S&P Capital IQ

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Allianz SE DB:ALV

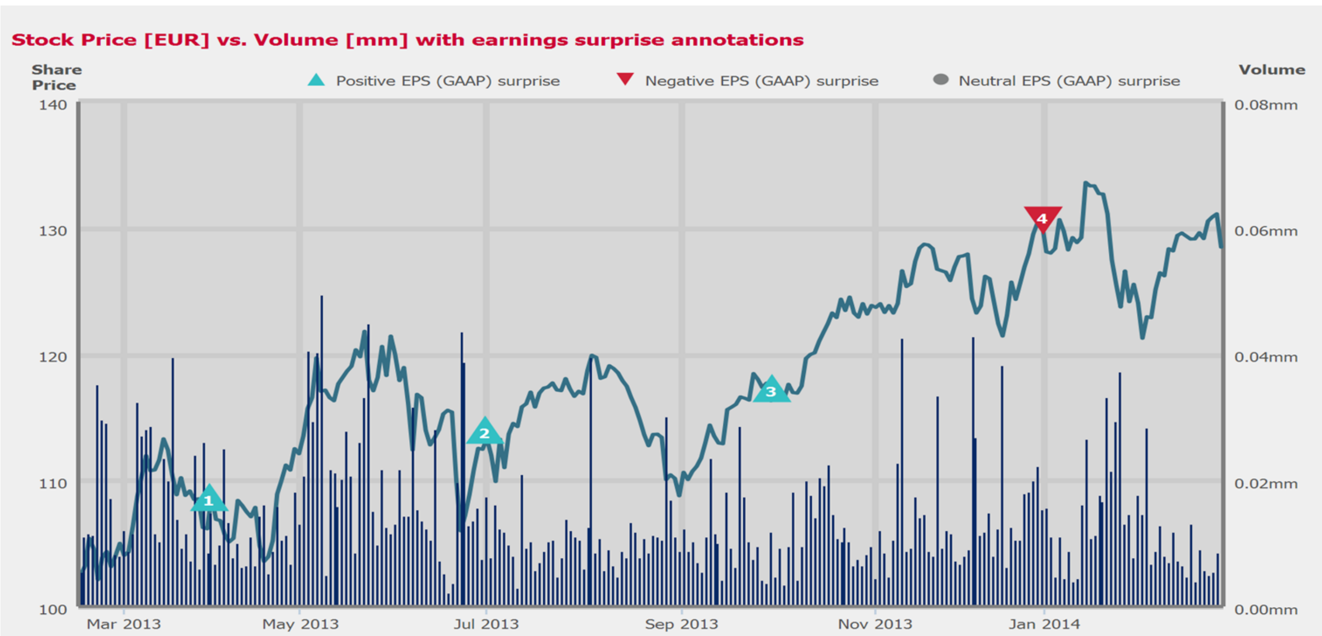
FQ1 2014 Earnings Call Transcripts

Wednesday, May 14, 2014 12:00 PM GMT

S&P Capital IQ Estimates

	-FQ1 2014-			-FQ2 2014-	-FY 2014-	-FY 2015-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS (GAAP)	3.28	3.55	▲8.23	3.32	13.65	14.08
Revenue (mm)	32711.00	34000.00	▲3.94	27558.00	110363.62	111289.91

Currency: EUR
Consensus as of May-14-2014 9:28 AM GMT



- EPS (GAAP) -

	CONSENSUS	ACTUAL	SURPRISE
FQ1 2013	3.24	3.69	▲1 13.54 %
FQ2 2013	2.97	3.47	▲2 16.84 %
FQ3 2013	2.74	3.14	▲3 14.60 %
FQ4 2013	3.10	2.72	▼4 (12.26 %)

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Presentation

Operator

Good day, ladies and gentlemen, and welcome to the Allianz Conference Call on the Financial Results for the First Quarter 2014. For your information, today's conference is being recorded. At this time, I would like to turn the conference over to your host today, Mr. Oliver Schmidt, Head of Investor Relations. Please go ahead, sir.

Oliver Schmidt
Head of Investor Relations

Thank you, Susan. Good afternoon, from my side as well, and welcome to our conference call about the results of the first quarter 2014. I think I can keep it brief. We have published key numbers already last week, you have seen our presentation this morning and all the details you will now get from Dieter.

Dieter F. Wemmer
CFO & Member of Management Board

Thank you very much, Oliver. And good afternoon or good morning for everybody on the phone. I will run you, as usual, through the presentation and before I get into the numbers, let me start with the business highlights of the first quarter.

On the product level, we are continuing to upgrade and update our non-motor retail products in Italy and Germany here. As an example, Italy, we have now fully digitalized the sales process in the agency, and I did recently in Italy with some investors actually, meetings in a digital agency. If one of you would be interested, happy to organize this.

In Germany, our new non-motor retail product, which is also modular and covering all lines, sublines of business is actually supporting our growing number of retail customers as we already talked about in Q4, and we increased here to 170,000 additional policies in Q1.

Life and Health, I will talk about it also when I come to the Life numbers. Our new fixed index annuity product in the U.S., which is selling really very well. It offers better upside for the customer and still a protected downside. And then we have launched our Allianz Global Benefits team, which offers for multinational companies, employee benefit solutions out of one hand for the whole company and its international subsidiaries.

Perspektive. Perspektive is our German product, which is a hybrid between guarantee and unit linked. I think it's a product very well made for the Solvency II world and giving customer and shareholder the better end of both sides, and it is selling really well.

In Asset Management, I think I mentioned it already in some of the meetings before, PIMCO launched its largest private closed fund ever, replacing the fund, which expired a year ago. So EUR 5.5 billion committed capital, and it will focus on distressed banking assets. And Allianz Global Investors has seen very strong demand on its upgraded income and growth funds with EUR 2.3 billion inflows in Q1.

