S&P Capital IQ

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Allianz SE DB:ALV

FQ3 2012 Earnings Call Transcripts

Friday, November 09, 2012 1:00 PM GMT

S&P Capital IQ Estimates

	-FQ3 2012-	-FQ4 2012-	-FY 2012-	-FY 2013-
	CONSENSUS	CONSENSUS	CONSENSUS	CONSENSUS
EPS (GAAP)	2.81	-	11.07	12.01
Revenue (mm)	23215.07	21847.14	103104.53	101106.18

Currency: EUR
Consensus as of Nov-09-2012 9:00 AM GMT

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	- EPS (GAAP) -		
	CONSENSUS	ACTUAL	SURPRISE
FQ3 2011	1.65	0.34	(79.39 %)
FQ4 2011	2.17	1.06	(51.15 %)
FQ1 2012	3.00	3.02	0.67 %
FQ2 2012	2.70	2.68	(0.74 %)

Call Participants

EXECUTIVES

Oliver Bäte
Chairman of Management Board & CEO

Oliver Schmidt
Head of Investor Relations

ANALYSTS

Andrew Broadfield
Barclays PLC, Research Division

Andrew James Ritchie
Autonomous Research LLP

Atanasio Pantarrotas
CA Cheuvreux, Research Division

Brian Shea
BofA Merrill Lynch, Research Division

Fabrizio Croce
Kepler Capital Markets, Research Division

Jonathan Michael Hocking
Morgan Stanley, Research Division

Michael Hermann Haid
MainFirst Bank AG, Research Division

Michael Igor Huttner
JP Morgan Chase & Co, Research Division

Nick Holmes
Nomura Securities Co. Ltd., Research Division

Thomas Jacquet
Exane BNP Paribas, Research Division

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

Vinit Malhotra
Goldman Sachs Group Inc., Research Division

William Hawkins
Keefe, Bruyette, & Woods, Inc., Research Division

Presentation

Operator

Ladies and gentlemen, welcome to the Allianz conference call on the financial results for the first quarter of 2012. For your information, this conference is being recorded. At this time, I would like to turn the call over to your host today, Mr. Oliver Schmidt, Head of Investor Relations. Please go ahead, sir.

Oliver Schmidt
Head of Investor Relations

Yes. Thank you, Sarah. Good afternoon to everybody, and welcome to our conference call about the result of the third quarter 2012. I know it has been a very busy week for all of you, but I hope you still have some energy left for the next 90 minutes to come. Oliver will present the key facts and figures to you, and afterwards, we will be available for questions as well.

Now I don't want to become sentimental and it is still too early for goodbye, but let me remind you that this will be the last conference call Oliver will conduct in his current role, so let's, at least, have some fun. Oliver?

Oliver Bäte
Chairman of Management Board & CEO

Talking about fun, good afternoon, everybody. We have some fun numbers to share with you for this quarter that was obviously very carefully planned and timed to make my life easier today. I -- hopefully, you're understanding we've been out. So I think on the headline numbers, there shouldn't have been too many surprises. What I think is important to note is this was not due to one-offs but all the operating cylinders of Allianz firing well.

Let's go through the deck. As last time, I'll try to be through with the presentation and the comments in about 30 minutes, focusing on the highlights. So I'm not going to touch every slide and try to lead you through what, from our perspective, would be the key messages. Then I'd like to have the Q&A focus on the main drivers. I think you probably have questions around sustainability of some of the earnings that you are seeing. And if there are any detailed questions, technical ones, Oli Schmidt and team are happy to address them.

Another comment before we dive into the substance matter. My colleague, Max Zimmerer, is going to host next Tuesday, 11:00, in Frankfurt, a talk to go through what the main elements are of our investment strategy. So if you have questions around where are and how are we investing new monies, what do we think about renewable energy, what is our view on government debt, please focus on that day. You are invited by Allianz to attend this session.

Now, let's go to the facts. Page 3, and I'll start with a view on the 9 months number and then dive into the Q3 data. Our 9 months' numbers are very nice: EUR 80.5 billion revenues, EUR 7.2 billion in operating profit, net income at EUR 4.2 billion and our capital position was strong, remains strong and is going to be strong as we're spending a lot of energy on continuously fortifying our balance sheet position.

Now Page #4 give you an overview of the movement in the segments. All operating KPIs have improved. Combined ratio stood at 96.6% for 9 months. New business module at 1.7%. But operating profit at almost EUR 2.5 billion in Life, Asset Management of almost EUR 2.1 billion and Corporate and Other segment at EUR 747 million minus for the quarter because of lower interest income, but we'll be talking about it.

So these are the 9 months number. They're very strong, and they led us to change our outlook for the year. And despite everything we know as of today about Sandy, we will be confident to be north of EUR 9 billion in our operating profit for the total year.

Now, third quarter details. Starting at Page #6, EUR 25.2 billion in revenues, EUR 2.5 billion in OP and net income at EUR 1.4 billion are a very good base in terms of our financials.

Page #7 gives you the typical run-up, and you see very nicely the strong profitability numbers, particularly for the last 3 quarters that have shaped our outlook a bit.

Shareholders' equity on Page 8 is up. No surprise, given the strong earnings and the decline in interest rate, which was supporting unrealized gains, particularly on the fixed income side.

And our conglomerate solvency as depicted on Page #9 continues to trend up, of course, because of insensitivity to interest rates.

Now in terms of economics solvency that we are describing on Page #10, we'll be probably talking about it. It has improved back to more than 200%, like we -- where we were at the end of the first quarter. The improvements here are driven by a decline in the risk-capital requirements. The available funds are basically stable, small, decreased.

Now for those of already that have the sharp pencils of how does this work, because your MCEV is considerably up. Let me remind you what we told you on the first quarter. We've introduced fairly strict transferability restriction in the AFR computation. A lot of the MCEV movements are restricted and can't be transferred to the group level and, therefore, don't move the group AFR. I think that's a very conservative view on things.

The other item is on the required capital. Just to address some of the question, the calming and recovering markets have increased policy holder participation in stress scenarios. That's about an EUR 800 million movements. We have continued our derisking, for example, selling some of the Commerzbank at Hartford exposures. We've increased the duration of our German Life book. This has reduced the risk position by more than EUR 500 million, and it's continuous.

And we've done an update on correlations, and that means we are now reflecting the positive correlation of interest rates and nominal future claims at a higher level in the group. That is agreed that's about another EUR 900 million, and we have a few additional local changes.

So that explains the picture of the solvency. We feel very comfortable with that. The stress scenario still remains, interest rates down further 100 basis points and equity markets down. With that, we'll still be, I think, well capitalized.

Now, let's move to the group section and the various revenue movement on an internal basis. We see the strongest growth in Asset Management, 25 plus -- 25.5% up in nominal terms is more than 39%. P&C up 1.7%, and Life and Health, shrinking on an adjusted basis by 1.6%. This is in line with our expectation because we are continuously protecting our margin. We'll talk about it when we get to the Life section.

Page 13 show you the movement of the operating profit. I don't want to comment about it.

But Page 14 give you a view on the operating profit in the Corporate segment. Lower interest income is really what is driving it here and some smaller-cost items.

The nonoperating items this quarter are also, mercifully, easy to understand. When you look at the right-hand side, impairments are significantly lower, both for equities and debt. And we are also having less realized gains and losses. So some people were asking whether that is leading to an improvement in our result, that is not the case on the non-OP side.

