

# China Pacific Insurance (2601 HK)

## Steady increase in operating profit

CPIC (2601 HK/601601 CH) announced 1H20 results on 23 Aug, which we think are largely in line with expectation. GWP increased 4.2% YoY to RMB 216.6bn in 1H20 (Life GWP +0.1%YoY; P&C GWP +12.4% YoY). Operating profit +28.1% YoY, although net profit shrank 12% primarily due to larger amount of tax paid in 1H20. The Company also made pragmatic moves to strengthen corporate governance, unleash Fintech capability, and set up health ecosystem development plans. All of these bode well for long term development.

- Life insurance suffered from COVID-19, but sequentially recovery was robust.** In 1H20, NBV decreased 24.8% YoY whereas NBV margin shrank 2ppt YoY to 37%. Individual FYRP was down 35% YoY. Monthly average agent headcount decreased 3.8% YoY, but agent team upgraded. The share of active and high-performing agents reached 27% and 15.8%. In 2Q, life insurance achieved sequential recovery in terms of premium income and agent headcount, which was a favorable trend.
- P&C business beat in GWP growth and underwriting profitability.** CPIC P&C achieved above-industry premium growth at +12.3% YoY (Auto +4%, non-auto +29.8%). Combined ratio improved 0.3ppt, in which expense ratio was reduced by 0.8ppt to offset higher loss ratio. Combined ratio of auto insurance +0.6ppt, thanks to reduction of both loss ratio and expense ratio. Non-auto combined ratio edged up 0.2ppt to 99.7%. However, some major non-auto business lines such as liability insurance and commercial property insurance achieved expansion in underwriting profitability.
- Investment business recorded steady performance.** Total investment yield held up at 4.8% in 1H20, in which fixed income yield dropped a bit while equity investment yield improved from 1H19. Third-party AUM of CPIC AMC and Changjiang Pension maintained rapid pace of expansion, rising 38.4%/22.6% from YE19, respectively, to RMB269.6bn/442.2bn.
- Initiatives to strengthen long-run capability of the Company.** 1) GDR issuance and diversification of board; 2) Set up of Fintech subsidiary; 3) Promoted SOE reform and designed new incentive programs for talents.
- Valuation.** We adjusted our forecast to reflect w-t-e life NBV decline in 1H20, tax policy's disturbance on net profit, as well as b-t-e equity investment. We mildly adjust TP to HK\$33.22 based on SOTP method, which corresponds to 0.63 FY20E P/EV. Maintain BUY.

### Earnings Summary

(YE 31 Dec)	FY18A	FY19A	FY20E	FY21E	FY22E
GWP (RMB mn)	321,895	347,517	356,778	380,643	403,874
YoY growth (%)	14.3	8.0	2.7	6.7	6.1
Total income (RMB mn)	353,103	382,682	395,351	417,409	441,433
Net profit (RMB mn)	18,019	27,741	28,175	32,364	33,599
EPS (RMB)	1.99	3.06	3.11	3.57	3.71
YoY Growth (%)	22.90	53.95	1.57	14.87	3.81
Consensus EPS (RMB)	n.a.	n.a.	2.83	3.10	3.47
P/B (x)	1.30	1.09	0.94	0.85	0.77
P/EV (x)	0.58	0.49	0.45	0.41	0.37
Yield (%)	4.66	5.59	5.68	6.53	6.78
ROE (%)	12.55	16.92	14.64	14.87	14.00

Source: Company data, Bloomberg, CMBIS estimates

### BUY (Maintain)

Target Price	HK\$33.22
(Previous TP)	HK\$33.93)
Up/Downside	+33.1%
Current Price	HK\$24.95

### China Insurance Sector

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#### Stock Data

Mkt Cap (HK\$ mn)	307,074
Avg 3 mths t/o (HK\$ mn)	401.13
52w High/Low (HK\$)	31.62/16.92
Total Issued Shares (mn)	<b>2,775 (H)</b>
	6,287 (A)

Source: Bloomberg

#### Shareholding Structure

Shenergy (Group)	14.64%
Fortune Investment	14.17%

Source: HKEx

#### Share Performance

	Absolute	Relative
1-mth	5.5%	2.0%
3-mth	15.2%	3.4%
6-mth	-6.9%	-2.2%

Source: Bloomberg

#### 12-mth Price Performance



Source: Bloomberg

#### Auditor: PwC

#### Related Reports

- "Prepared for headwinds" 23 Mar 2020
- "Margin priority may compensate FYRP decline" – 31 Oct 2019
- "Potential GDR unlocks global access" – 24 Sep 2019