On the investment space, we could add to our portfolio 2 shopping centers in Germany and a large financing of a motorway in Belgium. Reconfirming our chosen direction of investments, but still volumes could be bigger as we have more money to wait for investments. Acquisition, I think you have all seen the deal we did with UnipolSai. If there is still a question, I'll be happy to answer it. We signed the United Nations principles for sustainable insurance in the first quarter and we continued to invest and buy on Munich [ph] to strengthen our international brand in particular.

So now let's move to the numbers. Actually, why are we calling the start into Q1 a strong result despite that there's 2.6% down face -- on face value compared to previous year? Because we feel that it clearly demonstrates how our 3-segment business model works, falling operating profit in Asset Management compensated by Life, and in particular P&C. But also, actually, when you look at one-offs we had last year, I think last year was already a strong result, when I take out all one-offs then I would consider this year first quarter results even a notch stronger than last year in quality. And we had EUR 40 million or EUR 46 million of impact of FX in the operating results this year compared to last year. So therefore, I think, also in size, it is more or less unchanged.

The revenue story started very well into the year. 6% up, excluding foreign currency, it's actually 7.4% up mainly driven by Life revenues. And it really shows that our new product generations, which we are selling in the market are really matching customers interests and it resulted in very high net inflows for the Life segment in the first quarter. Net income was unchanged. Deduction from the operating profit and tax rate is the same unchanged story.

So let's move to the capital ratios. Shareholders' equity up EUR 3.5 billion. Actually only 2 drivers that is higher unrealized gains and the bond portfolio and the retained earnings of the quarter. There is almost 0 FX impact in the quarter. So the whole currency volatility took more place in 2013 and not yet observed in the first 4 months or 3 months of the year. Conglomerate solvency is the old Solvency I calculation, higher shareholders' equity compensated by higher revenues in particular on the Life section. Therefore, it is more or less, the same number.

Economic solvency, the 203% at March end is a very strong number because it includes already the reduced interest rates at quarter end, because the numbers we are presenting are always using the interest curves at the end of the period that might be different with some peer calculation and presentation. Secondly, we have embedded all the changes we talked about at the year end. So it is really a very strong ratio with 203%. And as we have included also the charge for the government bonds, which makes about 15 points, 1-5, and here the discussion with the regulators is not yet over. I still believe it would be an unfair punishment for the Allianz Group., if we are one of the few to bear this additional burden. S&P capital, we are still nicely ahead of the AA requirement. So in line with the other solvency numbers, strong development.

Let's move on to the P&C segment. Internal growth, 1.9%. Actually, the foreign currency impact is even more than 2%, but that added up in total to a flat nominal revenue development, positive numbers seen in Germany then with the large corporate business, credit insurance developing on a nice track, and then Allianz Worldwide Partners adding real good growth.

On Turkey, an unchanged good internal growth and also still helped by the first time consolidation of the now third quarter of Yapi Kredi, where the negative numbers we see lower premium in France, Italy, the U.S. part of our underwriting changes. And in Latin America, we are facing in Brazil a transition of IT platforms, which created a shortfall of volume in the first few months, but that we assume will be closing over the rest of the year.

Let's look at the performance of P&C. A strong jump in the underwriting profit to almost EUR 1.5 billion, making a good, good half of the total operating profit. So what are the drivers? First, I would like to mention that we have reduced our expense ratio, so Germany very much on track to achieve -- or actually, have achieved the 26.0% expense ratio in Q1, and maybe there is more to come. And the loss ratio is a combination of really further improvements already on a very good attritional loss ratio, a benign capital situation in the first quarter and also good results on large losses.

The runoff ratio is higher than a year ago, so it's 2.4%. But actually, 2.4%, is still below our long-term average for the year in particular, when you compare it with the previous years. So I think it is really a great start of the underwriting result. And as the underlying loss ratio and the expense ratios are moving in the right direction, it should also help us in the next quarters.

When we look at the operating profit of the various entities, it is not surprising when a EUR 44 billion portfolio has a combined ratio below 93%. That's a heavy weight, all must have good combined ratios, so Germany below 91%; France at 93%; Italy in the low-80s; AGCS, 92%; credit insurance below-80%; and the only outliers or you can also say, we could afford 3 areas above 100% combined ratio that is at the moment Central and Eastern Europe only driven by Russia.

The Russian motor markets with the changes in the claims practice, but still the old limitation on rates is really unprofitable and we have to work our way through how we get it back on track. Latin America, that is mainly an effect coming from Brazil. And the U.S. has 2 negative impacts, which moved the combined ratio to 107%. There is on one hand the long winter, maybe some of you have observed in person in the U.S. So therefore, we have really consumed our cap budget for the first quarter at least twice.

And additionally, we had additional negative development on last year's crop business. We had to book for the accident year '13 in crop, additional 6 points. I think we all and also the other players in the crop market got surprised that the total yields for the harvest was lower than expected because prices were lower realized, so it was not only the yield of the harvest but also the rates. And therefore, it's actually good that our crop exposure has been substantially reduced compared to previous years.

Turkey, higher combined ratios than last year, driven by 2 facts. Actually, it's the medical inflation, which drives the combined ratio up. It has nothing to do with the split between Yapi Kredi and our own business. And on the other hand also, the profitability in the motor business is a bit reduced as the weaker currency in Turkey has, of course, a negative impact on the prices of spare parts, which is, in the motor business, an important part of the claims handling. Altogether, 96% is still a number which is ahead of our business plan we put together for Turkey. So operating profit is actually on a very nice level.

The P&C result got supported by a very stable current yield on debt securities overall. On a run rate, you would have expected a falling yield compared to last year and actually, that has also happened. But in the beginning of 2013, we had a negative hiccup on some of the inflation linked bonds, which we are keeping in France and Belgium to protect lines of business, which are absolutely -- where the claim is absolutely linked to inflation development like workers accident in Belgium, for example. So therefore, on a like-on-like comparison, I think it is a bit weaker this year. Actually, in the last quarter '13, our average yield was 81 basis points, now it's 77. So that is actually the normal path of development you should expect with the reinvestment yield of 2.6%, which is 60 basis points below the average yield roughly.

