Industry situation and competitive environment

Old-age provision

In the past year, the market environment in the old-age provision business continued to be characterised by low interest rates. Following a strong period of sales at the start of 2020, the corona pandemic dampened growth in the German life insurance sector. According to data published by the German Insurance Association (GDV e.V.), the pandemic also shifted the focus of households towards short-term provision and putting long-term provision measures on hold. The corona pandemic also meant that the topic of occupational pension provision was no longer on the radar of company directors and HR managers.

Based on the results of a survey conducted by the German Pension Institute (DIA), some 20% of private individuals surveyed had less disposable income available in March and April 2020 as a result of the corona pandemic. 19% also reduced the amount they pay into their old-age provision investments or even stopped saving altogether for the time being as a way of cutting down their regular expenses.

Support for statutory pension dwindling

The trust of German citizens in the statutory pension system has suffered during the corona pandemic, as highlighted by a survey conducted by HDI Lebensversicherung. Indeed, only around a fifth of those surveyed consider the statutory pension a primary option when it comes to saving towards their old age. Only around 1 in 4 trust private life or pension insurance policies. However, the clear winners here are real estate and investments in the capital markets.

Product landscape undergoing change

The product landscape in the old-age provision business has undergone radical change as a result of the low interest rate environment. The structural realignment also becomes apparent when examining the growth recorded in the individual segments. According to data published by the German Insurance Association (GDV), more than half (58%) of all newly signed old-age provision products are now policies with alternative guarantee models. Based on the most recent figures provided by the German Insurance Association (GDV e.V.), classic life and pension insurance policies with maximum technical interest rates represented just short of one third (30%) of all new contracts concluded. Pure unit-linked policies make up a market share of 12%.

Occupational pension provision suffering due to the pandemic

The corona pandemic has negatively impacted new business in the field of occupational pension provision. The greatest challenges here revolved around the difficulties in accessing clients due to the lack of personal contact and the fact that companies started to consider occupational pension provision a low priority. In addition to this, uncertainty among corporate clients led to reservations in terms of new business.

Downturn in the entire market

Based on current figures provided by the German Insurance Association (GDV e.V.), the corona pandemic led to a significant decline in premium income from life insurance policies in the reporting year (–0.4%) to almost € 103 billion.

Wealth management

In the reporting period, the market environment in wealth management was influenced and correspondingly volatile due to the corona pandemic, yet it was also characterised by rising stock markets, as well as persistently low interest rates. The effects of the corona pandemic represented a significant factor of uncertainty worldwide during the reporting period.

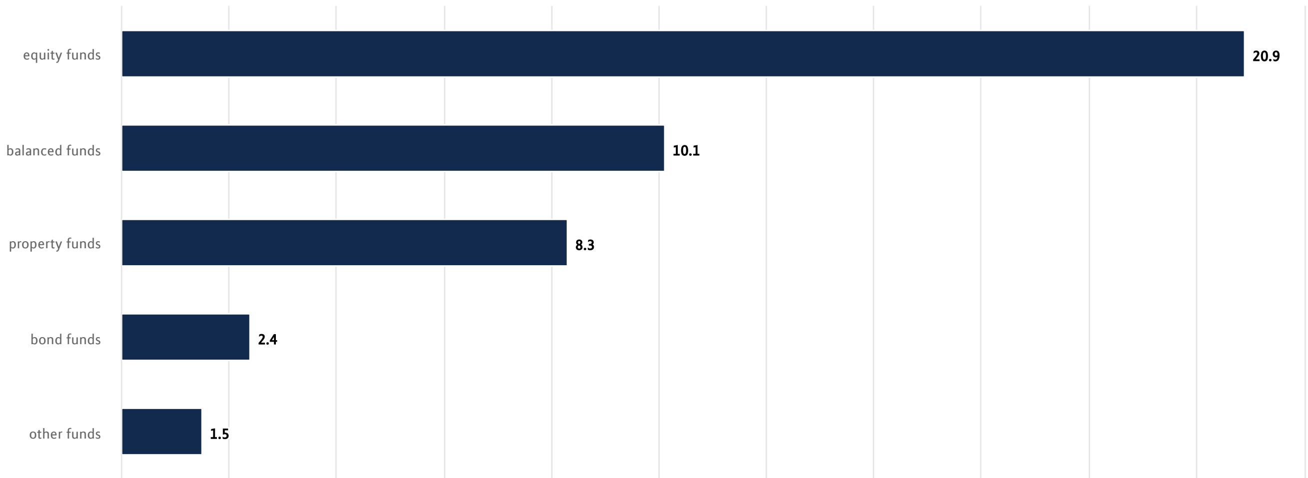
Following a temporary slump at the start of the corona pandemic, private assets in Germany rose to around € 6,738 billion in the third quarter. Monetary assets in the form of cash, securities, bank deposits and claims against insurance companies reached thereby a new all-time high. The transaction-related increase in households' cash and deposits of € 41 billion was strong, but not unusually high compared with previous years. At the same time, households' exposure to the capital market recently experienced a rapid upswing. In the third quarter, private households invested € 20 billion in equities and investment funds, almost three times as much as the average of the past ten years. According to the Global Wealth Report published by Credit Suisse, the number of US Dollars millionaires in Germany also rose by 58,000 to 2.1 million in the first half of 2020.

