Future industry situation and competitive environment

The aforementioned influence of the individual fields of consulting on the operating business segments applies accordingly to the future industry situation and the competitive environment.

Old-age provision

In future, private and occupational pension provision are likely to assume an increasingly important role in Germany. Despite the latest proposals of the German Federal Ministry of Labour and Social Affairs, the objectives of which include strengthening the statutory pension, in its 2016 Pension Insurance Report the German government is keen to stress that constant reduction of the guaranteed statutory pension levels is necessary in order to keep the premiums stable. This can be compensated through additional provision.

Higher subsidy for the basic pension from 2017

The state supports supplementary old-age provision in Germany. In 2017, the maximum tax-deductible amount in Tier 1 is to increase from € 22,766 to € 23,362 for single persons (joint allowance with spouse € 45,532). At the same time, the percentage of premiums paid that is taken into account by the tax authorities is set to increase from 82% to 84%. A maximum of € 19,624 can therefore be deducted as special expenses in 2017. These figures are doubled for married couples. Furthermore the state support levels for the Riester pension remain the same as in 2016.

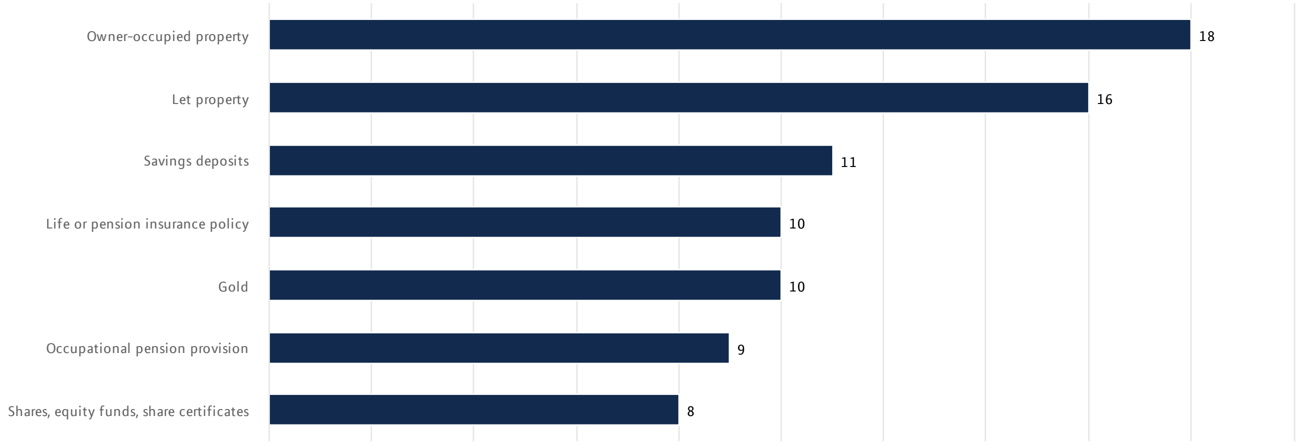
Vast majority understands the importance of supplementary old-age provision

A survey conducted by the German Consumer Research Association (GfK) indicates that most German citizens are aware of the urgency of private old-age provision. Four out of every five respondents (80%) consider it extremely important to put financial provisions in place for their old age. Many Germans also take a pessimistic view of their personal pension prospects, as reported by a survey undertaken by TNS Infratest on behalf of Industrial Union of Metalworkers (IG Metal): According to this, 64% do not think that they will be able to live well off their statutory pension when they retire. This figure increases even further to almost three quarters (73%) in the 18 to 34-year old bracket. A study of investors commissioned by Gothaer Asset Management AG highlighted that 59% of German citizens are still struggling to achieve their old-age provision saving goals in light of the ongoing period of low interest rates. 32% are of the opinion that this has actually become even more difficult.

Worries about a drop in standard of living in later life

The vast majority of German citizens are worried about the risk of old age poverty, as underlined by a Forsa survey commissioned by Gothaer: Accordingly, three out of every four German citizens (75%) are worried or extremely worried about their old age prosperity and fear impoverishment. A survey performed by Axa suggests that those in gainful employment in Germany are predominantly choosing real estate as investments to cover their old age living costs. Indeed, more than one in four (27%) is planning to purchase property either to live in or rent out. One in ten Germans in active employment is keen to invest in savings deposits, private pension/life insurance policies or occupational pension provision to provide for their old age.

