S&P Capital IQ

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Allianz SE DB:ALV

FQ2 2015 Earnings Call Transcripts

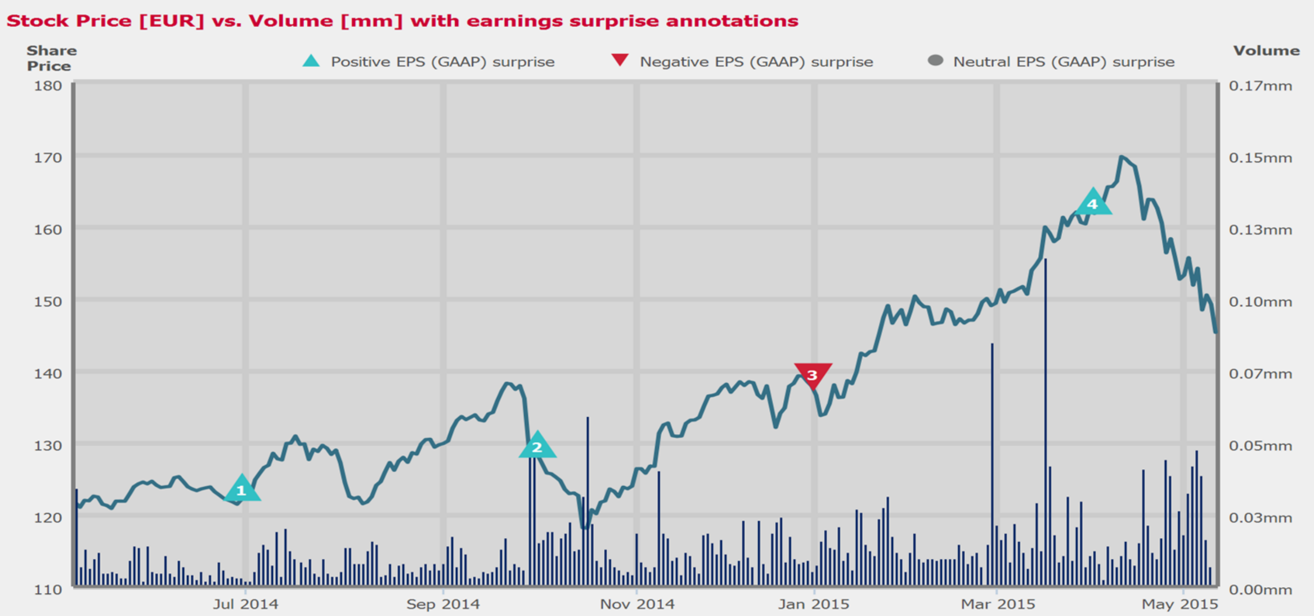
Friday, August 07, 2015 12:00 PM GMT

S&P Capital IQ Estimates

	-FQ2 2015-			-FQ3 2015-	-FY 2015-	-FY 2016-
	CONSENSUS	ACTUAL	SURPRISE	CONSENSUS	CONSENSUS	CONSENSUS
EPS (GAAP)	4.01	4.38	▲9.23	3.36	14.50	14.67
Revenue (mm)	31459.00	30200.00	▼(4.00 %)	30086.00	127391.85	134889.45

Currency: EUR

Consensus as of Aug-07-2015 12:22 PM GMT



- EPS (GAAP) -

	CONSENSUS	ACTUAL	SURPRISE
FQ2 2014	3.37	3.84	▲1 13.95 %
FQ3 2014	3.34	3.52	▲2 5.39 %
FQ4 2014	3.22	2.67	▼3 (17.08 %)
FQ1 2015	3.70	4.00	▲4 8.11 %

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Presentation

Operator

Ladies and gentlemen, welcome to the Allianz conference call on the financial results for the second quarter 2015. 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

Thank you, Adele. Yes, good afternoon from my side as well, and welcome to our conference call about the results of the second quarter 2015. There's nothing specific to add from my side. So without further ado, I hand over to Dieter.

Dieter F. Wemmer
CFO & Member of Management Board

Thanks so much, Oliver, and also good afternoon and good morning to the U.S. colleagues to our second quarter results call. I am very pleased to present today another excellent quarter. Before I go into the numbers, let me just start on the business highlights. We continue to drive the digitalization of our retail products. We add new claims app to the system to simplify and improve the service to the customers. And on the investment side, we had a very successful quarter, actually, including a very successful July, really to gain a number of important and large real asset investments. And also on Asset Management, we have opened a number of new products, which should help to secure future process and future success in the Asset Management.

Now let's go to the numbers. EUR 30 billion revenues for the quarter internal growth, corrected for foreign currency at minus 3.8%, driven by Life and Asset Management where P&C is still growing organically but resulting in an improved operating profit over the quarter of EUR 2.842 billion, adding already to a very good quarter in Q1 and with EUR 5.7 billion out of the half year, we are 5 percentage points ahead of our suggested mid-point. And therefore, before we forget it, we are increasing and lifting our outlook to the upper end of the range. That means EUR 10.8 billion, which would be exactly a 4% growth over 2014 full year result, and we are confident that we can reach it.

Net income, up 15% for the quarter, 13% for the half year, clearly indicating that we can, together with the solvency we have reached, support a very good dividend payment. But we will certainly, I assume, in the questions talk about this in more detail.

Let me move on directly to our solvency numbers. And shareholders' equity is flat to beginning of the year. The additional gain in unrealized gains at end of Q1 with a low point of the yield curves vanished, so that we are more or less flat actually. Unrealized gains in bonds at the half year are slightly lower than beginning of the year. Very simple, the interest rates are a bit more ups in beginning of the year. And additionally, the bond got 6 months older. Therefore, there's a natural amortization of unrealized gains.

So the solvency ratio, 212%, and most of you expected more 202%. So actually, what has happened? And when I use our own disclosed volatility from Q1, I can actually explain already a lot of it. So the interest rate movement is actually more than 50 basis points. The most relevant point in the interest rate curve is a 20-year euro swap. The 20-year euro swap moved 92 basis points in the quarter. So when you take our disclosed sensitivity of 9 points for 50 basis points, I have taken the simple math, 16 points for the 92, and that is also how the more detailed analysis confirmed it.

Equity markets are roughly down by 5% when you take a mixture between U.S. and Europe. That has cost us 2 percentage points in the solvency. Gov-e [ph] spreads, a little reignited due to crisis with the whole Greece and Greek debates that cost us 3 percentage points in the solvency ratio because gov-e [ph] spreads are up by 30 basis points, and that is in our gov-e [ph] disclosure, 100 basis points equal to 11. And then corporate spreads were up in the quarter by 15 basis points. We said 100 make 8 points, so 15 make roughly 1 point. So when you add all these numbers up, you would have seen a 10% improvement but we moved 20%. So what are the remaining 10? 4 percentage points are actually coming from the interest rate curves steeping, 4% comes from the sharp volatility decrease, and 2% comes from additional management action where we did much less further improvements than in Q1 because we watched the developments very closely, had our contingency plan in place, but only executed in line where we felt what is necessary. We are still doing some more derisking in the third quarter, but only to a smaller extent.

So adding up all the details, you end up exactly with the 20 percentage point movement from Q1 to Q2. And we feel very comfortable with the number, with the development and, in particular, what we have achieved with all the changes in Q1, also with the sensitivity. When you look at our shown sensitivities, you will see that in all the stress scenarios displayed, the low point is above 200, and that is a very good achievement.

And I will show you also additionally, a bit later in the presentation why the high volatility and the solvency we still have in our German business in the end is not so relevant for your considerations.

