S&P Capital IQ

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# Allianz SE DB:ALV

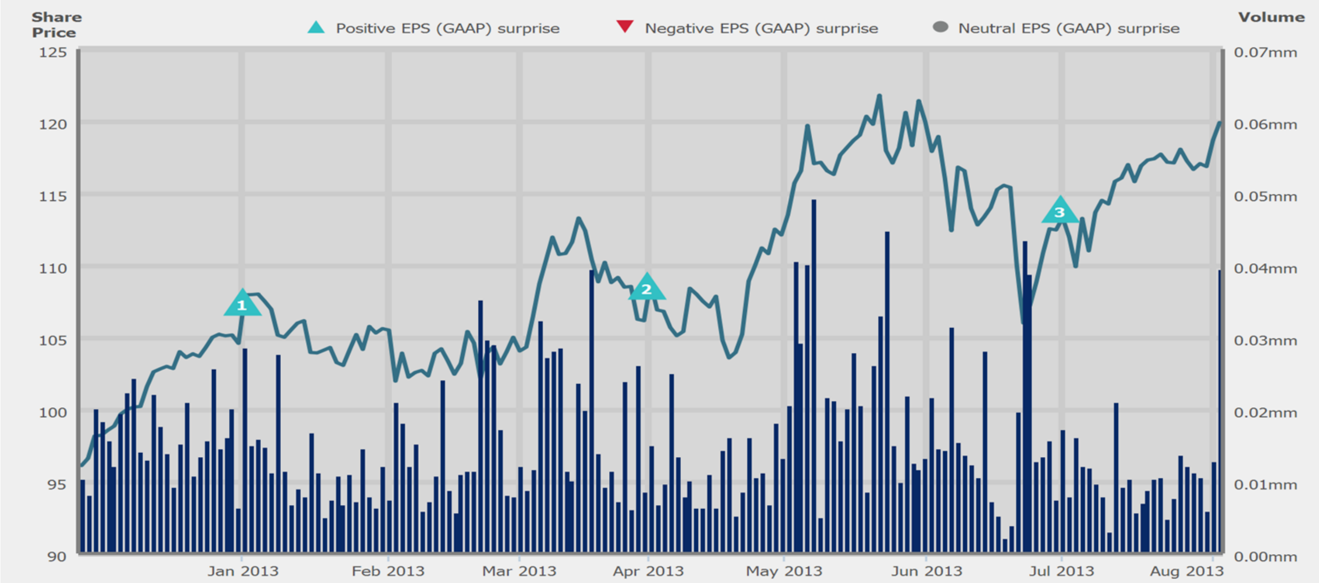
## *FQ3 2013 Earnings Call Transcripts*

Friday, November 08, 2013 1:00 PM GMT

## S&P Capital IQ Estimates

| | -FQ3 2013- | | | -FQ4 2013- | -FY 2013- | -FY 2014- |
|---|---|---|---|---|---|---|
| | CONSENSUS | ACTUAL | SURPRISE | CONSENSUS | CONSENSUS | CONSENSUS |
| **EPS (GAAP)** | 2.74 | 3.14 | ▲14.60 | 3.30 | 13.21 | 13.46 |
| **Revenue (mm)** | 25747.00 | 25144.00 | ▼(2.34 %) | 26641.00 | 105572.59 | 103522.73 |

Currency: EUR
Consensus as of Nov-08-2013 10:39 AM GMT




**- EPS (GAAP) -**

| | CONSENSUS | ACTUAL | SURPRISE |
|---|---|---|---|
| **FQ3 2012** | 2.81 | - | - |
| **FQ4 2012** | 2.55 | 2.66 | ▲1 4.31 % |
| **FQ1 2013** | 3.24 | 3.69 | ▲2 13.54 % |
| **FQ2 2013** | 2.97 | 3.47 | ▲3 16.84 % |

# Call Participants

**EXECUTIVES**

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*CFO & Member of Management Board*

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*Head of Investor Relations*

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# Presentation

**Operator**

Good day, ladies and gentlemen, and welcome to the Allianz Conference Call on the Financial Results of the Third Quarter 2013. For your information, this conference is being recorded. At this time, I would like to turn the call over to your host today, Mr. Oliver Schmidt, Head of Investor Relations. Please go ahead.

**Oliver Schmidt**
*Head of Investor Relations*

Thank you, Patrick. Yes, good afternoon, from my side as well, and to welcome to our conference call about the results of the third quarter 2013. For the sake of time, I hand over directly to Dieter.

**Dieter F. Wemmer**
*CFO & Member of Management Board*

Yes, thank you very much, Oliver, and good morning, and good afternoon to all of you on the phone. I'm really very proud to report to you about another successful third quarter of Allianz Group and let me go directly into the presentation, which you hopefully all found on the screen.

Starting with the business highlights, I would like to point out only a very few one. Following demand from customers, we have also launched a new product for our large customers first to address online losses arising from online risks or general IT failures. That product has been rolled out in the German-speaking world first, and so then will be also, step-by-step, rolled out to a larger audience.

In investment category, we have now reached EUR 1.7 billion investments just for alternative energies. You can add to this roughly the same amount of general infrastructure investments. And in direct distribution, we are now in premium and policy #1 in Italy surpassing direct Allianz Italian operation and we reported about our newest activity on the globe lines, Allianz Worldwide Partner, which has 1 of the arms international health business. Here, we reached already, after 9 months, our 12 months target and that should certainly help us also to reach here the global market-leading position.

So now, let's go after the 2 points into the numbers. I should maybe start to explain the impact of foreign currency movements compared to last year. On the revenue side, all the FX changes are actually adding up to EUR 730 million, that is about 2.9% of the revenues, so quite a heavy number. And in operating profit, it makes about EUR 140 million. So with this background, I think unchanged revenues in total, unchanged operating profits, and a higher net income, is a pretty strong performance for the quarter. And also in operating profit, we actually replaced 10% of supported, which was last year coming from one-off performance fees from PIMCO by underlying profits in all 3 segments. So actually, I think that is, from a profit growth, a pretty strong performance, but I will highlight the individual contributions when we come to the segments.

Now let's move on to Page 5, short look on shareholders' equity and solvency ratios. Actually eventless quarter. Compared to end of June, equity up EUR 1 billion, that is mainly retained earnings added, minus a movement in FX and almost no movement in unrealized gains and losses because little losses on the bond side were compensated by gains on the equity side.

So therefore, conglomerate solvency, so the Solvency I unchanged and economic solvency slightly up that is clearly coming from the higher interest rates in Q3, in particular at the long end. So overall, outlook for the balance sheet quality continues to be stable and strong.