Which forms of investment do people in gainful employment intend to use for securing their pension income? (amounts in %)



Source: AXA Germany Report 2016; adjusted by possible multiple responses, 27% of all people in gainful employment intend to purchase property (owner-occupied or buy-to-let)

Statutory pension continues to decline in stages

According to the latest Pension Insurance Report published by the German government, the standard pension level is already at 48%. This figure is likely to drop further to 44.5% by 2030. In its most recent forecasts, the official group of estimators expects the pension level to fall to 41.7% by 2045 and the premium rate to increase to 23.6%. The pension shortfalls are even greater for citizens that enjoy a high income.

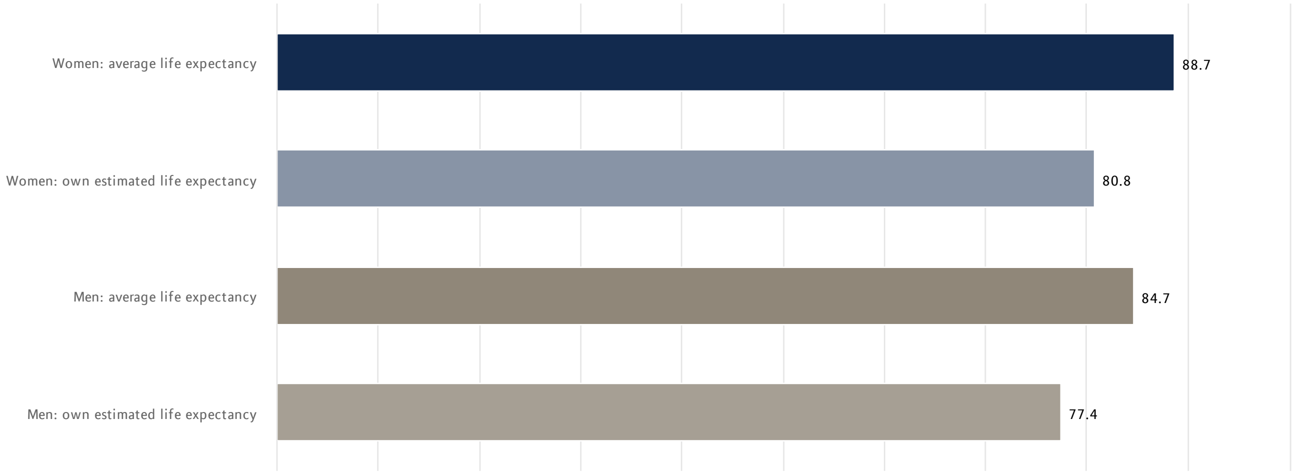
According to a survey conducted by market research institute YouGov on behalf of MLP, almost two thirds (62%) of German citizens do not believe that the government can prevent a decline in the pension level. The results show that neither an increase to the statutory retirement age nor higher premiums would be accepted by the population as a way of stabilising the statutory pension system. Only 10% / 13% of those with statutory pension insurance who have not yet retired would be willing to do this. 58% prefer other approaches to stabilise the declining pension level, such as occupational pension provision.

Own life expectancy underestimated

According to the generation mortality tables of the German Federal Statistical Office, the average life expectancy in Germany is 84.7 years for men and 88.7 years for women. However, the results of a Forsa survey indicate that 90% of German citizens underestimate their actual life expectancy – and thereby also how long their old-age provision will need to last. Based on this, men live an average of seven years longer than they expect, while women live almost eight years longer.

New calculations performed by Cologne-based economist Eckart Bomsdorf suggest that life expectancy is likely to continue increasing quite markedly. Based on the figures provided, girls born in 2016 are likely to live to an average age of 93 years, while boys are likely to reach 90 years – meaning they would have a very long period of retirement. According to official German pension insurance figures, the average pension benefit period has doubled from 10 to 20 years over the course of the last five decades. In 2015, it was 18.8 years for men and 22.8 year for women.