So moving to the Life segment. As I already mentioned in my introduction, strong growth to EUR 17 billion in revenues, leading to about EUR 5 billion net inflows in our balance sheet, which is a record number for a quarter. If you compare the 2 growth rates in revenues between the face value revenues and then the present value of new business premium, you'll see the huge difference in growth rate, and that tells very easily that we are growing faster in single premium than in periodic premium. We see a shift here in Germany that our single premium products are selling better, despite the sale successes on our new product, Perspektive, but just the level of guarantee premium products is substantially down to historical levels.

And maybe one single additional item, with the introduction of the unisex tariff January 1, '13 in the EU, we had this last minute fire sale in December 2012, where a lot of the policies were actually then administered in the beginning of the year, instead of the end of the year. That is one of the drivers.

But let me talk about our new fixed index annuity product in the U.S. It is a product which offers an unkept participation in the performance of the index you invest in, and it is -- the downside protection is still the same as in with all fixed index annuity products. And we are using here a new Barclays index, which is a combination of the Barclays Aggregate, so fixed income, and the S&P 500.

And this product, I would call it, may be moving slightly away from a traditional fixed index annuity, as it attracts also a lot of people who would have invested otherwise into VA products. And our sales organization, which is the broker-dealer sales channel, is strongly used to VA, and they really love our new fixed index annuity product. Therefore, we have an increase in sales of this product of EUR 1.2 billion. And we have seen a reduction in our VA sales of EUR 160 million. I think that is overall for our balance sheet, a very good development. And also, when we talk about the operating profit, you will see it there as well.

As a strong contributor to Benelux, France, Italy, I think on the Life segment, we do in all areas quite nicely. Also, Asia Pacific had actually good sales numbers. I should mention that even Korea is up in sales and we have an 11% growth, which shows that also the restructuring in Korea is actually on a good way.

Let's now move on to the operating profit. It is very much unchanged compared to Q1 '13. The little edition of EUR 25 million can be completely [indiscernible] to the transfer of the pension fund companies on Asset Management, that is a EUR 26 million transfer, so roughly the same. Although, within the Life results there is, of course, a lot of moving parts. So it is at face value, the same result as previous year, but quite different from the nation.

You will see that -- that the expense load is substantially higher, but there are the sale successes in the U.S. and compensated as we are almost taking 100% of the acquisition expenses in the U.S. by impact of change in deck, so that is a profit-neutral number. Our investment margin is slightly down and that is all coming from Germany, where we have a lower harvesting, so lower realized gains than before we had this year only in basis points, 2 basis points compared to 12 basis points previous year.

If we look then at more detail how it breaks down into the individual units, you actually see what I just said last week, confirmed for Germany, where the operating profit is 20% down. France is up. There is a bit more net realized gain, as well as a higher technical result. Italy is down as a consequence of our reduction of Italian government bonds in 2012 and '13, where we just have a lower yield income. U.S., up driven by 2 factors. On one hand, the falling interest rates in Q1 have reduced the amortization of old deck. And on the other hand, we are earning more on the fixed index annuity business which is, in total, substantially up. I think that are the biggest drivers in the results. Benelux has some higher fee income, Netherlands improved health business. So there are some smaller changes. But all in all, I think that are the main drivers of the result.

And the health check on Page 23, how did the investment margin develop? Almost no movement. In total, net-net, we had 21 basis points in Q1 2013, now it's 19 basis points in Q1 2014. So still the level on -- for the total of about 75 basis points for the year that is very much what we expect. When you look at the last line of the page, you will see that the book value of our assets and also aggregate policy was nicely up. And that is driven by the good inflows we have seen already in Q4 and continued in Q1 2014. The unrealized gains year-over-year, there is probably not too much change. There was a lot of change in the last quarter. But over the 12 months, it is probably pretty unchanged.

So now, Asset Management sector. First, our third-party assets under management compared to year end are slightly up. So all the constant news flow about PIMCO got clearly compensated by market impact. So therefore, in total, we are at EUR 1.342 trillion of assets under management. Allianz Global Investors had EUR 2 billion inflows in the quarter. PIMCO had EUR 21 billion outflows in the quarter. That is roughly half of what we have seen in the fourth quarter. And it is half the EUR 21 million or EUR 22 billion can be split half, half between what we have called core or non-core products. So between the products which are like the total returns fund and the other.

So, overall, actually an expected outcome for the quarter, expected and baked in, in our outlook for the year. So we think that things are on track and we have now to see that the turnaround at PIMCO continues over the next quarter. But let's look at the revenues and then it's consequences for the operating profit. On face value, 19% down quarter-over-quarter. And there is, besides some FX impact, which makes about 2%, I think there is, in particular, the one-off performance fees from last year and the total volume of performance fees dropped from EUR 274 million to EUR 90 million, which gives actually most of the difference. The other -- for the regular fees, if you want to call it like this, dropped from EUR 1,585 million to EUR 1,497 million. And of this, 2%, 3% are actually explained by FX, the rest is falling AUM.

So the margins on the business, actually, if you look at PIMCO, 40.8 to 41 bps, almost unchanged. Allianz global investors from 61.6 to 58.8 only a small reduction. And hence, our cost income ratio stayed very stable as you can see on the next page. Our cost income ratio for the whole moved from 48.4 for PIMCO to 52.2. But now how does it compare when we exclude performance fees? PIMCO's baseline cost income ratio was 52.0 in Q1 '13 and it is 52.4 in the first quarter '14. And for Allianz Global Investors, it moved from 75.7, down to 73.6. In the total calculation as the rating between Allianz Global Investors and PIMCO's slightly changed, there are the currency impacts, as well as Allianz Global Investors some small goals in AUM, PIMCO some reduction in AUM. So therefore, in total, the average moved 1 point up.

So when we look now on the drivers of the operating profit. Last year, EUR 877 million, and I think we were always saying that this is probably a peak number because we can't repeat the one-off performance fees so quickly. And also the dollar-euro exchange rate is hard to control for us. So therefore, a EUR 646 million operating profit for the quarter is a very decent result, which we can really live with and have a good outlook for the rest of the year. We should really look at the underlying performance and the cost income ratio, which really gives a very strong number.