Figure 1: 1H20 results summary

(RMB mn)						
P&L	1H20	1H19	YoY	2Q20	1Q20	QoQ
Gross written premiums	216,597	207,809	4.2%	85,449	131,148	-34.8%
Net premiums earned	192,770	185,485	3.9%	75,703	117,067	-35.3%
Investment income	37,766	31,952	18.2%	17,853	19,913	-10.3%
Total income	232,712	219,132	6.2%	94,690	138,022	-31.4%
Insurance benefits and claim expenses	(166,864)	(154,579)	7.9%	(65,378)	(101,486)	-35.6%
Underwriting costs	(22,619)	(26,966)	-16.1%	(10,401)	(12,218)	-14.9%
G&A expenses	(20,396)	(18,101)	12.7%	(10,470)	(9,926)	5.5%
Total expenses	(215,032)	(204,418)	5.2%	(87,616)	(127,416)	-31.2%
Associates and JVs	279	277	0.7%	95	184	-48.4%
Pre-tax profit	17,630	14,485	21.7%	6,806	10,824	-37.1%
Income tax	(3,039)	2,041	-248.9%	(805)	(2,234)	-64.0%
Less: Minority interests	(352)	(343)	2.6%	(150)	(202)	-25.7%
Net profit	14,239	16,183	-12.0%	5,851	8,388	-30.2%
<b>B/S</b>	<b>1H20</b>	<b>2H19</b>	<b>HoH</b>	<b>2Q20</b>	<b>1Q20</b>	<b>QoQ</b>
Total assets	1,685,465	1,528,333	10.3%	1,685,465	1,611,323	4.6%
Insurance contracts liabilities	1,181,122	1,068,021	10.6%	1,181,122	1,143,897	3.3%
Total liabilities	1,483,775	1,345,013	10.3%	1,483,775	1,420,404	4.5%
Equity attributable to shareholders	196,798	178,427	10.3%	196,798	185,925	5.8%
<b>Key indicators</b>	<b>1H20</b>	<b>1H19</b>	<b>YoY</b>	<b>2Q20</b>	<b>1Q20</b>	<b>QoQ</b>
Life GWP (RMB mn)	138,586	138,428	0.1%	46,713	91,873	-49.2%
Life FYRP from agency channel (RMB mn)	14,741	22,800	-35.3%	5,076	9,665	-47.5%
New business value (RMB mn)	11,228	14,927	-24.8%	n/a	n/a	n/a
P&C GWP (RMB mn)	76,672	68,247	12.3%	37,628	39,044	-3.6%
Auto insurance GWP (RMB mn)	47,962	46,133	4.0%	24,438	23,524	3.9%
Non-auto insurance GWP (RMB mn)	28,710	22,114	29.8%	13,190	15,520	-15.0%
P&C combined ratio	98.30%	98.60%	-0.3 ppt	n/a	n/a	n/a
Net investment yield	4.40%	4.60%	-20 bps	n/a	n/a	n/a
Gross investment yield	4.80%	4.80%	0 bps	n/a	n/a	n/a
Comprehensive solvency ratio - Life	242.0%	257.0%	-15 ppt	242.0%	254.0%	-12 ppt
Comprehensive solvency ratio - P&C	275.0%	285.8%	-10.8 ppt	275.0%	290.0%	-15 ppt
<b>Key indicators</b>	<b>1H20</b>	<b>2H19</b>	<b>HoH</b>	<b>2Q20</b>	<b>1Q20</b>	<b>QoQ</b>
Group investment assets (RMB mn)	1,552,866	1,419,263	9.4%	1,552,866	1,482,004	4.8%
Group embedded value (RMB mn)	430,420	395,987	8.7%	n/a	n/a	n/a

Source: Company data, CMBIS

Figure 2: Forecast revisions

RMB mn	New			Old			Diff		
	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E
GWP	356,778	380,643	403,874	358,220	378,698	397,616	-0.4%	0.5%	1.6%
Total income	395,351	417,409	441,433	392,272	413,893	433,226	0.8%	0.8%	1.9%
Net profit	28,175	32,364	33,599	29,546	31,063	32,465	-4.6%	4.2%	3.5%
New business value	20,731	24,999	28,833	22,425	25,939	29,016	-7.6%	-3.6%	-0.6%
NBV growth	-15.7%	20.6%	15.3%	-8.8%	15.7%	11.9%	-6.9 ppt	4.9 ppt	3.5 ppt
Embedded value (group)	431,359	473,971	518,366	428,943	471,130	516,558	0.6%	0.6%	0.4%

Source: Company data, CMBIS estimates

### Figure 3: Forecast revisions

#### Life business

Three-year avg. RoEV (2020-2022E)	14.4%
Terminal growth	2.0%
Discount rate	16.0%
Fair P/EV multiple (x)	0.89
2020E EVPS (98.29% stake, Rmb)	36.09
<b>Value of life business (Rmb)</b>	<b>31.99</b>