So turning to the P&C segment. The story on the top line this quarter a bit more complicated. The headline number is a reduction or shrinking of 6.5%. Excluding acquisitions and FX movements, still a shrinking of 5%. That looks like not a good outcome. But actually, how we see it, it is a 3% growth of most of our OEs and of all of them. I actually will explain you the difference. We have 2 effects coming from the U.S. corp business. On 1 hand, we explained already, in the beginning of the year, that the reinsurance we get out of the corp business has been half-ed, so that our net earned premium coming out of corp is only half what it's what in the years before. And additionally, actually the corp carrier belongs to Allianz until 5 years ago roughly, and we sold it. 5 years ago, we sold the corp business, but kept the fronting and the issuing of the policies. And this one has now been transferred to the buyer of the business. They are now writing the business on their own papers and we are only participating through the reinsurance. So therefore, we have a double drop in top line and that explains the difference between the shrinking and the underlying growth of 3% for all the active businesses.

So in particular, I would highlight that Turkey, half of the high-growth number is the first time consolidation of Yapi Kredi. The other half is still the organic growth. And also in Central and Eastern Europe, as well as Latin America, we continue to grow nicely. AGCS, which looked worse in the second quarter, has now a much better volume number that was actually a shift of some AIT business between second and third quarter and it is now back on track. I would also like to point out that Italy was 2% growth in a shrinking market, I think is setting really a benchmark for its peers, who are struggling more with the top line at the moment.

So moving on to the P&C results, the combined ratio improved to 94.8%. So one of you who have already looked at the pages will say, "Yes. But it is only driven by a higher runoff result, so where is the improvement?"When you take out the runoff result, as well as, actually, fairly high cat losses in the quarter, you can calculate that the underlying loss ratio actually improved by 2.7%.

Is the runoff result unusually high? Yes, 4.3% is certainly above our guidance of 2% to 3%, but it is -- that is simple coming from the fact that each and every OE contributed a positive runoff. So we don't have any negative numbers. So when you compare 2013 with 2012, actually, we had in 2012 a negative runoff from the Thailand flood that was booked beginning of the year 2012. And then during the year, we had in 2 steps reserve increases at Fireman's Fund. When you take these 2 negative OEs from last year out and then you compare the numbers, then you will actually see that the total positive volume is plus/minus EUR 30 million, almost the same for the full 9 months. And that explains actually why we have such a individually high number in Q3, strong contribution from everywhere, and that resulted then in total in an improvement of the underwriting result of EUR 150 million and operating profit 6% up against last year.

Expense ratio, one [ph] remark is 60 basis points higher than previous year. You can actually see in every quarter this year. Just as a reminder, it has 3 effects. Consolidation of Gan Eurocourtage, 10 point higher expense ratio than our French business, the loss of the reinsurance on the corp business, which had almost no expense ratio, and then also, the premium tax and policy collection fee in Brazil, which is now booked to top line and expenses and was before outside.

So if you now look at the individual contributions in P&C, actually a broad support of the good combined ratio. The number which is negatively peeking out is Germany, with 105% combined ratio. But actually with a quite high NatCat loads, not only this quarter, actually during the whole year. And you remember, we had the floods in the second quarter and in the third quarter already preannounced at our last analyst call, the big hailstorm, which I think muted from a heavy hailstorm to the highest hail event in the German market history, and which hit then Allianz EUR 330 million in total, of which EUR 200 million are included in the German number.

It's German started, which we explained to you in our May Capital Markets Day in detail and where we said we are on track. Is this endangered? We don't think so, because when the normalize the cat losses in our -- for the 9 months -- the 9 months German combined ratio, it's 96.3%, including the normalized cat of 4 points. And that should allow us to reach next year's 95.0% as calculated [ph].

Italy, extraordinarily low combined ratio, certainly supported, also again as last quarter, by good runoff. But again, also continue to outperform the market, and we believe we have here a sustainable difference to the markets.

Moving on to the investment income. A 10% drop in investment income is unusually high and also unexpectedly high. Half of it, so 5% drop would be our normal expectation in reduction and that is then also in the line interest and similar income explained. Actually, the line net harvesting and other and investment expenses explains the other 5% drop. And these are trading losses out of FX coming from investments in other currency. So emerging market bonds as the main category. And investment expenses, there are some one-off expenses on real estates.

Otherwise, our running yields stays actually continues to be good, but you can also see that reinvestment yields are still low. And if you all believe in rising interest rates, interest rates still need to raise a lot to reach the level of the current yields.

So now moving to the Life segment. We continue the story of good growth also in the third quarter. I think customers like our product and also the security and safety, which we are representing. That is very much visible in the German growth number, slide to quality, and also the modernized product offerings clearly helping here. Our new product generation, which is quite a bit as modified guarantees. So they are on one hand, offering more attractive return of opportunities for the customer, otherwise, they have guarantees which are also working very well in the Solvency II growth, making already on our agent sales more than 30% and continue to grow.

The other important area of growth is Italy where we are now -- almost all of the growth is coming from our new unit-linked product and I think that is a success story we have already spoken about before. The other markets, in particular, the one where you'll see a negative growth numbers is a focus on profitability, which I will highlight when we look at the development of the new business margin, it's quite visible.

Asia Pacific, the reduction is almost all coming from the discontinuation of our immediate annuity product in the Korean market and we certainly will talk about Korea at the end of the presentation, again.

So going to the Life and Health operating performance. EUR 769 million operating profit compared well to the midpoint of our operating profit for the year. The midpoint outlook is EUR 2,800,700,000 [ph] a quarter, so we are actually still 10% ahead of our midpoint outlook, which is a very strong performance. There are 2 numbers actually peeking out on the waterfall chart, that is a reduction in investment margin, the EUR 172 million, that has 3 factors. We had a higher level of realized gains in the U.S. a year ago, so that is more a baseline effect. Germany is EUR 58 million down, that is mainly coming from FX losses. Again, mainly the category of emerging market bonds. And Italy, EUR 20 million down. That was the planned effect of the de-risking and when we reduce our exposure to Italian government bonds.

In the U.S., you see a counter effect from the deck movement. So most of the EUR 100 million-plus is actually linked to the VA and FIA business in the U.S., and that is a more complex started to explain. It is actually following exactly the U.S. GAAP mechanic line by line. So each product category has its own deck. And depending on the investment results, which are also affected by hedge results in the U.S., it is actually ending up with the EUR 100 million plus. It's -- actually, you can only track the number by line of business. You cannot give 1 explanation, which would cover all the movements in 1, but it is the normal mechanic of this deck logic.