Let's now close the discussion with a short look on the corporate segment. Not really exciting, although the 2 movements look big. We had, last year, a one-off coupon payment from the silent participation from Commerzbank, which was paid back and resulted into EUR 68 million one-off coupon for the holding and treasury segment. And then we have, this year, also some less investment income in general. Last year, we have closed the German retail bank, Allianz Bank, that costs us EUR 88 million restructuring charge. Our small banks, actually, in general, did a little bit better in the beginning of 2014, so we are producing a small operating profit. So therefore, the swing is EUR 101 million positive and giving in total an operating loss in the corporate segment of EUR 222 million.

Now adding up all the numbers and translated into shareholders net income, that is done very quickly. We have, in total, the same non-operating items as a year ago, but there are 2 special effects, the realized gains are more than EUR 100 million down compared to last year. But we have a one-off positive compensating for this lacking realized gains of EUR 160 million, which comes of a change of the German accounting rules for pension liabilities, which changes actually the discount rate GAAP between IFRS 19 and the German calculation. And that is actually -- when you look at the net income numbers of our segment, it creates a little bit of a mess between the segment numbers because we keep, as a holding company, all pension liabilities for all existing and former employees of Allianz Group in Germany.

Therefore, the change in the German GAAP law had to be paid in cash from the subsidiaries to the holding companies. Therefore, it is an expense item on the local legal entity level, and it is all consolidated out of the group level. And this creates then these deteriorations and distorting effects in the net income numbers of the segment, in particular, visible when you compare the net income of the P&C segment and the net income of the corporate segment. So it's a bit complex, therefore, just focus on the total numbers here as a one-off that is the best explanation I can give.

So tax rates, unexciting, unchanged at 33% as last year, ending with a good net income of EUR 1.64 billion for the quarter. Therefore, let me summarize: EUR 34 billion of revenues, a record quarter in revenues for the group. Operating profit at EUR 2.7 billion, ahead of our quarterly EUR 2.5 billion of the outlook. The same shareholders net income from start into the year. Capital position and balance sheet may be even a notch stronger as the year ends. And I think, also, the composition of our operating profit is really a very good one.
And with this one, I would finish here and we start the question-and-answer session.

Question and Answer

Operator

[Operator Instructions] Our first question will now come from Peter Eliot of Berenberg.

Peter Eliot
Berenberg, Research Division

First question I had was just on PIMCO. I was wondering if you could comment on how the flows developed across the quarter, i.e., perhaps, how March looked relative to January and February? I don't know whether you'll be able to comment at all on how you're feeling about events after the end of Q1. And then, perhaps, just 2 non-Life questions on the capital ratios that didn't quite live up to the very strong group combined ratio. In the U.S., I mean, I appreciate you're always hostage to weather and that was a big headwind in Q1. But just looking at the underlying rate, it maybe, it looks like 100% combined ratio is now a bit of a stretch for the full year without sort of any further improvements. I'm just wondering whether you do still see improvements coming through or whether that was the case? And then on the CE, your comments applied a little bit that there was little you could do there. I'm just wondering whether that was the case or whether there are things you can do? And if not, what your view on Russia would be going forward?

Dieter F. Wemmer
CFO & Member of Management Board

Peter, very happy to answer the question. Well, PIMCO, I think, that is a very flat development month over month. And actually, before somebody is asking it also, April is pretty much unchanged compared to January, February and March. I think what I did not say before, but actually you see in the whole industry outflows out of actively managed fixed income, you can look at BlackRock, Black Mesa and Vanguard, there is -- the inflows at the moment in the fixed income sector are more going to the passive funds than to the active managed. But I think that is, at the moment, a seasonal topic. And I think the performance of the active managed will, in the end, I think, attract the customers, which are at the moment probably trusting more into the passive funds. The P&C result, I think you asked, you are spot on. The underlying, with having this additional booking for the corporate and from last year, was really an ugly first quarter. And actually, also April in the U.S., I think that was an almost immediate transition from winter storms to tornadoes is certainly also not supporting a strong improvement of the combined ratio. So the 100% combined ratio at year end is probably a stretch and our dream of the double-digits is probably postponed for a quarter or 2. CEE, Russia, what can we do? Yes, and when you still play in the market and in the provinces which have the highest litigation frequency, you have just to pay the losses. So what you can do is change the composition of the portfolio, get down to 0 in the provinces where you have the high litigation. Because the litigation frequency is not the same in every part of the country, and it is a very large country. And that mix change is the only thing what you can do and you can, of course, rework your pricing on MOD, and see that you get a higher share of MOD compared to motor liability. And you can be really very strong and very hard on your expenses. And that are the 3 things, the 3 levers you have available. The rest is as long as the Russian Parliament is not voting in favor of a change of MTPL pricing. And it seems, at the moment, Russia has other priorities than dealing with motor insurance. So with this one, next question.

Operator

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

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

Couple of questions for me. Firstly, on the Asset Management business, you mentioned this EUR 5.5 billion private funds launch, which replaces one of the previous private funds. And -- would you care to comment on the structure of that private fund? Essentially, does it have similar kind of performance fee arrangements to the prior funds that brought the large performance fees through in the past? And the second question is on the Life business, particularly the U.S. So you always had a lot of success in the fixed index annuities market, what would you say is the outlook for this business? And essentially, how unique is your new product in that market is this going to be a sustainable competitive advantage for the foreseeable future?

