January 21, 2025*

# Market Segment Outlook: Germany Life Insurance

**Although the segment is expected to return to growth in 2025, that growth will likely be sluggish.**

AM Best is maintaining a Negative outlook on the German life insurance segment. Factors considered include:

- The weak and uncertain economic environment, as well as competition from other non-insurance savings products, weigh on-top line growth.
- Continued environment of interest rates above the three-, five and 10-year average will only gradually lead to more favourable conditions for life insurers.
- Life insurers' transition to capital-light products continues.
- Downward pressure on regulatory solvency positions has reversed.

**Weak And Uncertain Economic Environment as Well as Subdued Consumer Spending Weigh On Top-Line Growth.** AM Best expects life insurance premium growth in Germany to have remained constrained in 2024 and to grow only modestly in 2025. The segment's top line is sensitive to the wider economic conditions and consumer confidence. Additionally, the demand for single-premium products has been weak and AM Best expects this to remain the case in the near term.

Germany's economy is expected to maintain a path of sluggish recovery in 2025, in the face of continued headwinds, such as the collapse of the German coalition government and uncompetitive high industrial energy and operating costs.

The International Monetary Fund (IMF) expects gross domestic product (GDP) growth to be absent (0% growth) in 2024, in part attributed to what appears to be a trend towards the beginning of a German deindustrialisation, a continuous stagnation of private consumption and weakness in interest-rate-sensitive sectors. The latest economic trajectory is likely to lead to a modest but underwhelming economic recovery over the next 12 months, underpinned by a current GDP growth forecast for 2025 of 0.8%.

The German life insurance segment has shown declining premium levels since interest rates started increasing in September 2022. Although the segment is expected to return to growth in 2025, that growth will likely be sluggish. AM Best notes that although a continued higher interest rate environment is having a positive impact on the life insurance segment due to improved profitability, the top-line growth remains constrained by competition from other non-insurance savings products.

Life premium growth levels have shown a correlation with the strength of economic conditions and consumer sentiment in the past. AM Best believes that an improvement in household savings rates that is linked to real income developments is needed to notably improve the segment's premium growth path.

**Analytical Contact:**
Angela Yeo, Amsterdam
Tel: +31 20 308 5421
Angela.Yeo@ambest.com

**Contributor:**
Konstantin Langowski, Amsterdam

**Editorial Managers:**
Richard Banks, London
Tel: +44 20 7397 0322
richard.banks@ambest.com

Richard Hayes, London
Tel: +44 20 7397 0326
Richard.Hayes@ambest.com

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The weak demand for single-premium business has been the main driver for the decline in the segment's overall top-line volumes. A reversal of the current inverted yield curve would likely introduce a revival of single premium business. However, this yield-curve reversal might not be a realistic outcome in the near term, as the flare up of global protective measures in the form of tariffs is likely to lead to prolonged inflationary pressure.

### Higher Interest Rate Environment Will Only Gradually Lead to More Favourable Conditions for Life Insurers.

Generally, a higher interest rate environment is positive for life insurers, as higher investment returns can be achieved. However, as long-duration, traditional life products, with contractually fixed-interest rate guarantees, still dominate German life carriers' portfolios, some challenges remain, despite so-called capital-light products dominating new sales.

Back-books with high average guarantees are slow to run-off due to high policyholder persistency rates, as consumers hold on to their traditional, long-duration products that enjoy a level of guaranteed returns no longer available in the market.

AM Best notes that the collapse of two planned German life insurance back-book transactions during 2024 seems to have put the brakes on short-term back-book consolidation activity.

Overall, the higher interest rate environment has led to improved margins. In parallel, the higher interest rate environment has also gradually resulted in more favourable crediting rates, however these are not notably more competitive than other non-insurance market savings products.

Life insurers generally also have a long asset-duration profile, which limits return flexibly as only new or reinvested assets can benefit from the higher interest rate environment.

German life insurers will be monitoring their surrender rates, as a significant increase could result in forced sales of asset holdings. AM Best notes that it has not seen any indication that this scenario will materialise.

AM Best also notes that the change in the interest rate environment 24 months ago led to a significant position of unrealised losses on the balance sheets of life insurers. These losses would pose a challenge if insurers were forced to realise them.

This risk is partially offset by insurers' effective asset and liability management strategies, strong capital buffers, and adequate liquidity profiles. Furthermore, AM Best believes that because of active asset liability management, market players' exposure to those unrealised losses on their bond holdings will vanish gradually over the next 12 months.