So let's move on to -- sorry, I lost my paper. So let's move on to the P&C results. First, the growth. 1.6% internal growth for the 6 months, 9% including the currency effects and the small acquisitions we did over the last year. It is still okay number. We had some movement in Germany and France between March and April. So therefore, the second quarter growth of the 2 countries looks fairly weak, but a strong Q1. If you look at the whole P&C segment over the 6 months, I think you get a better picture of how it is developing, also supported by the net earned premium growth, which is 8% in euro nominal and it is close to 3% in currency adjusted. So I think our organic development is still pretty fine. The biggest contributor to organic growth continues to be Allianz Worldwide Partners, our global assistance and health business, with almost 10%. And not shown here on the page, our Turkish business, which is the market leader in P&C and health in Turkey is growing with 22.8% without currency effects.

So how did this all result in our operating profit? Operating profit's up exactly EUR 400 million, on one hand, supported by a very strong combined ratio of 93.5%, and I'll come to this in a moment. And plus additional premium growth makes EUR 178 million plus in underwriting profit. And in the line other, that is mainly a benefiting from EUR 220 million net gain on Fireman’s Fund we booked in the second quarter.

The run-off results at 3.4% level or 3.3% for the half year, a very stable development without any big impacts. So 1 percentage point improvement in our combined ratio can be split, half in lower cat or weather-related events of 50 basis points less than last year and the same improvement level in the expense ratio where I would expect that in the expense ratio, more 30 basis points are probably sustainable and 30 basis points are less sustainable.

So is Fireman’s Fund sale altogether for our half year a positive one-off. Well, actually, when I add all the payments and benefits around Fireman’s Fund, I'm coming in total to a 0. And let me explain why. We booked already EUR 90 million restructuring charge for the integration of the commercial business with AGCS in Q1. We booked here a EUR 220 million gain. That is again a USD 365 million of sales proceeds minus restructuring costs. So when you take the EUR 220 million minus the EUR 90 million you booked, you end up at EUR 130 million. And we had additional reserving for the Fireman’s Fund commercial business of EUR 134 million. So when you add all figures up, you actually end up pretty exactly with 0. And to some extent, that was the concept of the personal line disposal. On one hand, we didn't see the opportunity to scale up the business on our own and pay for the new systems necessary. So therefore, the sales proceeds are exactly paying off a restructuring of the commercial business and helping a successful integration with AGCS. That has already happened very much on the sales formed and renewal premium broker appreciating the new setup. Commercial premium volumes are above our own expectation also in Q2. And A.M. Best has also welcomed the integration by lifting actually the rating for the Fireman’s Fund company. We have now in the U.S. for both entities together an A+ rating, which is the best rating possible. So we are really -- we are very much on track with what we want to achieve.

Moving on to the page showing the individual results of the largest P&C units, Page 13. Germany with a stellar combined ratio of 86%, certainly supported by low weather events. In Q1, it was the opposite. So Q2 is a bit the offset for Q1. Italy continues to perform at a mid-80% level, which is a very strong performance because the market environment is getting tougher and tougher in Italy. France, at 95%, really very good. AGCS, looks bad on this page. But that has now the reserve increase for Fireman’s Fund included. And we separate out the 2 pieces, AGCS also in the second quarter at 94% combined ratio, there is actually on Page 57 in the appendix. As you can see, the half year numbers of AGCS separately, which is a 93.6% combined ratio. So we continue to see a strong performance.

Fairly light second quarter in large losses. We had more large losses in AGCS in Q1, but Q2 was fairly light. In the U.K., we have seen more weather-related claims, but also our start-up costs for growing our motor direct brands have deteriorated the combined ratio in the U.K. Australia also, a deterioration against last year, driven by a lot of hail damages we had in the area of Sydney. And Latin America is an improvement over Q4, for sure, but we couldn't completely have sustained good development as in Q1, in particular in Brazil. We have -- we are seeing a more soft market -- or more the impact of a soft market in industrial lines in motor, and we are still having some cleanup on the group health business.

Central and Eastern Europe, very good improvement because the cleanup of Russia and the closure of the business progressing very well. And the other Central European markets always had a very good combined ratio. I think still without Russia, the 96% we show here is a 94% ratio. Russia has still a combined ratio above 100%, but at a very small premium volume.

Investment income in P&C, probably a surprising positive. EUR 840 million is a strong number for a quarter. Q2 has, of course, accounting for the dividend yields of our equity investments, and we have increased over time our equity investments, and also companies are paying better dividends. Still the low yield environment is visible because our current yield is falling 6 basis points and will continue to fall as the reinvestment yields with 2.2% [ph], a big number for P&C reinvestment. But it is still substantially lower than our running yield of the portfolio. We have slightly increased the duration further in the second quarter. And also, we have invested a bit more in emerging market risk where we hedged the currencies to a large extent.

Moving on to the Life segment. Premium volume, as I've said, 6% down adjusted for currency minus 1.4%, nominal. The driver for the reduction is our German Life business where we are writing less single premium business. That is not a question of can -- is the markets drying out? It's a question that we reduce our risk appetite here because we want to grow the business with our new products stronger, so it is about driving the new business mix. And I will talk about the German Life business in a few moments in much more detail.

Italy, very nice growth with huge volumes of unit linked in the U.S. We had this really fantastic second quarter last year when we introduced the BUDBI product, the fixed index annuity product with a special index from Barclays. Now we are a bit a victim of our own success, and we couldn't repeat it. There is also more competition on this product class. So therefore, it was also expected that's a big number could not be repeated.

Asia-Pacific, important growth in unit-linked business in Taiwan, which we sell through various local banks so avail [ph] diversified unit-linked growth. And the other market is Spain, where we have launched a new product which is being sold through Banco Popular, a savings product that takes benefits.

Moving to the operating profit. Maybe some of you would have expected a bigger number than EUR 850 million. But I think it is not surprising, as the second quarter saw, in some instances, the opposite financial market movement from the first quarter. And when we showed EUR 1,100 million profit of the first quarter, I mentioned -- I believe I mentioned in the call that there is a EUR 200 million positive one-off included, among others, the high positive derivative result, in particular in Germany. We had in Germany about EUR 1 billion gross derivative results, which is under the 90-10 split roughly EUR 100 million for the shareholders. And in Q2, we had exactly the opposite. So that means that the 2 derivative results over the half year, so companies who only have half year reporting, would have shown you a 0 movement. And we showed EUR 100 million up in Q1, EUR 100 million down in Q2. And the other negative one-off is we have further reserve increases out of reserve deficiencies in the Korean business. Here, the guarantees required more reserving. So therefore, Korea, in the current yield environment will from time to time pop up as an entity consuming some of the well- and hard-earned operating profit.

So taking this into account, the EUR 850 million is a very strong result for our Life business. And, in particular, when you now add it up with Q1, I think both numbers together make a really strong first half year.

Where do you see the Korean impact? That is on one hand hitting the investment margin with 95; and then you look on the right-hand side, where we show the operating profits by line, it is actually in protection and health because this -- some health rider [ph] was savings share and guarantees products being written some-20 years ago.

So now moving to the new business margin and mix analysis. The new business margin at 1.5%, may be still below your expectation. I think that is a very good result compared to Q1 because we have achieved more mix changes and have actually stabilized the new business margin. And please remember, we are calculating the new business margin with the opening interest rates of the quarter. So we are using here the April 1 numbers for calculating the new business margin. When you do the same calculation with July 1, the new business margin jumps from 1.5% to 2.6%. So maybe if you want to have a fair weighting for the quarter, it is the average, between 1.5% and 2.6%, as we are selling policies every day and not only on April 1. But I also believe that when you add up many quarters, that is, anyway, averaging out and it is probably not so relevant. Certainly, for beginning of July, our new business margin calculations are substantially easier.