Private households wealthier than ever before

Based on information provided by the German Association of Investment and Asset Management (BVI e.V.), the total value of assets managed by the German fund industry rose by 13.4% to € 3,850 billion as of 31 December 2020. Around € 127 billion had been channelled into investment funds by the end of December 2020. The main options selected are open special funds with € 79.7 billion in new money and open mutual funds with € 43.2 billion. Closed-end funds secured investment of € 4.5 billion. The sales list of open-end mutual funds in the current year is led by equity funds with € 20.9 billion, followed by balanced funds with € 10.1 billion.

Mixed funds very popular

Cash inflows and outflows in open mutual funds in Germany from January until December 2020 (in € billion)



Source: German Association of Investment and Asset Management e. V. (BVI), Date: 31 December 2020

According to the Wealth Barometer 2020 of the German Savings Bank Association (DSGV), the topic of sustainability is now of appreciable importance for those looking to make investments. As such, almost a third of those surveyed have already considered sustainability, whereby younger investors and those with a higher income are particularly interested in this. According to the industry association BVI, sustainable funds currently manage € 147 billion. MLP has already been offering sustainable funds since 2012.

Increased demand for sustainable investments

The market for providing consulting services and managing the investments of high net-worth individuals, in which the MLP Group is active through FERI, has become more challenging and fiercely contested. According to the European Asset Management Survey 2020, produced by management consultancy zeb, the key challenges for the sector revolve around the advancing market concentration, as well as the dwindling profit margins, despite the overall increase in assets under management. In addition, the continuing low interest rate environment is making clients more price conscious.

Ongoing consolidation in private banking and wealth management

As a result of the ongoing low interest rate environment and the rising risks on the stock markets, institutional investors are showing increasing interest in alternative investments. According to the BAI Alternative Investor Survey 2019, which is performed by the German Association of Alternative Investments (BAI) among institutional investors, 82% of all respondents increased their commitments in this asset class.

Institutional investors strengthen commitment to alternative investments

Non-life insurance

The corona pandemic was also the dominant issue in the business with non-life insurance policies during the reporting year – and put significant strain on the entire sector. Not only did the restrictions in terms of social contact have a dampening effect on business development, the corona pandemic also led to a rapid increase in the digitisation of consulting services in the field of non-life insurance.

Based on estimates of the German Insurance Association (GDV e.V.), the coronavirus pandemic led to a slump in business development and virtual stagnation in premium income in the accident and damages business. Since some of these effects are not likely to be felt until 2021, the GDV is still anticipating an increase in gross premiums of 2.2% for the financial year 2020.

Considerable decline in growth momentum

According to the German Insurance Association (GDV e.V.), various effects could be observed during the corona pandemic. For example, greater use of individual transport was recorded, which could potentially have a positive impact on new business in future, particularly in the field of motor vehicle insurance.

The sector recorded slight growth overall for 2020, even if negative effects could be felt as a result of the coronavirus pandemic. Liability insurance and motor vehicle insurance policies made a particular contribution to the growth recorded. The effects of the coronavirus on the various insurance segments varied in the market.

Growth recorded, particularly in liability and motor vehicle insurance

Health insurance

According to data from the Association of Private Health Insurers (PKV), private health insurers (PHI) were able to reduce their net portfolio loss to a slight minus of 0.1% in the reporting year of 2020. The number of persons holding comprehensive health insurance amounted to 8.7 million.

For the third year in a row, 2020 saw a rise in people switching from statutory health insurance to private health insurance instead of the other way round. According to data published by the industry association, this resulted in an overall increase of 21,400 policy holders in favour of private health insurance (2019 balance: +17,400).

