

New China Life (1336 HK) – Unrated Life & health industry

Key Data

H-share price (HK\$)	22.75
Target price (HK\$)	NA
Upside potential (%)	NA
52Wk H/L(HK\$)	36.9 / 22.6
Issued shares:	
H-shares (mn)	1,034
A-shares (mn)	3,117
H-share mkt cap (HK\$mn)	23,523
30-day avg vol (HK\$mn)	58.6
Major shareholder (%):	
Central Huijin	31.2
Baosteel Group	15.1

Source: Company, Bloomberg, ABCI Securities

Revenue composition in 2011 (%)

Net earned premiums (NEP)	88.1
Investment income	11.7
Other income	0.2

Source: Company

Share performance (%)

	Absolute	Relative*
1-mth	(4.2)	(5.2)
3-mth	(21.2)	(25.8)
6-mth	(32.4)	(26.0)

Source: Bloomberg

*Relative to MSCI China

1 year price performance



Source: Bloomberg

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Positive surprise justifies a re-rating (1H12 result review)

In 1H12, New China Life (NCI) reported better-than-expected EV and net profits. Also, its VNB was in-line with the market consensus. NCI is trading at 1.01x 2012E PEV and 0.1x 2012E VNB, the cheapest among the top four life insurers. NCI has been underperforming China Life, Ping An and China Pacific by an average of 33.8% since early Jun. We believe this set of results will halt its underperformance against peers. More importantly, the stock trades at a big valuation discount to peers (1.01x PEV versus an average of 1.33x of big three). Hence we view NCI as a prominent catch-up play in near term. Lastly, NCI is a contending constituent of MSCI China and HSCEI, and set to attract passive fund flows in case of any index inclusion. Therefore, we hold a positive stance towards NCI at present.

Positive surprise on EV. Group EV came in at Rmb56.2bn, 7.1% better than street consensus of Rmb52.4bn and up 14.6% HoH, due to higher bond prices. Its EV growth HoH was faster than 7.3% of China Pacific and 9.9% of Ping An. To sum, NCI and China Life reported the fastest growth in EV among peers for 1H12.

Beating net profits driven by tax credit and better investment income.

Net profits recorded Rmb1.9bn, ahead of Bloomberg consensus of Rmb1.4bn and up 7.3% YoY. This is driven by a one-off tax credit of Rmb397mn. Also, the company reported higher investment income at Rmb7.3bn, up 7.2% YoY, despite an impairment loss of Rmb2.0bn.

Stable solvency position but with limited room for more sub-debts.

Solvency ratio edged up 2ppt HoH to 158% in 1H12. After the planned sub-debt issuance of Rmb10bn in 4Q12, the ratio will further improve to >200%. However, NCI has a very limited room to further issue sub-debt, in accord to the 50% NAV limit set by CIRC.

Risk factors: Better/worse-than-expected investments and underwriting performance, looser/tighter-than-expected industry regulations

Valuation

FY ended Dec 31	2008	2009	2010	2011
Revenue (Rmb mn)	48,979	73,906	102,709	108,610
Chg (YoY)		50.9	39.0	5.7
Net profit (Rmb mn)	649	2,660	2,249	2,799
Chg (YoY)		309.9	(15.5)	24.5
EPS (HK\$)	0.62	2.53	2.23	1.51
PER (x)	36.9	9.0	10.2	15.0
BPS (HK\$)	1.3	4.0	6.5	12.3
P/B (x)	17.3	5.6	3.5	1.9
EVPS (HK\$)			27.9	19.1
PEV (x)			0.8	1.2
VNB (HK\$)			4.71	1.70
VNB (x)			(1.1)	2.1

Source: Company, Bloomberg, ABCI Securities



1H12 result review

Positive surprise on EV. Group EV came in at Rmb56.2bn, 7.1% better than street consensus of Rmb52.4bn and up 14.6% HoH. This is partly due to higher AFS reserves (net addition of Rmb1.6bn, 5.1% of end-2011 shareholders' equity). Group book value went up 11.6% HoH to Rmb34.9bn. Its EV growth HoH was faster than 7.3% of China Pacific and 9.9% of Ping An. We believe the rise of bond prices was the key reason for the EV increase.

In-line VNB but slow expansion in NBM. Value of new business (VNB) was reported at Rmb2.34bn, slightly better than street consensus of Rmb2.29bn by 2.2% and down 1.4% YoY. This is primarily because of the expanding new business margins (APE basis, up from 22.4% in 2011 to 23.3% in 1H12), despite a 6.6% YoY decline in FYP. We believe the lift of NBM was driven by higher portion of bancassurance regular FYP sales (61.4%, higher than 58.0% in 1H11) and increasing sales of bancassurance regular products with payment periods of 5 years or above (88.7% of banc FYP, versus 79.7% in 1H11). However, the 0.9ppt HoH improvement in NBM is behind major peers' (China Life up 4.2ppt HoH and China Pacific up 2.3ppt HoH). We view it as a concern to the investors.