Other nonoperating is also significantly improved. Please remember, last year, we had trading losses out of the Hartford warrants of EUR 200-and-odd million that have not repeated themselves. And we have had some amortization, again, on intangibles for this quarter at EUR 91 million. That leaves us with a positive balance of EUR 233 million for other nonoperating.

The balance of unrealized gains now is approaching EUR 10 billion. The number for gains that are unrealized on equity stands now at EUR 2.5 million.

If we move onto the net income slide, the comment I'd like to make is on the tax rates. For those that are constantly updating their spreadsheets, because you see a tax rate at 34%, that is not in line with our planned tax rate. We have planned with a tax rate of about 29%. What has happened? Now as before, if we write down equities or intangibles as we did, you don't get any tax benefit. That's a part of it. A key part, however, is that we are seeing an increase in trade taxes. As fiscal budgets are under pressure, the tax man is trying everything in order to increase revenues, and we are feeling that across the group, and that has been driving up our tax rate by about 2.5 percentage points. And I'd like to make sure and be transparent about the fact that what you've seen in the past, tax rates of about 29%, will not be the tax rate for the future. We have to expect tax rates more in the range of 33% for the foreseeable future.

Now with that, I'd like to move onto the segment starting with P&C on Page 18: good revenue growth; good operating profit, however, supported by lower NatCat claims; combined ratio at 96.3%; runoff at 1.5%. This reflects the fact that we have significantly strengthened our reserves at Fireman's Fund. Without the Fireman's Fund reserve strengthening, we would be at about 3.5% to 3.6% runoff, which is in line with our expectations for this year. In terms of medium-term runoff, you can expect anything, as -- and we said in the past, between 2% and 3% in this type of environment.

In terms of reserves strength, I just would like to point out to the study that's been done by Bank of America Merrill Lynch that gives you a very good indication of how we're doing, that is we have significantly strengthened our reserve position. And with what we're doing at Fireman's Fund now, we're taking the last step to make sure we are best in class here.

Now, revenue development by business you see on Page #19, very positive momentum in a number of markets. We're growing very strongly in emerging markets, double digit. We're growing in our core markets. It's also very good. We have a few exceptions, where we are either derisking or we have a tough economic environment, like Eastern Europe or in Spain, or where we are making sure that certain under-profitable lines are being addressed. A big sample, in Russia, that's accounting for a big part in Eastern Europe, we've been cleaning our health care portfolio with very good results. In the U.S. you see a decline in crop revenues. That's reflecting in a lot of the numbers that makes sense -- that are relevant for Fireman's Fund.

In terms of profit, Page #20, EUR 148 million improvement. The vast majority is driven by either the high NPE base and the -- in particular, the lower NatCat that we've experienced this quarter.

Now, combined ratio improves to 96.3%, says Page #21. When you go across the portfolio, you see very, very strong numbers, except for Fireman's Fund. I think many of them are the envy of anybody that wants to play in P&C. But I'd like to comment on a few.

One of the questions we received is whether Italy, with an 81.2% combined ratio, can sustain these numbers. Now, we are seeing extremely strong numbers because of strongly falling frequency and severity in Italy, and we'll see very good numbers for a while, but obviously that cannot be sustained over the midterm period. But for the foreseeable future, we will have very strong profitability in Italy, which we are going to reinvest to strengthen our market position.

You can see also, when you look at Spain, that being in a difficult economic spot, and particularly in terms of revenue, doesn't mean you need to have low margins. Our Spanish colleagues are demonstrating yet again, superior performance, and you see that across the portfolio, many, many combined ratios significantly below, 100-and-some cases even been below 90, and I think that's a very strong result.

Now, when you look at the accident year loss ratio -- and we've changed a little bit the format. That's why I'd like to spend 2 or 3 minutes on the Page 22. We show you the -- now the 9-quarter average accident year loss ratio, including/excluding NatCat, with a new middle bar. It's hovering around 69.9%. But to be fair, it actually looks worse than it is because the crop losses are in for this quarter, and that is adding about 60 basis points. So we have had a positive trend on the accident year loss ratio down that is masked by some specific events here in the portfolio and some movement on the credit side as well. But we are carefully monitoring this number. And given the price increases we are taking on the portfolio, it needs to improve going forward.

Runoff ratio, I've mentioned it's impacted by the reserve strengthening that we've done again in the third quarter. Otherwise, again, it is more at 3.5% to 3.6%.

Talking about investments, I'd like to point out Page #25. We have EUR 795 million operating investments for the quarter. It's a little lower than usual. You should be focusing more around EUR 810 million, EUR 830 million per quarter investment income for the foreseeable future.

And on pricing, in Page 26, we're seeing positive momentum amounting to a total of 2.1% in the first 9 months of the year, and we're taking pricing wherever we can. Please remember, our rate numbers are including adjustments like bonus/malus in our net numbers. Now that's P&C.

Life/Health, similarly strong. Page 28 give you the highlight, and let me directly go to Page 29 to show you the growth numbers. Now just to give you a few highlights, the first one is around Germany. Here, we have a reduction, particularly in short-term single premiums, the so-called [indiscernible], and that has lower margins that we didn't renew. The underlying business is doing extremely well, has nice margins as you see later in the deck.

We have had growth in the number of markets that we are very happy about, except for Italy. There, we still have outflows in the bancassurance side. On the bancassurance side, we know that banks are competing for deposits with very high rates. And if you want, as a life insurer, to get flows, you need to offer uneconomically high guarantees, which we're not going to do. So it is a conscious decision to have appropriate margins and going towards appropriate margins rather than going for top line.

The same is true for Eastern Europe. We have a number of products that are deposit light with very low margins, which we've discontinued. That's why you see the numbers decline.

And in the U.S., the story is exactly the same. The U.S. market, overall, is not profitable at this point in time. We had a low new business margin for the third quarter, which we've used the opportunity now to reprice and rather let volume go to protect our margin.

In the Benelux, you have -- you see a lot of growth in terms of percentages. Mind you, as explained, the last time a number of sales in Luxembourg happened on behalf of the French company, so there's an accounting gimmick here. Please note the footnote.

New business margin is at 1.6%, leading together with present value of new business premiums to EUR 149 million in new business value.

And the interesting numbers are on Page 31, showing you the still strong margins on Germany and, in particular, on our strong growth markets in Latin America and in Asia. The U.S., I mentioned, is 20 basis points.

Now what's important, we've been using the opportunity to reprise easy life measures. It's new business margin on a biweekly basis. As of September, the margin is back up to 69 basis points. So we're doing everything we can in order to improve margins there. And we are working, also, on Western and Southern Europe, that's, by and large, France and Italy, to improve the margins and the capital returns. Please note the capital returns we've provided you on the right-hand side of the page.

The operating asset base grows further. We had some good flows, net flows in Germany, in particular, and we're having back positive flows in Asia, which is important for us. After we've been closing Japan last year, we had a number of quarters of outflows. Now that's back in positive territory, given that we have very strong margins there. That's very important for us. We still have some slight outflows in Eastern Europe. I mentioned the closure of some of the deposit products. And Italy, as I said, correlates to the effect on the bancassurance channel that is driving the outflows here, again, in line with strategy to protect margins.