Private health insurance attractive for those willing to make the switch

According to data published by ratings agency Assekurata, only relatively few policy holders made the switch during the corona pandemic due to difficult economic situations. However, the ratings agency anticipates that the field of comprehensive insurance will come under pressure in future as a result of the corona pandemic. The private health insurance sector recorded additional expenditure overall in 2020 due to the impact of corona. This is estimated at over € 1 billion, or almost € 1.4 billion when considering benefits paid. The statutory health insurance funds were also increasingly impacted by the effects of the pandemic, which left deep marks in terms of both income and expenditures. Indeed, the statutory health insurers recorded a deficit of € 1.67 billion in the first three quarters of 2020 and must therefore be subsidised to a greater extent by the federal government.

Corona pandemic putting pressure on both private health insurance and the statutory health insurance system

To close coverage gaps in the statutory health insurance system, more and more patients are signing up for private supplementary insurance policies. According to the most recent surveys performed by the Association of Private Health Insurers, there were around 27.3 million private supplementary insurance policies in place in 2020 – approximately 2.4% more than in the previous year.

Supplementary insurance policies on the rise

The growth recorded in the field of occupational health insurance continued. According to the Association of Private Health Insurers, around 13,500 companies in Germany offered their employees a fully employer-funded occupational health insurance policy in 2020 – this means an increase of 29% compared to the previous year (2019: 10,500 companies). The number of employees who benefit from an occupational health insurance policy increased by 18% to around 1.04 million persons.

Occupational health insurance as a growth driver

Real estate

Despite the corona pandemic, the real estate market in Germany displayed robust development. The demand for residential property rose further and remained consistently high, particularly in major cities.

Based on information provided in a survey undertaken by HDI Lebensversicherung, a slim majority (51%) of those in active employment in Germany are relying on their own home as a way of providing for their old age. One in three respondents stated during the corona pandemic that they now considered it more important to own their own property as a way of providing for their old age. Accordingly, the "Living in Germany 2020" survey performed by the Sparda banks noted that the level of interest, particularly in purchasing a house, has increased markedly.

Price increases not affected by of the pandemic

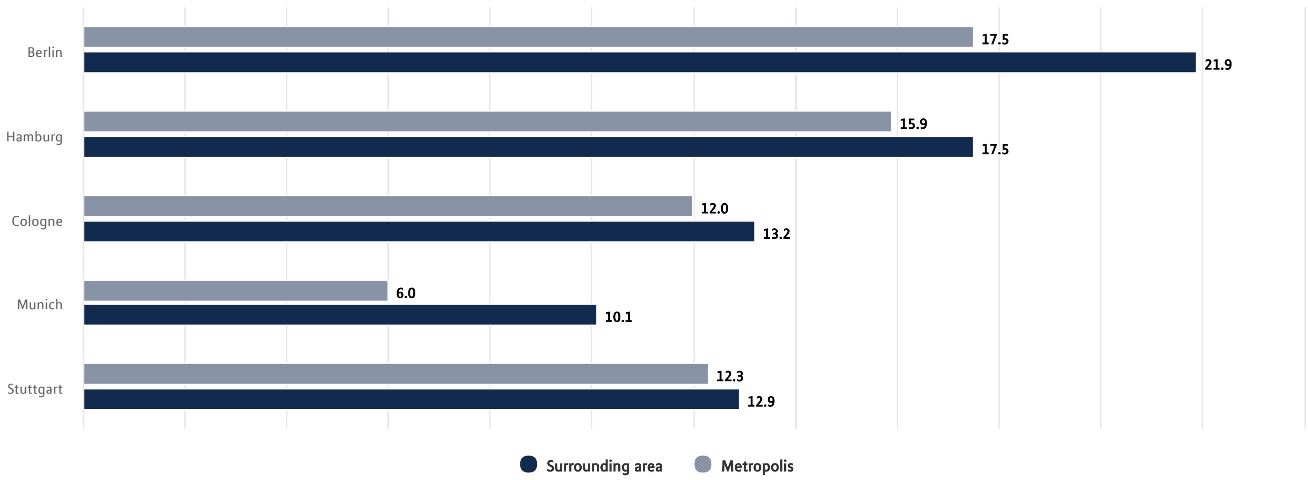
The corona pandemic has not been able to halt the upwards trend in property prices, which has now been holding steady for ten years. The Real Estate Price Index of the Association of German Pfandbrief Banks (vdp) reached a new high in the fourth quarter of 2020 (172.8 points) – having increased by 6.0% since the start of the year.

Prices, particularly for residential properties, continued to rise irrespective of the corona pandemic. Indeed, prices throughout Germany rose by an average of 7.1% between Q3 2019 and Q3 2020 according to the vdp index. The price dynamics for commercial property, on the other hand, came to a standstill. The cultural sector, hotels, as well as the restaurant and retail trades were particularly hard hit by the lockdown and associated movement restrictions during the corona pandemic – with corresponding dampening effects on commercial property prices.