So if you go now to the valuation of the new business. So value of new businesses is actually back to a number above EUR 200 million, EUR 215 million. A strong recovery over last year, but also compared to previous quarters. So with 2.3%, I think we are starting to get into a range where we, as 1 of the leading life providers, should be standing. And I can -- I would only like to highlight a few of the numbers. And if you have more question, we can discuss it later on. I think the jump in the U.S. is very visible, 3.8 points is a great profitability number for U.S. FIA and VA business. Two drivers; one, the restructuring of the product, which we did already end of last year. And the second one, the impact of the rising yields in the U.S. added to this strong recovery. And then

I should highlight France, where we had really, a very disappointing and sobering new business margin in Q2 of close to 0. And here, we actively changed our business mix and took out from the shelf some of the products, which had negative margin and recovered now to a margin of 1.3%.

I think the other areas like Switzerland, reduction in volume but the redesign product allow us to earn at least some margin for us.

And then I would land over to Page 13, the investment margin. At first glance, the number's very stable year-over-year. But I would like to draw your attention to the margin, which shows here at 0.2%. 0.2% looks unchanged, but when we look at the second decimal point, then we had last year 22 basis points and this year, 17 basis points, so a reduction of 5 basis points is actually quite a lot. But this is mainly driven by the movement in trading losses, which I have explained before. Actually from a running yield perspective, I think we can keep the sound margin also into next year. And we said in the beginning of the year, we would expect for full year 75 basis points as a good and expected level of the margin, and we are very much on track in the 9 months. And I assume almost that we can stay there also for 2014.

And then I would move on to MCEV. A EUR 1 billion up is actually not a surprising movement, mainly reflecting as a change in interest rates. That is actually the main driver, and that is coming from quite a number of countries. Net capital movement is a number you all like very much that -- and me as well, that is EUR 1.3 billion of upstream dividends to the center form our Life units and is 63% higher than a year ago.

Now we come to asset management. A very reliable provider of operating profit and cash flows to the group and it continues to be one. The assets under management are pretty flat over the 9 months and also over last quarter. The only real driver who changed it is actually the dollar-euro exchange rate. And end of June, the Euro-dollar was 1 30 and now at end of September, it's now 1 35. And this movement of 3% in the exchange rate explains actually almost all movements under this -- of the third-party AUM. And the own assets which are being administered by AGI and PIMCO did not move at all. All effects there neutralized each other.

So what does this stable source of AUM result then in operating points. Well, actually, when we look over 12 months, the other net fee and commission income is substantially up by more than EUR 100 million despite the FX effect. And that reflects actually the increased margin of the book, which grow in total from 42.5 to 45.7. And when you look at the right-hand side, the margin increase is contributed by both PIMCO and Allianz global investors. Where we have a substantial drop is in the performance fee, but I think we were very consistent and always very transparent in our communication, that the high performance fee in Q3 2012 was based on settling one-offs as private equity funds, which will start at the post-subprime crisis and focused on subprime mortgage investments, and with the current interest and created this high performance fees.

And I would like to move to Page 17, where we have actually shown the complete waterfall in operating profit year-over-year. Actually, volume, as well as margin gives us additional EUR 200 million of operating profit. The drop in performance fees I just explained. Expense is not a big movement. And then we have also here in the operating profit, a substantial loss due to the dollar that is EUR 38 million for all of the elements explained in the waterfall. And so from an underlying operating performance, I still see PIMCO and Allianz global investors as a growing contributor to our base profit line.

Now coming to the last segment, our Corporate segment, with holding and treasury banking and some special investments. No big movements here. We had -- we have 2 effects; one is the release of expense provision from last year, which was linked to some investment activities, which we -- which did not realize the way we thought. And the other movement is we have here some additional profits coming from MA [ph] because we have some operational hedges in the holding book. But that is not a big number.

So now let's -- all the good news about the operating profit, how that now the operating profit translate into net income? Net income up 6%, and it is actually, from our perspective, a fairly eventless quarter. The non-operating items at a fairly low level, realized gains and losses and impairments are at the same level of EUR 130 million, interest expense from external debt slightly falling, and no special amortization or impairments on intangible assets. So therefore, the EUR 1.4 billion is probably a good and reasonable level coming out of an operating profit of 2.5.

Tax rate of 33% is very much at the normal level. What are the impairments? Actually, the impairments are linked to 2 disposals. One is a real estate activity in Italy, a joint venture which we are dissolving. And the other one is actually a state which we had in a smaller private bank in France, which we sold the bank to the owner -- back to the owner family.

So with this, despite all the FX movements, stable revenues, operating profit EUR 2.5 billion stable and also more sustainable than 12 months ago, shareholders' net income 6.3% up, and capital position really strong on all measurements.

Translating the third quarter and adding it to the previous 2 quarters actually gives then for the 9 months figures a 4.4% growth of the revenues to EUR 84 billion, EUR 7.7 billion operating profit means 8% up, and shareholders' net income, EUR 4.7 billion, up 19% over last year.

So a strong performance in the 9 months contributed and really added over the whole 9 months period.

So after all this strong messages, so what does it mean for the outlook? Should we just take the average of the first 3 quarters and add it at the fourth quarter? I think from the underlying performance, that is probably not a bad idea. But actually, I would like to point out that we are looking at a couple of very special points in the fourth quarter, which potentially reduce our operating performance in the fourth quarter between EUR 100 million and EUR 400 million. And let me explain the points.

There is 1 repeat [ph] question which took place and which is clearly a reality. So first estimates say EUR 100 million, but might also be a bit higher. I was also a bit too fast on August 2 to estimate the hailstorm from July 30, and it came in EUR 100 million more than the first day estimate.

So let's see how it develops. Technically, we are reviewing our new business and product strategy in Korea. And when we would close and open certain lines, we have probably to move in the DAC calculation from a total portfolio consideration to an individual line consideration. And that's potentially creates and accelerate the DAC amortization between 0 and EUR 150 million.

And last but not least, as we want to prepare also for a -- continue a successful future into 2014 and '15, we are starting additional IT investments. And one bigger investment is the data center consolidation and outsourcing, we are negotiating currently and that might lead to additional one-off expenses in the fourth quarter than we have to close and shutdown data centers, which are then being emptied and therefore, not anymore being operated.
So in total, these are all numbers, which are uncertain. Therefore, we put for all the items in total a range of EUR 100 million to EUR 400 million. And this one I would reflect also against a good underlying operating outlook for the fourth quarter. So that in total, our outlook is adjusted. Yes, we are optimistic to beat the 9.7 upper end of the range, but only slightly. And with this one, I would stop here and the hand over back to you to the questions.

