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Allianz SE DB:ALV

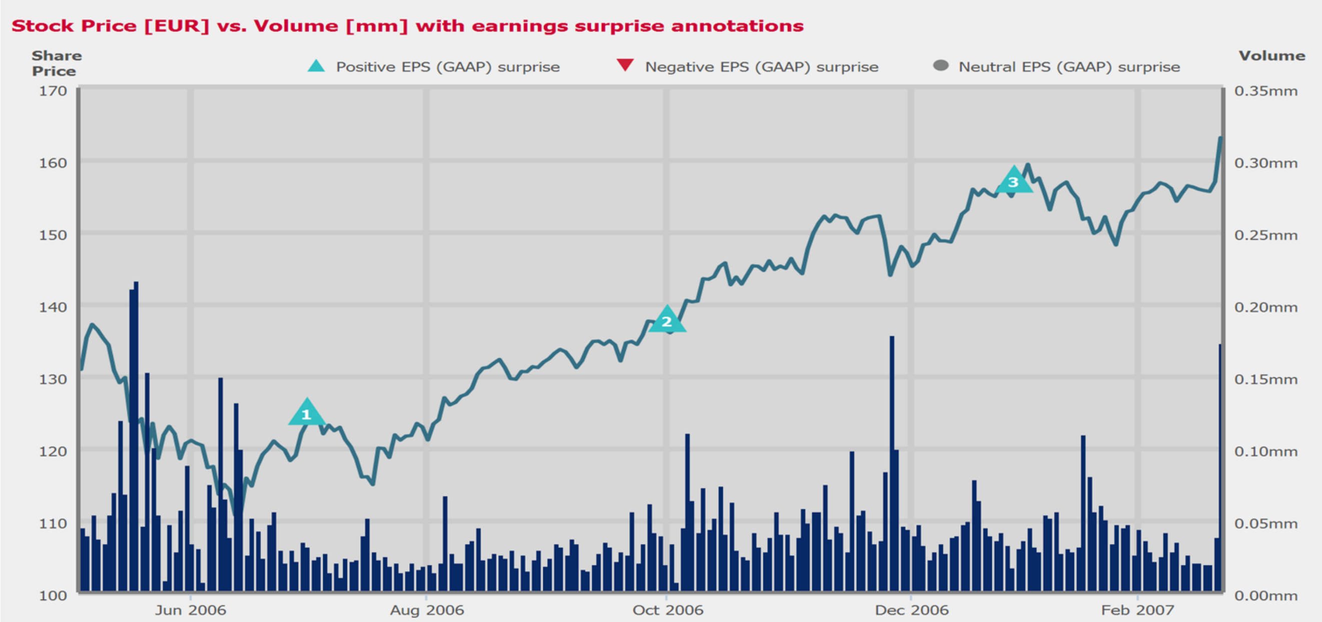
FQ1 2007 Earnings Call Transcripts

Tuesday, May 08, 2007 1:00 PM GMT

S&P Capital IQ Estimates

	-FQ1 2007-			-FQ2 2007-	-FY 2007-	-FY 2008-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS (GAAP)	5.92	7.34	▲23.99	4.44	16.74	18.27
Revenue (mm)	29532.50	29323.00	▼(0.71 %)	-	101582.57	105822.56

Currency: EUR
Consensus as of May-08-2007 1:42 PM GMT



- EPS (GAAP) -

	CONSENSUS	ACTUAL	SURPRISE
FQ1 2006	-	4.39	-
FQ2 2006	3.82	5.62	▲1 47.12 %
FQ3 2006	3.25	3.93	▲2 20.92 %
FQ4 2006	3.10	3.20	▲3 3.23 %

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Call Participants

EXECUTIVES

Helmut Perlet
Former Chairman of Supervisory Board and Member of Joint Advisory Council

Oliver Schmidt
Head of Investor Relations

ANALYSTS

Brian Shea
BofA Merrill Lynch, Research Division

Franklin Stoffel

James B. Quin
Citigroup Inc, Research Division

Michael Hermann Haid
CA Cheuvreux, Research Division

Michael Igor Huttner
JP Morgan Chase & Co, Research Division

Spencer Horgan
Deutsche Bank AG, Research Division

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Presentation

Oliver Schmidt
Head of Investor Relations

Well, good afternoon, ladies and gentlemen. Welcome to the Allianz conference call. As you know, we have published some core figures for the first quarter already last week. Today, we want to discuss the financial and strategic development in detail. As always, Helmut will be guiding you through the presentation and answering your questions afterwards.

Due to the absence of major funnies [ph], I doubt that we'll have a long call today, but if needed, we are happy to spend some 90 minutes with you. We have to finish at 4:30 German time at the latest. If this is still not enough to cover all open issues, the Investor Relations team will, of course, be happy to take remaining questions after the call as well.

And with that, I'd like to hand over to Helmut.

Helmut Perlet
Former Chairman of Supervisory Board and Member of Joint Advisory Council

Yes, hi. Good afternoon. I'm happy to talk you through the numbers. I think we had a good start to 2007. The operating profit is up 7.2%, and this is likely effect of the ongoing operational improvement across all segments, as well as a result of what I think a well-diversified portfolio, which allowed us ultimately to compensate for significantly higher NatCats than we had in Q1 of 2006.

I think, in addition to that, we have taken the advantage of the strong performance of our equity portfolio over the last months and harvested about EUR 2 billion in net capital gains, which really added significantly to that big chunk in net income, 82% up to EUR 3.2 billion.