German women and men significantly underestimate their actual life expectancy (in years)



Source: German Federal Statistical Office; Forsa

Despite all of these factors – including state subsidies/allowances for private and occupational pension provision, the declining pension level and increased life expectancy – German citizens continue to display reservations when it comes to signing long-term contracts for old-age provision. Although the market potential remains promising in the mid-term, Assekurata, for example, is forecasting stagnating sector growth.

New stimuli anticipated for occupational pension provision

The German government is planning to launch a pension concept for the statutory pension before the 2017 parliamentary elections. Among other things, this new concept will stipulate harmonisation of the pensions in eastern and western Germany. Compulsory provision for self-employed persons is also being discussed and the foundations for strengthening occupational pension provision have already been laid. The planned legislation to strengthen occupational pension provision in Germany has been available as a draft bill since November 2016 and could provide positive stimulus for occupational pension provision in Germany. It is expected to enter into force in 2018. Among other things, the draft bill will provide for an expansion of the existing tax benefits. The ceiling for tax incentives on premiums paid into pension funds, pension schemes and direct insurance is set to be increased from its current level of 4% to 8% of the income threshold. You can find more details on the planned amendments in the forecast section entitled “Competition and regulation”.

Maximum technical interest rate down again; also impacting occupational disability insurance premiums

On January 1, 2017, the legislator once again reduced the maximum technical interest rate for life and pension insurance policies – from 1.25% to 0.9%. Based on the estimates of ratings agency Assekurata, this reduction represents another challenge for life insurers, as it is becoming increasingly difficult to maintain gross premiums in the coverage assets. Indeed, this can now only be guaranteed for long contractual periods.

The reduction is also leading to higher premiums for new contracts in the occupational disability insurance segment. Model calculations performed by MLP show that the monthly premiums could rise by up to 5%, depending on age group and coverage period.

The further reduction of the maximum technical interest rate is likely to contribute to further reservations among German citizens in the financial year 2017. On the product side, concepts with new types of guarantees are likely to gain ground throughout the sector.

Health insurance

Further reforms are to be expected in the health insurance area over the course of the next few years, particularly following the German parliamentary elections in the autumn of 2017. In future, statutory health insurance funds will face financing challenges, while the private health insurance sector will face challenges resulting from the low interest rate.

Statutory health insurance funds anticipating significant premium increases

For 2017, Germany's Federal Ministry for Health announced that the average additional premium for statutory health insurance will remain stable at 1.1%. From 2018 onwards, however, those with statutory health insurance should expect significant premium increases. According to estimates provided by Association of Health Insurance Companies (vdek), the additional premiums paid exclusively by employees will increase. According to the forecast, this increase is likely to be 1.4% in 2018 and rise to 1.6% by 2020 to ultimately reach 1.8%.

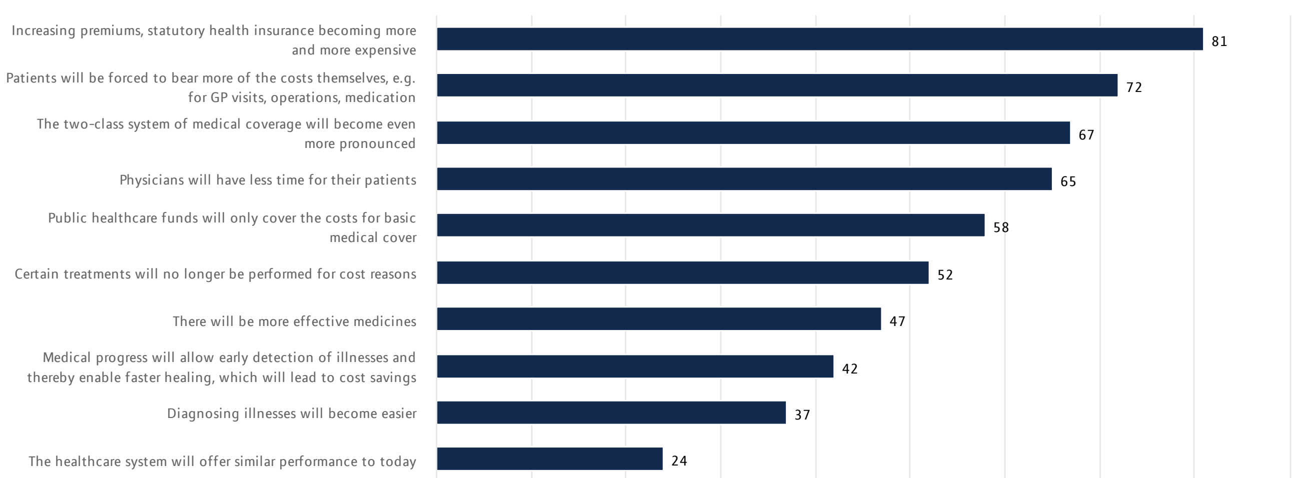
MLP believes that the willingness of numerous statutory health insurance policy holders to switch to a private policy will be boosted as a result of the increasing additional premiums. This in turn should once again inject more dynamism into the private health insurance market in the mid-term. According to ratings agency Assekurata, however, no such desire to switch to private policies should be anticipated in the short-term in the comprehensive private insurance segment. The experts are therefore predicting portfolio losses to continue at a similar rate until the 2017 German parliamentary elections. This view is also shared by the other market members. Based on a survey performed by Assekurata Solutions GmbH, more than half of insurance brokers surveyed (52%) expect business developments in the comprehensive insurance segment to deteriorate in the next twelve months.