# Question and Answer

**Operator**

[Operator Instructions] I'm going to take our first question from Peter Eliot of Berenberg.

**Peter Eliot**
*Berenberg, Research Division*

Three questions please. The first one on the asset manager. I was wondering if you're able to provide any comments told on trends past the end of Q3 in terms of flows or indeed anything else? Secondly, I was going to ask one -- there's been some press commentary around your reinsurance requirements that you might be looking to reduce your consumption. So I was wondering if you could talk to it about your appetite going forward? And then thirdly, just on the Life, I know your duration gap has closed quite significantly in the quarter, as a result of the duration of the liabilities falling from 8.4 to 7.9 years. I was just wondering if you could explain that move.

**Dieter F. Wemmer**
*CFO & Member of Management Board*

Okay. Peter, I'm very happy to explain this, the trends and flows. Well, since the Fed announced the potential tapering, actually our net in and outflows has certainly have worsened. We have given back quite a lot of our outperformance and inflows from the first 5 months of the year, and we are still at EUR 22 billion of net inflows from the beginning of the year, still a very strong performance also compared to our peers. But in the last months, we have given away some of the outperformance. So what is the expectation for the rest of the year and maybe also for the beginning of the year? I think you can have 2 series here. On one hand, well, it just continues as the last month. Every month a little bit of reduction and little leakage. So some small monthly outflows. Or you look at the short-term performance of PIMCO's funds, which had probably some weaker months in June, July and August, who are in a great catch-up in the outperformance in September and October, which could then also lead to attracting more customers. And I think the tools we will then all see together in 3 and in 6 months, and that is probably somewhere in the range of the 2 scenarios. Reinsurance consumption. On the cat buying and purchases, nothing is changing. It is true that on the more bread-and-butter reinsurance of our OEs, we are considering to keep more in-house and that would certainly help this net on premium and also maybe the one or other euro of additional profit. The duration gap in Life has 2 drivers -- or the closing of the duration gap. I think 1/3 of the closing -- of the gap closing comes really from the change in interest growth and in the second quarter, actually, there was more movement between 20 and 30 year on the swap curve than in May, June. And that has more impact on actually MCEV and also duration gap. And the second point is we changed also our model in our German Health business, as well as our German Life business. And the main change in our German Life business is actually that we updated our assumption. How many customers will, at point of retirement, take the annuity option and which one are taking the lump sum payments. And that changed this generation calculation.

**Operator**

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

**Farooq Hanif**
*Citigroup Inc, Research Division*

I've just got 3 question areas. Firstly, when you look at your underlying loss ratio, you talked about how this has improved and you can see that there's been a roughly 2 or just over 2 percentage points improvement since 2012, but that's roughly also equals your improvement from lower frequency. So I'm just wondering to what extent is this both comfort? Could we see a reversion with economic improvement and normalization going forward? So that's question one. Question two, on your economic solvency, could you perhaps share with us your internal solvency or at least qualitatively give us an idea of whether you're now moving into a more fruitful surplus capital position? And lastly, in Turkey, can you just confirm that the Q3 number is a good guideline for combined ratio with Yapi Kredi now included?

**Dieter F. Wemmer**
*CFO & Member of Management Board*

Okay. Well, underlying loss ratio improvements, I think, sure frequency is a driver of it. But I don't think that frequency is down only because of the weak economy in Italy and Spain. I think we see any way in the motor business a reduction in frequency, also as a consequence of technical improvements. And that is in particular visible on the heavier bodily injuries. There you see, clearly, a drop in frequency, which I link more to development of car technology and not of poor economy in Italy and Spain. And the other sobering version of the answer would be well, following Mario Draghi from last night, there will be no improvement in -- a rebound in frequency in Italy and Spain so quickly. So therefore, there I think our 2 points where I think we will continue to do this and actually it is also our underwriting and risk selection, which is also an important driver of frequency reduction. Otherwise, we could not say that we are in Italy 15 points in the loss ratio better than the competition, because the impact of the economy is the same with our competitors and with us. Economic solvency, are we in the surplus position? Well, we have not defined for ourselves where fruitful surplus position starts. Very simple for the reason that we are saying, well, potentially the EU gets to an end with the debate on Solvency II. Then Solvency II is finally calibrated and then we are also doing a final calibration step on our economic solvency. And after that, we start to think about whether we have really too much capital or whether it is just okay. Turkey combined ratio, I think the answer is yes, the third quarter reflects also what Yapi Kredi is contributing. However, the Turkish market is certainly more volatile than matured markets in Western Europe. So therefore, the number can certainly also move faster than in other markets that is not a form of a profit warning, that is just an experience with this market. So therefore, a guidance for this market is much more difficult as in other markets. The business is very short tail and the market is very price-sensitive, so you have really to continue to manage well and also the competition has to help that we keep it there. But in the low-90s, that is certainly something we should aim it.

**Farooq Hanif**
*Citigroup Inc, Research Division*

May I just quickly come back to economic solvency. You shared a 212% ratio with 1 and 200 year calibration. But where does it go to on your more sophisticated and harsher internal calculation?

**Dieter F. Wemmer**
*CFO & Member of Management Board*

Well, I think we are disclosing already enough solvency numbers. We should now not add another metric in public space. I'm more concerned that we are then confusing everybody.

**Operator**

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

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

A couple of points, really. Firstly on the P&C business, given the significant level of NatCat hits across Europe this year, would you guys comment a little bit on the pricing direction in some of your main markets? And then second point, just looking at the Korean business, obviously, you've made some changes there, and you've signaled there's going to be further restructuring and changes to the product mix there. If you could just talk a little bit more about what the products are in that market and how you're changing them, that would be great.

**Dieter F. Wemmer**
*CFO & Member of Management Board*

NatCat, yes. We are clearly believing that the pricing will continue to be hard in particular in markets like France and Germany. Germany is really hit the most by the cat events this year. And with the heavy cat events last -- actually, also, a yield environment, which is not too promising. I think we -- certainly, as you said, we reconfirmed this yesterday. There is only a chance for the insurance industry to focus on pricing and P&C. And that actually makes us also positive for these 2 markets. Although I think the cat events were, for us, manageable, yes, Germany had to bear a big share in it. But actually overall for the 9 months as a group, is pretty much on the level of our global cat budgets. Unevenly hit, but that is the global diversification as a market leader which helped here a lot. Korea -- well actually, when we would exactly know how we change the product mix and what will be our distribution and sales and product strategy going forward, then we would have already booked everything in the third quarter. So I have only really done this as a pre-announcement that this is work of the fourth quarter. And I'm very happy to answer your question in full detail and in a more satisfying way in February.