With that, let's look into the details of the drivers of the result, and let's start out with revenues. Revenues are down 1%. And let me clearly state, we cannot be satisfied, albeit this result is in line with expectations, and it should not come as a surprise to you. Maybe let me quickly explain why I think, first and foremost, the major impact came from our situation in the life insurance business in the United States, which you are well aware of. Just to remind you, in 2006, the production went down from about USD $3.3 billion in Q1 '06 all the way to USD $2.2 billion in the first quarter. We have now, in the first quarter 2007, based on all the activities and measures I've told you during our annual analyst conference, based on those measures, management has been able to stabilize the premium shortfall, which I think is a good result. Well, long story short, we are missing EUR 1.1 billion of premiums, and that, of course, adds to the negative growth of 3.9% in the Life Health business. And on top of that, revenue development was also impacted by a weak U.S. dollar, which apart from the impact on the insurance business is immediately visible. If you look to the Asset Management figures, total growth 3.9% without the weakening of the U.S. dollar, i.e. unstable FX rate, that growth would have been about 9.9%, i.e. in line with our target.

Now looking at the other 2 segments, revenues in Banking, growth is strong at around 8%. Markets in the P&C business remain difficult, that is to say, very competitive, and we are still favoring profit over volume. We are successfully executing this strategy, and therefore the 0.3% internal growth is what we expected for Q1.

Now with that, let's look at the operating profit, Page 4. And I think if you look at this picture then you see, A, that there's a shortfall in P&C. That was largely driven by the winter storms, EUR 350 million of negative impact. The good news is really that this has been all compensated by improvements in the other segments, including the corporate segment. And I think that points to the already high level of profitability we have achieved in those 4 segments. What I'm really particularly pleased about is that we had -- in previous quarters, we had very often discussions about high dependency on the P&C contribution to operating profit, 55% plus. Now this quarter, the contribution from P&C is only around 44%, and still we have improved significantly from a group point of view.

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Now -- and I come to that later on, 7.2% doesn't precisely equalize the 10% target we have put out, but please keep in mind, A, this 10% target is an average target over the 3 years and cannot be applied mechanically quarter-by-quarter as there is seasonalities, and as we have seen this quarter, there's also some one-off impacts where we have a clear balance on the negative side with the impact from NatCat which by far outweighs positive impacts which we had, for example, on the banking side. But again, I will talk to that in more detail when we come to the segments. Against this background, to summarize this, I remain confident that we are able to deliver to our target of 10% growth in operating profit.

Nonoperating, Page 5. I think the main impact I have already mentioned, equity harvesting 6.6%, or in absolute terms, approximately EUR 2 billion of net capital gains. That is against the background of various considerations and activities. We clearly went for an early cancellation of our exchangeable bond by paying back in kind using Munich Re shares. We also executed a broad range of divestments in order to fund the minority buyout of the AGF shareholders. And with all that, we clearly reduced our equity gearing to 0.66, even against the background of further increasing equity markets, and we are on a good way to our target, which we mentioned is 0.6. Now I think apart from that, there's really nothing spectacular with nonoperating items.

So let's look at net income. Our income before taxes and minorities is up roughly 50% to now EUR 4.5 billion. Income taxes remain more or less flat. The effective tax rate is 21.2%. That has to be understood because of the fact there is high tax-exempt capital gains, and also, our minority interests remain more or less flat, thanks to the -- a 100% ownership of RAS. So altogether, that gets us to EUR 3.2 billion of net income. But please do me a favor and don't multiply this number by 4 in order to come up with some estimates for 2007 net income. I think, all things being equal, we have no further appetite for realizing a large number of capital gains. I mean, that obviously depends also a little bit on specific situations and facts and circumstances on the market. But as of today, with EUR 2 billion of net capital gains, we are already ahead of a normalized level of gain taking, and so, again, we are not planning for further major initiatives here.

Shareholders' equity, Page #7, has increased to EUR 52.3 billion. That is up 3.6% or roughly EUR 1.8 billion. Now you might ask, why is it only up EUR 1.8 billion while you guys have made EUR 3.2 billion of profit? Please keep in mind that realizing unrealized gains is just a shift in the categories of surplus with no real addition to surplus.

Our overall capital base, I think, remains strong. We are still, end of March, we are at a -- and that is on Page 8, we are at a solvency ratio based on the financial conglomerate directive of 194%. Also, if you look at the risk capital, there's not a lot of change, we are still remaining slightly below 200% internal solvency ratio.

And now we have talked during our annual conference in February about the impact of the minority buyouts, and we've given you some update, A, on the result of the AGF tender offer on Page 9. I think you all know the news, so I do not need to spend a lot of time. We are now owning 95.4% in AGF. That would give us the opportunity to initiate a squeeze out, and as soon as the formal procedure is initiated we will, as soon as possible, give you all the details and information to the public. But today, apart from the fact that we are intending to do the squeeze out, I beg your understanding that I cannot give you any more details.

But what you might interested in -- be interested in on Page 10 is here, we have some pro forma information, pro forma information on the basis assuming that we have already owned 95.4% shares in AGF since January 1, 2007. And then you can see that based on that, our solvency ratio is going down to 176%. I think if I remember correctly, I gave you 173% in February, but here you have to keep in mind the delta of that number was calculated on 100% basis, which of course, would have some impact again. And then, we've given you pro forma information on the EPS. EPS going up from EUR 7.51 to EUR 7.54. So the transaction is accretive from day one.

Now again, maybe to answer already one of your questions. Because when we announced the deal in January, we said we do expect 2% accretion in EPS, which you can see here. But please bear with me for a second, that number of EUR 7.45 is somewhat understated at that point in time because of the fact that we had very high capital gains in the group, and none of these capital gains really was taken at the level

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of AGF, and that, of course, has a negative impact on this accretion. So over the course of the year, all things being equal, I would expect that we are getting to the originally announced up to 2% accretion.