### Shift to Capital-Light Products

In the past, life insurers responded to the low-yield environment, by adjusting product features of new policies and so slowly shifting their product mix to more capital-light offerings.

These products have either no guarantee or flexible guarantee features, which give insurers more flexibility to manage the transition out of the low interest rate environment that ran from 2009 to 2022.

AM Best does not believe that German life insurers will return to a strategy that overly focuses on products with guaranteed rates, despite the higher return prospects in a higher interest rate environment.

It is expected that the share of capital-light products will continue to grow as insurers seek to reduce their risk by focusing sales resources on products that pass the investment risk to policyholders. However, changes in new business are likely to affect the overall composition of the back book only gradually.

### Downward Pressure on Regulatory Solvency Positions has Reversed

Regulatory capital adequacy, as measured by Solvency II, is overall strong for the German life insurance sector and will likely remain so. The strong correlation of solvency capital ratios (SCR) to the interest rate environment reflects the fact that life insurers tend to have liabilities with a significantly longer duration than the assets that back them. As a result of this mismatch, the increase in long-term yields resulted in a large upsurge of the life market average SCR.

BaFin, the German financial regulator, implemented a recalculation of transitional measures on technical provisions (TMTPs), based on current rates. This has resulted in TMTPs falling to zero, as yields now exceed the average investment guarantee on most insurers' traditional life portfolio. This development does not have an adverse effect on the segment's SCR ratios, as the general dependence on transitional measures, which varied greatly from company to company during the low-interest rate environment, has dissipated.

Overall, AM Best expects the German life insurance segment to face challenges despite the higher interest rate environment, as positive influences on margins are still hampered by weak top-line development.

Economic headwinds and competitive alternative deposit options from outside the insurance market continue to weigh on new business development. However, AM Best could revise the outlook to Stable should the new-business trajectory turn around, alongside improving economic conditions.

# GUIDE TO BEST'S MARKET SEGMENT OUTLOOKS

Our market segment outlooks examine the impact of current trends on companies operating in particular segments of the insurance industry over the next 12 months. Typical factors we would consider include current and forecast economic conditions; the regulatory environment and potential changes; emerging product developments; and competitive issues that could impact the success of these companies.

A Best's Market Segment Outlook can be Positive, Negative, or Stable.

| Best's Market Segment Outlook | |
|---|---|
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**A.M. Best Company, Inc.**
Oldwick, NJ
CHAIRMAN, PRESIDENT & CEO **Arthur Snyder III**
SENIOR VICE PRESIDENT & TREASURER **Cynthia Young**
SENIOR VICE PRESIDENT **Lee McDonald**

**A.M. Best Rating Services, Inc.**
Oldwick, NJ
PRESIDENT **James Gillard**
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SENIOR MANAGING DIRECTOR & CHIEF RATING OFFICER **Kenneth Johnson**
SENIOR MANAGING DIRECTORS **Edward H. Easop, James F. Snee**

**AMERICAS**

**WORLD HEADQUARTERS**
A.M. Best Company, Inc.
A.M. Best Rating Services, Inc.
1 Ambest Road, Oldwick, NJ 08858
Phone: +1 908 439 2200

**MEXICO CITY**
A.M. Best América Latina, S.A. de C.V.
Av. Paseo de la Reforma 412, Piso 23,
Col. Juárez, Alcadía Cuauhtémoc, C.P. 06600, México, D.F.
Phone: +52 55 1102 2720

**EUROPE, MIDDLE EAST & AFRICA (EMEA)**

**LONDON**
A.M. Best Europe - Information Services Ltd.
A.M. Best Europe - Rating Services Ltd.
12 Arthur Street, 8th Floor, London, UK EC4R 9AB
Phone: +44 20 7626 6264

**AMSTERDAM**
A.M. Best (EU) Rating Services B.V.
NoMA House, Gustav Mahlerlaan 1212, 1081 LA Amsterdam, Netherlands
Phone: +31 20 308 5420

**DUBAI***
A.M. Best Europe - Rating Services Ltd. - DIFC Branch*
Office 102, Tower 2, Currency House, DIFC
P.O. Box 506617, Dubai, UAE
Phone: +971 4375 2780
*Regulated by the DFSA as a Credit Rating Agency

**ASIA-PACIFIC**

**HONG KONG**
A.M. Best Asia-Pacific Ltd
Unit 4004 Central Plaza, 18 Harbour Road, Wanchai, Hong Kong
Phone: +852 2827 3400

**SINGAPORE**
A.M. Best Asia-Pacific (Singapore) Pte. Ltd
6 Battery Road, #39-04, Singapore
Phone: +65 6303 5000


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