



Financial Statement Analysis
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CFRA / Shenanigans

Paper on Allianz Group

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Introduction

I work for the information technology (IT) subsidiary "AGIS" of Allianz Group (ISIN DE 000 840 400 5; ALVG.DE) so my personal interest leads me to focus on financial analysis of Allianz Group. This is a major challenge because Allianz Group is a full financial service provider also owns full-licensed Dresdner Bank AG as a 100% subsidiary.

Therefore total revenues (2003: \$128.47bln; 39% rev. growth because of acquisition of Dresdner Bank; Goodwill \$19mln) demand on insurance premiums and trading results of investment banking division Dresdner Kleinwort Wasserstein (DrKW).

Liabilities represent customer's deposits such as giro accounts, savings accounts and others. They are announced as accounts payable and short/current long term debt in the balance sheet. An operative part is held in foreign currencies, which can lead to further fluctuations under evaluation. Allianz Group current assets, divided in cash and cash equivalents and net receivables contain loans Dresdner Bank AG has assigned to private or corporate clients.

Dresdner Bank AG has set up an own division "IRU" (Institutional Restructuring Unit), who's objective is to place bad debt (resulting from long-term problem loans and real estate specs) of €35bln on international finance

markets. This has a quite huge impact on the stock market price consequently market value on common stocks and EPS (Earnings per share; 0.951 ttm – 12 month).

On this special circumstances mentioned above Allianz Group cannot be analysed with common ratios out of the box (Altman's Z score 0.404!). There are several ratios especially for analysing banks (i.e. Loans to Deposit).

In cause of the tremendous decrease (2001: €62bln 2004: €36,7bln) in group market value, the management board has raised common equity by offering stock options or bonds the past two years to stabilise their group market value.

Even so Allianz Group was the first foreign financial services company granted to New York Stock Exchange (NYSE). It ranks number 2 in global insurance business. Allianz Global Investors (formerly Allianz Dresdner Asset Management ADAM) has approximately €1bln assets under management. Subsidiaries in USA are names like Nicholas-Applegate and PIMCO.

Biggest competitors in North America are AXA (2003: Revenue \$125.46bln), Aegon NV (2003: Revenue \$36.19bln) and American International Group (2003: \$89.93bln).

Main aspects

By Definition of Dr. Howard M. Schilit, Financial Shenanigans are actions or omissions designed to disclose the real financial performance or financial condition of a company. There is no one-to-one relation to unlawful actions, i.e. not all shenanigans violate accounting regulations.

Under the above mentioned circumstances the following financial considerations should be mentioned:

1. A major part of liabilities are held in cash and accounts payable
2. Most of cash or net receivables are loans pending with customers
3. Transfer costs for in group commutations
4. Price-rigging on insurance markets (blows-up premium earnings)
5. Floating exchange rates of foreign currencies

Possible Shenanigans

The following table reflects the possibilities (partly already revealed) of shenanigans within Allianz Group:

Type	Date	~ in Mio. €	Background
(1) Undisclosed Reserves	-	-	German Commercial Code (HGB) vs. German Income Tax Act (EStR)
(2) IRU Financial Outplacement	2004	70 (90 \$)	Private Equity Portfolio North America
(3) AGF – DEGI Real Estate Transfer	01/10/2004	220	Tour Mirabeau properties unit in Paris
(4) Institutional Clients – Business Clients	24/07/2002	Pending procedure	“Property/Casualty Insurance” Price-riggins with AXA, Provenzial and Gerling
(5) Exchange rates on foreign currencies	-	-	German law has deregulated foreign exchange markets since adoption of the euro.

Table: Possible Shenanigans

Comment on (1)

According to IAS 22 Purchasing method undisclosed reserves must be identified. This is also a reason for the generation of goodwill in M&A. Altogether the intentions of IAS 37: Provisions, Contingent Liabilities and Contingent Assets are recognizable to avoid the distortion of real conditions by undisclosed reserves.

Check on retained earnings on the balance sheet (Stockholders equity) related to cash flow listings such as dividends paid or sale purchase of stock. It is also very common to stockpile reserves on pension funds, because the interest can be calculated in on a variable basis. The Company is free to estimate this interest rate therefore it is possible to raise disclosed reserves under the aim of pension funds.

Comment on (2)

This has an impact on extraordinary income from non-strategic business or discontinued operations. It blows up the gross profit especially the net income with announcements in discontinued operations and extraordinary items.

Check on income statements, in detail income from continuing business, respective cash flow generated from operating activities or core business relating to total other income.

Comment on (3)

This might be a transfer for tax reasons. Even so sometimes transfer prices are not published, especially when non-strategic business is disinvested. Those figures remain under silence. In group transfers must be based at common market prices. In History German Law required a segmentation of several insurance division's (i.e. Life/Health and Property/Casualty) in own legal entities. This is why those restructuring cases are in order of the business - daily.

Check on abnormal transfers in assets (real estate), extraordinary costs relating to non-operational business. Also a write-off based on a self calculated market value is used in common to disclose financial information. If a company is willing to build a strong relationship to all stakeholders, you find that information in 8-K Filings, additional footnotes or special reports from investment analysts (Merrill Lynch, J.P. Morgan).

Comment on (4)

This inflates premiums earnings from property/casualty insurance contracts. As pricing is unique, this in fact is a cartel, absolutely forbidden by German law and European Union regulations. Anti-Trust division has already taken action on insurance companies. Government penalties such as financial punishments and environments projects could be a consequence.

Check on abnormal increase of earnings in segment overview, especially in growth markets. They can be found in the management report or statement of affairs (i.e. 8-K SEC form), but also in quarterly reports or investment ratings for the stock exchanges.

Comment on (5)

Since the adoption of the euro by the EU-12 Countries German Exchange Supervisory Authority deregulated the unofficial foreign currency market. The new model for euro fixing rates is a consortium of the twelve major German banks (such as HypoVereinsbank, Deutsche Bank, Dresdner Bank, WestLB). Whoever is offering the best exchange rate for this particularly foreign currency is the guideline for the official buying or selling rate. This is done on a day-by-day basis. That puts official foreign exchange rates into a more flexible financial scope or margin to the euro. For the reporting banks this is an additional risk for their Cash Flow.

Check on "Effect of Exchange Rate Changes" in Cash Flow listing (2003: €120mln). Within Dresdner Bank AG currency risks are limited by applying the following principle: all loans and deposits in foreign currencies are refinanced or reinvested in the same currency with matching maturities.

Role of CFRA – Center for Financial Research & Analysis

The Center for Financial Research & Analysis (CFRA) was founded 1994 by an accounting professor and is an independent research and educational organization. It has two service commitments. One is to provide research on the quality of earnings; the other is offering training to communities.

They focus on financial statements public available, to expose unusual accounting practices. Those might be early warning signs for business deterioration. The CFRA currently has the capability to monitor financial data of the more than 15,000 companies that file report with the Security Exchange Commission (SEC), as well as various international regulatory agencies. The demand for this kind of information has grown exponentially in the past years, making the CFRA a valuable entity serving its customers.

■ *Conclusion*

The duties for Certified Public Accountants (CPA's) associations have become more important and widely spread. Shenanigans as a trigger for financial disaster happened to Enron and World Com must be prevented. Financial Research & Analysis is fundamental for preventing companies from fraud in financial reports. This is necessary to isolate accounting gimmicks in the future.

In my opinion the problem persist also for shenanigans, which are not violating law or accounting principles, because they also have an impact on the transparency of the “real” condition of a company.

Readings

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