Are we happy with it? No. I think with all the plans we are setting up for the rest of this year, and in particular for the next years, we will work even harder on getting a more stable new business margin and also continue to reduce the interest rate sensitivity on this one.

U.S. with 2.6%, I think, is an okay new business margin. We have further done repricing during the quarter, so you probably will also see further recovery of the new business margin in the U.S. over time.

Page 23 is only a documentation and to create transparency how safe are the guarantees can we still afford to pay the guarantees, can we still afford to take out a sufficient shareholder piece? And I think when you looked at -- actually, the 20 basis points investment margin for the quarter is being fully paid out of the current yield. That's net harvesting. That means the movement of all derivatives, all realized gains and everything end up with 0 across the portfolio. We have really a good quarter because 21 basis points means 84 for the full year, and I think that is a really a very relaxing number, supported by a reinvestment yield of 2.8% during the second quarter, and we have also kept up with the duration management. And I think the mismatch is pretty small.

So now turning to Page 25. There is a lot of recent press about the sustainability of Continental European Life businesses and the German Life Insurance business in particular. I read all these articles with interest, all these experts who after they asked -- finalized -- to analyze the banking crisis, 10 years later are now trying to work on the insurance industry and try to understand what could be the next crisis. I'm absolutely not sharing the analytical papers I have all read because they are all missing important points of our industry. And certainly, I should now not start to speak for the whole European insurance industry. Let me focus just on our German Life business.

So Page 25 gives you a number of additional details. First of all, and that is still important because we are living from our customers' money and nothing else, we are selling products, which are attractive for the customer because we have an annual crediting rate that is still at 4.2%. And we are sharing all investment returns we are producing with more than 90% for the policyholder.

So how sustainable is the model? Well, look at the middle column. We are showing here for our German business the investment margins above the guarantee. The guarantees you can see on the left-hand side, so that was in 2014, 2.8% on average. And the 1.9% we show on the 2014 in the middle column is the excess running yield above the guarantee. And that one is not including additional harvesting. But obviously, it is not including any noise and movement coming out of derivatives. So that shows that this margin is pretty high. And in the internal model we have filed with our German regulators, the BaFin, the solo Solvency II ratio for our German Life business without applying any transitionals is above 300%. That is a big number and also shows how well sustainable this business is stand-alone. So now don't start to calculate what does it mean for the remaining legal entities of the group because in the group solvency ratio, the 300% or the above 300% number is haircut to a number slightly above our average 212% for the group. So it is not driving the average highly up. Because this -- a lot of this capital is nontransferable because it is hybrid capital, which sits actually in the customer accounts and so finally, eventually, go to the customer but temporarily not there as a risk buffer.

And this risk buffer actually allows us to invest stronger in real assets, but also to bear some volatility in the interest rate market. So even if the markets are moving, you will not see that we are injecting any capital in the company, but also the IFRS equity in this company is fairly limited. We can also not take out a lot additional beyond a very strong dividend, which we take out every year.

So from looking at the volatility of the solvency ratio, it also drives the volatility of our group solvency ratio. But it is, in the end, a bit capsulated in itself and it is not -- this volatility actually does not affect the rest of the group. And that is, in particular, visible on the right-hand side because we are producing fairly strong and stable operating profit and we have also a good flow of dividends. We are now at the EUR 500 million level, which is a pretty strong number because that is 50% of the operating profit. Or when you do it as a percentage of net income, so subtract another 33% tax from the operating profit, you see that it is a very stable, a very nice payout ratio.

And in ROE terms, it actually generates return on equities between 15% and 21%, which is in today's world, for a financial institution, a very strong ROE. And that for a business, where everybody is now writing, that is so dangerous and not sustainable. I must say, I'm absolutely not sharing the analysis, and I really don't understand how people are getting it.

So let me move on to the Asset Management business after this x course [ph] to the German Life business. Assets under management, pretty flat over the half year, lower than end of Q1. Continued outflows at PIMCOs come negative market movement. Quite obvious, interest rates went up; equity market slightly weaker. And also the dollar weakened a little bit over the last 3 months. So actually, all 3 factors added to in total a EUR 70 million -- EUR 70 billion of outflows. The PIMCO outflows reduced to EUR 29 billion, USD 32 billion, slightly a bit less than half of Q1. So actually, very much on track with what we said how we are seeing the progress. Allianz Global Investors was another EUR 7 billion of inflows, continued their very successful development. I think that is now the eighth quarter of continued growing success.

Is PIMCO with its product policy, with its customer management on track? We believe yes. We believe that the returns of the funds are actually in very good shape. Customer service had, anyway, not a blip over the last quarters and years. And when I look at the July outflows, which are around EUR 3 billion for July stand-alone, I think we are also developing in the right direction.

And the income fund, for example, is one of the most successful mutual fund products in the U.S. market, very good inflows, very high performance, almost at the top, I think 98 percentile or something like this, and so very strong performance.

And overall, in Europe and Asia, we see inflows in PIMCO. In the U.S., we still have some adjustments, also in the old core funds. The noncore businesses have already in total inflows overall. So I think we are really developing in the right direction, but it still affects negatively our operating profit and our revenues.

So in the revenue, Page 29, it is more pronounced than on the AUM page. PIMCO in revenues, 10% down. Yes, Allianz Global Investors, a very strong 20% up, but the number is still too small to compensate fully for the reduction at PIMCO, but I think overall, in a very good development. To be fair, the PIMCO number is helped by the dollar in the minus 10% and the minus 27% when we adjust for foreign currency.

So when we now look at the waterfall for the operating profit. Yes, operating profit in the segment Asset Management is down to EUR 500 million from EUR 676 million the year before. That is 37% down corrected for currency or 25% down when I allow for the appreciation of the dollar. That is driven by a non-corrected expense base at PIMCO. And I said already last time that we are not planning to fix [ph] company, that we keep the management team and the staff in place because business -- portfolio performance and customer service comes first and then the other things come second. But I think we are now also prepared to work hard on our cost income ratio, and we believe we can get it back to a 60%

level at the end of the year. And then we have to work even harder next year to get it also below the 60% mark.

And that allows me already to come to the last 2 pages. The corporate segment is more or less unchanged, a little improvement in the banking sector. The holding and treasury segment shows a small worsening. But that is mainly driven by higher expenses for all the employee pensions, which we have in Germany because they are all booked under the corporate segment. And here, we are, of course, suffering from the low-yield environment. Actually, the quarterly booking is up EUR 47 million. That means the rest, we have reduced some expenses, in particular for internal loans, as our cash flows are really running very highly and the cash flows to the corporate center are at record positions.

And now let me summarize the results from EUR 2.8 billion operating profit to EUR 2 billion shareholders' net income. Yes, realized gains are up. On one hand, we realized equity gains of about half of the number and the other half is active management of our debt portfolios. And please be reminded that this other position in our P&C portfolio and our corporate segments. And end of the first quarter -- I think compared to the end of the first quarter, we have maybe realized about 1% of our unrealized gains in the 2 segments or a little bit more. So that is a tiny portion when you do active management. Otherwise, you have really to sit on all your papers until the end of maturity, which is hard to do on equities. So at some point, you need to trade and adjust to what you believe is the right outlook for a paper.

The equity realizations were all in areas where they were tax rate. So we have picked the places wisely, and that supported then the reduction of the effective tax rate, so that the savings and the tax rate are all linked to our realized gains.