**Operator**

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

**Jonathan Michael Hocking**
*Morgan Stanley, Research Division*

I've got 3 questions, please. First 2 on economic solvency. Can you comment please on where the negotiations are with Solvency II in terms of the conversion sales forward rates for the German Life business and whether you're hopeful about getting a deal before the New Year? That's the first question. And then secondly, presentationally, with your economic solvency ratio, if we do get an agreement with Solvency II, you're going to recast that on the new rules, what are you going to do in terms of the grandfather? Are you going to effectively share the Solvency I position with the backbone and Solvency II for the new business? That's the second question. And the follow-up question, in terms of the cash from the Life business, can you give us some idea about the normalized sort of level of remittance from the free surface generating Life business who seems like the pretty punchy transfers for the 9 months.

**Dieter F. Wemmer**
*CFO & Member of Management Board*

Okay. I think the Solvency II negotiation are all very much on track. I think there is, at the moment on the volatility adjustment, there is one discussion open that is a treatment of this credit adjustment that is the parallel shift of the swap curve to adjust it towards 3. The Yapi proposal was 35 base points. We think from economic analysis, it is more 10 base points. What is actually the credit risk within the swap curve and there is, at the moment, a discussion who is actually setting this parameter? Should it be in the legal tax, should it be shifted into EIOPA's responsibility or should it be set by the EU Commission? And this 3 versions I think is on the whole compromise for the LTGA so for the long-term guarantee assessment, the main open points. When we change to the new Solvency II model, we would expect that our economic solvency model and the ratio is similar. And -- but of course, we have not yet done the final numbers and we have also not seen the final compromise. So therefore, that is our current assumption. And on cash for our Life business, I think in the last quarter, there are 1 or 2 bigger dividends still coming, so that we could end up the year roughly with EUR 1.5 billion in total that would be the expectation for the full year. Did I answer all points or did I forget something?

**Jonathan Michael Hocking**
*Morgan Stanley, Research Division*

No, no you did. I can come back to the second point, so...

**Dieter F. Wemmer**
*CFO & Member of Management Board*

Okay. One important point for us for the application of the transition rules, we are not considering to apply those transition. And I personally believe that a listed company would be ill advised to use the transition rules, because all of you would then wanted to know what is the solvency without transition and what that mean for future dividend paying capabilities. So to me, it's a no go for us.

**Jonathan Michael Hocking**

*Morgan Stanley, Research Division*

Okay. So should a fully loaded Solvency II. ratio. And depending on where Solvency II lands, are you potentially going to have your own economic solvency rule and use that as a binding constraints or are you going to use the Solvency II as a binding constraints, such as the number you published. If you think it ends up somewhere on economic, is it possible that you have a stronger definition yourself, which actually is the metric which constrains the distributors in capital, et cetera?

**Dieter F. Wemmer**
*CFO & Member of Management Board*

Well, there is an obvious binding constraints. We are a strong AA company and we are not BBB and we are also not planning to become BBB. So that is #1 constraint. And #2 also in the model itself, we have certainly on some of the parameters a different views than the EU and EIOPA, and we will continue to apply this whether this will create than in practice any big binding constraints I cannot say this yet, that has to be seen and practiced. And as this anyway a calculation, which has a lot of volatility coming from the financial market, it is actually impossible to predict which number will move how in certain financial market conditions and it's, I think, we have to gain altogether some experience when the models are spaced.

**Operator**

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

**Thomas Jacquet**
*Exane BNP Paribas, Research Division*

To come back on the reinsurance question. Could you share with us whether it's going to have an impact on the capital consumption of the group? And also, maybe a word on the earnings volatility that would derive from higher attachment points?

**Dieter F. Wemmer**
*CFO & Member of Management Board*

Well, as I said, we are not changing the purchase of the catastrophe coverages which are, from a group perspectives, the main driver of volatility. Here, we are talking more on reinsurance covers for large fire or large accidents or large liability cases on an individual OE level. On the group-wide diversification, I would not expect that this is giving any visible change in the volatility of the total operating profit. It might create, in individual countries, some couple of millions up or down. But for a group that should be really diversifying if these are all very independent and uncorrelated events. The capital consumption out of keeping this business, yes, it is additional earns premium we keep and as you can multiply earned premium with a certain factor in capital, but it is not a big number in our capital ratio, maybe 1 point or 2 in the capital ratio. So that is nothing which severely changing the world, but simplifies a lot administration.

**Operator**

We will now take our next question from Andy Broadfield of Barclays.

**Andrew Broadfield**
*Barclays PLC, Research Division*

Two main questions. One, so I just returned back to the capital question. I wanted to know you've explained this, obviously, to the uncertainty around that has been a major driver for your hesitance to give any firm levels, about the levels of guidance around targets on solvency coverage. I was wondering would -- if or when Solvency II finally is finalized, would you predict that, that would trigger a certain some sort of guidance that you would then subsequently give given these uncertainty around the requirements. That's question number one. Number two, on the asset management side, on the flow side, clearly, the -- you've got a lot of visibility around the mutual funds, but is not around the what we call the non-core assets. And we're seeing continued increase in that proportion of your overall assets, income in particular.

I was wondering whether you can give us a little bit more insight as to what's happening in the non-core funds rather than the core funds?

**Dieter F. Wemmer**
*CFO & Member of Management Board*

Yes. Andy, very happy to do so. So let's first with -- for sure, when we went to the full condition with Solvency II and everything is included, we will do a guidance on capital position. Unfortunately, and you all know this, the Solvency II story is not the last step in the capital story for our industry. There is this comp frame, I estimate, about the new capital requirement -- global capital requirements for international groups and an additional backstop for systemic important insurance group. And that flows then, certainly, during next year and 2015 still take some time before this part is also getting clearer and more transparent. Although I'm not expecting that this would, in the end, create a constrain for us. At the moment with regulatory road so much influx, you should be prepared for everything on the regulatory road, how this will work out. The volatility and the movements at PIMCO, the third quarter, our inflows in this non-core was fairly small. We had only EUR 2 billion of inflows in the non-core and the core had then the resulting number, which -- that leads to the EUR 28 billion, EUR 29 billion of net outflows. To some extent, you can describe the situation as a bit of last in, first out. It shows the retail growth we have seen in the first couple of months of the year as the one who has been taking the money out. So that is more the volatile part of the business. The rest is actually a very, very stable.