Significant majority considers additional private health provision necessary

The long-term potential of private health insurance is also underlined by various studies. The "Continentale Survey 2016" concluded that many of those paying into the statutory health insurance system remain sceptical about the future of the healthcare system in Germany. Almost two thirds (64%) of German citizens surveyed do not believe that the statutory health insurance system will be able to provide them with proper medical care in future. More than three quarters (81%) believe that good healthcare provision can only be secured through additional private provision either now or in the future.

The MLP Health Report 2016 also comes to similar conclusions. A large percentage of German citizens are anticipating increasing statutory health insurance premiums (81%) and are worried about having to pay for a greater proportion of their medical care costs out of their own pocket (72%). More than one in two respondents (58%) expect the healthcare funds only to cover the costs of basic medical care.

What do German citizens expect from the healthcare system over the next ten years? (amounts in %)



Source: MLP Health Report 2016

A survey performed by market research institute YouGov came to the conclusion that private supplementary health insurance offers excellent sales potential. Based on this, one in ten policy holders (11%) aged between 18 and 59 is considering signing up for one or more policies over the next six months. Just under one in five (19%) stated they consider it.

Supplementary insurance policies need to catch up

The majority of those paying into the statutory health insurance system believe that private provision plays an important part in ensuring good medical care. According to the Continentale survey, they believe long-term care (78%) and dentistry (77%) are the key areas in which they need to have additional insurance coverage. The latest Healthcare Barometer published by PricewaterhouseCoopers indicates that just under two thirds (61%) of statutory insurance policy holders in Germany currently do not have any supplementary insurance in place. Ratings agency Assekurata therefore sees great growth potential for products such as supplementary dental insurance.

The third part of the Care Enhancement Act (PSG) is likely to inject new impetus into the private long term care provision market. With the care reform, the three former care levels were replaced by five degrees of care on January 1, 2017. (You can find more detailed information on this in the → "Competition and regulation" chapter). Due to the increased coverage in the media associated with this, the topic of insurance cover for long-term care remains very much in the public mind. Based on estimates of ratings agency Assekurata, this could again boost sales of supplementary long-term care insurance policies, as statutory long-term care insurance provision will remain just a partial solution even after the change in legislation.

Long-term care provision offers significant growth potential

Looking ahead to the German parliamentary elections in 2017, a reform of the healthcare system could once again become a key issue with potential to improve the tax conditions for occupational health insurance schemes. At a time when skilled specialists are in short supply, positive stimuli can also come from employers that have recognised the power of occupational health insurance cover as an instrument for winning the best staff and keeping them loyal. To date, the occupational health insurance policies offered by insurers have essentially comprised discounted standard products with pricing modules. However, ratings agency Assekurata expects more individual and innovative product solutions to hit the market over the next few years.

Occupational health insurance attractive for employees

Employers consider occupational health insurance highly attractive. Indeed, according to a survey performed by Gothaer Versicherung, they actually value it over benefits such as company cars, job tickets or company phones. 61% of respondents stated that they would like to have occupational health insurance in place, but only 4% of employees have received a corresponding offer of additional occupational coverage from their employer. Supplementary dental insurance policies are the most popular, followed by supplementary outpatient coverage policies.