The operating profit is depicted on Page 33, very strong at EUR 822 million. It's the third strong quarter. Now again, we get the question what is a sustainable number. I told you last year, normally, in a good year, we should be expecting around EUR 700 million per quarter. That is still the guidance, leading you to about EUR 2.8 billion and -- on most of the KPIs. So we are currently slightly above that run rate, given that we have used the opportunity to lengthen our duration that has led to some investment gains on the bond side.

However, if I may show you on the investment slide, Page 35, where you have interest and similar income and net harvesting, the movement and the strong positive movement is not driven by taking huge gains on the harvesting side, but the reversal of the impairments we had to take last year in the third quarter. So realized gains and losses, which you see later down, is exactly at the level of the prior year. So there is no monetization of reserves going on that you should be worried about.

MCEV, we will quickly talk about. There's lots of technical backups. Yes, we provided a huge deck -- a backup for that. Any bean turd [ph] question, Oliver Schmidt will be happy to answer, including with the help from our Chief Actuary, Oscar Buchauer.

So let's move on to the Asset Management section, starting at Page #38, please. We've had excellent results again. The asset base growing 15% now to 8 point -- EUR 1.8 trillion. Third party flows have been second-best quarter ever EUR 31.5 billion. The operating profit is stellar, exceeding EUR 800 million, and cost income ratio is now at 54%.

Let's look at some of the details. Page 39 gave you the movement on the AuMs, both internal and third party. The flows are 2.3% of end-of-period AuM, which are very strong, and net fee and commission income is up 36%.

So let's stay on Page 41 for a second. You see here in the third quarter, we had performance fees of about EUR 284 million. And people are saying, "therefore, the results are non-sustainable." Let me point out, that is not the case. The other fee -- net fee and commission income has grown strongly now, from 3 years ago, EUR 1.2 billion to EUR 1.3 billion, now to EUR 1.5 billion. So we had an extremely strong growth in the underlying profitability before performance fee. They are a very nice icing on the cake. They are significant. But the underlying performance improvements are also very strong.

Moreover, we will have more performance fees to come in the fourth quarter. I cannot tell you exactly how large they are because they're dependent on when and how assets are being sold. And also for 2013, we are expecting significant performance fees. However, they -- you cannot expect them to be always at the same level that we've just experienced.

So let's move to Page 42, where you see the movement of the OP. And here, you can clearly see the strong increase in net fee and commission income has moved the numbers up, despite an increase in operating expenses. We continue to invest in the broadening of our platform. We have a lot of wind under our wings to support the business, and we'll be investing.

Now given that we have reduced investments in the first quarter when markets were very tough, some of the investments are catch-up, and they will continue to go. So we will not always see EUR 850 million in quarterly OP. But you see the quarters below, before they are significantly above EUR 600 million, and that is about a 20% increase from what we had seen in prior quarters before. So there is a systematic improvement and structural improvement in profitability. That is going to continue, given the fundamentally raised level of assets under management, of performance and of scale advantages.

Let's move to PIMCO, that's Page 43. Outperformance at a staggering 97%. Flows, I have talked about, and operating profit for PIMCO stands at EUR 748 million.

Now, I would like to dispel a few myths about PIMCO today, because I'm still amazed how little their performance is reflected in our share price. And so let's spend a minute on Page 44. We've provided you with 3 splits here: regional split, client groups and investment strategies.

So here's the first myth, PIMCO is only a U.S. company. Now while we're continuing to build out the core of PIMCO in the U.S. still, and doing this extremely successfully, as you see, they are also growing very strongly outside of the U.S., and that's in Europe and in Asia. All of these numbers are continuously up.

Second myth is it's an institutional investment company, that's why the margins are low. It's not true. As we've been discussing the last 3 years, the margins are going up with volume. And it's not just because of scale, but also because of product and client mix. You see -- nicely seeing the numbers. The institutional business continues to grow 10% relative to last year, but the big growth is also in retail and, by the way, also in retail Europe.

And the last myth is that this is all extending the core fixed income strategies, but the reality is another one. The so-called noncore product, the new platforms are growing very strongly, and they are already accounting for 58% of the investment strategies in terms of share of the third party AuM. So an extremely encouraging story that will continue to drive growth and profitability.

Now going back to Allianz Global Investors, Page 45. We saw an uptick in 3-year outperformance. The flows have been slightly negative. Given the environment, that's okay. And a new set of managers, EUR 300 billion in assets, that's also not small. The profitability was EUR 77 million is in line with a decent OE. In Allianz, however, we're targeting a cost-income ratio below 70% and, hopefully, rather sooner than later.

With that being said, I'd like to summarize my comments on the third quarter with the page on 47. We had a good third quarter, contributing to very strong 9 months results with more than EUR 80 billion in revenues, more than EUR 7.2 billion in operating profit and EUR 4.2 billion in net income. At the same time, we've been able and willing to further strengthen our balance sheet and improve our solvency. And therefore, we have decided to change our outlook from EUR 8.2 billion, plus or minus EUR 500 million, to now exceeding EUR 9 billion.

However, I have 2 comments. First, as you saw in the first 2 quarter, and it was true in the third, net income development doesn't go parallel with operating profitability because we're using every opportunity and they're still very, very unclear environment with lots of risks to derisk the investment side and to conduct restructuring activities that allow us to outcompete in the future.

Second, even with Sandy in, we feel comfortable, at this point in time, to achieve the EUR 9-billion-plus result, but we can, at this point, make no comment and give you no number on what exactly the losses on Sandy are going to be. This is an extremely complex storm that has happened, has started as a hurricane. We don't know how it ended up at landfall. We had a lot of flood losses that are very difficult to settle. So we will not provide you with a precise number on whatever we have looked at, again, it keeps us comfortable to meet our revised outlook.
With that, I'm done, and I'm happy to have beat my 30 minutes. And now -- we are now ready for your questions.

Question and Answer

Operator

[Operator Instructions] We will now take the first question. It comes from Thomas Seidl of Sanford Bernstein.

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

I have 2 questions. One on the P&C and one on the Asset Management. P&C, you outlined the one-off effect of the crops on the accident year loss. However, any way I look at it, on an annual basis in there, it seems to be fairly flat. And although the chart on the page seems to indicate that price changes are good enough to make up for claims inflations, so I just wonder, shouldn't we see, now with the stronger price increases reported here, more of a turnaround sooner in the P&C? And secondly, on the asset allocation. I wonder if you could give us a bit of a color of an outlook here in terms of asset mix and duration. 2% net equity exposure, 2% real estate. Is Allianz sort of at a peak invested in fixed income at the moment? And you also extended the asset duration, is this part of a longer side show? Or could we some of it whenever in the future?

Oliver Bäte
Chairman of Management Board & CEO

Yes, let me start with the second one. That sounds defensive, but is not meant in this way. We don't make forward-looking statements on asset allocation. Again, what we have to say, Maxim is going to say on Tuesday, because if I were to say we are selling this and that, then the markets will move, yes? so that's -- I think it's very important to bear that in mind. Now obviously, given the liability structure, we are a core fixed income investors. And given capital charges on equities, we have no chance than to invest less in equities than we would probably otherwise do. Now -- however, we are diversifying our investment significantly. If you look south of the Alps, we had, historically, a very large share of our investment in government debt, which we are investing less of our new money, and we are looking into other products beyond government. So that's covered, corporate, ABS and so on and so forth. The total yield at 9 months was, by the way, 3.6%, so comfortably in line with what we were expecting and we were needing. So that's question number one. Question number two is on the accident year loss ratio. Yes, you're right. You see exactly that the trend is flat, and that we've only slightly had, and that's the lower left-hand side, increased the prices more strongly than the movements on frequencies and severities. But I hope that the pricing strength, and we have planned further price moves in -- over the next few quarters, will help us to outpace frequency and severity movements. But I would agree with you, it has been a flattish trend. But by the way, I wouldn't call it for a turnaround. If you run a 96.6% combined ratio, I wouldn't call this a turnaround case. We have a few other turnaround cases in the industry if you think about that.