With that, let's move on to P&C. If you look at the numbers, I think one can say this is another strong quarter, keeping in mind that Kyrill resulted in a net burden of EUR 350 million or more precisely EUR 340 million. The other EUR 9 million of EUR 10 million was from a flood in Jakarta but overall, NatCat load was EUR 350 million. That translates into about 3.7 percentage points combined ratio. And actually, if you look at the right-hand side at the development of the operating drivers, you can see that the underwriting result is only down by roughly EUR 200 million, i.e. only 2 percentage points combined ratio. Having said this, obviously, the conclusion is that the business, apart from NatCat, shows further significant improvement. We see also some positive movement in our operating investment income. That is, without capital gains, but the matter of the fact is that the book yield due to higher yields for net new investments has increased by 10 basis points for the whole segment, and then of course, it's the first to be a sustainable contribution also for the rest of -- for the other quarters of this year.

Now let's look at the development of gross premiums written. Top line is more or less flat. Adjusted for FX, we have an internal growth of 0.3%, which is not much but looks positive against a minus 1% last year. I think if you look on the left-hand side, across the development of the various countries, you see mixed developments. We have in some major markets like Germany, France, Italy and in the United States, there is slightly declining or flat development. In Europe, the decline in the gross premiums written is largely due to the development on the motor business where we have, based on better frequency, we have to brand higher bonuses for our customers, and we could not compensate for the reduction in bonuses by price increases. But nevertheless, apart from the impact on top line, this is good news because with lower frequency that should also have some positive impact on the loss ratio and you will see this actually on the next -- on one of the next slides.

One comment on Fireman's Fund, the minus 4%, obviously in absolute terms it's more than just minus 4%, but above EUR 80 million of this development is due to the weak dollar. And the rest, the minus 4% is more or less a reduction premium in our agriculture business. Part of that is timing, the rest is real reduction. What is more important that Fireman's Fund, I think, good news is that the company has managed in a pretty sharply declining commercial lines market in Q1 to maintain the pricing and, with that, to also maintain the same level of combined ratio in these lines of business.

Now those impacts have been made up by some significant growths in other markets and segments. It's probably worthwhile to mention 2 things to you, A, that is not visible from the slides. We have increased our net retention also in line with the communication from February by 0.86% up to 88.8%, plus having just talked about the motor business, if you look at the total motor business, Allianz Group worldwide, our combined ratio in motor in Q1 was 95%. And then I think it's a pretty good result.

Now let's look at the combined ratio. If you look at the graph on the right-hand side, you'll see that the combined ratio has worsened by 2.1%. And I come to the details as far as the loss ratio is regarded on the next slide. Where I'm clearly disappointed is the development of the expense ratio, 28.5% last year, 28.6% this year. This is clearly not what we can be satisfied with, and we are working hard on that. Clearly, the major point of this development is going to be addressed with the reorganizations in Germany, Italy and the United States, and all of you know the figures, plus the introduction of our target operating model. All those measures have not yet shown significant impact on the loss ratio that is in line with our plan and the execution, but apart from that, we need to make sure that also for the rest of our expenses that there is the necessary accountability and discipline in place. In particular, in times where you have very strong and very favorable loss ratios, we absolutely need to make sure that there is no complacency, and this is high ranking on our priority list.

Now if we look in more detail on the development of the loss ratio on Page 15. Then you can see on the left-hand side, upper point, that the accident year loss ratio is 70.4%. There's an impact of 3.7 percentage points from the NatCats as opposed of only 0.4% in Q1 in 2006. You'll see on the bottom on the left-hand side that we have again solid development and stable development in our run-offs, positive run-off result of 2.2%, slightly higher than in Q1 in 2006. If you reduce the calendar year loss ratio, if you adjust the calendar year loss ratio for the change in NatCats, for the change in run-off, then you'll come

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to, right-hand side, what we call accident year or underlying accident year loss ratio of 66.7%, one percentage point better than in the 2 quarters of '06 and '05. And this is what I referred to earlier on that the underlying quality of the business has further improved. And if you bear with me for a second, that for the full year, we are ending with a normalized NatCat exposure of round about 2 percentage points. I'm very comfortable that we're going to make and achieve our 94% combined ratio target.

Now on Page 16, you have all the details on investment income. I just would like to draw your attention to the lower part of the left-hand side, current yield of debt securities, that is what I have referred to earlier on. 10 basis points improvement of our run rate.

With that, let's move on to Life Health. On Page 18, you see that we topped an exceptionally good first quarter in 2006. Operating profit is up 3.7%, now at EUR 750 million. On balance, this improvement was a result of lower expenses, i.e. higher expense margins that you can see on the right-hand side, operating profit drivers. And there was also some contribution and positive impact on that improvement in expense margin from true-up effects on DACs.

If you look at the technical margins and investment margin, those are pretty much stable. One comment regarding the investment margin, we see improvement of the investment margins in almost all of our companies. But that has been compensated by accounting volatility concerning our hedge approach or hedge activities in the -- more than compensated by these accounting volatility regarding our hedges in the United States.

Now if we look at the premium developments, top line minus 3.9%. Half of this drop was driven by FX effects, in particular by the U.S. dollar but also by Asian currencies. The major impact you can see on the table on the left-hand side, Allianz Life U.S. is down 34.4% in euro terms. That is one impact, and I'm going to comment on that one in just a second.

The other impact really is -- or the other thing I would like to mention is Italy. If you take the 2 companies together, RAS and Lloyd, we see a growth over Q1 '06 of 24.8%. That is largely driven by Credit RAS, our joint venture company with UniCredito, which has posted significant growth and outperformed the markets clearly. That was somewhat supported by the fact that you'll remember, I told you starting January 2007, our share in the production will be reduced to 50%. That has been postponed to April 1 so still, depending to what -- we had a production share of 65%, but nevertheless, apart from that, still really for us on an apples-to-apples basis was, of course, growing very strongly.

Let me make 2 remarks. If you look at the left-hand side, you see rather moderate numbers on German Life and AGF. In Germany, there is basically 2 impacts. One is, last year, we are benefited from a step in the so-called Riester staircase. That was significant influence plus we see also a pretty large shortfall of close to EUR 100 billion in short-term savings products in Germany where we stayed to a rather unattractive interest rate for the policyholders, and therefore, they declined to invest into this product. But this is product, as I said, is only short term and was very little or close to 0 margin.