The advantages for employers are clear. Almost two thirds of employees surveyed (64%) stated that receiving occupational health insurance as an additional benefit would strengthen their loyalty towards their employer. Almost half (43%) go further and consider the combination of occupational health insurance with workplace health management a key factor when selecting a future employer.

Wealth management

The need for high-quality wealth management services is set to increase in the long term, due to the constantly growing number of high net-worth individuals. In its 2016 Global Wealth Report, the Boston Consulting Group (BCG) expects global private assets to increase at an annual rate of 6% and exceed US$ 224 trillion by 2020. The percentage of millionaires in the German population is likely to increase from 1.1% today to around 1.6% by 2020. According to the BCG survey, these individuals will together control 31.5% of all assets in the country. The current level is 27.6%. A survey conducted by consultancy Capgemini also suggests that there is massive growth potential for wealth management companies. To date, only 32% of assets owned by dollar millionaires are managed by wealth management companies.

Growing need for wealth management advisory services

The European Central Bank's interest rate policy is slowly motivating German citizens to rethink the way they invest their savings. According to a Union Investment survey, 41% of savers now consider it prudent to channel at least a portion of their money into investments offering a better return. This is 5% more than at the end of 2015. Just over a third (36%) consider shares an attractive investment. In addition to this, investors are optimistic about the price trend. Three quarters of those taking part in the survey expect the prices to remain stable or improve slightly.

Shares slowly becoming more attractive to savers

The European Central Bank's monetary policy and its effects on personal financial investments are motivating more Germans to seek investment advice. According to Union Investment, one in two German citizens consider it important to attend a personal meeting with a consultant as a way of finding the right investment in a sea of choices.

Over the next few years, we expect to see major shifts in funds due to inheritances. According to a survey performed by the German Pension Institute (DIA), private households in Germany alone will inherit around € 3.1 trillion by the year 2024 – representing just under 30% of the entire assets held by private German households. Based on the DIA survey, an average of € 363,000 will be handed down per inheritance.

Wave of inheritance in Germany

The topic of inheritance already commands a great deal of attention in modern society. Indeed, a survey undertaken by Deutsche Bank indicates that the majority of German citizens (52%) have inherited or expect to do so. Just under half of potential heirs stated they would use their inheritance for financial investments, capital accumulation and old-age provision.

The 50+ generation is the only population group in Germany that is continuously growing. It also controls 75% of all assets. We already serve clients in this age group and the group itself is likely to become even more important over the course of the next few years. The primary focus of retirement planning activities is on determining what assets clients have already acquired and how these values can best be invested to meet their specific needs and achieve their goals.

Retirement planning becoming increasingly important

Given the significance of this topic, we will be both further expanding the training offers at our CU and extending our range of services for clients in 2017.

For years, the independent wealth management market has been characterised by ongoing consolidation under massive cost pressure. Clients are increasingly demanding customised solutions, multi-asset concepts and passive investments. The key with investment management services, such as those we offer through FERI Trust GmbH, is therefore to seek greater diversification with comprehensive hedging of risks through a wider, more diverse portfolio. This commitment paired with an ever increasing regulation of the finance sector and the loss of confidence among investors requires well-founded research.

Ongoing consolidation in the wealth management area

Based on a survey performed by Universal Investment, alternative investments are proving increasingly popular among institutional investors in light of the low interest rate environment. Accordingly, four out of every ten investors are keen to invest three to six percent of their funds in alternative investments in future. One in four is looking to increase their alternative investment quota to between nine and twelve percent, while slightly more than one in ten will be seeking to invest more than twelve percent in this asset class.

Alternative investments increasingly in demand among large-scale investors

PwC expects that around US$ 15.3 trillion of global assets under management will be invested in alternative investments in 2020.

In light of low interest rates, the ongoing debt crisis and geopolitical risks, the capital market environment is likely to be characterised by pronounced volatility and remain challenging in the financial year 2017. Within this context, in the long term we expect to see an increased need for consulting services in the professional wealth management area among all of the Group’s target client groups.