Dieter F. Wemmer
CFO & Member of Management Board

Let me start with the Life question. Well, actually, I'm convinced that the insurance industry never lives on innovation and intellectual property rights a longtime. Usually, you have an advantage of up to 90 days and then you are -- then somebody else will also bring a similar product. So therefore, I would assume that we will not see the same growth rates continued over the next quarter. However, I believe that, in particular, as we have some proprietary channels, that they really like the product and also will continue to sell well. This really gives us a level of new business volume that we are also have not the risk of expense overrun on the sales channels, which is very good. On the Asset Management side, yes, I can understand that you try to estimate the future inflows coming from performance fees. It think, we, of course, are not disclosing all contractual details for private funds, because it is a close fund. And therefore, if you have invested early enough, you would get a copy of the rules. But I can also maybe add that we have still some private funds which are at work, which should be scheduled for repayments to investors in 2016 and '17. And that would what be then, for me, the first year where we would see additional one-off performance fees. And this one here it's, I think, it's actually called Bravo II, will come in a few years later. But in the next 3 years, there are -- there is certainly some money, which could come but you are also aware that actually the revenue recognition holds are only allowing us to show it and book it when the money is being paid back to the investor, and that is a good rule. It's a bit conservative, but the right way to do it.

Operator

Our next question comes from Andrew Ritchie of Autonomous.

Andrew James Ritchie
Autonomous Research LLP

Two quick questions. First of all, just looking at the underlying loss ratio movement year-on-year, I noticed in the appendix at the back of the presentation, we don't have any effect this year from frequency/severity. Now that's been running at kind of a minus 2 percentage point year-on-year impact for the last 5 quarters, and it's gone to 0 now. Can you just comment on -- and I appreciate this in probably large loss noise in there, et cetera, and I guess some of the crop noise. Can you just give us a sense, Dieter, as to what's happening frequency trends and whether these are going to slow down in the benefit from what has been a run of pretty benign frequency trends? Second question, just on PIMCO, just wanted to clarify what your comments meant. You were talking about kind of your much more confident for the rest of the year, and the outflows Q1 were in line with expectations. Is your expectation that, that rate of outflows continues over the year or are you expecting net inflows at some point this year? I mean, maybe just give us a color, I'm not quite sure what you meant when you referring to the outlook or you're just referring to the fact that there's been good kind of operating efficiency despite the outflows?

Dieter F. Wemmer
CFO & Member of Management Board

Andrew, let me start with the last question. I think we discussed this question. Actually, that was end of -- beginning of March in our small group in London. And I think the answer is still the same and I was only reconfirming what we already said 3 months ago that we did not expect that the outflows would go completely to 0 in the first half of the year but that it would get smaller over time. And I think as Q1 was at half of the level of Q4, I think that it's pretty much what we indicated already in this discussion. And yes, I think PIMCO has certainly to prove that it stops at some point and then after bringing it to 0, the next step would be bringing it to a positive number. That is probably everybody's expectation. And also, I think when you know the people working at PIMCO, that is also exactly their ambition and that is very,

very normal development. But I think that they did really a great job to work on the variable expenses and really kept the profit margin at the same level. So it is a very active management process and shows you also that actually the whole organization is really working in the same direction, which is, for us, internally very important although there is always an external assumption that this is not the case.

Andrew James Ritchie
Autonomous Research LLP

Just on the -- I think in March, you said that your position with consultants on the institutional side, they have been broadly welcoming, I think, of the changes. I mean, has there been any change, have you been put on watch by more consultants? Or is there any kind of major changes in your perception there?

Dieter F. Wemmer
CFO & Member of Management Board

No, there is no change in the perception. And you-- well, you know the asset management industry probably better than I do. The consultants who advise institutional investors are all doing a due diligence locally before they recommend an asset manager. Therefore, almost all the consultants we are working with have all personally visited for 1 or more days the PIMCO office in Newport Beach in the past. They are fully aware of the business culture and the capabilities of the organization. And that is a personal judgment each consultant is doing. Now coming back to your loss ratio question. Well, I think that -- let me break down your question because the whole frequency debate was very much a question of motor frequency in Southern Europe. And did we see a change? Well, actually not. If I just take the Italian example, our frequency in Q1 was even slightly lower than before and that has nothing to do with the economic circumstances. I think that is also consequent of the continued risk selection process, which has obviously also an impact on frequency. However, for the total portfolio, we are moving in total our growth, much stronger to short-tail portfolios. AWP is our strongest growing line. They have a high number of tiny claims. So therefore, as we can see, it's certainly upcoming from these lines of business and what this appendix number is showing you is that on a portfolio in total, it is unchanged. But yes, it's probably difficult to interpret how this one number is really driving EUR 44 billion of P&C portfolio. So therefore, you can only take it as it is shown here, the impact in the overall loss ratio of frequency and severity is very much flat. We see a positive impact coming from price and we have less NatCat. So underlying loss ratio, yes, I think we are in maybe 30, 40 basis points better than a year ago. And I think we are moving overall on a very good level and we are not nervous about the rest of the year.

Operator

Next question comes from Thomas Seidl of Bernstein.

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

Three questions, please. Number one, on PIMCO, again. I think you stated the outflows were pretty much in line with expectation. However, I do note a drop in the fee margin, 43.9 is 1.6 basis points lower than in Q4. You mentioned in the notes that this is driven by the lower number of trading days but I also note that the retail share of EFSF has gone down in Q1. Is this the main driver and should we hence expect the fee margin at best to stay at this level for the remainder of the year? Second question on P&C. Here, we note that the price trend is further down 1.4% in the quarter. It's lower than the previous quarters, given that investment income is further coming down, reinvestment yields coming down. Shouldn't we expect more and stronger price actions of Allianz in these markets? And finally, on Page 8, you note that the accrued dividend is at 40%. How should we read that, assuming that this is meant for 2014?

Dieter F. Wemmer
CFO & Member of Management Board

So let me start with the dividend. Actually, when I did read yesterday evening one last time the analyst presentation and the comments, I made a mental note to myself that this question would immediately come, and thank you, Thomas, for confirming it. We said we will talk about the dividend and the way forward and we will certainly not implement a new dividend policy by hidden footnotes that we have changed a coil [ph] for the dividend. So really sorry. In the end, that it's the status quo and the update comes when it comes. So PIMCO, yes, I think that the margin is indeed unchanged and it is probably more fair to compare Q1 over Q1. Although the way how the number is calculated, the trading days of the quarter have an important impact as it is calculated on a daily basis. So therefore, I think the margin is indeed on a good level, but I would not assume that it is a growing number. And I would say, well, it is pretty much stable and the margin includes already the retail institutional split. Therefore, when we say stable, it includes already both.