So in total, another very strong quarter. Operating outlook up at the other end, so 4% up over the year; and our shareholders' net income, 15% up or 30% for the half year. And I think we have a really good capital position and balance sheet to accompany the future direction of Allianz.
And with this one, I stop here, and I'm curious to learn about your questions.

Question and Answer

Operator

[Operator Instructions] We'll now just take our first question from Farooq Hanif of Citigroup.

Farooq Hanif
Citigroup Inc, Research Division

My first question is going back to German Life business. Do you think BaFin will still stop your competitors paying dividends if they take transitional rules or stop them growing? And do you see a source of competitive advantage in your not taking transitionals? Or do you think this is going to be ironed out? That's question 1. And the second question is going into your Fireman’s Fund. You also made a massive reserve increase. You're joining it up with AGCS. I just wanted to get a feel for what you think is left? And so if you didn't have this reserve increase, is the underlying profitability still pretty poor there? And what's the trajectory for fixing this problem once and for all?

Dieter F. Wemmer
CFO & Member of Management Board

Okay, thank you. Yes, let me start with this Fireman’s Fund. That is obviously the easier question. The other one I have still to think what is the politically correct answer. So Fireman’s Fund, the EUR 134 million additional reserves has to be split in 3 categories, and all are actually linked to businesses, which we are not actively doing anymore. We had an external review of our workers' comp and construction business reserve. There was a very small increase compared to the work we have done internally. And as we are transferring the business to our -- to a reinsurance subsidiary, which is manning the -- managing the run-off called San Francisco Re, the regulator has asked us to transfer the reserves exactly at the amount of the external review. Therefore, we increased the reserves there slightly. Otherwise, we would have not done it because the 2 reviews [ph], the internal and external, are too close. The second part is that we increased slightly the unallocated loss adjustment expenses. Our colleagues at AGCS felt that this was needed, so we supported this. And the biggest point of the EUR 134 million, almost EUR 90 million or EUR 100 million out of it, is linked to professional liability for law firms. That is a line of business Fireman's Fund enjoyed for some years, which was already shut down some years ago. And these are, in the end, excess policies, which have a very late reporting. And this development, you have to face from time to time. That is not a correction of how well is your actuarial process. That is also, to some extent, random pop-up of large losses, which were not known before. So from this one, we feel that we also, in this point, have reduced the likelihood of further pop-ups of surprises. But that would be really naïve to say, you know this for 100% or for sure. But we have certainly taken here a big step. On all the other, I say, "normal lines and contingent lines," we have not seen any reserve movements. We are not yet at an underwriting profit in the commercial business in the U.S. because we have now put up a lot of restructuring costs. We have also reduced already some expenses. But the expense restructuring, that will still take some time and that is still the key element to make this business profitable. So the German Life business, on the transitional. Look, I think as we are always seeing ourselves as a very conservative standard on our balance sheet management, the goal for transitional would be a very strange decision and, for me, a clear sign of weakness, which we don't have. Above 300% at Q2 2015 was a 10-year German government bond somewhere at 70 basis points. That is a very, very strong solvency ratio for a large German Life business. And we're talking here about on in-force business, 20% market share; on new business, close to 30% market share. So therefore, I think we are representing really a very strong dividend. And what BaFin, is doing with the one who have applied for transitional, whether there are certain restrictions on dividend payments or restrictions on growing the business or policyholder sharing, I don't know. That is a question you better ask to BaFin. Sorry for this, a bit evading the answer.

Operator

Our next question comes from Thomas Seidl of Bernstein.

Thomas Seidl

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

First question on PIMCO, close, still negative, but I think I understood, you expected to be a level in Q3 revenue margin down to 42 bps because of a mix away from mutuals and certainly cost income ratio should not be rising. You mentioned you're going to act to bring it down below 60%. If you fast-forward yourself 12 months, can you give us an indication on all those 3 dimensions, where you expect PIMCO to be in 12 months' time? That's my first question. And secondly, capital, as you outlined, very clearly strongly up and even [indiscernible] is above 200. And you have in addition, as you outlined, of course, contingency plan. So my question is what keeps you from a modest capital action in the order of 10% of a EUR 3 billion now?

Dieter F. Wemmer
CFO & Member of Management Board

I think as you have seen, we are really in a very good capital position. I think nothing is keeping us. As I said, we are really prepared for supporting Oliver Bäte's decision in the next quarter with the balance sheet. So that is certainly not stopping us to renew the company. And for the PIMCO question, that is a more difficult one. I can -- I have certainly a dream how PIMCO should look like in 12 months. But sometimes dreams are coming true, sometimes not. The 60% cost income ratio or slightly below, that has to be certainly our target because the measurement of success is -- at PIMCO that we can just follow on the success we had in the past years. And as I said, clearly, we are not satisfied to be a smaller company. So that is absolutely not our plan, and PIMCO has to come back. By the way, the fee income margin in Q2 has really stabilized. That is very much the same as in Q1. So we are not seeing further movements on the fee margin. And then PIMCO has to create new products and they are working on it. We are not yet disclosing future plans. I think it is much better to speak about it when they have -- when they are starting to realize and when you can see it in the numbers.

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

On the capital, did I get it right? So do you -- you are basically at the moment just holding back until we know what's coming out of the strategic review?

Dieter F. Wemmer
CFO & Member of Management Board

Look, I think we have our strong dividend policy in place. You should remember this, that it is a 50% payout ratio. We have another 20% per year tucked away for M&A. So -- and if we don't do the M&A, then we would pay it out. And I heard from some of your colleagues after the Q1, everybody got nervous whether we would be able to pay the dividend and stick to our policy. I never questioned it, but some of your colleagues questioned it. And I think we can clearly stick to it. And with the net income, which is also developing in the right direction, I think everybody should be happy. So there's a piece in it for everybody.

Operator

We will now take our next question from Paul De'Ath for RBC.

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

Couple of questions. Firstly, on the U.S. Life business and the proposals by the Department of Labor. And I appreciate mainly variable annuities will be impacted by this. But just if you could give any color as to whether or not the fixed -- or the FLAAs [ph] you're selling are impacted in any way by the proposals. And then the second point is on the new product that you've designed in Germany and the KomfortDynamik. And is that a new product, as in, no one else in the market is doing that? And do you think that you're going to be able to replicate the Perspektiva success with that product in Germany?