#### P&C business

2020E BVPS (Rmb)	5.28
Fair PBR (x)	1.0
<b>Value of P&amp;C business (Rmb)</b>	<b>5.28</b>

Total (Rmb)	37.26
Conglomerate discount	20%
Target price (Rmb)	29.81

<b>Target price (HK\$)</b>	<b>33.22</b>
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Implied 2020E Group PEV based on TP (x)	0.63
Implied 2021E Group PEV based on TP (x)	0.57

Source: Company data, CMBIS estimates

## Financial Summary

### Income

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Gross written premium	321,895	347,517	356,778	380,643	403,874
Incl: Life GWP	202,414	212,514	214,915	224,530	233,501
P&C GWP	117,808	132,979	141,863	156,114	170,374
Net premiums earned	299,724	313,246	319,004	339,362	359,050
Investment income	49,999	65,730	72,573	74,032	78,135
<b>Total income</b>	<b>353,103</b>	<b>382,682</b>	<b>395,351</b>	<b>417,409</b>	<b>441,433</b>
Insurance claims and reserves	(226,444)	(260,850)	(264,429)	(271,569)	(287,746)
Other operating expenses	(98,986)	(94,360)	(95,888)	(102,278)	(108,470)
<b>Total expenses</b>	<b>(325,430)</b>	<b>(355,210)</b>	<b>(360,317)</b>	<b>(373,847)</b>	<b>(396,216)</b>
Associates and JVs	335	494	519	545	572
Pre-tax profit	28,008	27,966	35,553	44,106	45,788
Income tax	(9,574)	388	(6,755)	(11,026)	(11,447)
Less: Minority interests	(415)	(613)	(623)	(715)	(742)
<b>Net profit</b>	<b>18,019</b>	<b>27,741</b>	<b>28,175</b>	<b>32,364</b>	<b>33,599</b>

### Key ratios

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
<b>Group (%)</b>					
Total GWP growth	14.3	8.0	2.7	6.7	6.1
Total income growth	10.6	8.4	3.3	5.6	5.8
Net profit growth	22.9	54.0	1.6	14.9	3.8
EV growth	17.5	17.8	8.9	9.9	-
Net investment yield	4.9	4.9	4.3	4.2	4.1
Total investment yield	4.6	5.4	4.7	4.3	4.1
Investment assets growth	14.1	15.1	16.8	10.0	8.7
<b>Life (%)</b>					
GWP growth	15.3	5.0	1.1	4.5	4.0
Agent FYRP growth	(9.7)	(22.4)	(23.5)	19.2	13.8
NBV growth	1.5	(9.3)	(15.7)	20.6	15.3
NBV margin (NBV/agent APE)	63.2	73.1	79.6	80.4	81.3
Life comprehensive solvency	260.8	256.8	282.0	278.4	275.9
<b>P&amp;C (%)</b>					
GWP growth	12.6	12.9	6.7	10.0	9.1
Auto GWP/total P&C	74.7	70.1	66.4	63.3	60.3
Loss ratio	56.3	60.2	59.5	59.3	59.2
Expense ratio	42.1	38.1	39.2	39.0	39.0
Combined ratio	98.4	98.3	98.7	98.3	98.2
P&C comprehensive solvency	305.9	292.6	271.7	260.0	249.7
<b>Returns (%)</b>					
Life RoEV	24.7	23.1	14.2	14.5	14.5
P&C ROE	10.0	16.6	14.2	14.1	13.3
<b>Per share</b>					
EPS (RMB)	1.99	3.06	3.11	3.57	3.71
DPS (RMB)	1.00	1.20	1.22	1.40	1.45
EVPS (RMB)	37.09	43.70	47.60	52.30	57.20
BVPS (RMB)	16.51	19.69	22.77	25.26	27.70

### Balance sheet

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Investment assets	1,233,222	1,419,263	1,657,355	1,823,008	1,982,106
other assets	102,737	109,070	82,199	97,118	121,031
<b>Total assets</b>	<b>1,335,959</b>	<b>1,528,333</b>	<b>1,739,555</b>	<b>1,920,125</b>	<b>2,103,137</b>
Insurance liabilities	981,926	1,143,527	1,294,809	1,446,831	1,598,473
Subordinated debt & others	199,985	201,486	232,403	237,727	246,142
<b>Total liabilities</b>	<b>1,181,911</b>	<b>1,345,013</b>	<b>1,527,212</b>	<b>1,684,558</b>	<b>1,844,614</b>
<b>Shareholders' equity</b>	<b>149,576</b>	<b>178,427</b>	<b>206,379</b>	<b>228,866</b>	<b>251,055</b>
Minority interest	4,472	4,893	5,964	6,701	7,467
Total equity	154,048	183,320	212,343	235,567	258,522

Source: Company data, CMBIS estimates

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