Good investment opportunities in the periphery

In the past, those seeking to buy affordable apartments and houses have generally found what they were looking for on the outskirts of major cities. According to an analysis performed by the Institute of the German Economy (IW), however, apartment prices are also on the up there. Based on the "Living in Germany" survey performed by the Sparda banks, property prices in the areas surrounding most urban centres have seen greater rises in the last few years than the city centre districts themselves. As such, property in these areas remains highly attractive as an investment opportunity.

Increases in the purchase price of an existing condominium from 2017 to 2020



Source: "Living in Germany 2020" survey of the Association of Sparda Banks (VSB e.V.)

Completion of building projects not satisfying demand

According to the Institute of the German Economy (IW), there are no signs of a speculative bubble in the real estate market. Indeed, many cities and districts are still seeing demand outstrip supply. No major city is engaged in sufficient construction work to cover the demand for housing.

Loans and mortgages

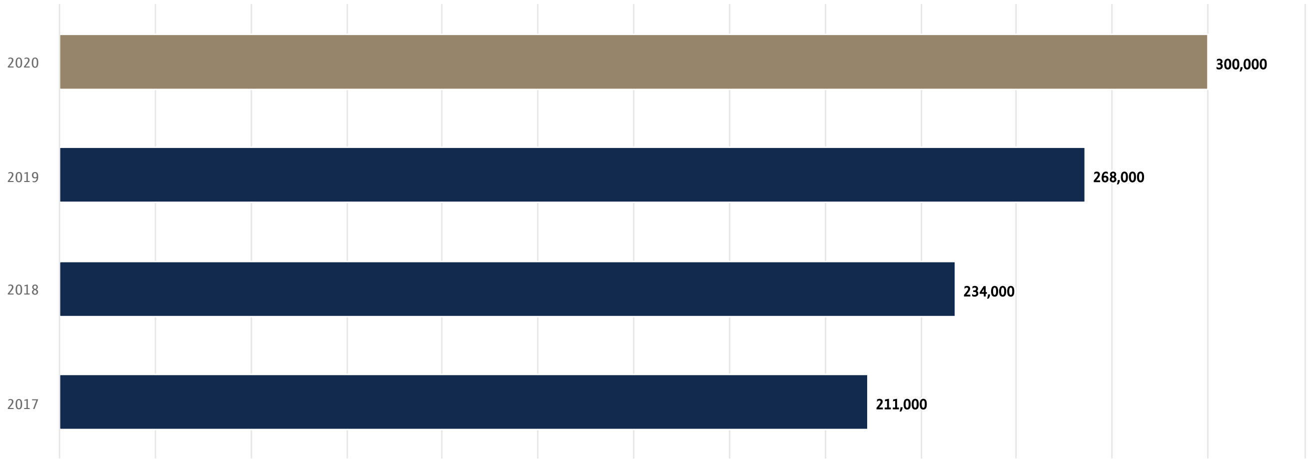
Set against the background of the corona pandemic, the European Central Bank (ECB) kept the prime rate unchanged at 0% in the reporting year. The deposit rate for banks was also left unchanged. Accordingly, mortgage lending rates also remained at a very low level. The interest for a ten-year mortgage was below 1 percent at the end of 2020.

Loan amounts for property financing continue to rise

Based on estimates provided by mortgage broker Interhyp, the corona pandemic has not had a negative impact on the demand for property financing, but rather shifted focus more onto the idea of owning property. As a result of the persistently low interest rates and increased property prices in Germany, there was also another major increase in the average amount borrowed in the last financial year. According to data provided within the scope of the Dr Klein Trend Indicator for Mortgage Lending, the average amount borrowed was € 300,000 in December 2020 – which is € 32,000 or around 12% higher than the figure from the previous year. The average amount borrowed has therefore increased by € 89,000 or around 42% (see chart).

Mortgage amounts at record level

Average mortgage amount in €



Source: Dr. Klein Trend Indicator for Mortgage Lending (DTB), Data as at 31 December in each case

Competition and regulation

The competitive situation in the German market for financial services did not change significantly for the MLP Group in 2020 compared to the previous year. The sector remains very heterogeneous and is characterised by consolidation trends. The providers include numerous financial service providers, single agents, banks, insurance companies and free finance brokers. However, the quality of consulting provided by these companies can vary quite markedly. In addition to this, there is competitive pressure in the entire sector as a result of digital business models and fintechs.