Market environment remains difficult

Non-life insurance

Non-life insurance will play an increasingly important role in the market. According to a survey performed by AssCompact, 81% of insurance brokers expect the private non-life insurance business to become much more important over the next few years. The brokers taking part in the survey believe that commercial non-life and homeowners’ insurance policies hold particular potential. More than half of the brokers surveyed are anticipating a significant increase in revenue here.

According to a survey performed by Assekurata, just under 40% of brokers believe that private non-life insurance policies will enjoy positive development in the coming year, while one in three (34%) expect the same of commercial non-life insurance policies. 60% expect the market to remain more or less stable.

Brokers anticipate positive business development

The AssCompact survey also suggests that many insurance brokers are worried about losing their standardised bulk business to the internet. Indeed, more than half of the brokers surveyed are concerned about strong competition from direct insurers or price comparison websites. After all, many of the newly founded fintechs/insurtechs are focusing their attention on the non-life insurance sector with the goal of using simple apps to push their non-life portfolio.

Ratings agency Fitch is anticipating slightly lower growth of around 2% for the property and casualty insurance segment in 2017.

Competition and regulation

The entire market for financial services and the insurance sector are facing consolidation. Germany is considered to be the market with the greatest potential in Europe, in which both national and international service providers are competing. Due to stricter regulations, pressure is in particular mounting on low-level providers, which will lead to a further reduction in the number of market actors. In addition to this, competitive pressure is growing throughout the entire sector as a result of new, digital market members (so-called fintechs). Ratings agency Assekurata also believes that digital competitors will play an increasing part in the mid-term. According to a survey undertaken by the German Consumer Research Association (GfK) for the German Insurance Association (GDV e.V.), four out of every five Germans (82%) are already using the internet to gain more information prior to signing up for an insurance policy. However, the majority (55%) cannot ever see themselves signing up for an insurance policy on the internet, even in the future.

The number of registered insurance brokers also declined again in 2016, as the sector lost around 5,100 brokers. Since reaching its peak at the start of 2011, the number of brokers has fallen by 35,200. As regulatory requirements are becoming ever stricter, this trend is unlikely to change in future. At the same time, it presents MLP with many opportunities as a quality-driven provider.

Further consolidation among statutory health insurance funds

Further consolidation is likely to be expected in the healthcare sector due to increasing cost pressure. The number of statutory health insurance policyholders already dropped quite sharply in previous decades. While there were 1,815 health insurance funds in 1970, this number had already almost halved to 960 by 1995 and currently stands at just 118 (previous year: 124). Today, there are just 132 healthcare funds, and this number is likely to drop even further in future. According to a survey performed by PwC, the statutory health insurance funds believe consolidation to be indispensable as a way of reducing costs and increasing efficiency. Two thirds of respondents believe that 40 to 100 statutory health insurers will be enough in future.

New definition of "need for care" as of 2017

The second part of the Care Enhancement Act (PSG) came into force on January 1, 2017. With this step, a new definition of the "need for care" is being implemented in practice – with five degrees of care instead of the three previous care levels. In future, physical and mental disabilities will both be taken into account equally when classifying the need for long-term care. In addition to this, the statutory long-term care insurance premium increased in 2017 – by 0.2% points to 2.55% for parents and to 2.8% for those without children.

Legislation set to strengthen occupational pension provision from 2018 onwards

Within the scope of the planned pension reform, the German government is keen to offer greater incentives for occupational pension provision. The German Federal Ministry of Labour and Social Affairs presented a draft bill of the legislation to strengthen occupational pension provision in Germany in November 2016. The strategy being employed to boost this market is to offer a larger subsidy framework and make it easier for employers to get on board. The key issues of the draft bill include increased tax relief from the current level of 4% to 8% of the income threshold, a state subsidy for those on low incomes, as well as the opportunity to opt for defined contribution commitments rather than minimum or guaranteed services in terms of the target pension, thereby eliminating liability risks for employers. In addition to this, the basic allowance for the Riester pension is to be increased from € 154 to € 165 p.a. The legislation is scheduled to come into force at the start of 2018.