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

Okay. And the retails of all, do you think it's linked with this discussion about PIMCO, the negative headline news?

Dieter F. Wemmer
CFO & Member of Management Board

Well, I think it is also because people are nervous about what is happening to the interest rates. And certainly, I think salespeople who live on upfront commission payments certainly will not miss opportunities also for switches. I think that is certainly a very normal routine thing in the asset management sector. Also, I think it is, from this prospective, still very small and I would not see this as a big trend.

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

And then on the P&C pricing trend?

Dieter F. Wemmer
CFO & Member of Management Board

P&C pricing trend, sorry. The P&C pricing trend, it is slightly down. When we just look at the big flagships, so our large OEs, we had -- a year ago still 2%, maybe now we are down to 1.4%. Is this a big change? Well, in the end, the inflation is probably even more benign than before. So what argument do you have to increase rates? And when you actually look at the trend of our loss ratios, I think we are very comfortable there. We are standing to push through another 2%, 3% of rate increases probably you can do. You end up with a lower volume in total. You end up with an even better combined ratio. In the end, we have to produce and deliver operating profit, which is a product of volume and profit margin. And we feel that our current strategy is trying to optimize exactly this challenge.

Operator

[Operator Instructions] Our next question is from Marc Thiele of Mediobanca.

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

My first question is on economic solvency. The full year number has been restated as previously indicated and the slide mentions model changes with a EUR 10 billion boost to owned funds and almost EUR 9 billion to the requirements. This seems to have contributed to the 9 percentage point increase in the first quarter, is this right? And can you detail the impact of the declining bond yield in percentage points? Or even better, maybe you can reconcile the main components of the movements? And then the second question is on the P&C reinvestment yields that has increased to 2.6% in the first quarter from 2.5% for full year. And I guess the reason is we're looking at averages with Allianz taking more investment risk. Do you have a quarter-end number or current rate that we can use as a good guidance for projecting investment results?

Dieter F. Wemmer
CFO & Member of Management Board

Well, I think the -- let's start with the investment results. Our usual guidance is that we see in P&C still a reduction of 15 to 20 basis points, but we are not giving further guidance than the one we have disclosed, but you can make a very simple calculation. On average, we have to reinvest 5% of our P&C investment portfolio every quarter. So when you average yield is 3.2% and your reinvestment yield is 2.6%, then the 5% dilution every quarter is a very simple-rule-of-thumb calculation. And on the Life side, you can do the same, only the turnover of the investment portfolio is, of course, lower. There it is probably more between 2% and 3%, which we reinvest every quarter. And hence, the dilution effect of the current market environment is smaller. What you cannot anticipate is when we do large deals with attractive yields in the infrastructure sector of real estate that are the positive one-offs, which help supporting our old yield levels. So on economic solvency, that is a longer story. I hope you all have nothing else this afternoon. We have -- let's first look what we did at year end. We have included the sovereign credit risk, including the credit -- the spread charges. We have updated all our correlation because they are based on a model how the correlation factors are being calculated. We have added a charge for our internal pension. We have implemented the impact of the volatility adjuster on the spread risk. We have some scope changes, which actually have also reduced our solvency ratio. And also, we have a capital add-on for some best estimate outcomes so there is -- in case where buffers are used more than once, we have taken a general haircut. So -- and for example, we have reduced transferability with restrictions, but we still have kept some. And the positive developments during the first quarter, that is the net income, the plus, in particular, Non-Life. And when you look at our MCEV development, I have moved the MCEV slide into the back because it seems that nobody wants to hear anything about MCEV anymore. But we had a very strong earnings, organic earnings, in the MCEV so that added to the available funds than we issued in the first quarter, a small hybrid. And we have some market effects in Non-Life. What has consumed more is increasing equity markets and then the decreasing yield, obviously, interest rates and peripheral spreads who came down, which has a reduction of credit charges on one hand. On the other hand, of course, it's even a smaller yield.

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

And do you have like a number for the interest rates? Just to give a feel for how significant that was because I would presume, looking at the embedded value disclosure, we are moving slowly back to the record lows that we've seen. I think it was a year ago.

Dieter F. Wemmer
CFO & Member of Management Board

Well, the effects are a bit more. Well, first of all, we have in the appendix various interest rate sensitivities. However, on the MCEV, actually it is a bit complex because you have, in the end, to compare how the swap rates move and then I think we have seen more reduction in Italian and Southern European spreads than in the swap curve. Therefore, I think, overall, our -- the impact of the interest rate in our MCEV is actually pretty small in total. Yes, so it's EUR 580 million. EUR 580 million was the change in the German market and the Southern Europe was even positive. So we have in total EUR 0.5 billion coming from the interest rates in the MCEV, so not in the risk model.

Operator

Our next question comes from Michael Huttner of JPMorgan.

Michael Igor Huttner
JP Morgan Chase & Co, Research Division

I have 3 questions. The real estate, I was surprised to see it was still at 2%. I keep reading in the paper and you keep highlighting that you're making all these real estate investments. But it doesn't seem -- you're actually not paying any money for this, as well [ph]. On Russia, given that it's clearly not getting better for the time being, what's the risk of an impairment? And I know you say the impairment is set to the whole CEE, but now the whole CEE is actually negative. So I was just wondering if you can give a feel [ph] for that? On Italy, can you give us a feel for what the underlying is? I know it's a bit of a silly question because we keep getting positive surprises on the reserve releases so there seems to be that the negative inflation is working through, but maybe any indication would be very helpful. And then a little bit of follow-on from Marc Thiele's question. The EUR 8.3 billion uplift of IFRS versus -- sorry, of MCEV versus IFRS with what's in the balance sheet. It was EUR 9 billion at the year end. Can you give us a little bit of a feel if we were to think about even lower interest rates or just a feel for how robust -- what I'm trying to see is how robust that 203% figure is? What could drive it back to the 190% level, which where we -- we were all a little bit surprised at the full year.