More importantly, from my point of view, AGF, 2.1% is significantly below the numbers you are used to from 2006. Now there's one specific impact, most of you, I think, are very familiar with. You know that there is the so-called push-on, push-off [ph] transfers, where a traditional life policy of -- the policyholder was offered the option to transfer from a traditional life policy to a, what the government calls more attractive unit linked policy. We made a lot of those conversions from a legal -- yes, I shouldn't say a legal point of view, but from an accounting point of view, to me, this is nothing more than a novation. We did not account for this novated premiums in our gross premiums written. What we are talking here about is amount of roughly EUR 700 million, which some of our companies do reflect in their gross premiums written. We don't. But that is not the important thing. The important thing is this has locked up sales capacity, which we are now able to free up going forward and still focus on the normal business, and therefore, I do expect that AGF will get back to the numbers you are used to from 2005 and 2006.

I would just make one comment on -- down on New Europe, that is growth very significant of 38.6% together with a very good growth also on the P&C side. I guess what I want to say against the background of some publications in the last couple of weeks and months, we are -- we were the #1 in international

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provider in Eastern Europe. We are still the #1 international provider in Eastern Europe. And with this kind of growth rate, I think we have a very good chance to maintain that position going forward.

Now let's talk quickly about AZ Life. I think if you look at the numbers on the graph, in the middle part of the left-hand side, that illustrates what I've told you. We have -- our management has managed to slow down the shortfall in premiums. That has bottomed out based on all the measures. I think we will already see an upturn and a change -- shift in trend in Q2, where we will see some significant improvement over Q1 2007. So that makes me confident that we are able to achieve the USD $11 billion for the full year. That is just for the sake of clarification is U.S. dollars. So in U.S. dollar terms, we do expect flat premium growth depending on the development of the U.S. dollar. It might well be that in euro terms that is then still below previous year.

In terms of operating profit, while operating profit is down in Q1 '07 compared to Q1 '06, that is largely driven by the implied accounting volatility of IAS 39. A good part of that is supposed to reverse over time and come back into operating profit. But more generally, I think the operating profit will trend higher as our operating asset base is growing. And as you can see from the lower point of this chart, our operating asset base is still growing significantly also, thanks to typically low lapses, which do continue to stay at a very low level because the product is still very much appreciated by our policyholder. So long story short, I think the traffic light as far as the operating profit target of USD $600 million is concerned, this traffic light is still green.

Page 21. I would like to flip over. That's the usual details to feed your models.

Let's move on to the Banking results. Operating profit is up 28% to EUR 677 million. Yes, overall, we benefited from one-off effects in the revenues. You see in this footnote that in the operating profit, also in the revenues, of course, that does include an equity pick up from disposals of an associated company in the order of magnitude of EUR 170 million. But before you start to adjust, please keep in mind that there has been other nonrecurring items, both in Q1 '06, as well as in Q1 '07. What I'm referring to was a sale of real estate in last year of round about EUR 25 million and some EUR 40 million of impact trading in Allianz shares and related derivatives.

If you were to look at the net number, then we are talking basically about something like EUR 100 million, EUR 105 million of positive, yes, call it one-offs, but adjusted for that still we would see some nice growth of EUR 50 million in the Banking business operating profit in the first quarter. More importantly, on the right-hand side, there's consistency in the development of our underlying profit drivers. Revenues are growing. Operating expenses are still on their way down, and we are continuously benefiting from a very disciplined risk-taking approach. As you can see, the loan loss provision is still on a very low level as a result of this risk strategy.

Now the revenues, next page, up 7.4%. If you look at the development in the operating segments, private and corporate clients and revenue development is more or less flat, 0.7% negative. There is some compensating issues. We have higher revenues from leveraged finance, but lower revenues from our credit business and having talked early on, on the Life segment about the Riester staircase last year, of course, there's also commissions missing on the Banking side for the absence of this business that's round about EUR 10 million.

On the investment banking side, we had one of our strongest quarters ever with a growth of 3.1%. Now all this one-off type events are included in the corporate segment, Other. As said, it's round about EUR 100 million or EUR 105 million. The remainder of this improvement is explained by higher interest income out of our treasury function, and that was one of the issues I mentioned to you earlier on where we need to improve.

If you look in terms of revenue categories, the usual picture, you see that interest income is significantly up. But this is driven by this equity pickup plus that positive effect from IAS 39. The remainder of that increase is made up by 5% growth in the operating divisions and the increased contribution from the treasury function.

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Net fee and commission income is fairly stable. And if we go to the net dealing income, yes, there's a sharp decline of 31.4%, but this is explained, A, by a change in IAS 39 minus EUR 79 million; secondly, by the aforementioned impacts on shares and derivatives thereof; and thirdly, we have a slight decline in the operating divisions of 3.2%.

Next slide, revenue development. You'll see that there's ongoing efficiency improvement, both on a cost-income ratio, as well as if you look at just the kind of fixed investment income, fixed cost expenses. We are now down at 66.9% or on a fixed basis and down to 50.2%. Well, now you can make all kind of adjustments. Regardless whatever you adjust, you will come out with some lower numbers than in the respective quarter of 2006. And I think that is another step in the right direction where we want to address the 75% as a next step and then medium term over the 3 to 4 years the below 70% cost-income ratio. In terms of loan loss provisioning, I think the only comment I want to make, if you look at new provisions is that we are still reserving to normal levels, i.e. in line with expected loss.

Now last, but not least, Asset Management. We have a growth in operating profit of "only" 2.6%. However, if you look at this on an FX adjusted basis, 75% of our business is U.S. dollar denominated, then we would be at roughly 10% improvement, which is more in line with the normal track record of this division. I think the development, there is nothing new. The development of operating profit is based on a strong revenue generated asset -- generating asset base on solid net flows and on strict pricing discipline and effective cost management.