Beating net profits driven by tax credit and better investment income. Net profits recorded Rmb1.9bn, ahead of Bloomberg consensus of Rmb1.4bn and up 7.3% YoY. This is driven by a one-off tax credit of Rmb397mn. Such credit arose from the reversal of deferred tax assets on earlier investments markdowns. In this half, the company reported higher investment income at Rmb7.3bn, up 7.2% YoY, despite an impairment loss of Rmb2.0bn on equity investments. At the same time, NCI recorded an unrealized valuation gain of Rmb1.6bn from its bond portfolio. We view this as a satisfactory result.

Average investment results. Investment results were largely in-line with peers. Gross investment yield was 3.6% for the half (versus 3.9% of China Pacific and 3.7% of Ping An). Net investment yield was 4.4% during the same period (weaker than 4.9% of China Pacific, parallel with 4.5% of Ping An and China Life). We view the impairment loss of Rmb2.0bn on equity investments a removal of future drag to investment results. At end-Jun, NCI placed only Rmb33.4bn, or 7.4% of investment assets, on equity investments, lower than an average of 12% allocation to equities by peers. Such a prudent investment policy may safeguard NCI's investment results against the feeble A-share markets in 2H12.

Satisfactory but not exciting life underwriting results. VNB went down 1.4% YoY despite a 6.6% YoY decline of FYP and 11.2% YoY drop of APE. But NBM improvement was minimal during the half. NCI still relies heavily on the bancassurance sales, which embed lower NBM than agency. In 1H12, 68.2% of NCI's FYP was derived from the bancassurance channels. This is compared to 60% or less of China Life, China Pacific and Ping An.

Stable solvency. Solvency ratio edged up 2ppt HoH to 158% in 1H12. After the planned sub-debt issuance of Rmb10bn in 4Q12, the ratio will further improve to >200%. However, NCI has a very limited room to further issue sub-debts, in accord to the 50% NAV limit set by CIRC. With shareholders' equity at Rmb35bn in 1H12, additional sub-debt issuance will be limited to Rmb2bn.



New China Life: 1H12 profit & loss

	2009	2010	2011	1H10	2H10	1H11	2H11	1H12	HoH	YoY
	RMBmn	RMBmn	RMBmn	RMBmn	RMBmn	RMBmn	RMBmn	RMBmn	Chg (%)	Chg (%)
GWP & Policy fees	65,422	91,956	95,151	53,675	38,281	50,843	44,308	56,114	27	10
(-) Premiums to Reinsurers	(30)	(32)	(584)	(18)	(14)	(238)	(346)	(40)	(88)	(83)
NWP & Policy fees	65,452	91,988	95,735	53,693	38,295	51,081	44,654	56,154	26	10
Chg. in Unearned Premium Res.	(72)	(128)	(71)	(165)	37	(193)	122	(227)	(286)	18
NEP & policy fees	65,380	91,860	95,664	53,528	38,332	50,888	44,776	55,927	25	10
Investment income	8,362	10,521	12,754	4,114	6,407	6,813	5,941	7,303	23	7
Other income	164	328	192	118	210	101	91	83	(9)	(18)
Total revenue	73,906	102,709	108,610	57,760	44,949	57,802	50,808	63,313	25	10
Claims & Life insurance benefits	(10,763)	(13,250)	(21,178)	(5,908)	(7,342)	(9,896)	(11,282)	(12,046)	7	22
Div. & Int. to PH & Net Inc. in PH Res.	(46,961)	(71,133)	(66,608)	(43,333)	(27,800)	(37,966)	(28,642)	(40,494)	41	7
Ttl. Claims / PH Benefits	(57,724)	(84,383)	(87,786)	(49,241)	(35,142)	(47,862)	(39,924)	(52,540)	32	10
U/W & Policy Acq. Expense	(5,623)	(7,252)	(7,317)	(3,884)	(3,368)	(3,689)	(3,628)	(3,825)	5	4
General & Administrative Expense	(7,206)	(8,410)	(9,229)	(3,925)	(4,485)	(3,998)	(5,231)	(4,517)	(14)	13
Other Expense	(509)	(147)	(199)	194	(341)	108	(307)	(135)	(56)	(225)
Total Expenses	(13,338)	(15,809)	(16,745)	(7,615)	(8,194)	(7,579)	(9,166)	(8,477)	(8)	12
Net profit before Tax	2,844	2,517	4,079	904	1,613	2,361	1,718	2,296	34	(3)
Associate P&L and Finance Cost	(193)	(262)	(804)	(62)	(200)	(311)	(493)	(788)	60	153
Tax Expense	10	(5)	(475)	(265)	260	(275)	(200)	397	(299)	(244)
Net profit after Tax	2,661	2,250	2,800	577	1,673	1,775	1,025	1,905	86	7
Minority interest	(1)	(1)	(1)	0	(1)	0	(1)	(1)	0	0
NP to New China Life Shareholders	2,660	2,249	2,799	577	1,672	1,775	1,024	1,904	86	7

Source: Company, ABCI Securities

New China Life: Embedded Value (EV), Value of New Business (VNB) & New Business Margins (NBM)