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

I was more referring to a single market. And the duration, the lengthening thereof, is this where you want to be, I mean?

Oliver Bäte
Chairman of Management Board & CEO

Yes, we have, and that's particularly happening in the Life segments, where we have, in the German book, too much of a mismatch between the -- of the duration between the liabilities and the assets, and we've been driving that up. Some people have commented, why do you do that with Italian government bonds? Because we bought some of that in the first quarter, and I can tell you, for everybody, in hindsight, that was probably one of the smartest things we ever did and, by the way, made EUR 2 billion along the way in terms of risk reductions. So I don't think that was a bad move to the opposite.

Operator

We will now take the next question. It comes from William Hawkins of KBW.

William Hawkins
Keefe, Bruyette, & Woods, Inc., Research Division

This slightly picks up on your last comment, Oliver. In recent meetings, I think you've been discussing the risk management measures you've been taking in the context of the Eurozone crisis. And I'm not quite sure myself exactly what you've been doing. So could you highlight to us what your intention has been with regards to managing risk in the Eurozone? What you've done, and what you still have left to do? And if I can finish off then with just a precise question. To the extent that I understand you're managing to be able to withstand an extreme tail risk and acknowledging that it is an extreme tail risk. In the context of that tail risk, what would happen to your economic solvency ratio that's 202% at the moment?

Oliver Bäte
Chairman of Management Board & CEO

Yes. We're not forecasting sort of the stress test, Will, that we -- in the deck give you an indication of what of the most severe stresses are. But you are right, we have decided that we don't look at the diversified exposures that you typically see in our base model. But we defined absolute shocks, like a 50% haircut on any major government, a very severe downturn of financial markets, particularly on equities and financial equities. And we've decided that none of these scenarios should lead us to having to take capital measures. Let's leave it at that. And therefore, we've been systematically derisking our exposures. So for example, you go on the Spanish position, we've significantly decreased our exposure just since the full year, for example, on government debt in Spain by more than 50%. The overall position by the way on spend -- Spain being down more than 25%. The same is true for Portugal. The same is true for Ireland and so on and so forth. Now then you will say, "so how about Italy?" We've explained our position in Italy various times, so I'm not thinking about repeating that so much. The important factual explanation I'd like to give you is if you compare the position of the Italian government and differentiate nominal values versus market values. Now given that the spreads have tightened a lot, market values for Italian debt are significantly up, but they mask the fact that on nominal terms, we've reduced our exposure by about EUR 2 billion just over the last 3 months. And we've taken the profits as part of the process, as I just mentioned a minute ago. What we are going to do going forward is to slowly, but surely, rebalance our portfolios in the investment side, particularly south of the Alps, from being predominantly government debt focused into a diversified investment strategy. For example, the [ph] Germany will never have more than 25% of the investment of Allianz Leben. If I remember correctly, in government debt, for Southern Europe, they went up to 50%, right. So you can see the misalignment, and we'll get some more diversification in local portfolio. So again, for details, talk to Max next Tuesday. He's going to be your happy host on investments. Frankfurt, 11:00 is the exact timing.

Operator

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

Jonathan Michael Hocking
Morgan Stanley, Research Division

I've got 3 questions please. First, could you just talk a little bit through the reserve addition in Fireman's Funds, what the process was is just the year-end reserve review and the materials [ph] of the additions you've made to the reserves by line of business? That's the first question. Second question, in Italy, given that frequency and severity are falling pretty quickly, would you expect prices to fall eventually? And how are you seeing prices tracking at the moment on new business? And then third question, just coming back on your comment about the tax rate. To what extent is this actually corporate tax rate in countries going up, or countries getting more aggressive about multinationals managing cross-border tax rates for your transfer pricing, et cetera?

Oliver Bäte
Chairman of Management Board & CEO

Let me quickly hit the trade -- the last one is less about what you described, but more on trade taxes, yes? And you have, for example, in France, the reserve cap coming, where they're suddenly describing it as something that they need to do to monetize. So it's not yet corporate tax rates that are moving, but one cannot exclude that for the future. But at the moment, they have a more, how do I say that, a below-the-carpet approach in order to raise more money. Maybe that's a nice phrasing for that. The second point is on reserve strengthening for Fireman's. Jon, just a pure fact, what we are doing, we are consistently reviewing the results in all of our units. In America, we are now doing it on a continuous basis, looking at the various lines of business, ranging -- not just on asbestosis and environmental, which I explained to you in the past that we did a big review in 2010 across the group, not just for Fireman's Fund, and have moved from a 3-year update to an annual update. That also, therefore, leads to annual increases in reserves if they are needed. We have the group level reserves at Allianz that we are partially using to offset the effects. So we're downstreaming the -- our group level reserve to the businesses. That is referring to asbestosis only. And then we're going to specific lines. Like, for example, in the U.S., commercial lines workers' compensation or professional liability. If you look at the reserve strengthening we've done on the U.S., the numbers are EUR 227 million. Professional liability has been around $100 million. Workers' comp was around $90 million. Asbestosis was around $35 million, and various others were around $58 million. This is all, sorry, in dollars, individual numbers, where the total was in euros. And then on the U.S. side, as I said, you had a crop effect also in the quarter. We, by the way, might have some more losses on crop coming, which we don't know about. It will only be at the end of the fourth quarter when we will know the total number. And we'll continuously be monitoring inflation, and we would be booking the reserves as appropriate. Now the last item was on Italy and what is happening going forward. Now clearly, the industry, overall, is having higher levels of profitability, not at the level of Allianz, of course, but still better results. And therefore, we expect competition on prices to increase. For us, however, we believe we can maintain very high levels of profitability, because our tariff is really superior to the rest of the industry, and therefore, we can maintain higher profitability, even if prices go down a bit. More, I cannot say at this point in time because that would be reading tea leaves.

Operator

We will now take the next question. It comes from Michael Huttner of JPMorgan.

Michael Igor Huttner
JP Morgan Chase & Co, Research Division

And just 3 questions. Can you possibly walk us through the movement in the solvency, the economic solvency from 178% to 202%, what the moving parts there? And specifically, maybe given the example -- because I'm never quite sure how it works. If MCEV moves, you made all these adjustments, by say EUR 700 million, did -- how much does it move the solvencies, is there kind of double-whammy effect? And the other is on jumbo -- it's a pricing, my favorite topic. Could you gives a little bit some more outlook here and maybe what's happening? Because I heard that the fleet business is improving, and that seemed quite interesting. And then the last point on Fire Funds. So I worked out, excluding crop and reserving, that you're roughly at 114% combined ratio, which is still very, very high. And I just wondered when this -- when does the underlying combined ratio actually trend to 100% or below?