**Andrew Broadfield**
*Barclays PLC, Research Division*

And any guidance on the sorts of products that you've been seeing that -- I mean, that's only a small inflow, but whether sort of the fashions aligned?

**Dieter F. Wemmer**
*CFO & Member of Management Board*

Yes. As I said already, when Peter asked the first question, I think you can really look at the 2 series. Either it is -- this is a small leakage and dropping months over months until the interest rates curve have found more ground in that certain position and not uncertainty anymore. Or I think also an important factor on that is the more optimistic version as that PIMCO has a bit underperformed, in particular, in its mutual funds in the end of Q2 and beginning of Q3, and has actually now taken ground again in September and October. And that should be then also visible in customer confidence. So those are the 2 versions to look at. And I'm sure that PIMCO is fighting hard to get us to the more optimistic version. But I think small deductions is when you want to be very conservative, still leaves us with a lot of operating profit for the next quarters is the other version. And I leave this up to the individual analyst.

**Operator**

Our next question comes from Michael Huttner of JPMorgan.

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

And 2 questions. One of the one-off a kind of maybe a high-level view of these one-offs in Q4 might be to say that the pairing, the moving profits from 1 year to another by introducing them now. I mean, these one-offs could be next year potentially and potentially leaving a nice bigger upside to 2014 profits, which you will then report in your Jubilee year. I wonder if there's any kind of whatever on that. Secondly, 4.3% reserve release, which is also a grand number, could you give a little bit more color on this and maybe you did -- and I'm sorry if I didn't follow it. My question here is to understand whether this level is kind of maybe sustainable certainly from the conference calls of the reinsurers and not your direct business. There seems to be a general trend for inflation, low-inflation linked reserve releases, which seems to be -- well, at least, low inflation I see at the moment kind of sustainable. And then the last one on the German pricing, I wonder if you could give a little bit more color. I was specifically looking at Slide 67, and there tax sounds positive, but the color is kind of orange, which I'm taking as negative. And I just wondered how these squares with the view that maybe pricing should firm for solvencies and natural catastrophes.

**Dieter F. Wemmer**
*CFO & Member of Management Board*

Thank you, Michael. As always, very sophisticated question. I think your first question is what should I say? I think in the end, we are not in the phase that we have to derisk our balance sheet, that we have to do any financial restructuring because we are in balance sheet constraints or capital constraints. We are certainly very healthy in our capital position. Therefore, our focus is clearly on improving our business models and see what we can do. And I think the data center outsourcing is nothing created to manage results that is actually to reduce expenses for the future. And I think has, at least in the German press, already been announced some weeks ago that we are in final negotiation with the big blue in the U.S. to take over the management of our data center. So that is not a secret really. And that will require then some write-down of operating assets, very simple computers in the country, which are not used anymore. You cannot amortize over the rest of their life spend anymore. So that is one element. And then the Korean case, I think that it's anyway something we are discussing internally already for some time. We have a new head for Asia starting his job on January 1. And I think that is all a driver that we have now at the moment and a closer look at what we are doing also there. Interest rates in Korea at also at a level -- they were higher than in Germany, but still at a low level. And it is not the markets where you can get rich with traditional life products. And that is exactly all the drivers what we are doing and when it has done a consequence on the debt calculation, we book it when the numbers are clear. I would have been pleased to book it already in September, but I think we are not yet there that we can say the strategy is finalized. Inflation linked reserve one-off, yes, certainly that's lower inflation. It's also helpful for -- in P&C insurers that it's clear. And it beats the case that inflation is low and that is helped by various things actually in -- again, in Italy, you have not only the frequency reduction, you have actually also for some of the large changes they did a year -- a good year ago, less bodily injuries, in particular the big [ph] losses substantially down by law. And so therefore, that certainly has also helped average case size. Is this exactly linked to the low inflation environment, yet. Well, yes and no. The garages and cost of garages are not increasing and also spare parts are probably not increasing in cost. So that part all helps to keep the numbers where they are. And would also make me carefully optimistic that our reserve situation is in, at the moment, very sustainable position and that we have not emptied or drawn [ph] to create a one-off in Q3.

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

And on the pricing?

**Dieter F. Wemmer**
*CFO & Member of Management Board*

The price changes. Well, first of all, orange is the color we always use for the P&C segment, so that should be good matching. I think that we are showing here the increases for the first 9 months, and it is more a backwards-looking statement, and I understood also the earlier question more, what are you expecting on price increases going forward and what is the impact of the cat losses? And I think in general, in Germany, the market is very hard. And I wouldn't see that there are any serious competitor who has the guts but also the money at the moment to be very aggressive on pricing. And in France, people are also looking very much on increasing prices to bring the combined ratios to a good level. I think in France, we for ourselves will see a combination of general price increases but also weak underwriting. We will continue to drop some of the portfolios we have taken over from Eurocourtage that was part of the acquisition plan. And I have spoken about it write off from the beginning after the acquisition. And in France, we have at the moment also higher expense ratio because we are doing a very large investment into a single IT platform replacing the existing 65 IT platforms. And that is a fairly large investment project, which has also driven up expense ratio and combined ratio in France. So that is -- we are not shying away at the moment from bigger investments into a better future because we have certainly, at the moment, the money to finance these investments.

**Operator**

We will now take our next question from Michael Klien of Nomura.

**Michael Klien**
*Nomura Securities Co. Ltd., Research Division*

I have 3 questions. Firstly, I would like to return to the asset management business, you have spoken quite a bit about flows as a leading indicator, I guess, of earnings. Can you maybe talk about the mix change or give us -- help us understand how the margins were in the inflows and outflows and, therefore, the margin of the net outflow number and, therefore, maybe give us an idea how this might be changing in the coming quarters as well. And second, I guess, going back to these one-offs that you're guiding for in Q4, how should we think about these in terms of your slightly above 9.7 billion guidance. If you have closer to 100 million in overall sum of these charges, would you then be at closer to 10 billion or is it sort of a number and then some of it you might use into 2014? And my third question would be on restructuring costs. If I saw correctly in the operating profits for Q3, you had a positive 16 million release. Is this now something that we should be expecting in coming quarters, i.e. that we should be expecting either very low restructuring charges or releases to come through going forward?