Dieter F. Wemmer
CFO & Member of Management Board

Yes, that is a very good question. I should have mentioned it myself. So actually, thank you very much for the question. Let's start with the U.S. and the DOL. So in the end, the proposal of the DOL says when you sell a savings product to the customer, ensure that the customer is really getting benefits and that the value for money is sufficient. And I think the fixed index annuity business is doing this and is in actually easier position also to demonstrate this than variable annuity business. And you will hear from variable annuity producers that they're also delivering value for the customer. But actually to demonstrate it because the product is technically much more complicated is more difficult to do. The fixed index annuity products are much more straight and also slightly lower in the commission schedules. So therefore, I'm not concerned about it. We would even dare to say that it will increase the markets for fixed index annuity business midterm to long run. And that is all with caveats because the DOL proposal is a proposal which goes now through many vetting periods. And what will be the final outcome, let's see and wait. And when there is a change in government in between, then the whole thing might be completely different. So that is -- therefore, we are not making any warnings about sales volumes based on this. So now the German product. Yes, the KomfortDynamik is certainly even a step further than Perspektiva. And maybe I should have explained this in our changed -- new business mix strategy. Most of the Life companies are telling you it's all about biometric risk and unit linked, and that is the only solution for the world. We are strongly believing that this is absolutely insufficient to keep the separate status of the Life Insurance industry from the Asset Management industry. And the missing third pillar in the Life strategy is, for us, the business which we call business with alternative guarantees. Actually, internal, we call them capital efficient alternative guarantees. That's our products which are offering a guarantee to the customer. But a guarantee, which is clearly matchable, plus they offer the customer upside from investing in real assets but managed by us and not managed by a customer decision what unit-linked fund I'm picking. So therefore, the customer gets the comfort of the high-quality investment management, plus a small guarantee but a manageable guarantee. And Perspektiva has roughly a 0.4% guarantee, let's say, on average for 20 years instead of the classical products in the German market, which are still at 1.25% guarantee and guarantees including the annuity phase of 60, 70 years. When you compare the products, Perspektiva product consumes 30% of service capital under Solvency II of the classical product. So you save 70% in the risk capital for in the end debt boat [ph] because putting capital behind asset liability mismatches, nobody is earning anything. And this allows us actually to put more money in real assets than our competitors. And that is a real competitive advantage we are having. And now the KomfortDynamik, a new product, is coming on top because the guaranteed part goes, so to speak, in Perspektiva, to put it simple, and that is, at the moment, 70% of the money. And the remaining 30% is then a unit-linked fund picked by the customer, so you can go fully into equities, and you have 70% more or less guarantees with benefiting from the strong general account returns of Allianz label. And so the remaining 30%, you could have the full benefit but also the full risk of the capital markets. And I think with this mixture, we are positioning the Life business and the service provided by a life insurance company a bit stronger than just being a copycat of an asset management distribute.

Operator

Our next question comes from Michael Huttner of JPMorgan.

Michael Igor Huttner
JP Morgan Chase & Co, Research Division

But on the cash flow, you said it's at a record level at the corporate center. And I just wondered if you could give some figures. It's always enough [ph] to dream a bit on dividend. And then a similar kind of question. So now the EUR 10.8 billion, you have a fair idea of gains and tax, whatever, for the remainder of the year. How should we think about what it would translate out of net income? The question is, of course, really what the dividend could be.

Dieter F. Wemmer
CFO & Member of Management Board

Well, as we are not taking the decisions on the realized gains to manage results, it's mainly active portfolio management. Therefore, it's, for me, hard to say what would be the final outcome for the year. It depends also when you see that a stock needs urgent selling because the fundamentals of the company have changed. You realize a gain or a loss without asking whether it fits your November or December planning process. As you know, I'm always a conservative guy. Therefore, I would probably not just double the number for the year. But I think we will, for sure, end up in a good single-digit growth of the [indiscernible] income. So -- and the cash flows, well, I will only want to reconfirm to you that all our subsidiaries are paying dividends, that they are actually paying all the dividends we put in the plan for them. And some have even delivered a little bit more. And our restructuring of the group which allows to lift excess capital is also exactly on plan, this execution. Therefore, paying the dividend from a liquidity point of view is not the question. That is because you are always concerned about do you have some liquidity?

Michael Igor Huttner
JP Morgan Chase & Co, Research Division

No, no. I was thinking there was -- there'd be upside...

Dieter F. Wemmer
CFO & Member of Management Board

That is clearly there. If I would tell you the number that would only be seen as a teaser, and then I think I could only disappoint you afterwards with what out of it is being paid out.

Operator

Our next question today comes from William Hawkins of KBW.

William Hawkins
Keefe, Bruyette & Woods Limited, Research Division

Yes, the 86% excellent combined ratio in Germany, can you let us know roughly how you'd normalize that? Obviously, NatCats are being very light. I'm not sure about reserve development. And can you just tell us a bit about the future? Because one of your major peers is talking more concerningly about motor TPL claims inflation. Munich Re was on the record yesterday saying that July was terrible weather in Germany. I'm sorry about that. So if you could just let us know sort of what you think about the second half for Germany and going into next year. Presumably, it would be remarkable to maintain 86%. And then your EUR 1.2 billion M&A budget for this year, are we still roughly at that level? I'm just trying to -- presumably, we're roughly at that level. I'm wondering if Fireman's has taken it up a bit. But I don't know how you've treated the reserve strengthening and I'm not sure if there's been other small stuff going on behind the scenes. So where are we in terms of how much of your budget you've used up this year?

Dieter F. Wemmer
CFO & Member of Management Board

Well, thank you very much for the question. Indeed, the 86% translates probably in the normalized somewhere between 80% -- 90% and 91%, not 80%, would be really great [ph]. But we have still a substantial net cutbacks in Germany for the rest of the year. And I think July is not cutting too much into it, at least I have not heard anything about it. And actually, our German CFO is sitting opposite of me. And he means if it's really bad, then it would have consumed EUR 80 million [indiscernible] Which would already be a conservative estimate. So not something which is taking and changing any management decision. The M&A budget...

William Hawkins
Keefe, Bruyette & Woods Limited, Research Division

I'm sorry, if I can just come back. There's no concern on your side about motor claims inflation?

Dieter F. Wemmer
CFO & Member of Management Board

No, no. I must say I'm not aware of it. And in general, this modernization of the fleet in the market, you still see a general trend to reduce heavy bodily injuries. So therefore, I'm not sure really what we are talking about. And the M&A budget, yes, we had some tiny acquisitions this year. But it's a positive from the Fireman's Fund disposal. So I think the EUR 1.2 billion is still fully intact, not being used so far. And it's not at a Swiss [ph] bank, so don't worry.

Operator

Our next question today comes from Thomas Jacquet of Exane.

Thomas Jacquet
Exane BNP Paribas, Research Division

I have only one question, it's on Turkey. You achieved a 2-digit combined ratio, which is probably the -- you're probably the only company in the sector to achieve that in Q2. Have you seen, like, your peers an increase in the Motor TPL claims? Or is it -- is there something in your business model that is different?

Dieter F. Wemmer
CFO & Member of Management Board

No. You are fully right with your question. Motor TPL is clearly up, but we have also increased the prices, and we have started maybe a little bit earlier than the rest to raise prices. We have also after we have seen that inflation, and the court decisions on larger cases were against the insurance industry. We have actually also increased our reserving level in Q2 slightly after a review done by our central actuarial team. So Turkey is a market -- as it a young market, you have to watch. But as far as we can see, it's also our -- the largest competitors are now starting to increase rates very sharply. And we believe we are doing our rate increases more selective because our [indiscernible] is more diversified. Still, remember from the history that actually we could export it in a very early phase our motor tariff knowledge from Italy to Turkey. And since then, we have really continued to develop the tariff in the local circumstances. And the technical team in Turkey is maybe still a little bit behind the Italian colleagues, but pretty close in their professionalism and that really pays off. I'm an absolute believer. We see the same in Greece. It is a very difficult market. But also second quarter, our small portfolio increase was in the mid-80s in the combined ratio and that in a horrible economic environment, but actually, high-quality pricing is still a competitive advantage. And that allows also Allianz to run an underwriting results which is, every quarter, better than most of our peers.

Operator

Our next question today comes from Peter Eliot of Berenberg.

Peter Eliot
Berenberg, Research Division

The first one was on the -- just puts high level on the Life underlying results. I mean if I take your comments, Dieter, it sort of sounded almost like one can sort of add back the interest rate impact, and if one adjusted for career as well then one is looking at a sort of run rate of around EUR 1 billion per quarter, which I guess is clearly above your full year target. I was just wondering if you could comment perhaps on there, that could take quite an optimistic interpretation, but I was wondering if you could just comment on that perhaps? And I was just going to ask as well, given the various comments you've made on the growth budgets and building those again, maybe optimistic, but I'm just wondering if you can share anything on how you view the M&A environment as developing at the moment?