Oliver Bäte
Chairman of Management Board & CEO

Okay. Now solvency, Michael, having 15 different pages on front of myself to explain the numbers. Let me try without a page and explain it to you in detail. Now the first one -- and I'll explain that together with the MCEV, because obviously the 2 are, hopefully, connected, right? So the first thing is that the MCEV is significantly up because of the fact that, I had mentioned earlier, that have been driving it, in particular falling interest rate volatility, falling spreads in Italy, but also adjustments on annuitization rates in Germany. Now the MCEV movements do not translate automatically in improvements of the available financial resources. Now why do they not do that? Because in the group level, we consider capital only, and that's consistent at least with the most conservative interpretation of Solvency II, because you can only use fungible and transferable capital to account for group solvency. And we've decided with the movement at the year end in the first quarter to put -- become a lot more conservative in terms of what we consider to be fungible. So for example, we had almost EUR 4 billion in improvement in MCEV that we do not deem to be fungible and transferable to the group level, so they are not improving our solvency ratio. So you can call us being overly prudent or overly conservative, but that's why the MCEV increase is not funneling itself through to the economic solvency. On top of that, just give to you an example, we have taken EUR 1 billion in activated IT assets out of the computation because it would check all of the conservative requirements from our regulators, and it says you can only activate the following assets if you can clearly prove that you can sell them. We have decided, in the past, we don't take any gambles anymore. We have become the most prudent shop around, and that's why we've been taking it out. So that's another one, just to take an example. So the movement really on the solvency has been coming from the decline in risk capital that I've described earlier that you need to bear in mind. And the risk capital movement, if you look at the position changes, have a number of effects that relate out of, for example, the correlations that we have between interest rates and combined ratios, that I mentioned earlier, and other items. In particular, that because of the increase of policyholder participations, in the event of a shock, due to the fact that spreads have tightened, we have less effect on shareholders. So that's the explanation. And with the 202%, we're back to where we were at Q1, right? But I think that's in terms of quality of the number that is at least as good or even better. Now your favorite subject, German motor. Year-to-date price movements for asset lease, we are 4.1% on the retail side, 3.4% on the commercial price, and that fits to what you have on Page 26, please.

Michael Igor Huttner
JP Morgan Chase & Co, Research Division

And on the Fire Fund?

Oliver Bäte
Chairman of Management Board & CEO

On the Fire Fund, your question on what? Let me be a little facetious, you'll have to wait awhile for underlying improvement. We're in restructuring mode, and we'll be there for a while.

Operator

We will now take the next question. It comes from Andy Broadfield of Barclays.

Andrew Broadfield
Barclays PLC, Research Division

Two questions, please, one on economic solvency and just one on your use of U.S. Life we -- capital [ph] as well. So just on the economic solvency, given the volatility of your solvency so far, I know you're working on reducing that, and the absolute level of just over 200% how are you thinking about target levels at the moment, given the financial -- or the economic markets? And how -- have you got a certain level you think is a range that you're going to have comfortable in and that you might think about other things beyond it and -- or not? Was it too soon to think about that? Second question, you mentioned earlier about the tax challenges, local regulators, when government is being a little bit more, I don't know, in some terms it's tax captures. Do you have any of those similar issues in terms of -- I suppose the first question is do you use capitals in your U.S. Life business and elsewhere? And if that's -- if you do, are you finding that that's getting tougher in terms of the benefits you're getting and possibly being rescinded or moved by regulators and the tax men?

Oliver Bäte
Chairman of Management Board & CEO

Yes. I can directly answer the second one, we don't, and that's very important. They're obviously -- historically been moved to optimize taxes between countries. But we are a big taxpayer in the U.S., particularly due to PIMCO. We are proudly supporting the American recovery. And on the economic solvency side, the numbers are volatile. As we said in the past, they reflect the best estimates Solvency II, and they show you that they are at, in my mind, unacceptably high economic volatility. And we are, indeed, working to reduce the volatility and have taken number of measures, not just on the model side, but for example, actually managing duration on the Life book appropriately, derisking our exposure to peripheral debt, we've talked about that today, in order to make the number more stable. In terms of the target level, I think even with Solvency II, it's a little bit futile to talk about the Solvency II level. But we have communicated then in the past that we want to see this number to be north of 130%, even though that is no hard line. And we -- as you can see, it's very important that the shock that we have put in there, which is not the worst case but is a very strong one, given where we are with interest rates today, still leaves us comfortably above the 130%. Now at the same time, please don't forget another capital criteria for us is our rating position. We've worked very strongly on supporting our rating. While at the beginning of the year we were significantly deficient, for example, in terms of capitalization to a Standard & Poor's AA rating, as of today, we have completely closed that gap. And so we are feeling very well on the capitalization side at this point in time. That would be my answers.

Andrew Broadfield
Barclays PLC, Research Division

Okay. So we're not -- we're still a little way before you start thinking you're overcapitalized?

Oliver Bäte
Chairman of Management Board & CEO

We, indeed, are away from being overcapitalized.

Andrew Broadfield
Barclays PLC, Research Division

So they were the small that wouldn't have transferred.

Oliver Bäte
Chairman of Management Board & CEO

Yes, exactly.

Operator

We will now take the next question from Fabrizio Croce of Kepler.

Fabrizio Croce
Kepler Capital Markets, Research Division

I have actually 2 only questions. The first one is I noticed that on the Swiss markets, you are actually growing very fast, I mean, for being a very steady market, plus 26% in Life in Q3. In general, it seems the past 9 months, 14% in Life. So in the -- in Other and P&C with 5%, while your combined ratio is actually worsening. So my question is are you actually executing a price war in -- or did you just start a price war in Switzerland? And the second question is more related to the crackling of the trough towards U.S. We just saw that Germany is trying to get its gold back from U.S. And in that frame, I mean, PIMCO is sensational. I mean, how better could they go from now? And so here, the question is are you thinking sometime to some sort of IPO? Because I saw they're still 71% is U.S. related.

Oliver Bäte
Chairman of Management Board & CEO

The answer on the IPO is no, and it doesn't make any sense. And PIMCO doesn't want it, and we don't want it either. We love the cash flow that's coming now. I think if we are right, we can almost pay the dividend just out of PIMCO cash flow. So that's pretty cool, no? On Switzerland, I don't know how you got there. Actually, the combined ratio, if you look at the table on Page 21 shows a significant improvement relative to the third quarter of '11. So I haven't really understood the question. And on the Life side, this is reflected from some special items on the group Life side. The contracts here are designed in a way that we can exit the contracts within a year. So we're not locking in very long-term guarantees at negative spreads, if that's what the question is implying. But we are satisfied with the new business margin on this business, okay? And PIMCO can obviously go further up, of course.

Operator

We will now take the next question from Brian Shea of Bank of America Merrill Lynch.

Brian Shea
BofA Merrill Lynch, Research Division

I just have 2 questions, please. First of all, the cost income ratio for asset management, it's been very good. It's just doing nothing but coming down. You talked about a target to take the AGI ratio down a bit further. Is there anything else you need to mention here? I mean, I don't want to over-extrapolate how it's been very good so far. In the past, you've set targets. It comes down to below that target. Is there any kind of caution you want to inject into that discussion?

Oliver Bäte
Chairman of Management Board & CEO

Yes, Brian, I think that's very helpful question. Yes, we'll talk about that.