Dieter F. Wemmer
CFO & Member of Management Board

Michael, you lost me a bit on the MCEV question.

Michael Igor Huttner
JP Morgan Chase & Co, Research Division

Okay. Just very simply, what could drive the 203% back to the 190%? What kind of scenario do we need to think about to get to -- it's not a scary number but a number where you won't feel it's a bit less comfortable about, what you might say at the end of the year?

Dieter F. Wemmer
CFO & Member of Management Board

Look, if you can look at our disclosures on Page 42, I think there we have actually done all the tests of the various calculations and that is what moves the number. But I think for the time being, I think we are clearly keeping the risk very much under control and managing the ratio very well. The real estate question, sure, it is only a small number. But also, you have to remember that in our balance sheet different than many others, our real estate is on an amortized cost basis. We are not giving the full market value. Therefore, there is a natural amortization, and therefore, a reduction of the booked real estate number year after year. That is one of the conservatism of the Allianz balance sheet. Also, one of the reasons why our capital strength is high. So -- but you are also right. We are really looking for quality investments from the real estate sector, which is satisfying our ambition and our returns. And therefore, the progress is slower than we would like to do but better good deals than speedy deals. Italy, we have a good 4% run-off result in Q1 '14. And the year before was no run-off result in Q1 and that gives you, I think, a good indication of the development of the underlying. Russia, we have to watch the development. We have to look what management comes up with, with operating plans and then we have to look what impact it has on the accounting number. And also on the balance sheet, that is a standard process, which we are very systematically working through.

Michael Igor Huttner
JP Morgan Chase & Co, Research Division

Is the -- how significant is that risk? When we asked at full year, the feeling was not very. Now from the answer, I would say we're in the kind of 30% area. I don't know, is that fair?

Dieter F. Wemmer
CFO & Member of Management Board

I think the risk is certainly higher than it was at year end, but it is not high enough that we would book it. So therefore, it is on the watch list.

Michael Igor Huttner
JP Morgan Chase & Co, Research Division

Excellent. And the amount it relates to, I can't remember. Is it somewhere around EUR 800 million?

Dieter F. Wemmer
CFO & Member of Management Board

No, no. EUR 800 million, that's for Russia. No, that -- I think it is -- well, it is embedded in the overall CEE goodwill, but I think it is somewhere between EUR 300 million and EUR 400 million.

Operator

Our next question comes from Blair Stewart from Bank of America.

Blair Thomson Stewart
BofA Merrill Lynch, Research Division

Three quick questions. Firstly, with the drop in U.S. bond yields, any comments you can possibly make on the performance at PIMCO in terms of the fund performance with a view to perhaps slowing down the outflows? Secondly, on the Life business, the fee-based revenues were a bit better than expected. Is that a good base to forecast for the rest of the year? And thirdly, maybe just a few comments on this new U.S. product that you have been so successful with. What's the expected duration of that and anything to worry about from a risk management perspective on the product?

Dieter F. Wemmer
CFO & Member of Management Board

Blair, I think -- I'm not sure that I can link the movement of U.S. bond yields with the fund performance because they are completely different funds with different strategies, and therefore, I think things are quite specific for each fund. Income funds, very high performance. I think our 1-year performance for was below historical average. Our 3-year performance is, hence, down to 88% outperformance, which is still a market-leading number. And I think we have a good recovery story on global unconstrained and the total return fund I think you are all reading probably every week on your Bloomberg screen, so I don't need to explain this. In Life, the fee-based revenues, I think, I'm not aware that there was anything special in Q1. As I would anyway say, the Life results in Q1 might not be a predictor of what we will have every quarter as an operating profit. But I can also not say that there was any special one-off in the numbers, which I could isolate and know. So there will be some volatility in the number. In particular, I think the [indiscernible] write-downs are more volatile. That is the U.S. GAAP logic and the old VA book which creates this. But that is probably a volatility, which exists. The new U.S. product, I don't think that it has any special additional risk features. So I think from a risk management point of view, it is a well-designed product.

Blair Thomson Stewart
BofA Merrill Lynch, Research Division

And the expected duration of it?

Dieter F. Wemmer
CFO & Member of Management Board

The stakes [ph] that we are using, that is when you want to look it up, it's called BUDBI. So that is -- it stands for Barclays U.S. Dynamic Bond Index. That terrible acronym, and it has embedded a balance between bond and equity components and the index manager is also doing a reallocation between the 2 classes depending on the market development. So I think it is also a self-regulating index and that actually supports our risk management efforts a lot. Therefore, I think it is a really a very, very good and interesting solution. To some extent, we have outsourced rebalancing between the fixed income portion and the S&P 500 components to this index, and therefore, we have internally to spend less money on the hedging.

Blair Thomson Stewart
BofA Merrill Lynch, Research Division

Okay. And the duration of the product?

Dieter F. Wemmer
CFO & Member of Management Board

Duration, I think it's the normal 5, 7 years or 8.

Operator

Our next question comes from Nick Holmes of SocGen.

Nick Holmes
Societe Generale Cross Asset Research

Just 2 of them. The first is coming back on PIMCO. Wanted to ask, with the outlook for performance fees, I know this is incredibly difficult for you to comment on. But I think you've said in the past, 3 to 4 percentage points of revenues is the sort of level that you would expect. Now I wondered whether you can comment on that in the light of Q1. And also, really, same question with the cost income ratio, which has risen from 53% to 57%. And it's really the same question isn't it, whether you expect the level of performance fees to cause that ratio to remain higher? And then second question is coming back on the solvency ratio, the new definition. Just wondered if you could explain exactly what it is that you mean when you say you've reduced transferability restrictions.