Cost-income ratio was 60%. I think is on a still very competitive level. It's slightly up, but please keep in mind, we've invested some serious money in European distribution, in U.S. retail and in corporate center restructuring in Asia Pacific. All that is driven by ongoing outstanding performance, both in the fixed income side, you'll see the respective numbers on Page 30, as well as on the equity side where we are still in line with our target to have at least 70% of our assets under management outperforming their respective benchmark.

And finally, you see on Page 32 that together with market inflows -- was net inflows and market effects, our third-party assets under management have increased by 3.3% on a total basis, reducing or -- adjusted also for exits -- effects. That's round about 2%. So even taking into account a weak dollar I think we have still a chance to get to the 10%. In any case, we will get to the 10% on a stable FX basis. And this, if you might remember, was the caveat we made in our outlook.

That gets me to the summary, and I think just to summarize again. It was a very good start into 2007, in particular keeping in mind that this was not a no-brainer with the high NatCat. Our revenues are -- we are not satisfied with the revenue developments. Flat development in the first quarter was not a surprise. It was expected largely driven by the development in our Life business. Operating profit is up 7%. Net income clearly up at EUR 3.2 billion. All in all, I think I'm very confident that we are able to achieve our targets for 2007.
And with that, the floor is yours for questions.

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Question and Answer

Operator

[Operator Instructions] And we will take the first question from Spencer Horgan from Deutsche Bank.

Spencer Horgan
Deutsche Bank AG, Research Division

Could I just ask you, in terms of the Life & Health business, could you give us a flavor for what new business volumes are doing across your major territories and maybe if you've got a sort of hint as to what the new business value on an embedded value basis might be doing? And the second quick one is, can you just update us about what you expect for acquisition costs in the Asset Management business over the next 3 years?

Helmut Perlet
Former Chairman of Supervisory Board and Member of Joint Advisory Council

Okay, with respect to your first question, thanks a lot for that. That gives me an opportunity to make also some communication regarding our disclosure. We do intend to publish embedded value numbers for the first 6 months in 2007 and, then going forward in 2008, to move on to a quarterly publication of embedded value numbers. You might ask, "Why the heck do you give only half year numbers in 2007?" The simple reason is, as you remember or as you know, we have calculated -- we've changed to market consistent embedded values only last year, and we have not calculated on new assumptions quarter-by-quarter or recalculated on a quarterly basis the numbers for 2006. We have only done this on a solid basis for June 2006, and therefore, we're only going to publish our half year numbers in 2007 just to make sure that comparable numbers are on a solid basis. Now to give you some flavor, and that goes for the 2007 numbers only because -- and I give you some indication for 2006. The new business volume for 2007 first quarter is round about EUR 7.6 billion, and that is supposed to be slightly below the '06 numbers, which shouldn't be a surprise to you because we have a shortfall of 3.9% in gross premiums written, and there should also be some shortfall then on the present value basis. The margin should be round about 3%, i.e. more or less stable with previous year numbers, and the value of new business for the first quarter stays at EUR 218 million, and this is where I have the highest concern to give you previous year numbers. It is slightly less than in 2006, but against the background I was just telling, I would rather prefer to not give a number for 2006 because I cannot sign off 100% of the quality of this number. Then in terms of acquisition expenses on the B-unit side or Asset Management side -- and I have to make one caveat here because as you know, the old part of our Asset Management business affects the ultimate expense for the cancellation put for call of these B-units. If it's going up, then the expense will increase. If it's going down, the expenses will decrease. The numbers I give you is based on the 2006 situation, profitability of PIMCO, and against this background, we are expecting EUR 350 million, EUR 360 million for 2007, EUR 280 million in '08 and then close to EUR 200 million in '09.

Operator

We will now take a question from Michael Huttner from JPMorgan.

Michael Igor Huttner
JP Morgan Chase & Co, Research Division

I have 2 questions. The new market growth in both Life and non-Life and also both in terms of premiums and in profit, how long can you sustain rates of growth like that, which are sort of, well, above 20% in Life and around 20% in non-Life? That'd be the first question. And then on the cost side, the -- I was speaking to one of your colleagues earlier who very kindly helped me with this question, so thank you. It was -- part of it seems to be that because the premiums are falling in non-Life, you have a kind of negative operating leverage. Does that mean that you will accelerate the cost cutting or do more cost cutting than you'd originally planned and maybe give some timing on that? And then the final thing, I was hoping at some stage that we see the benefit of buying back these B shares in terms of having a bigger share of

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the profit pool for shareholders rather than for managers. When are we seeing that? Or if it's in these numbers, how much is it?

Helmut Perlet
Former Chairman of Supervisory Board and Member of Joint Advisory Council

Okay, so new market growth, you were referring to Eastern Europe?

Michael Igor Huttner
JP Morgan Chase & Co, Research Division

Yes, please.

Helmut Perlet
Former Chairman of Supervisory Board and Member of Joint Advisory Council