(Rmb mn)	1H12	2011	1H11	2010	2009	% HoH	% YoY
ANAV	26,348	21,966	17,673	6,400		20	49
VIF	40,257	36,818	33,798	29,866		9	19
Solvency Cost	(10,456)	(9,793)	(9,149)	(8,181)		7	14
EV	56,150	48,991	42,322	28,085		15	33
EVPS (HK\$)	22.16	19.22	19.70	27.85		15	12
APE	10,040	19,494	11,302	25,297	20,466	23	(11)
VNB	2,338	4,360	4,710	4,741		18	(1)
NBM (APE Basis %)	23.29	22.37	41.67	18.74		0.92	2.30
FYP	22,523	42,863	24,112	55,966	44,769	20	(7)
VNB	2,338	4,360	4,710	4,741		18	(1)
NBM (FYP Basis %)	10.38	10.17	19.53	8.47		0.21	0.54
VNB (HK\$)	0.92	1.71	2.19	4.70		52	(16)

Source: Company, ABCI Securities

New China Life: Investment & Yields

(%)	1H12	2011	1H11	2010	2009	% HoH	% YoY
Cash Equivalents	6.8	5.6	5.8	9.3	6.4	1.2	1.0
Deposits	36.0	32.9	30.2	18.9	9.6	3.1	5.8
Bonds	46.8	50.9	52.3	56.2	70.2	(4.1)	(5.5)
Equities	7.4	7.8	9.2	13.3	11.7	(0.4)	(1.8)
Others	3.0	2.8	2.5	2.3	2.1	0.2	0.5
Total Inv'ts (RMB bn)	453	374	335	293	197	21.1	35.4
Net Investment Yield (%)	4.40	4.10	4.00	3.80	3.90	0.30	0.40
Total Investment Yield (%)	3.60	3.80	4.40	4.30	4.60	(0.20)	(0.80)

Source: Company, ABCI Securities



New China Life: Operating data

(Rmb mn)	1H12	2011	1H11	2010	2009	% HoH	% YoY
Gross premiums	55,950	94,797	50,662	91,679	65,040	27	10
Individual Agency	23,030	35,871	18,791	28,688	20,248	35	23
Banc.	31,393	56,692	30,731	61,690	43,962	21	2
Wealth Management	622	932	368	221		10	69
Group	905	1,302	772	1,080	830	71	17
FYP Regular	8,653	16,897	9,879	21,889	17,766	23	(12)
% of FYP Ind. Regular	38.4	39.4	41.0	39.1	39.7	(1.0)	(2.6)
# of agents	207,000	200,000	204,380	198,771	226,776	3	1
FYP Regular per agent (Rmb)	41,802	44,390	24,009	47,924	29,637	(6)	74
Individual FYP	5,851	9,758	5,374	10,416	7,299	(40)	9
Individual FYP per agent (Rmb)	28,266	48,790	26,294	52,402	32,186	(42)	7
Persistency 13 mo (%)	90.6	91.5	92.4	91.7	89.4	(0.9)	(1.8)
Solvency (%)	159	156.0	106.1	35.0	36.2	2.8	52.7

Source: Company, ABCI Securities

New China Life: Embedded Value (EV) Movement Analysis

	2010 RMB mn	2011 RMB mn	1H11 RMB mn	1H12 RMB mn
Embedded Value				
Adjusted net worth	6,400	21,966	17,673	26,348
Value of in-force	29,866	36,818	33,798	40,257
Cost of solvency margin	(8,181)	(9,793)	(9,149)	(10,456)
Embedded value	28,085	48,991	42,322	56,149
Vnb (long term)	5,095	4,681	2,558	2,419
EV Movement Analysis				
Opening Embedded Value	20,333	28,084	28,084	48,991
Expected return	2,654	3,858	1,974	2,430
Value of New Business (VNB)	5,095	4,681	2,558	2,419
Inv't R Var + Mkt Val Adj	(203)	(11,894)	(4,168)	2,539
Capital Raising & Dividends	0	25,621	14,000	(221)
OpEx Var, Model Chg & Others	204	(1,359)	(125)	(9)
Closing Embedded Value	28,083	48,991	42,323	56,149
EVPS (HK\$)	27.85	19.22	19.70	22.16
VNB (HK\$)	5.05	1.84	1.19	0.95
EV Contributions 1				
Expected Return on Beg EV	13%	14%	7%	5%
IRV + MVA Contribution to Beg EV	-1%	-42%	-15%	5%
VNB Contribution to Beg EV	25%	17%	9%	5%
VNB Contribution to Beg VIF	17%	16%	8%	6%
EVPS (HK\$) Growth		-31%		
EV Contributions 2				
Beginning EV	72%	57%	66%	87%
Expected return	9%	8%	5%	4%
Inv't R Var + Mkt Val Adj	-1%	-24%	-10%	5%
Value of New Business (VNB)	18%	10%	6%	4%
Capital Raising & Dividends	0%	52%	33%	0%
OpEx Var, Model Chg & Others	1%	-3%	0%	0%
Ending EV	100%	100%	100%	100%

Source: Company, ABCI Securities



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