Brian Shea
BofA Merrill Lynch, Research Division

Okay, great. And the other one is on the target you -- kind of rule of thumb you mentioned on the Life operating profit, about EUR 700 million a quarter. Given that your expense margin seems to have turned the corner now and you're back in positive territory, given the mechanics of how you're running income is coming out in Life and the asset base is growing and the kind of guidance you mentioned for the non-Life running income should come down, it's hard to see how the Life earnings will be as low as EUR 700 million. The mechanics don't really support that. It seems that it should be holding a bit more stable than that. Can you just -- is there anything else going here that I'm missing here?

Oliver Bäte
Chairman of Management Board & CEO

Yes. So let me talk about the cost-income ratio. Historically, we've been giving guidance to say we want to be below 60% cost-income ratio, and we've been beating that for a while. Given the strong growth in PIMCO, in particular, that had better numbers for now the last 3 years. Remember, third quarter 2010 was already 58.5% and it has improved from there, so we can expect below 60 CIRs for the foreseeable future if nothing happens on a shock basis, yes, which we can never fully exclude. The second point that you've mentioned on the Life insurance side, yes, we are improving the expense side of things, and we are also planning to improve the risk component. But we do not have the stability yet in the development that I'd like to see. So before I start to raise the outlook for the Life segment, let's continue to work on the improvements for a while, but we are on the way. Yes, we've been, at some point, at EUR 1 billion in terms of technical income that fell down to EUR 700 million by 2009 when I came. We want to bring it back up to EUR 1 billion. But we're not -- given the strong headwinds that we've seen and the significant investments we have to do to change the business model, that might take a while. The declining yields are also affecting it, even though they're not strong over the next few quarters. And to be very transparent, Brian, we're not out of the woods in terms of capital markets. When everybody is happy at this point and markets are in a lull, you cannot continuously plan for -- with such a low level of impairments. So some might actually happen to come. So I'd rather be, as you know, on the conservative side in terms of forecasting results, but they are conservative.

Brian Shea
BofA Merrill Lynch, Research Division

Okay. Just on the first question. So you target below 60%. I mean, you're at 56% now. Is that going to -- I don't want to be too precise here. But I guess the question is, can it stay at 56% is, I guess, is my question.

Oliver Bäte
Chairman of Management Board & CEO

No. I don't give precise numbers, I'm sorry. The movement tends to be so extreme. If you have -- remember, last year we had 1 or 2 bad quarters in PIMCO, and then suddenly, you see outflows that then came quickly back. So the movement can be quite strong. Now we have some comfort in, but we also remain cautious here. Maybe because the party has been too good, yes.

Brian Shea
BofA Merrill Lynch, Research Division

You do accrue -- just to make sure, you do accrue bonuses, right? I mean, it's not as if there's seasonality in respect to how the expenses are accrued.

Oliver Bäte
Chairman of Management Board & CEO

Yes. I want before we move to the next question, Tom Wilson was so nice to point out on a clarification, because one of the prior questions was on whether we have capitals, Life capitals. We do have onshore Life capitals in the U.S. and so in others, but we don't use them for tax purposes but to better support risk management. I just wanted to make sure in hedging that there is no misunderstanding, right? Because the question was around do we have capitals to manage tax position. So the answer is no, but we have capitals for other purposes. So next question please.

Operator

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

Michael Hermann Haid
MainFirst Bank AG, Research Division

Two questions. First, on Central and Eastern Europe, in your quarterly report, you mentioned increased competition in Poland, motor insurance. Also I read on Bloomberg that you were quoted that in -- that Life insurance in the Central and Eastern Europe region was becoming more competitive. Could you elaborate a little bit on the competitive situation in the CEE area overall? And the second question is, again, on Italy. Obviously, you showed very good results after 9 months. To my understanding, Italy decided on some changes in motor insurance, which could increase competition. It's kind of -- what I heard is kind of a Bersani II law to steadily to a significant increase in competition from your perspective.

Oliver Bäte
Chairman of Management Board & CEO

Yes, Michael, let me address them in turn. In terms of the competitive situation, we need to separate margin and profit pools from the revenues. There is a lot of competition for market share that's depressing margins, and Allianz measures itself in terms of how successful are we in terms of addressing the profit pools. But we have, relative to the top line, a very, very strong position that we are protecting. So for example, Poland motor was an interesting example because the competition on the pricing side is very significant. Second, on terms of the Life products, the -- our product that we can sell through agents and through the broker partners are very good. The new business margin is very strong. At the same time, we have had, in the past, products that we've been selling through banks that more -- do more resemble deposits. There, the margins have been extremely under pressure because the banks are trying to put money into their own deposit base. By the way, that is not restricted to Eastern Europe. We see that in many, many other places. And there, the margins have deteriorated to a point where we say enough is enough, we don't play anymore. The Polish Life parts -- deposit products were a case in point and in time. And there, we have discontinued that. We remain committed to protecting margins. The same is true, by the way, as I mentioned earlier, in Russia. We have been restructuring and re-underwriting our health care business. We had a lot of large corporate accounts that were providing a lot of revenues but very little profitability. We've been letting go, just to give you another example. So that's Eastern Europe. Let's turn to Italy, the Bersani II was the question and how do you feel. They call it a little bit differently, growth 2.0. That's really funny because I'm not sure what the growth is meant by. It's probably growth in something -- I don't know. And that it might be mandatory discounts, increase and price increases only every 2 years, la, la, la, la. This Decreto Sviluppo and previous laws have been designed, but we do lack final interpretation or even execution, so-called secondary laws, so we don't really know what the outcome is. However, the outcome is there will be a most likely negative for the average MTPL premium.

And I personally believe that the impact is not going to be as negative because there are countermeasures also in the laws. So for example, we do have support on antifraud. We do have support, if I remember correctly, on bodily injury claims. So in a strong technical environment, like in Allianz Italy, you might see actually very balanced effects. That's different for other players potentially. However, margins will come under pressure, and as I said earlier, we'll see for a while, extremely strong results on Allianz Italy. I cannot predict the same strengths for the midterm however.

Operator

We will now take the next question. It comes from Nick Holmes of Nomura.

Nick Holmes
Nomura Securities Co. Ltd., Research Division

Just a couple of questions. First one is on U.S. Life, and I wondered, can you explain some more why the margins is so very [ph] much when you were repricing the products? Because I would've thought that, that should've actually helped the margin. And then second question is on German P&C. You've got a target. It's the combined ratio to fall to 95% by 2014. And this is a really nice question, Oliver. You've already got to 97%. So does this mean that we should be expecting better than 95%?

Oliver Bäte
Chairman of Management Board & CEO

Yes, I'm very confident that the German colleagues will deliver on their targets. They've done a great job in restructuring the shop. It's been a lot of work in distribution, in the back offices. You saw a number of further restructuring this year. And in combination with a significant price increases that we've been taking and are planning to take further, I'm confident they will reach their results. I'm very confident. It's very important for Allianz group not just for Germany. Second point, in terms of repricing the cost, what is really driving that? It's very important. We have, in order to protect margin, let a lot of top line go. And one of the effects is that because we've been investing in new distribution, we had some cost overruns. These will go away in 2013, because we've been culling costs in order to balance the lower revenue. So that will disappear. By the way, very well spotted, Nick. Thank you very much for the question.

Operator

We will take the next question from Thomas Jacquet of Exane.