Yes, I think we have to be -- if I could make a distinction. We have this high growth numbers on the Life business in particular driven by Poland, where we are running a fairly successful corporation with UniCredito through Banco Pekao. That is subject to kind of the same adjustments in the production going forward than it was the case in Italy. So you should expect the production levels in Poland coming down. That is, in itself -- yes, it's probably not exactly good news. But that is a unit-linked business with very low new business margins as you normally know from this kind of joint ventures, so in terms of profitability, it will not have that much of an impact. We think that for the rest of the region, we can still achieve, for the next 3 years and more, but we are not planning for more than 3 years, as you know, double-digit growth rates, clearly say anywhere between 10% and 15%. Now with respect to expenses, just a quick explanation. In absolute terms, the expenses in Q1 are up EUR 11 million. Yes, now there is some negative impact because of higher retention. We have also higher net retention. We have also higher expenses, EUR 30 million. We have high expenses from the first half consolidation of ROSNO. That is another EUR 17 million. So on an apples-to-apples basis, you could argue expense ratio should have come slightly down. Nevertheless, this is, as you rightfully pointed out and I have said, this is not good enough. I've been pushing for more cost cutting, Michael. I'm still confident that with the aforementioned activities, the restructurings in 3 of our major countries and the target operating model, that this will give us a significant improvement in the cost-income ratio. I would just like to make sure, and I hammer this message into the organization, that there is no room for complacency, in particular as we have now very favorable results in Germany -- not in Germany, in the P&C business overall, and we need to make sure that also in other areas, and that goes from consulting fees and all the other good stuff, that we have really high cost discipline in place. Buying back B shares, there is a predetermined schedule in place of when and how much of those B shares can be called or put by management. So apart from, say, outside this agreement, if there's any side negotiations, there is no way to speed this up. We had already, in 2006, we called roughly 22,000 of these B-units, and there was another redemption of B-units in Q1 this quarter, which obviously had impact on the number of expenses in the first quarter of close to 16,000 B units.

Michael Igor Huttner
JP Morgan Chase & Co, Research Division

But when does this -- presumably buying back these shares gives you a bigger share of the profit pool. When will we see that?

Helmut Perlet
Former Chairman of Supervisory Board and Member of Joint Advisory Council

They should. That will evolve over the next 5 years. And then based on that, what I've mentioned, predetermined schedule, the last B units are redeemable in 2011.

Operator

From Citigroup, we will take our next question. Question from James Quin.

James B. Quin
Citigroup Inc, Research Division

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The -- 2 questions please. The first one is a sort of techy question. The second one is on Dresdner. But the first one is really, just looking at the net earned premiums in Germany in P&C. They were 6% down on Q1 last year and 10% down on Q4 2006, and I was just wondering if there's anything driving that specifically. The second question is just, as I say, on Dresdner. And I was just wondering, obviously, there's quite a few moving parts between the first quarter of last year and the first quarter of this year. I guess if we stand back, I mean, to what extent do you see the business is reflecting restructuring, which is underway now? And to what extent do you think that's something that will come through in later quarters?

Helmut Perlet
Former Chairman of Supervisory Board and Member of Joint Advisory Council

Okay. The answer on the German business is -- sorry, the answer on the German business is, you might remember, that we transferred the industrial business from the German P&C operation to AGCS, and that, of course, has an impact on the net premiums earned.

James B. Quin
Citigroup Inc, Research Division

Right, okay.

Helmut Perlet
Former Chairman of Supervisory Board and Member of Joint Advisory Council

Yes. Then on Dresdner, how much is that reflecting the change? I think is -- as far as our program, Neue Dresdner Plus, is concerned, we are very much on track. We had a layoff of about 400 people already, which is slightly ahead of plan. And you'll see that reflected also in a reduction of the expenses. So I guess -- but still, we were talking about EUR 250 million in expense reduction on an apples-to-apples basis. So the good point of this program has still to come through.

James B. Quin
Citigroup Inc, Research Division

I mean, do you have a sense of what the sort of a fair cost-income ratio might be if we adjust the first quarter of this year against the first quarter of last year on an underlying basis?

Helmut Perlet
Former Chairman of Supervisory Board and Member of Joint Advisory Council

I think a fair adjustment is that this is probably one percentage point or 2 percentage points in terms of cost-income ratio improvement. If you were simply to adjust for this Kyrill impact, EUR 170 million, then instead of 73.9%, we have 73% cost-income ratio. But again, I said there's some one-offs on the other side as well, so that accounts for roughly another percentage point.

Operator

We will now move to Paul Goodhind from Bear Stearns.

Paul F. Goodhind
Bear Stearns Companies Inc., Research Division

I've got a question on reserving, if I can. You're showing prior year development, which is positive about 2.3% in the first quarter. I'm trying to get a feel for what sort of level of prudence that you've built into the current new business. And maybe as a way of getting at that, could you give us a feeling for how the 2004 and 2005 accident years have developed since you wrote that business?

Helmut Perlet
Former Chairman of Supervisory Board and Member of Joint Advisory Council

Well, in general terms, what I can say to you is that our objective is to maintain the same level of prudence in our reserving policy, and we are looking very closely around this. And I think I've given some explanations in February. Movement or development of the 2004 and 2005 accident year losses, I can't

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give you out of the top of my head. But certainly, Oliver, I need to go back to my statistics and look into that. I don't have it out of the top of my mind. I have no problem to share that with you. But in general terms, there is positive development.

Paul F. Goodhind
Bear Stearns Companies Inc., Research Division

Where I was coming from with that question is that I'm guessing that the level of positive development for those accident years is perhaps above the sort of 2% level of releases that you're showing. In other words, if you maintain a current level of new business conservatism, is there scope for larger levels of reserve releases going forward?

Helmut Perlet
Former Chairman of Supervisory Board and Member of Joint Advisory Council

Well, that's a very good question, but we had this discussion very often in the past. What -- all I can say here, Paul, and I mean, we have also here some regulations where we need to look at, that we are applying and try to apply consistency and not to do kind of funny games in order to manipulate or to bring those earnings to the positive or negative side.

Paul F. Goodhind
Bear Stearns Companies Inc., Research Division

Yes, okay. And just lastly, could you give a bit of texture on the claims trends around the business in non-life insurance and in particular claims frequency? That seems to have been pretty favorable in most territories over recent years. Is that trend continuing? Or do you have any examples that you could give us?

Helmut Perlet
Former Chairman of Supervisory Board and Member of Joint Advisory Council

Well, obviously, it's a little bit difficult for Q1 with the impact of NatCat because, I mean, if you take all this stuff into consideration, then frequency has gone up, of course, and severity has gone down because there's also a lot of smaller claims. But if you, for example, look at the motor business only, frequency has improved by another percent, and severity has improved -- who can help me out, I think was something like 2%. So net-net, that is still improving.