**Dieter F. Wemmer**
*CFO & Member of Management Board*

Thank you, Michael. I think the average margin for our asset management business in Q3 increased by another half a point over Q2. And probably, we are now in total at a good level that we are, that the margin continues to move up every quarter that would require more movement in the underlying funds. And as I explained before, the shift of non-core -- or core to non-core was less pronounced in Q3 than in previous quarters. So therefore, I think it is a good level of where we are at the moment. The positive restructuring costs, that is easy, that was in the cost of the segment, where I said we released a provision for a restructuring plan, which did not play out as planned. And therefore, we released it. That is, I think, a very unusual situation. And I would not expect that this is happening regularly. That would be not a good quality of setting restructuring provisions. And here, it has a good reason because the negotiations went in a different direction and we found an economically better solution. Therefore, the restructuring charge was not needed. But otherwise restructuring charges are being consumed as set. So on the guidance, for sure, we are explaining here expectations. There is still volatility in the numbers, otherwise, we could publish now already our Q4 results, and it would be so easy. Therefore, I think there is always a range around the outcome also of the underlying, and everything is possible. We are giving here an outlook. It is possible that we miss the outlook. It is possible that we outperformed the outlook or maybe we hit it. So I don't think that besides the outlook, I can give now any guidance to give a second version of the outlook. I think that would be not part of the outlook system.

**Operator**

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

**Andrew James Ritchie**
*Autonomous Research LLP*

A couple of quick questions. Sorry to go back, first of all, on asset management, on the non-core flows. And I'm just referring to the transcript from the 2Q call. And then, Dieter, you seemed a lot more confident about the ability of non-core flows to offset outflows in the core, and that, to some extent, happened in Q3. Can you just give us any more color again on what particular product areas saw inflows and outflows in non-core? And how sensitive do you think those non-core flows are to rises in benchmark yields? They seem to have been quite sensitive in Q3. Just any more color on non-core. You seem to give a bit more around 2Q. So specifically, the product areas that are seeing the most traction. Second question, real asset deployment. You talked at the very beginning about your infrastructure investments and you said, I think, you want to use 1 billion of economic capital roughly a year. Where are you on that for this year, and what's the feeling about further realized investment next year? And final question, just on normalized business and the underlying performance, underlying loss ratio. If I look at your business, it looks like kind of 1/3 of it is underperforming versus where it could get to, 1/3 is kind of in-line and 1/3 maybe is enjoying supernormal profitability. What do you think is the outlook for the underlying loss ratio from this point? Can it really get much better from here?

**Dieter F. Wemmer**
*CFO & Member of Management Board*

Okay. Let's start with asset management. You are absolutely right, Andrew. I was more optimistic on the non-core flow offset. I think PIMCO's products are more focused on long duration income, emerging markets and then an unconstrained bond families that were not customers' favorite in the third quarter. So customers looked more at multi-assets alternatives. The shift to equities is actually more out of cash and not out of fixed income investments. But also, our peers are learning and, certainly, did not watch silently how PIMCO is taking a lot of the inflows in the first 5 months and waiting for the rest of the year. It is a very excess and heavy competitive market. And I think competitors have also successful months, and I'm sure that PIMCO is striking back on this one, and this will not be happening after the month. But certainly, our general confidence in PIMCO is unchanged. That does not mean that you have to be the winner of everything in every month.

**Andrew James Ritchie**
*Autonomous Research LLP*

There was a bit of -- I guess, there was a specific issue on emerging markets particularly at which wouldn't have helped, I guess?

**Dieter F. Wemmer**
*CFO & Member of Management Board*

Sure. And let's see how -- when the currencies are stabilizing again or, actually, changing again, then probably the money will also flow back into these categories. But also the long-duration funds were also not really high in demand in the third quarter. And that were products which were very well working in the first 5 months. On the real asset side, yes, we have already increased our investments in infrastructure, renewable energy or other infrastructure lots. But also, I mentioned it in the beginning that we have now 1.7 billion in renewable energy and about the same amount in other infrastructure. Actually, plus we have invested this year 1 billion additional in real estate, and here, I mean investments, not capital. And we have increased our equity quarter by almost 1 percentage point. And that is one of the investments into real assets that actually had a result of already a nice unrealized, additional unrealized gains during Q3. And that part, I think, is very much on track. So I think, at the moment, the EUR 1 billion capital allocation is well spent. I did not mention that a new investment which closed in the first quarter was this infrastructure investment, Net4Gas. That is a Czech gas pipeline system. And that was a EUR 400 million investment for us.

**Andrew James Ritchie**
*Autonomous Research LLP*

Okay. So more or less, it's being spent for this year pretty much then? And then...

**Dieter F. Wemmer**
*CFO & Member of Management Board*

Well, I think that, that process on generating infrastructure and real estate is a continuous process because these are 400 million in a single investment. These are like M&A deals and they run as transactions, so you cannot schedule it quarter by quarter. You have to see there is something good. And when it closes, it closes. Otherwise, there might also be quarters where everybody else get something and we don't get anything.

**Andrew James Ritchie**
*Autonomous Research LLP*

But we should think about that as still ongoing, essentially, that sort of capital investment?

**Dieter F. Wemmer**
*CFO & Member of Management Board*

Yes, we announced it as a 3-year program and you have to see it as a program which will continue for this period. Underlying performance. Well, I'm not sure where you see this 1/3 of the P&C business which is not doing so well. I think you are probably looking very much to the German numbers, which make already almost 1/4 of the portfolio. Germany is only hit by cat losses. And I think on cat losses, global diversification is a fair argument and not an invented argument. And therefore, I think that we see a lot of upside, therefore, in Germany because we are not assuming that we will have this historical hailstorms every year. Otherwise, we have to change prices a lot, that would help our top line a lot.

**Operator**

We will now take our next question from Michael Haid of MainFirst Bank.

**Michael Hermann Haid**
*MainFirst Bank AG, Research Division*

Michael Haid, MainFirst Bank. Two questions. Regarding German P&C insurance, as you just said, the top line, minus 0.3% actual growth, 1.0% internal growth. Can you explain the difference here? I'm not aware of any that it should be different. And more broadly speaking, we've seen price increases in motor, other business. My understanding is more stable, in light of that, I would've expected higher volume in Germany. Can you explain this? And second, the hailstorm losses, you have given a fee -- net losses of 332 million and I think 107 million. Can you give us also the gross losses?

**Dieter F. Wemmer**
*CFO & Member of Management Board*

I'll start with the hailstorms. 330 million is the gross loss, of which, 200 million are booked under the German OE and the rest under the reinsurance division, roughly. There is no external reinsurance on this hail event. That is all in-house because our mega cat cover, I think, starts at 600 or something like this. So that -- therefore, it's really all 100% for ourselves. The gross number, minus 0.3%, and internal growth, plus 1%. Yes, there is certainly no currency impact. It is a very simple transfer of the joint venture with VW from the German OE to the unit Global Automotive, which we are showing under Allianz Worldwide Partners. So the premium moved up on the slide from the first line to line #6. But it is still the same premium on the page. And therefore, on the Allianz Worldwide Partner, you'll see the opposite effect. They have a lower premium than -- in internal growth than in absolute growth, and they have only very small currency effect because it is mainly euro dominated business -- denominated business. So therefore, that is the counter-effect.