Dieter F. Wemmer
CFO & Member of Management Board

Yes. Thank you, Peter. I am both waiting for the M&A question. It took more than 35 minutes for it. So, that's a pretty long time. So Life results, as I indicated, I would like to look at the half year results. And in the EUR 2 billion, I probably would still take out EUR 100 million from the half year. Yes, you can see, Korea is a one-off. But we also know that in the yield environment that there might be also, in future, we are reaching more break points until we are there for the number that might be necessary still from time to time to put more money into it. Therefore, I personally like to take the 1.9 as well earned and then use it for the future. It depends almost a bit also what we are doing on the investment side. There is some volatility in it, and it is a big portfolio. And in the end, it is about creating long-term value, therefore, we cannot, every quarter, deliver the accounting results because sometimes the accounting works not in favor with the long-term decisions. And that allows me, actually, to make a little advertising. When we move to IFRS 9 for the insurance industry, faster than IFRS 4 Phase II, we will spend every quarter another 10 minutes on explaining the movement of the financial assets versus the liabilities and why the numbers are one-off and not one-offs. The whole story will get even more complicated, that I promise to you. But if you reserve 10 minutes more for each call you do in the quarter with each of our peers, then it's fine with me, but don't complain afterwards.

The M&A environment. The smaller assets are all very highly priced. So you see high earnings multiples people are expecting, well, even on some of the bigger deals. So you have really to think through very well what is your strategic move as an acquisition. Does it really close a strategic gap? Is it worthwhile to pay a high multiple in this situation, or is it just a simple add-on acquisition to help you with your scale and profitability? Then I think you are more limited in paying a strategic premiums. And therefore, you have to watch the situations fairly closely. Opportunities coming up is less easy. We have seen actually in various private equity deals we did more on the investment portfolio, but in the end, they are following the same logic as M&A in the insurance industry. There, we have seen that we could actually get to better outcomes. And the competition was more rational than actually in the insurance space where people are probably desperate because they don't find anything to acquire. And you have really to watch out how you want to play it. In the end, it is about making money and returns and not just showing some shiny deals.

Operator

Our next question comes from Jon Hocking of Morgan Stanley.

Jonathan Michael Hocking
Morgan Stanley, Research Division

Got 3 questions please. On Italy, on the P&C side, it's a very strong combined ratio in the quarter, but the rate movement looks quite weak. I just wondered what the outlook is there. Are you looking at taking down policy counts and how sustainable is that combined ratio number? That's the first question. Second question, I wondered whether you could comment on the press articles in the week, talking about the Wells notice which PIMCO's received. And then finally, just on the point you're making, Dieter, about the very strong capitalization in the German Life business and the volatility that feeds through. It's a great ratio. Given there's no sort of real burn-through risk here, I just wondered if you could sort of comment on the -- to what extent that's introduced the group volatility we've seen in the last few quarters, and whether it might be useful breaking that out given it's actually something which is fairly ring fenced?

Dieter F. Wemmer
CFO & Member of Management Board

Yes, Jon, that is a very good suggestion. I'm also thinking about to break it out. I would suggest we wait now until we have finalized our IMAP approval process. One of our German competitors got already their approval but they have a much simpler supervisory college and not having 12 supervisors debating the pros and cons of every feature of the model. So we probably still have to wait a number of months before we are through everything. And then we should certainly consider to break it out because I'm absolutely not nervous about the volatility of the German Life business. And the burns always -- well, look, a reinvestment rate of 0.8% is still enough. So I'm not sure how negative the euro spot curve has to go before it really burns fully through. But we will work on it after we have the approval and can really separate out all the numbers correctly.

Italy. In Italy, policy count is still growing, but only just slightly. The main growth is still in our direct business where we have also in premium, plus 5%. But the tariffs are down. The whole market is competing very strongly because all setting [ph] on a positive combined ratio. And that allows still the market to reduce rate, which then translate into falling total premium for the Italian P&C market. In Q1, we were with our shrinking, still growing market share, I think the market was 1 or 1.5 points more shrinking. For Q2, I have not yet seen market figures. But when I just compare ourselves to one of the large Italian peers, it shows that our Italian volume is still holding up slightly better.

So the Wells notice. Well, I think all the -- one of you are familiar with the processes at the SEC. It is recommendation of the working group to the commissioner level to follow-up on it. So it is not yet an action against PIMCO. The Wells notice is referring to the smaller brother of the Total Return Fund. That is a lift, that's ETF at the New York Stock exchange. It has, at the moment, $2.5 billion money under management. And it is a discussion what got criticized. It is about the disclosures in a specific phase in 2012, I think referring to 3 or 4 reporting months. Actually, no harm done to any customers or customers got their full money and values. So therefore, it looks to me from the current understanding, a very formal discussion. And we take it with respect because in any dealing with the SEC, we are very respectful what they are saying, but it's not alarming from a content point of view.

Operator

Our next question comes from William Elderkin of Goldman Sachs.

William Elderkin
Goldman Sachs Group Inc., Research Division

One on PIMCO and one on U.S. Life. Did I hear correctly in your speech that you said overall PIMCO outflows in July was EUR 3 billion. And I'm just wondering if I heard you correctly. Did that imply outflows on the portfolio, excluding the Total Return Fund, which I think has already given a figure for July with just EUR 1 million -- EUR 1 billion, rather. I may have misheard you. But it seems to be a dramatic improvement on the situation over the last 6 months or so. And then second question was just on the U.S. Life. The operating profit was EUR 2 97 million in the quarter. I just wondered, are there any unusual features in that? Is that number really sustainable?

Dieter F. Wemmer
CFO & Member of Management Board

I think there is on one hand, of course, the dollar translation helps out with our U.S. Life business. Then we have preserved the margin on reserve. And compared to a year ago, the whole balance sheet has a -- really had a nice growth, so that is very sustainable movement. Then we had some, I think, positive on hedging results on the BA [ph] book. And maybe in the year before, there were some negative. So some part is also derivative-driven, but not a lot. So the PIMCO number, it's around EUR 3 billion, I was referring to. It's total net outflow of the company. I did not highlight any specific funds, that is the total. And yes, everybody always looks at this Total Return Fund disclosure. I'm not sure, but I would remember that it was almost $3 billion stand-alone. So that tells you that actually the non-core parts of PIMCO are really doing fine.

William Elderkin
Goldman Sachs Group Inc., Research Division

Well, but that's why I asked the question. Because, I mean, it seems to be close to mutual on, by far, the largest parts of the assets under management.

Dieter F. Wemmer
CFO & Member of Management Board

I can also tell you that out of the 22 trading days in July, 10 were positive. It's already going in the right direction.

William Elderkin
Goldman Sachs Group Inc., Research Division

Yes, I mean I appreciate it's only 1 month. But is there anything sort of structural change in terms of having had very significant institutional outflows working their way through? Is the future sort of a little bit more positive in that respect, for example?

Dieter F. Wemmer
CFO & Member of Management Board

I think, overall, a very good performance. Look, even the -- lastly, criticized Total Return Fund got back its five-star Morningstar rating just this week. The year-to-date performance of the Total Return Fund is at 96 percentile or something like this. So the team is really doing an outstanding job. Because a fund, which has so large outflows and still showing performance, really, a very strong performance compared to more stable funds. That is a fantastic investment performance of the team. I really like what they are doing, and we should not forget this.