Thomas Jacquet
Exane BNP Paribas, Research Division

I have 2 questions. The first one is around the net profits because, actually, you raised the guidance for the operating profits. But you also highlight several elements for Q4 that will weight on net income, and it gives the impression that you have a clear view on what's going to happen in terms of restructuring and impairments. So what could you say about the net income maybe in relation to the level of 2010? And my second question is on deferred acquisition cost. They decreased by EUR 1 billion during Q3. Is it a change in methodology or mainly driven by ForEx movements?

Oliver Bäte
Chairman of Management Board & CEO

We'll deck out the second question, good spot. I don't have that in -- on -- from the top of my head. Well, somebody will dig that out while we are talking. Now in terms of the net profit. We have a reason why we do not provide guidance on net profits. By the way, most of our competitors don't even give guidance on operating profit, just to be clear. The -- and the reason is very, very simple. Number one, we have explained earlier that we do derisking of the balance sheets. And we've been very lucky with the spread movements and have timed our derisking very well so it hasn't caused any fee impact of any size that we need to report on. So well done to our colleagues on the investment side. At the same time, we cannot say that for the last 8 weeks of the year, that will remain the same. And on top of that, we are still debating on how to further improve competitiveness and, therefore, might decide on further restructuring in the weeks to come. We have a number of things that we are looking at, particularly on the P&C side in

Europe that might come through. So I'm not ready to provide you with any specific guidance. The thing I can give you, however, is that as in the first 2 quarters, you cannot see a parallel upward movement. So if somebody is speculating on a huge increase in dividends or something like that, I have -- can already disappoint you today. You don't need to wait for the fourth quarter. Now second point is in terms of the back movements. My experts tell me the movement in the Life and Health DAC is actually due to what we call the so-called shadow DAC, i.e., when the unrealized gains and losses move, then the DAC accounting also moves. For any technical details, please see Oliver Schmidt's team as, usually, he will give you a fantastic technical answer.

Oliver Schmidt
Head of Investor Relations

Looking forward to that.

Operator

We'll just take the next question from Vinit Malhotra of Goldman Sachs.

Vinit Malhotra
Goldman Sachs Group Inc., Research Division

Vinit here. A few things there. Firstly, I've been curious for a couple of quarters now that the total return fund, when you look at the fund flows, is not -- is becoming smaller and smaller portion of the pie of the total flows we see in this quarter. And we try a better bracket during the quarter, but it's becoming less and less. And if this -- is this linked somewhere to this higher profitability we are getting, excluding the performance fees? Is there some kind of a geographical mix or some other thing that you think it's commenting -- it's going to be commented on? And lastly, with -- my understanding has been that 70% has been the number you're looking at on the -- on this headline accident year loss ratio, and you're getting there. So what's stopping -- or what are the drivers that you could get -- will make you go towards 69%, a number that you would look at? Is it that...

Oliver Bäte
Chairman of Management Board & CEO

Are you talking 59% or 69%. 69% I think is plain. 59% will be tough.

Vinit Malhotra
Goldman Sachs Group Inc., Research Division

No, no, no. 69%, sorry. 69%, sorry. 69%, sorry, to be clear. 69%, just 1% more or better. And the idea is that -- is it that -- in the few quarters ago, we've discussed about how the German recession having any discount there. The question is, well, is it linked to that which stops you from thinking about 69% as the better number? And lastly, just on the dividend policy. From the previous year, was it not correct in understanding that you're also going to look at a certain ratio on operating profits as an indicator as well? That's the 3 questions.

Oliver Bäte
Chairman of Management Board & CEO

Very good. Let me start with the last one. We've historically said 40% payout of net income, and that will remain stable. And we said in years, where we have unusual volatility, like in 2011, we used -- using the OP and the balance sheet strength as a symbol to say we can support that despite enormous volatility in accounting net income. Remember, last year was driven by a lot of write-downs on the Greek government debt and financial titles. What is important to us, [indiscernible] is dividend stability, and I'd like to point that out. So in the more -- objective number one is not having to cap dividend is the most important thing, because many of our core investors do want to see dividend stability. But we remain committed that if net income grows continuously, that our shareholders will participate in the increased payout and through interest payouts. But we are far from being there yet. So let's wait for where we are at the end of the year, but we'll make sure that we stay, at least, stable. Sorry, no promises on the upside. Second question, total return flows on the third quarter were EUR 3 billion. This is a very profitable product. So

I think that it has anything to do. But what is really important is that we are growing the retail side of the business and the structural product side across the asset management space and that also comes with higher margins. So it has nothing to do with deemphasizing the total return fund. But the promise of PIMCO to become an investment authority rather than a bond house is reflected in the growth that we're seeing, both in terms of absolute earnings but in terms of margins. Last item, accident year loss ratio, yes, 69% is a nicer number than 70%, of course, and that's what we're trying to shoot for. As I mentioned earlier, the crop losses that do not count as NatCat have really had a impact here and some movements on the credit side and in terms of the target we need to go there. So we need to have pricing strength outpace severity growth, and that is one of the key objectives, together with maintaining some progress on productivity on the admin side for next year.

Operator

[Operator Instructions] We will take the next question from Atanasio Pantarrotas of Cheuvreux.

Atanasio Pantarrotas
CA Cheuvreux, Research Division

I have 2 questions left. First of all, on the volatility of your requirement capital according to the Solvency II model, I would like to know what is the timeframe that you use to evaluate the volatility in correlation to market, given that there was quite a significant swing between Q1 and Q2 and Q3 in your requirement capital? The second question is on the investment income. I saw that there was some volatility of your ordinary income in both the businesses, in spite that this quarter should be quite positive in term of ForEx, so if you can give us some more color on this.

Oliver Bäte
Chairman of Management Board & CEO

Yes. Tom is preparing a few items on the capital movement. I think what we -- what need -- we need to think about in terms of the investment income, quarterly numbers, to be honest, are very difficult to interpret. So I always caution people to take quarterly numbers on the investment side as any indicator. It think it makes more sense to look at the 9-month numbers. Now going at -- back to Page 25 on the P&C side, you actually see very stable interest and similar income numbers that are hovering between EUR 890 million and the peak was around EUR 960 million, and that's the mid-corridor. We had a decrease of net harvesting, and that's the thing that moves out the most, if you look to the second line. And then we had unusually high investment expenses, and that really impacted this quarter numbers. These are more around one-offs rather than anything else that is structural here. So I can assure to you that there are no major movements. Now in terms of the Life insurance side, let's move to the respective page, that is on 35. You also see very consistent levels of interest and similar income that have been trending upwards with the increase in assets under management. The volatility, again, here is coming from the net harvesting and other side. So in the difficult quarters like the third quarter of 2011, you see significant negative sensitivity down, and we are with EUR 400 million back up to a good value. The longer-term average is between EUR 250 million and EUR 300 million. So with that, we are slightly above what we normally have. And in that, you have some fair value movements. You mentioned that the change has been EUR 200 million this quarter, but it can also be EUR 200 million down. Overall, together with the investment movements, we are expecting around EUR 4.1 billion to EUR 4.2 billion in operating investment income for the next few quarters. But again, lower interest rates will eventually have a cost to it, and we're trying to balance that through better diversification and moving out of government debt into other asset classes as we can and see fit. Now the technical question and the technical answer. You answered what has happened in terms -- what were the timeframes. I didn't know that, so my experts gave me the numbers. Market correlations are based on weekly observations, and they are doing that since 2004. And what we do with the correlations, we actually update them every year based on both experience and also expectations going forward. We have a big group that is actually looking at that. I think in terms of the model, we've been overly conservative in the past, and particularly as it comes to think through interest rate movements on the one-hand side and the losses, and I think we are now where we need to be, okay?