**Michael Hermann Haid**
*MainFirst Bank AG, Research Division*

And why is the German business not growing more when we have these price increases in -- especially in motor?

**Dieter F. Wemmer**
*CFO & Member of Management Board*

I think the motor line shows a premium growth. We are losing in other lines of business.

**Michael Rohr**
*MainFirst Bank AG, Research Division*

And the reason for that?

**Dieter F. Wemmer**
*CFO & Member of Management Board*

I think it is retail customers are also saving on their insurance and look where they can save some premium. Certainly, that is still something where we are looking at how we can create more growth in the non-motor business. But that problem is not yet fully addressed.

**Operator**

We will now take our next question from Blair Stewart of Bank of America.

**Blair Thomson Stewart**
*BofA Merrill Lynch, Research Division*

Two quick questions left. Firstly, you talked, Dieter, I think, in the past about accelerating the pace of growth in Italian P&C. No obvious evidence of that yet. I just wonder if that is still the strategy and how that's going. And secondly, looking at your life business, I noticed for the cumulative 9 months that single premiums were up quite strongly but regular premiums were flat. I would have thought given the bias or the increased emphasis on protection, regular premiums might be starting to go up. Can you perhaps expand a little bit on the -- on what's happening within the mix there?

**Dieter F. Wemmer**
*CFO & Member of Management Board*

Well, let me start with the Life question. Even when you start focusing on protection business, premium volumes in relation to products that's even the regular premium product to savings is 1:10. So that means before you see premium growth in such a large balance sheet and large life portfolio coming from protection, you need to insure almost every inhabitant on this planet. So I think that is certainly something which will take quite some time before you see, and that is, in particular, we did never say that we would stop a profitable savings business or profitable single premium business. And when the new business margin are at a good level, we are happy to sell the product and we will continue to do so. We are more looking that the capital consumption of the product is being reduced. And that is what I mentioned, in particular for the German business but also the Swiss business, that we have redesigned products, or in Italy, with the unit-linked, which is replacing more the traditional, or in Belgium, where we have reduced guarantees to 0. These are all very positive changes in our business mix. And therefore, from my perspective, we like the gross number, what we have. The other question was on Italian P&C. Well, that is a question how you look at plus 2%. The market's number for the 9 months, I would expect that the market is shrinking some 5%, 6%, or even more. And then 2% plus is, in a relative position, 8%. So actually, when you look at our market share development, I think, we haven't grown our market share in Italy so strongly as in 2013 for many years, and -- that you get to a double-digit number in growth, that would also require that the market is expanding and, certainly, not in the current environment. As the Italian economy recovers, I think we certainly continue what we do at the moment.

**Operator**

We will take our last question from Nick Holmes of Societe Generale.

**Nick Holmes**
*Societe Generale Cross Asset Research*

Two questions on life. The first one is your investment margin fell partly due to lower realized gains. And I wonder if you could say whether we should expect lower gains going forward or whether this is a one-off? And second question is looking at U.S. life, I wondered if you'd give us a bit more color on the new products. I mean, you mentioned, I think, new products in fixed annuities, variable annuities. What are you doing? Are you basically just lowering the guarantees? And if so, I mean, they seemed to be selling reasonably well, so the question is how is the competition responding? Are you finding that it's a favorable competitive environment?

**Dieter F. Wemmer**
*CFO & Member of Management Board*

Nick, thank you very much. I'm not sure, maybe I have mentioned it on the investment margin, otherwise, I should have certainly done this. Yes, it is lower realized gains, but actually, included in this line are also the trading losses and -- which is actually the main impact factor in Q3. And that were mainly coming from the FX. That was, therefore, truly a one-off and has nothing to do with generating through our real assets also more potential for gain realization. I see it much more as a trading effect and trading items which grow P&L immediately without being realized. So it's not fading in the sense of selling and buying.

**Nick Holmes**
*Societe Generale Cross Asset Research*

Okay. So I mean, if you look at Slide 74, you can see that, historically, you've normally had reasonably large realized gains or large net harvesting, as you call it. And so we go back to that sort of kind of run rates, do we?

**Dieter F. Wemmer**
*CFO & Member of Management Board*

I think we will continue to have a harvesting. Look, as long as the yield curve has its current steepness, you get an automatic harvesting because you will never keep a bond which has, let's say, is in the last 18 months to maturity. You always trade it, because you are not getting for the last 18 months any real return with the low yields in the short end, which is probably not changing when the ECB is moving it's rates to nothing, that means that the short end is even more under pressure to stay low than the long end. That means we will continue to harvest also this part. So that will be actually be generated across the flow. On the life product, actually the life products were not changed in the beginning of this year. We changed it already a year ago. But we are now launching or have launched a new product this September, which is obviously not yet in the number. But what we are doing in general is we have a lower roll up of the fees. That means we keep for ourselves more flexibility on the fees that we can adjust it. We have higher mortality charges. We have reduced the rider options and the guarantees involved in the rider. That are the main changes which helped profitability. And we discussed it a year ago when we had actually a drop in new business sales because the new product has not sort of the easiest start. But in the meantime, I think the new products are selling well, the volumes are reasonable and the profitability is much better than before.

**Nick Holmes**
*Societe Generale Cross Asset Research*

So we should, therefore, take away the improvement in the U.S. life margin to 3.8% is due to the improvement in the macro environment? It's not new products?

**Dieter F. Wemmer**
*CFO & Member of Management Board*

Well, it is new products...

**Nick Holmes**
*Societe Generale Cross Asset Research*

Or repricing?

**Dieter F. Wemmer**
*CFO & Member of Management Board*

Repricing, yes, the products in its general nature as the same as before. There's a fine tuning of product generation. But our targeted new business margin for the year was 3.0%. So that was, anyway, the plan, and we certainly did not plan for the change in U.S. treasury rates. And that additional 80 basis points that you're now seeing 3.8% instead of 3.0%, that is the macro change.

**Oliver Schmidt**
*Head of Investor Relations*

All right. With this, we say, thank you, everybody. Thanks for having joined the call. We wish you a pleasant remaining afternoon and a hopefully undisturbed weekend. Goodbye.

**Dieter F. Wemmer**
*CFO & Member of Management Board*

Yes, same for me. Talk too you soon. Bye.

**Operator**

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