Paul F. Goodhind
Bear Stearns Companies Inc., Research Division

Is that Germany, that comment for motor or is that the whole...

Helmut Perlet
Former Chairman of Supervisory Board and Member of Joint Advisory Council

That goes for the whole business, for the whole motor business.

Paul F. Goodhind
Bear Stearns Companies Inc., Research Division

That's quite a big improvement.

Helmut Perlet
Former Chairman of Supervisory Board and Member of Joint Advisory Council

Yes, it is.

Operator

We will take our next question from Brian Shea from Merrill Lynch.

Brian Shea

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BofA Merrill Lynch, Research Division

I had 2 questions. Two questions please. On the combined ratio, if you kind of take that -- take out the Kyrill costs and put in 2 points of normal cat losses, you get about a 95% combined ratio in the first quarter. You're saying that you're confident of 94% for the full year. So is this all going to come in, in expenses? Or are we just putting too -- trying to split Q1 numbers too hard is the first question. And then secondly, in the corporate segment, you had an operating loss of EUR 101 million, which is a very low loss. I had thought we'd have maybe some AGF costs in there pushing -- costs for buying AGF in that, pushing up that number. The question is, that number has been so volatile over -- since you came out with quarterly reporting on that a year ago. Is that a decent run rate to use, or is there anything funny in that number?

Helmut Perlet
Former Chairman of Supervisory Board and Member of Joint Advisory Council

Okay. On the combined ratio, yes, adjusted for normalized NatCat, that would result into 95% combined. Now there's 2 things, A, clearly the expense ratio will come down over the course of the year. Point #2 is -- and that you can see if you go back, and I guess that is normal practice in Q1. Q1 traditionally is always, in terms of loss ratio, is the worst quarter in the year. And normally, what you do if you don't have very significant indication that it's going to changing, you book the first quarter to plan. So then you have an approach where you have a higher Q1 and then subsequent improvements in the quarters 2 to 4, and this is what I expect to see for the rest of this year as well. So against this background, I think you have to understand my comment that I'm still very confident we are making the 94% with the caveat that we apply the normalized NatCat rate, and that, of course, needs -- remains to be seen. On the corporate segment, improvement came from 2 sides, A, there was a higher operating profit from our private equity business. That was an improvement of roughly EUR 30 million. And then we had, in the corporate segment, we had higher net interest income as we are increasing the amount of free assets at the holding company level based on the results from previous year, and that added to this net-net, I think it was EUR 70 million -- or EUR 60-something million improvement. There is only little cost for the acquisition of AGF minority buyout in that number included because most of that has to be allocated apart of the acquisition expenses and, therefore, is ultimately ending up in goodwill. To give you a good number on a quarterly contribution from the corporate segment is not that easy. I told you early on I'm starting out with the easy point. I think the EUR 15 million or EUR 16 million of operating profit on the private equity side could serve as an indication going forward. What I also can give you is that in the group center, we do have a cost run rate of round about EUR 400 million. And then the other question, of course, is what is interest income and what is internal interest expenses? And that, of course, varies with the available assets or, i.e. transactions which need to be financed. Now what you should expect that going forward that interest income -- I've just mentioned we had higher interest income in Q1, that this will somehow disappear because we need these funds to finance part of the AGF transaction. Now I'm sorry that I can't give you a clearer guidance of what -- this is pretty complex to explain unless I publish my plan, which I beg your understanding, I won't do.

Brian Shea
BofA Merrill Lynch, Research Division

Okay, no, that does help.

Operator

We will now move to Frank Stoffel from Pioneer Investments.

Franklin Stoffel

It's Franklin from Pioneer. Two questions. The Banking results benefited from the impact of utilization of tax losses in the first quarter. Could you please elaborate to what extent -- what the extent this impact had? And also, please elaborate on what the range of tax rate we can expect going forward. And the second question is relating to the German Life & Health operations. There were changes with regard to the tax -- to the DAC treatment. Could you please elaborate to what extent the Q1 amount is representative and what kind of the DAC amortization is sustainable going forward?

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Helmut Perlet
Former Chairman of Supervisory Board and Member of Joint Advisory Council

Let me start out with your first question -- with your second question. For the first question, I need the support of Klaus Rosenfeld, who is sitting next to me. The range of tax rate, you can expect -- I mean, based on our aspiration level 2007, which calls for like 10% growth in operating profit and a normalized level of capital gains, the expected tax rate should be in the order of magnitude of 28% to 28.5%. And so what you should expect probably going forward for the next 3 quarters is a tax rate which is in line with this 28% -- in this -- within this 28%, 29% range. Now the true-up on the DACs in Germany, they had a positive impact in the order of magnitude, I think, anywhere between EUR 20 million and EUR 30 million on the results net of policyholders. We do this true-up once a year in Germany. This has always been done in the first quarter. We had, as you might remember, years where we had a negative contribution from this DAC true-up. This year, we had a positive contribution. The main driver on that is the change in interest rates as we always have to use new assumption in interest rates and depending on how the interest rate development is, that will go for the change in those DAC true-ups. So I call it forecast of what is to be expected out of true-up is very, very difficult.

Franklin Stoffel

Yes, but based on the similar conditions we had in the first quarter, given the change in DAC treatment that you reported on the year Q1 report, we can expect on a comparable basis the results [ph] to be lower?

Helmut Perlet
Former Chairman of Supervisory Board and Member of Joint Advisory Council

No, you should not expect any change during the remainder of this year. This true-up is normally done only -- not normally. This true-up has to be done once a year. That has been now done for Allianz Leben, and there's nothing more to come for the rest of the year.

Franklin Stoffel

Okay. And then on the bank the tax loss.

Helmut Perlet
Former Chairman of Supervisory Board and Member of Joint Advisory Council

Yes.

Klaus Rosenfeld
Dresdner Bank AG

As regard to the...