Maximum technical interest rate down to 0.9%

In the course of implementing Solvency II, the German government discussed dispensing with the maximum technical interest rate, but ultimately decided to keep it. However, the rate was reduced from 1.25% to 0.9% on January 1, 2017. This further reduction not only impacts pension insurance policies. Higher premiums for new policies are also to be anticipated in the term life insurance area and especially in the occupational disability and nursing care insurance areas. Based on a statement issued by the president of BaFin, the need for a guaranteed interest rate is to be reviewed again in 2018.

MiFID II on the home straight

After the European Commission postponed the introduction of the Markets in Financial Instruments Directive MiFID II by one year to January 2018, the Federal Finance Ministry presented the draft bill for the "Second Financial Market Reform Act" in the autumn of 2016. The goal is for the guideline to be transposed into national law by July 2017 and then applied with effect from January 2018. The objectives include greater transparency and better investor protection, both of which MLP generally welcomes. Consultation records in their present form are to be abolished and replaced by a so-called "suitability declaration".

As is the case for all other market actors, MiFID II and the Financial Market Reform Act will lead to significant implementation costs for MLP in areas including IT systems, cost transparency, customer information and reporting. With MLP's current position in the field of wealth management, however, we believe that we are well positioned to handle implementation of the requirements.

In the course of transposing MiFID II into German law, focus is once again shifting toward fee-based investment advisory services. If this leads to additional market potential, MLP is in an ideal position to exploit it, as its approach to new business in the wealth management area has been equivalent to fee-based remuneration for several years.

Product information sheets now only to be introduced in 2018

The European Commission has postponed the start date for the Packaged Retail and Insurance-Based Investment Products Regulation (PRIIPs) by one year to January 1, 2018. In future, providers of financial products are to draft a uniform product information sheet that describes the most important features in a brief and comprehensible way. The PRIIIP regulation applies to investment products such as funds and certificates, as well as to insurance investment products.

To improve the comparability of state-supported old-age provision products, a compulsory product information sheet has already been introduced at national level with the Old-Age Provision Reform Act (AltvVerbG). To this end, the Produktinformationsstelle Altersvorsorge GmbH (PIA) initiative has drawn up a uniform and binding standard for determining risk-return profile classes and calculating the actual costs of tax-privileged old-age provision products. Since January 1, 2017, providers of Riester and basic pensions must use a standardised product information sheet to inform clients of the main product characteristics when concluding a contract. In addition they must have the risk-return class of their own products certified by the PIA and document this accordingly. We generally welcome this step towards greater transparency. However, during a transitional period there will be a difference in the disclosure of costs between tax-privileged and non-tax-privileged products. This contradicts the objectives of greater cost transparency and, in particular, better comparability of products for clients.

Final sprint towards Insurance Distribution Directive (IDD)

In November 2016, the Federal Ministry of Economics presented the draft bill of the legislation for transposing the EU Insurance Distribution Directive (IDD) into German law. The ban on passing on commission in the insurance sector is to remain intact. However, there are no plans to issue a general ban on commissions. The draft bill also provides for the introduction of fee-based insurance consulting. In addition to this, the IDD sets important standards for better quality consulting with uniform principles throughout Europe. For example, brokers will in future not only have to provide evidence of their basic training, but also of their ongoing vocational further training. The transposition into national law must be completed by February 2018.

The analysts at Assekurata believe that the IMD will present insurers, financial services providers and broker pools with particular challenges in 2017. Business models and consulting processes need to be adapted to the new directive. However, no major effects on MLP's business model should currently be anticipated. MLP has always placed great emphasis on further training for consultants.

Bank regulation remains in focus

The capital requirements pursuant to Basel III will increase further up to 2019. The capital conservation buffer will increase in stages from 0.625% in 2016 to 2.5% in 2019. At the same time, intensive discussions to finalise Basel III are taking place. Due to the scope involved, however, many market members are already talking about a new package of regulations, Basel IV. These could potentially lead to even stricter capital requirements for the sector, which would also impact MLP.

Well equipped to handle new regulatory requirements

In summary, we consider our current competitive situation as good, thanks largely to the sustainable diversification of our business model. MLP was an early adopter of numerous requirements that will become binding law in future. Implementation expertise is required in order to comply with the legal documentation, qualification and transparency obligations. MLP believes it is well prepared for this. But irrespective of this, the regulatory developments will certainly represent a challenge for all market actors.