Operator

We will take the next question from Andrew Ritchie of Autonomous.

Andrew James Ritchie
Autonomous Research LLP

Two very quick questions. Obviously, part of the derisking has benefited you to the extent it's lowered your required capital over the quarter. You've indicated there's going to be further significant derisking in Q4. Would you, therefore, anticipate that the required capital would fall again in Q4 if we assume there's no major market movements, credit spreads or interest rates, obviously? Second question, I mean, part of the MCEV change is you've recognized to your benefit a much lower annuitization rate in Germany. I don't suppose you can tell us what the change is in term of annuitization rate, how dramatic a change that is. And secondly, are there not policyholder behavior issues going the other way in other parts of the world? So have you looked at policyholder behavior all over the world? Obviously, it has benefited you. Your assumption changed in Germany. What about other parts of the world?

Oliver Bäte
Chairman of Management Board & CEO

Yes, that's a good -- let me start with the last one. The first one is fairly technical, and I don't do forecast on the required capital. So I cannot tell you. This is an if-then question. But let's focus on the second one, which I very much like. The annuitization assumptions are driven in part by what we are seeing. And then you obviously are correct to say what is the rational behavior of clients, given that interest rates are down and that you have a certain guarantee. Shouldn't people be annuitizing more rather than less? Now that is very specific to a country's position and to the attractiveness of the terms and conditions that you lock in when you annuitize. Very important to understand that there are certain conditions that do apply when you annuitize. And we have found in the German environment that, sometimes, actually perceive it to be less attractive to annuitize rather than take the money out and, for example, invest it in other products. And that actually happens to improve our profitability relative to the underlying guarantee. So it has nothing to do with only client behavior based on where interest rates are, but that are specific to the concrete terms and conditions under which annuitization happens, because you're locking in certain returns. But -- by the way, also limit the upside as part of the policy. One part of that is also interesting because in -- just to give you an example. In the future, you will see more products that, upon annuitization, allow you a reset of the annuity. That also means a reset upwards in case that interest rates rise as we should be expecting going forward.

Andrew James Ritchie
Autonomous Research LLP

So what you're saying is the policyholders are not being efficient in Germany?

Oliver Bäte
Chairman of Management Board & CEO

Yes, and they are never efficient.

Andrew James Ritchie
Autonomous Research LLP

And then what -- did -- I mean, have you halved the annuitization rate of what -- I mean, what...

Oliver Bäte
Chairman of Management Board & CEO

We don't provide -- sorry, we don't provide disclosure on any specific item per country.

Andrew James Ritchie
Autonomous Research LLP

And are you seeing any inefficiencies that could result in positive assumption changes anywhere else in the world?

Oliver Bäte
Chairman of Management Board & CEO

Good question. Not that I know of at this point in time. And by the way, sorry, this is very important so let's not quickly move on. Let me give you a comment. It also obviously depends on what the competing offer is. Let me give you an example from the U.S. Why did you see on USDA, in the past, very significant lapses towards your 6, 7 and 8 of the A products, and they had 2 reasons. Number one, the lock-up period was ending. But number two, the industry was so competitive that everybody else was offering ever-higher benefits to clients that made it rational for brokers and clients to move the assets out of one product into another one. Now if the environment changes, where, for example, new product offerings become less generous, it becomes less logical and legally problematic for brokers to move clients from one product to another. So you cannot just look at client behavior in isolation, you also need to look at it relative to other offers. So let's not just look at the client behavior. It also depends on what the competing offers on the market are and what is the distribution behavior. Because only the vector of the 3 drive the effective annuitization behavior.

Andrew James Ritchie
Autonomous Research LLP

Okay, that's helpful. Just -- so just back to my first question. I mean, the broad -- first of all, I'm not asking to make a forecast for required capital during Q4, but I'm just trying to understand. You've done quite a lot to reduce required capital. Is that kind of the easy stuff done? Or is there other stuff you can just still do to reduce required capital? Or is there any sort of delta in that number going to be a lot less going forward...

Oliver Bäte
Chairman of Management Board & CEO

No. You shouldn't be expecting a lot less. If I -- I can help you with your forecasting a bit, and that you shouldn't be expecting huge movements.

Operator

We will now take a follow-up question from William Hawkins of KBW.

William Hawkins
Keefe, Bruyette, & Woods, Inc., Research Division

Just briefly, Oliver. It will be a travesty if I let you do your last conference call without telling us the surplus value of Life business in force in the MCEV?

Oliver Bäte
Chairman of Management Board & CEO

Coming as -- in a second, Oli Schmidt is sitting next to me. He was just waiting for this question. He's flipping the pages and very quickly will be there. And the exact number at end of the third quarter of 2012 would be EUR 2.624 billion.

William Hawkins
Keefe, Bruyette, & Woods, Inc., Research Division

Ending on a high.

Oliver Bäte
Chairman of Management Board & CEO

We're ending on a high.

Operator

We have one last question, a follow-up question as well from Michael Huttner of JPMorgan.

Michael Igor Huttner
JP Morgan Chase & Co, Research Division

What I really wanted to know is these numbers feel as if there's more to come. It's not -- you haven't actually shut the lights out. There's more for your successor. But you mentioned also a little bit that you transferred some of the excesses of -- which I guess were held by the holding, into the U.S. to -- for asbestos and stuff like that. And then you mentioned Brian's research showing that your reserves were sky high. But as a seal, did you actually -- in the quarter, did you strengthen reserves? Or did you weaken them? I mean, just as a feel. There's no numbers. Just to get a feel for how things happened.

Oliver Bäte
Chairman of Management Board & CEO

We never weaken the reserves. We always strengthen them, Michael. But kidding aside, it's escrow we've been working on, the 3/2. The margin has been going up. We've also balanced out the reserve strengths across the group. We had a mismatch at -- 3 years ago between some that were extremely high, and others, they were less high. We've also trying to bet that out with Oskar joining the team. And so there is, indeed, more to come. There's more strength to come now. Please -- you said we've pushed down some excess reserves to asbestos and like that. The comment was only focusing on asbestosis after the global study we've done in 2010 and utilizing the group level reserve that we put for that. It only applies to asbestosis. This is, by the way, it does not apply only to the U.S. but what we've been globally doing, because asbestosis is so unpredictable relative to what we do. Otherwise, as you know, Allianz is not a big liability writer, particularly not in long-term lines. It's the only area that we, from a group level, pay a lot of attention to. And I'm very happy to report that what we've been doing has been very comforting on the reserve side. More to come [ph] if you mean positive notes.

Operator

That will conclude today's Q&A session. I would now like to turn the call back to Mr. Schmidt for any additional or closing remarks.

Oliver Schmidt
Head of Investor Relations

Yes. Thanks for joining the call. We say goodbye to everybody, and we wish you a very relaxed weekend.

Oliver Bäte
Chairman of Management Board & CEO

Yes. And I wish you a lot of fun with Peter. You know him really well. He's in the room. So I'm very happy to hand over. It could not have been better after 3 years on the job here. I thank you personally for all of your support. It has been real fun, unfortunately, also a lot of work. And I'm very much looking forward to some more sun in the south of Europe. All the best, and see you there.

Oliver Schmidt
Head of Investor Relations

Okay. Goodbye to everybody. Thank you.

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