Helmut Perlet
Former Chairman of Supervisory Board and Member of Joint Advisory Council

Klaus is ready.

Klaus Rosenfeld
Dresdner Bank AG

As regard to the tax line, the tax line benefited from the tax-free capital gains and also from the fact that the KGAL one-off that we have in our net interest income is tax free. On top of this, there was a small amount of tax benefit from the revaluation of DTIs in the United States.

Franklin Stoffel

Okay, but this is smaller?

Klaus Rosenfeld
Dresdner Bank AG

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Yes.

Franklin Stoffel

Small contributions, okay.

Klaus Rosenfeld
Dresdner Bank AG

That was a very small, 2-digit contribution.

Operator

From Cheuvreux, we will take our next question from Michael Haid.

Michael Hermann Haid
CA Cheuvreux, Research Division

One question, only. You mentioned the combined ratio, global in motor business is -- was around 95% in the first quarter. Could you give us kind of a regional split, only a rough split would be sufficient for Germany, France, Italy, the U.S. and possibly the U.K.?

Helmut Perlet
Former Chairman of Supervisory Board and Member of Joint Advisory Council

Can I refer you to Oliver and his team later on because I don't have that table with me?

Michael Hermann Haid
CA Cheuvreux, Research Division

Okay, no problem.

Operator

[Operator Instructions] And we have now a question from Nick Holmes from Lehman Brothers.

Nick Holmes
Lehman Brothers Holdings Inc., Research Division

I think something went wrong with my telephone keypad, but I'll try and make up for it now. Just a few questions. Helmut, I think you mentioned that in U.S. Life in Q2 things are looking a little bit better, and I wondered if you could perhaps be a bit more specific about which products are driving this. Is it variable annuities or equity index? Now that's the first question. Then second question is in German motor, wondered whether you could confirm that pricing has -- that you have held pricing this year, and if so, as a result of that, have you actually lost market share? And then the third question is just on Banking. The level of loan loss releases has been coming down, and I just wondered, do you expect this trend to continue in the subsequent quarters of this year?

Helmut Perlet
Former Chairman of Supervisory Board and Member of Joint Advisory Council

Okay. With respect to your first question, U.S. Life, the upward -- the improvement in Q2 should come mainly from equity indexed annuities where we had some sales promotions started in the first quarter with which will show major impact now in April and May, and that's our redesigned equity indexed annuity product. We will see slight improvement also on the variable annuity product as we are expanding and getting more production over other distribution channels, but that will come through during the rest of the year, slowly but surely. Let me put it this way. On the German motor business, whether we have -- I mean, what I've said in a nutshell is that we have basically -- we have to granted higher bonuses -- to grant higher bonuses for the policyholders because of lower frequency. That has been more or less compensated by the price increase in the remainder of the portfolio. I cannot give you a market share number for Q1. Unless, Oliver, I think we don't have that for the industry. All I can tell you is that end of 2006, our share in the motor market in Germany has slightly declined from 17.47% to 17.39%. Now there

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might be a slight change in this number end of March. But again, I cannot give you any precise update on that one.

Oliver Schmidt
Head of Investor Relations

Nick, if I may, I might add that we have gained some 7,000 contracts, at least, in the first quarter 2007. I don't have the market share numbers either, but that should highlight that we have gained a little bit because I guess the entire market has suffered from the claims free bonuses we had to give to the customers.

Nick Holmes
Lehman Brothers Holdings Inc., Research Division

Understood. Just, sorry, on the pricing question, would you characterize your pricing policy in Germany this year as being to hold pricing, all other things being equal?

Helmut Perlet
Former Chairman of Supervisory Board and Member of Joint Advisory Council

Yes, absolutely. And then on the loan loss provision, do I expect releases coming down? Yes. I mean, this is a consequence, I think, of our declining nonperforming loans, which covers a good part of the loan loss reserves. And so you should expect that over time, this is maybe running at a lower number but not getting down to 0 really because also in the ongoing book, of course, I do expect that we will have some releases based on a fairly conservative reserving policy we are continuing to apply.

Nick Holmes
Lehman Brothers Holdings Inc., Research Division

Okay. In Q1, the level of release was pretty high compared to the level of new provisions. I mean, if that's not the source of trends that is sustainable for the rest of this year, or would you -- I mean, could you elaborate on that?

Helmut Perlet
Former Chairman of Supervisory Board and Member of Joint Advisory Council

Yes. I mean, 2 remarks, Nick. You know that when we talked about 2007 outlook I said I do expect something like EUR 250 million of loan loss provision for the full year 2007. As of today -- and I'm putting now my neck out of the window. As of today, it looks like that we do not need this EUR 250 million based on the solid quality of our book and based on very favorable market conditions, and you know as well as I do, the economy in Germany has picked up nicely, and that, of course, should be for the benefit of lower loan loss provisions, less defaults, et cetera. So the level of releases, recoveries, I mean, that depends on exit management of certain investments and other things so that it's hard to predict whenever this will be completed that we need to see.

Nick Holmes
Lehman Brothers Holdings Inc., Research Division

Okay, but your outlook for this year is for an improvement perhaps on your previous guidance?

Helmut Perlet
Former Chairman of Supervisory Board and Member of Joint Advisory Council

In terms of loan loss provision.

Nick Holmes
Lehman Brothers Holdings Inc., Research Division

In total, yes.

Helmut Perlet
Former Chairman of Supervisory Board and Member of Joint Advisory Council

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Yes, I really would be surprised if we were to end up at the originally expected number.

Operator

[Operator Instructions] We have no further questions.

Oliver Schmidt
Head of Investor Relations

Well, if there aren't any remaining questions, then let us thank you for joining this conference call. We say goodbye to everybody and wish you a very pleasant remaining day.

Helmut Perlet
Former Chairman of Supervisory Board and Member of Joint Advisory Council
Thank you very much. Have a nice day. Bye.

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