry. Are you still expecting an improvement in morbidity, though, at this stage? Or no longer?

Giulio Terzariol

CFO & Member of the Board of Management

Yes, we still expect some improvement. We didn't remove completely the improvement in morbidity, but we have reduced the amount of improvement that we might see in the future.

Operator

And now we take a question from Michael Haid from Commerzbank.

Michael Hermann Haid

Commerzbank AG, Research Division

Just one question from my side. On P&C, the expense ratio reduction, 80 basis points. You say that 30 basis points come from admin and 50 basis points comes from acquisition expense ratio reduction. Is there a reason why the -- what is the reason why the acquisition expense ratio reduced? Admin is clear, but acquisition expense ratio comes a little bit surprising. Any one-offs in there?

Giulio Terzariol

CFO & Member of the Board of Management

There is -- yes, there is also we did something in Germany on the acquisition side, but -- on the commission side, so this has also an impact there. And if you want to a certain degree for the quarter it's also, let's say, there is a little bit of one-off. But the point is, when we speak of acquisition expenses, in reality, acquisition expenses is not only commission. So we have administrative expenses and the acquisition expenses going to be the sum of commission and all the kind of expenses in the company, which are related in any way to acquiring the business. So in reality, you have also a large component, if you want, of expenses, which are similar to what in the nature of being fixed versus variable, they're similar to administrative expenses. So you need to keep in mind for that. Other point, and that's always very important -- that's really important to me, when you look at ratio of Allianz, considering the mix, you just need to have a little bit more of the growth -- especially on a quarterly basis, you just need to have a little bit more growth in a company as opposed to the other. You're going to have a different commission mix. So you should be always very cautious, especially when you start comparing 10 basis points up and down because that can be -- we are spending a lot of time, I tell you, in analyzing our numbers in and out. And it's very interesting when you start looking at the numbers and you start removing what is the impact on reinsurance, what is the impact on mix, then you can see how you might have a change in expense ratio, 10, 20 basis points, which is just driven by a different mix and has nothing to do in reality with productivity improvement. So always take this number with some sort of look at the trend over time, look at the magnitude, but don't overemphasize 10 or 20 basis points, especially in the quarter.

Michael Hermann Haid

Commerzbank AG, Research Division

Yes, absolutely. Also, I would say 50 basis points is quite a lot, but nevertheless. What is the issue in Germany?

Giulio Terzariol

CFO & Member of the Board of Management

We did some change to the commission, and that's what we did in Germany.

Operator

And we now take a follow-up question from Vinit Malhotra from Mediobanca.

Vinit Malhotra

Mediobanca - Banca di credito finanziario S.p.A., Research Division

Just one thing that struck me, I didn't ask earlier, the PIMCO outflow of EUR 10 billion you pointed out in October, is that you think just the volatility effect or rates effect? Because rates haven't -- is not that big. And it's important to understand your thoughts on this because rates are here to probably stay longer up, but volatility could even vanish or change. Just wondered what you thought between these 2 factors.

Giulio Terzariol

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The EUR 10 billion is just the volatility on the inflows. But remember this -- last quarter was positive. The second quarter was negative. You can see this kind of volatility. And the second quarter was negative because of the volatility that we had in February, March. But that's just flows. So as you, clearly, when investors have an expectation that rates are going up, they're going to wait a couple of months before they start putting their money into a bond fund. That's all what's happening. People take a position and they say, "Okay. [Let me wait that] rates up." And then they're going to start investing. So the EUR 10 billion was referring to is simply lower flows, and it's not to do with the change in the asset basis. That was your question?

Vinit Malhotra

Mediobanca - Banca di credito finanziario S.p.A., Research Division

Yes, I was just wondering between volatility and rate expectation, which is the bigger driver of the EUR 10 billion. It looks like volatility at the moment.

Giulio Terzariol

CFO & Member of the Board of Management

Yes, it's volatility. Yes. For me, definitely volatility. Yes. But it is driven by the fact that interest rates are going up. This movement is driving some volatility in the flows on a quarterly basis.

Vinit Malhotra

Mediobanca - Banca di credito finanziario S.p.A., Research Division

Yes. And referring to the volatility in the market, yes.

Giulio Terzariol

CFO & Member of the Board of Management

Yes.

Operator

As there are no further questions at this time, I would now like to hand back to Oliver Schmidt for any additional or closing remarks. Thank you.

Oliver Schmidt

Head of Investor Relations

Okay. Thank you, Stephanie. Yes, thank you -- thanks to everybody for joining the call, and thank you for your interest. We wish you a very pleasant weekend and say goodbye for now.

Giulio Terzariol

CFO & Member of the Board of Management

Bye. Good afternoon.

Operator

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

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