Operator

Our next question comes from Nick Holmes of Société Générale.

Nick Holmes
Societe Generale Cross Asset Research

I had just a couple of follow-ups on Life. Coming back to German Life. I fully understand what you're saying about the strength of the business, the value of the RSP [ph], but I just wanted to come back on Jon's question about the quantification of the sensitivity within the Solvency -- the group Solvency II ratio. I mean, can you, for example, tell us what proportion of your -- it's a 9-percentage-point movement, I think, for 50 basis points approximately in the group ratio. Are you saying, Dieter, that the German Life business does not contribute to that at all? Or are you saying that there is some contribution, but it's actually pretty small. That's the first question. And the second question is just coming back on Korean Life. I know that you've got a history of strengthening reserves here. And I wondered, could you just tell us a bit more about your methodology and your reserve strength? I mean, you're signaling that it's not the end of the story in Korea, dependent on what interest rates, et cetera, do. I mean, could you give us any kind of guidance on what we might expect. Because it was a pretty big charge, wasn't it, in Q2? And in 2014, you also had a pretty big charge for Korea.

Dieter F. Wemmer
CFO & Member of Management Board

Yes, Nick, thank you for asking. Now with the German Life business, I wanted to express more the opposite of sensitivity. The German Life business has an over proportional impact on our interest rate sensitivity. But as it is encapsulated, it is, anyway, actually not creating any capital action for the group. Therefore, maybe our total sensitivity appears bigger than it is really an impact. And from the 9% sensitivity, I would say probably slightly more than half is the German Life business. But it doesn't matter as it fluctuates in itself. And we will not inject capital, we will not take out capital, we just take the dividend and we grow the business. So that is -- therefore, actually, there is, from my perspective, too much focus on the sensitivity. But we are not standing still. We will also, in the future, reduce the sensitivity further. There are 2 elements which will, midterm, reduce the sensitivity in our Germany Life business. That is on one hand, our new business mix. But that is a slow process as you actually need to add a couple of years of new business mix before you really have the overwhelming effect of the business enforced [ph] under control. And the second thing is an activity of the German regulator, which is called ZZR. That is building up these additional reserves to reduce the average guarantee rate. And the ZZR will be from next year on, at the lower or -- let's say, the required interest rate will next year be lower than at the moment our average guarantee. That means it will help accelerating to get the average guarantee down, and that will take interest rate sensitivity further out. If you project the whole thing 10 years forward, and we have recently done it and have said, "Look, what would happen when we have a Japanese scenario?" We have used the April 1 interest rates and said, "Let's continue with this for 10 years." Then our solvency ratio will actually grow over time, which is maybe counterintuitive for most of you. But it is happening because it is a new business mix. And so ZZR effect will therefore be very relaxed about the sustainability of our German Life balance sheet. And that's really an important information, therefore, I'm spending so much time on it because I have read so many disorientated analysis over the last weeks and months. And I'm really fighting back now much stronger. So Korean Life...

Nick Holmes
Societe Generale Cross Asset Research

Sorry, Dieter, can I just very quickly follow-up because it's obviously a very complicated area. So the first point you were making is that you don't see any possibility for German Life to be ring fenced, separated out from the group solvency ratio? And sorry, before you answer that question, can I just ask, coming back really to Farooq's questions on transitionals. If that's the case, if German Life cannot be segregated out, why is it that you're not interested in transitional arrangements? I mean, it's something that the U.K. insurers are doing for their troublesome annuity books. Surely, transitionals would be quite an effective method of just ring fencing your German Life business?

Dieter F. Wemmer
CFO & Member of Management Board

Yes. Well, I think the decision on transitionals, it's a question how many digits does your solvency ratio have? Well, you have a 30% solvency ratio, then I would go for a transitional. If it's above 300%, and we have not disclosed the absolute number, we are only indicating it's bigger than 300%, I wouldn't see the reason for transitional. And why should we take any risk that we have to agree on a recapitalization plan with the regulator, because that is what transitional says. Transitional says file a plan with the regulator, how you recapitalize your business until the end of the transition period. That is very simple, the meaning of the word transitional. But at 300%, what plan should we file, saying we have too much capital, and we will dividend it out?

Nick Holmes
Societe Generale Cross Asset Research

Yes. No, that's very clear.

Dieter F. Wemmer
CFO & Member of Management Board

So the Korean life, is indeed a prescribed methodology. That is the loss of adequacy tests under the U.S. GAAP rules that is a very formulaic process without any leeway to interpret it left or right. You just apply the formula, and you look what is the outcome of the formula and then you book the difference or not. And that is just a test which is projecting the current investment income with future reinvestment rates. It is an averaging of the interest rates over 16 quarters of rolling -- averaging, and then you compare it with the discount rate you have in reserve and that is more or less the test. And therefore, I think we will see more additions in Korea. It depends a bit on the market development, and that is very sensitive where the markets are 50 basis points up or lower. But I would also expect that we would see some more of reserving in the future. It is not something which I think will damage our overall great profitability of the Life segment. And Nick, I have some additional information for you. The court in the U.S. dismissed our last open class action in Minneapolis. You are always asking about the status of our class action. So the last one got dismissed by the court without payment by us.

Nick Holmes
Societe Generale Cross Asset Research

Well, congratulations. Just a very quick follow-up, Dieter, on the Korean Life. Is there not a temptation to make an additional prudential reserve though for Korea, so that it stops appearing constantly in each quarter or every few quarters?

Dieter F. Wemmer
CFO & Member of Management Board

Look, my natural instinct would fully agree with you, and I would like to do this. But somebody needs to rewrite the formula for U.S. GAAP. And either we stick to what we disclose as our accounting principle or not. We cannot have it both ways. I said you are -- we are not on French GAAP. There you have more flexibility.

Operator

Your next question comes from Andrew Ritchie of Autonomous.

Andrew James Ritchie
Autonomous Research LLP

I just have 1 question really, Dieter. In the comments in the slides, you refer to looking at the attritional loss ratio, so the ex cap loss ratio. You refer to lower large losses, but on the other hand, some higher frequency effects. Could you quantify those numbers? And maybe just on frequency. There's a specific reference for higher frequency in PPL in Italy? Are you seeing any frequency upticks in any other markets?

Dieter F. Wemmer
CFO & Member of Management Board

It's Italy, and then probably a little bit U.K., where we have a small portfolio. I think also Australia, we have seen a slightly higher frequency. But overall, the attritional loss ratio, it's very close to last year's number because the Nat Cat effect, I would take out. We are also still, think, in a very good development here. So for the one who had already seen it peeking some quarters ago, we are very stable. It's the same, our reserving process is also in a very stable situation, where 2Q actually got hit by Fireman’s Fund again, but that is not the first time. So that is the other Korea, at the West Coast, yes. So I assume that we are, in Fireman’s Fund, are more getting to a closure of this evergreen episode, and the running has -- actually, our attritional loss ratio is in the right direction. We are still, I think, are not improving fast enough in Brazil. So that is also included, I think, in the uptick of frequency and in the motor business. So that is still where we have to work on, getting this stuff right.

Andrew James Ritchie
Autonomous Research LLP

And in Germany and France, there's no real frequency trends changing? Is it falling still or...

Dieter F. Wemmer
CFO & Member of Management Board

No, Germany is -- it's slightly down. In particular, we see it on the larger claims. We still see a trend to less larger claims in the motor business.

Andrew James Ritchie
Autonomous Research LLP

Okay. But the other question I have actually, your colleague, Mr. Bäte, laid out some of his new strategy this morning. And he's talking about that we will learn more about those initiatives at the end of November. I mean, do you anticipate any major restructuring costs in the second half of the year or is all of what he's laying out very much sort of business as usual?