Over the last few years, the legislator has exerted major influence on the financial consulting market and therefore also on MLP's market (with legislation including the MiFID, IDD, Investor Protection Act, Financial Investment Broker Act and Life Insurance Reform Act (LVRG)). The legislator's goal in taking these steps is to protect consumer interests. Among other things, it sets out comprehensive further training, documentation, qualification and transparency obligations for brokers of financial products. These measures mean that the provision of consulting services takes longer, which in turn puts pressure on product margins.

Draft bill for commission capping in the life insurance sector

Changes with relevance to MLP already came into force in 2015 with the introduction of the Life Insurance Reform Act (LVRG). The effects of these changes were also felt in 2020 and will continue to have an impact in the coming years. MLP actually welcomes the requirement to disclose effective costs, as well as the fact that no flat-rate cap has yet been introduced for acquisition commissions. The draft bill for capping commission that was presented by the German Ministry of Finance in the last financial year had proposed 1 January 2021 as a potential start date. However, the political process began to flounder in 2020 and relevant political specialists also remain critical of this regulation. The plan is still to include three components. These are basic compensation, a component for high-quality consulting and a compensation for services that is in line with the market, in case a broker such as MLP performs specific services for an insurer. Overall, MLP benefits from high-quality consulting in the target group which, among other things, leads to lower cancellation rates. However, the margin pressure resulting from the regulation that has already been implemented is also being felt at MLP – albeit to a lesser extent than at other market members thanks to the provision of high-quality consulting services.

Further training obligation for real estate brokerage

Since August 2018, commercially active real estate agents and residential property managers have had to meet a further training obligation of 20 hours within three years. This is regulated in § 34c (2a) of the Industrial Code (GewO) in conjunction with § 15b of the Real Estate Agent and Commercial Construction Industry Ordinance (MaBV). Fulfilment of the further training obligation is a prerequisite for the brokerage of real estate, which plays an important part in MLP's business model and is to be further strengthened. The certificate for the MLP consultants in question had to be produced for the first time in 2020, as the target had to be met by 31 December 2020. Since MLP has already made key investments in continuous further training while introducing measures for implementation of the IDD further training obligation, it was possible to address the requirements resulting from the MaBV without any major additional costs.

Cost transparency further improved

The legislator has taken action with binding stipulation of an effective cost ratio both in Germany through the Old-Age Provision Product Contact Point (PiA) for tax-privileged old-age provision products (basic and Riester pensions) and at European level (stipulated both in euros and as a "reduction in yield") with the Key Information Documents (KIDs) for Packaged Retail and Insurance-Based Investment Products (PRIIPS) that have been mandatory since January 2018. However, from our perspective even these most recent regulatory steps have not even come close to securing sufficient comparability of the products in the market or their associated costs. The methods of calculation should be adapted, so that calculations are performed based on the same prerequisites and the same cost factors.

Data protection intensified

As of May 2018, the regulations for processing personal data have been harmonised throughout the EU and the data protection requirements for both private companies and public sector institutions significantly extended with introduction of the General Data Protection Regulation (GDPR). This has also led to a wide range of new requirements for MLP with regard to reporting processes, statements of accounts, protective measures, information disclosure requirements, process documentation, as well as a significantly extended sanctions regime in the event of infringements. The implementation of the GDPR has permanently increased the expenses, especially in IT.

EU Money Laundering Directive transposed into national law

In 2020, transposition of what is now the fifth EU Money Laundering Directive into national law led to further key regulatory requirements for MLP. Overall, it is fair to say that the money laundering legislation is focussing primarily on the real estate sector, even after presentation of the findings from the "First National Risk Assessment in Combating Money Laundering and Financing of Terrorist Activities", the results of which have been available since the end of 2019.

Due to the special situation within the context of corona, a large number of further regulatory requirements and/or recommended actions were published in 2020. More are likely to follow in 2021. This in particular affects moratoria and value adjustments, as well as the way in which they are handled both in balance sheets and by the supervisory authorities. It also has a general impact on information provided regarding individual risk positions. MLP Finanzberatung SE has not made use of any state aid measures or incentives at any time in connection with the effects of the corona pandemic. At the same time, we do not see any significant influence on our credit portfolio. However, we are of course following developments very closely.

Special regulatory requirements in light of corona

The regulatory developments certainly represent a challenge overall. The effects of generally declining commission income per unit and increasing unit and administration costs – combined with increased price sensitivity among clients – can also negatively impact the profitability of MLP's business model. Irrespective of this, MLP considers itself well positioned in relative comparison with other market actors.

Challenging regulatory environment