Dieter F. Wemmer
CFO & Member of Management Board

Okay. I think for PIMCO, we reconfirmed what we said before and I think that it was also the answer I gave to Andrew, I think. And on the performance fee, the first quarter is seasonally weak because it is not the closing quarter for the funds, which have usually a 4-quarter calculation, as you probably know also from SocGen's asset management activities. So that -- and Q1 is a very low quarter where this calculations and building is being done. The transferability restriction is very simple, an internal process that we are -- that we have taken out conservatism as we had it in the past because we have also replaced top-down estimates on the market-consistent balance sheet by a proper bottom-up process, and our market-consistent balance sheet is now being produced by the same SAP system as our IFRS results and that is the same consolidation process. Therefore, you can also say that our current numbers are more precise and more detailed than this, and therefore, we have also removed some conservatism we had before as reserves of fund for sales [ph], so to speak.

Nick Holmes
Societe Generale Cross Asset Research

Okay. Dieter, can I come back just on the transferability, and in particular, with the question of the RfB. How do you treat that in terms of transferability? I know that under the conglomerate ratio, you actually have a lot of it available at group level. Is this something that you're also doing with the economic ratio?

Dieter F. Wemmer
CFO & Member of Management Board

The RfB is, of course, not transferable. I think the BaFin would really be upset. And also, how would you argue that something which belongs to the German policyholder can be transferable? That would be a very difficult argument to make but maybe we can learn from some of our peers.

Nick Holmes
Societe Generale Cross Asset Research

But do you not do that with the conglomerate ratio? You have over EUR 5 billion of free RfB, which is available, is it not, in the conglomerate ratio.

Dieter F. Wemmer
CFO & Member of Management Board

Yes, but that is the shareholder sharing it and not the policyholder. And it is a completely different calculation because that is, in the end, the share in the unrealized gains of the bond portfolio, which when they are being realized, they are split according to the normal formula between both sides, between policyholder and shareholder. Therefore, that this a different calculation. And we have certainly retained in our German Life business whatever is needed for running off the portfolio for all guarantees and also the announced profit sharing.

Nick Holmes

Societe Generale Cross Asset Research

Yes. I mean, I'm sorry, I was really referring to the free RfB, whether that is the subject of a change in your transferability restrictions, whether you've -- no? So no change there? Okay.

Dieter F. Wemmer
CFO & Member of Management Board

Absolutely correct.

Operator

[Operator Instructions] Our next question comes from Andy Broadfield of Barclays.

Andrew Broadfield
Barclays PLC, Research Division

Just one question left actually. It's just a follow-up on the fixed index annuity to the last question really. You mentioned that the consumer now got more of the upside but kept the downside. I think any product which sells very well, where that seems to be the shifting dynamic, raises an eyebrow. Can you say no particular concerns around the risk management? I don't know whether it's possible in this core to just give us a little bit more detail around those features that you haven't already given because I'm not sure I fully understand what the additional benefit is and why there isn't an additional risk to shareholders for that.

Dieter F. Wemmer
CFO & Member of Management Board

No, well, I think in the end, we have the same dynamic hedging on the product as with the other product. The only question is whether you are -- what costs are you consuming for the various hedges and I think the construction we have chosen here also with this very specific index. We are hedging the downside, but when the index runs positively, we can share the profit with the customer. The product itself has the same adjustment clause on the expense charges as the previous product. That means in case that hedging costs go substantially up, then yes, that might create a shortfall between collected expenses from the customer and the hedging costs in a month. But then due to the changed clause in the contract, we can then catch up in the following quarters, and that is the way how it works in all the fixed index annuity products.

Andrew Broadfield
Barclays PLC, Research Division

So is this effectively you saying you've got a more efficient hedging because -- partly because the index that you use...

Dieter F. Wemmer
CFO & Member of Management Board

Yes, and also this index itself, as it is recalibrated between equity market and fixed income market, is of course -- has therefore a lower volatility than when you do a plain S&P 500. So therefore, the hedging costs to start with are lower than with other funds and that allows the isometric treatment.

Operator

Our next question comes from Vinit Malhotra of Goldman Sachs.

Vinit Malhotra
Goldman Sachs Group Inc., Research Division

When you said that the PIMCO flows -- outflows were in line with expectations. What are the expectations also meant for the core and non-core lines? I just wanted a quick check on that, a quick clarification on that. And just one thing, I'm very curious, on the solvency to sovereign credit charges, after you had announced that in the slide, we didn't really hear this from the other insurance companies. And I'm just wondering, why was it that Allianz was sort of picked up for having to include these charges? Is it linked to the SIFI debate? Is it something else? It's just not very obvious.

Dieter F. Wemmer
CFO & Member of Management Board

Well, I think it is very obvious, Vinit, because it's -- the German regulator said they want to see it for internal models. And the 2 large and prominent user of internal models in Germany are Munich Re and us, and I think it is probably well known that Munich Re has also a charge for government bond risk in their model. So therefore, it is -- should be from this perspective not surprising. But having said that, we will certainly not accept if we are being disadvantaged against other European players. And in particular, on local market comparisons in -- whether it's in Spain, Italy or any other market, I think that would be an unacceptable disadvantage. We have now put it into our model also to demonstrate that our solvency ratio is still at a very comfortable and excellent level, even when we produce here a worst-case scenario. And actually, it is also the process we have told of you that we will reflect in our quarterly model updates the current status of our discussion with our regulator. And as BaFin is the owner of the approval process for our group model, that is the current view. So from this perspective, there might be more chances for upsides into the calculations than for downside. And I think, usually, you guys are always using for the downside in everything. So this time, you can search for the upside. Sorry, Vinit, I forgot the PIMCO question. I got too excited about Solvency II. So no, we have not refined our expectation between core and non-core. I think that would be too much of a forecasting process. And I think the overall number is what we felt is to be expected.

Operator

[Operator Instructions] As there are no further questions in the queue, I will now hand you back to your host for any additional or closing remarks.

Oliver Schmidt
Head of Investor Relations

Well, perfect. That was perfect timing. Thanks, everybody, for having joined the call. We say goodbye to you and wish you a very pleasant remaining afternoon.

Dieter F. Wemmer
CFO & Member of Management Board

Yes. Also, from my side, thank you very much for the call and let's continue the dialogue. I always enjoy it, as you know. Have a good afternoon.

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