Dieter F. Wemmer
CFO & Member of Management Board

Well, we did not answer this question this morning, and the answer should not depend on the audience of the call. Therefore, we not answering it. But very fairly, to also give you the rationale, it is much too early to do so, and it is more important that we get now the strategy work out. And it's very much about a cultural shift program and really getting the insurance industry much deeper into digitalized processes. That does not mean that we are all becoming fancy, but I think all the normal processes can be very much digitalized. And we have so great tools. We have, as we put on the first page, this new tool in Germany where automated camera system actually calculates hail damage. We have, with another claims solution provider, developed an app where you can actually -- little damages in your car, you can take a photo and it calculates the claims amount, and we can settle immediately without human interaction. That would be the midterm solution after a testing period. So there are so many things where our industry can really enhance base services. Or that our -- in international health business, allows you to take a photo of your smartphone integrated in the app, and then the billing and settlement process of the health bills is automated. So that are all the little improvements where we have yet even more in the 21st century. And I believe that our industry is still a bit reluctant to go with this full step, and that is the shift we are really pushing forward. There will be some investments, but there will be also savings. When I still look at our annual bills for printing and mailing, that is a substantial amount. I think we are printing, in Germany, 100 million pieces a year. That is a real forest which we're seeing running through the printers.

Operator

Our next question comes from Frank Kopfinger of Commerzbank.

Frank Kopfinger
Commerzbank AG, Research Division

I have 2 questions. My first question is on your Life reinvestment yield. You show a significant increase to 2.8% in Q2 from 2.2% in Q1. What were the drivers behind this, simply the rise in interest rates because you don't see or you don't show the same expense on the P&C side? Certainly, this is also on a lower duration, but I was wondering what the drivers were in the 2.8%? Then on German Life, with your 300% Solvency II ratio that you clearly show a strong situation, but I'm wondering how you see the whole sector because this is certainly not representative for the entire sector. And certainly not for the average local peer, I would say. So how do you see this sector, and how do you see or whether you fear a negative spillover effect for your group?

Dieter F. Wemmer
CFO & Member of Management Board

Two very good questions. The life reinvestment yield, as we are investing really long in the Life segment, and when you see that the 20-year euro spot curve moved to 92 basis point up, plus we have seen additionally, actually, a lift in credit spreads slightly in the second quarter, so the 60 basis points up is actually not a surprising number. You could almost say it is a lower increase than you would have expected from the market data, but that is always a bit the mix. And we have -- I think we had in the second quarter also more investments, U.S. investments, therefore, that is also an important driver. And the 2.8, as I mentioned already in my explanation, that is also a share of emerging-market bonds where we hedged the currency depending on the risk capacity. Yes, I agree that our results for the Solvency ratio in the German market is not reflective of the average, and actually, I hope so, that it's substantially better. But then the average would -- I therefore conclude that I'm in panic over the German market -- no, because we are not the only well-managed company, but we are clearly the market leader, which has also a clear scale advantage. Because our cost advantage allows us actually a much cheaper refinancing of the guarantees than the rest because the other companies needs more investment return to pay for their expense levels. And that is, I think, the advantage, and therefore what we want to offer the customer, more investments in real assets. And maybe the one-off you who have followed the press, we have done a large investment in both the fuel stations and restaurants at German motorways because that is one large umbrella company we're running for 300 places. And we have participated in a group here who has acquired 100% of it. We have done other investments in the U.K. There is a new wastewater tunnel under the Thames, which is a large public/private enterprise investment. So I think that allows us to really -- to derive better than the rest of the industry. But we are also not concerned that we have to bail out too many competitors, if this is was the question. I think the bailing out in Germany is a well-organized process, which makes it also even, for the rest of the industry, very absorbable. And I'm not expecting that we have to bail out over the next years many companies. Was the core of the question.

Operator

We'll take our next question from Vinit Malhotra of Mediobanca.

Vinit Malhotra

Dieter, just one, sort of [indiscernible] question based on the Page 25. Since German Life is so strong in Life, and we also agree with you. So if German Life is so strong, why not push into the classical, traditional products if they're giving you already 20% less ROEs? In a sense, that's where the real competitive advantage lies, don't you think? Because otherwise, everybody wants to sell nontraditional or -- I admit it's a bit off-the-hook question. But it's been a question I've been thinking of many -- for quite some time now. I'm wondering if you could shed some light on that. Also in Germany, the combined ratio. The comment that the [indiscernible] loss ratio is not guided, it's still stable. But I'm assuming it's Y-o-Y. But there have been price increases. Is it just the severity you mentioned, which is eating up some of that price increase? And lastly, just a quick clarification, Brazil -- the presentation mentioned temporary headwinds in the economy. But it sounded a bit more cautious in terms of the pricing cycle in the industrial and motor, as you mentioned, which one's the case? Is it -- are worried about turnaround or are just looking at the sort of temporary slowdown in the turnaround in Brazil?

Dieter F. Wemmer
CFO & Member of Management Board

Vinit, thank you for the question. I think that combined ratio in Germany is probably on a real like-to-like comparison, slightly improving over the year. But it's always tough to measure the large couple of basis points, so therefore, I would still keep it roughly at the same average as last year. And if you get some positive surprises out of it, it's also not bad. In the Life business in Germany, yes, indeed, you are right. We could continue the guarantee business without going into a better situation. But then we cannot put so much risk capital behind our investment strategy. And in the end for mismatch risk, you are not making any return. You are investing capital in something, which is not bearing any interest, and we don't need to do it to gain market share. Our products -- and in the end, we have also, in the long run, also offer our customers returns. When you invest in a classical and you have to go for low-risk investments, then it's easy to calculate what will be your long-term investment yield. And it will be below 2% in today's environment, and who wants to buy this product? I think it is really important that we are also leading the shift to other products in the German market, and I think it is for the whole market. I think for the customer and the industry, the better version when we could help to transition the German Life insurance market to a different product mix, and we don't want to stick to the old roads. And in Germany, we are in a very comfortable position that transitioned to different products that is also needed as a market. And I think we are running here also a group strategy. And do you think our other markets would follow it, when we would say German doesn't need to change? That would be a very strange decision for a group to manage something. Because it is, again, a cultural shift.

Vinit Malhotra

So roll-back would be lower than this 21 then, right?

Dieter F. Wemmer
CFO & Member of Management Board

The roll-back of the new products is substantially better than all the old products. And it is still, even in -- well, also when you have a strong balance sheet, the roll-back is not benefiting from a strong balance sheet when you consume a lot of capital for a product, therefore, you would be with the classical products, you are low double digits with attractive product or a new product generation, you are 20%-plus. But that also means, in translation, when you would stick to the classical products and we go through the Japanese interest rate scenario, you cannot keep the high ROE forever. So Brazil, yes, it was more a statement that we will see a delayed recovery because growth is lower, that means expense is actually faster up. We have a high inflation so that is pushing through, price increases is slower than expected because customers are not in the economic position to follow the price increases. They are then looking for the cheaper solution.

Vinit Malhotra

But the hedge portfolio is in control. This is the model you're talking about, right?

Dieter F. Wemmer
CFO & Member of Management Board

The hedge is, in general, in control, but also a bit suffering from the higher expense flow [ph].

Oliver Schmidt
Head of Investor Relations

All right, so we have to close the call. And we'll say thank you to everybody, and thanks for all your attention. We wish you a very pleasant weekend and hopefully a nice summer break. Goodbye.

Operator

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