



Company Report

China Life (2628 HK) – Buy Life & Health Insurance Industry

Key data

H-share price (HK\$)	22.55
Target price (HK\$)	26.45
Upside potential (%)	17.29
52Wk H/L(HK\$)	24.7 / 17.0
Issued shares:	
H-shares (mn)	7,441
A-shares (mn)	20,823
H-share mkt cap (HK\$m)	637,353
30-day avg vol (HK\$m)	688.1
Major shareholders (%):	
China Life Group	68.4
JPMorgan Chase	4.9

Source: Company & Bloomberg

Revenue breakdown in 2011 (%)

Net earned premiums (NEP)	85.8
Investment income	13.4
Other income	0.8

*Based on 2011 results

Source: Company

Share performance (%)

	Absolute	Relative*
1-mth	0.7	(3.4)
3-mth	5.1	(1.7)
6-mth	7.4	11.3

*Relative to MSCI China

Source: Bloomberg

1 year price performance



Source: Bloomberg

Analyst

Report Date: 29 October 2012

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Only a hiccup (3Q12 results review)

China Life reported a weak 3Q12 result, with net loss of Rmb2.2bn. However, we view this as a hiccup, instead of a weakening trend. Its comprehensive loss was trimmed to Rmb1.3bn from Rmb20.9bn a year ago. Most importantly, shareholders' equity remained flattish QoQ at Rmb214bn, despite an investment loss led by a 6.3% decline in A-share market. Therefore, we remain positive on China Life.

Net profits pinched by big impairment losses. Impairment losses on investments reached Rmb13.9bn in 3Q12 and Rmb29.0bn in 9M12, due to a 6.3% decline in A-share markets and about 1.5% drop in bond prices in the quarter. As such, China Life reported net loss of Rmb2.1bn in 3Q12, compared to net profit of Rmb3.8bn a year ago. However, comprehensive loss narrowed from Rmb20.9bn in 3Q11 to Rmb1.3bn in 3Q12, implying better overall performance on available-for-sale (AFS) investments.

Better than expected impact to AFS reserves. The company reported other comprehensive income of Rmb844mn in 3Q12, reflecting a gain in AFS reserves of a similar magnitude. In fact, capital reserves in equity increased 60.3% to Rmb53.9bn in 9M12. The increment of Rmb19.7bn is equivalent to 5.9% of 1H12 EV (Rmb334.3bn), exceeding our expectation. Notably, the impact of positive investment variance to EV is yet to be disclosed. We estimate EV to improve 19.0% YoY to Rmb348.5bn, partly due to the Rmb20.7bn increase in shareholder funds revealed in 9M12.

Lower IFRS profit forecast. While we are not concerned with the temporary setback in China Life's profitability, we adjusted down our IFRS profit forecast to Rmb13.1bn (Rmb23.8bn previously) in 2012E, due to the net loss reported in 3Q12. Notwithstanding, we maintain our profit forecast of Rmb29.3bn in 2013E.

Maintain BUY and TP at HK\$26.45. We maintain an appraisal value of Rmb598.1bn for 2013E, and adopt it as TP, or HK\$26.45/ share. The implied valuation of our TP is 1.53x 2013E PEV and 10.0x 2013E VNB. This represents 17.3% upside potential from the current share price. As such, we maintain our BUY recommendation on China Life.

Risk factors: worse-than-expected underwriting and investment performance, tighter-than-expected regulations

Results and valuation

FY ended Dec 31	2010	2011	2012E	2013E	2014E
Revenue (Rmb mn)	385,838	370,899	370,337	413,098	443,885
Chg (% YoY)	13.7	(3.9)	(0.2)	11.5	7.5
Net profit (Rmb mn)	33,626	18,331	13,052	29,332	35,938
Chg (% YoY)	2.3	(45.5)	(28.8)	124.7	22.5
EPS (HK\$)	1.42	0.79	0.57	1.30	1.68
PER (x)	15.8	28.4	39.7	17.4	13.4
BPS (HK\$)	8.8	8.3	9.2	10.2	11.9
P/B (x)	2.5	2.7	2.4	2.2	1.9
EVPS (HK\$)	12.6	12.6	15.2	17.2	20.4
PEV (x)	1.8	1.8	1.5	1.3	1.1
VNB (HK\$)	0.8	0.9	0.9	0.9	1.0
VNB (x)	11.8	11.2	8.3	5.8	2.2

Source: Company data, ABCI Securities estimates



China Life: 3Q12/ 9M12 profit & loss

(RMB mn)	3Q12 CAS	3Q11 CAS	% YoY Chg	9M12 CAS	9M11 CAS	% YoY Chg
GWP	77,618	68,727	12.9%	263,056	264,217	-0.4%
Premiums to Reinsurers	(138)	(63)	119.0%	(289)	(187)	54.5%
NWP	77,480	68,664	12.8%	262,767	264,030	-0.5%
Chg. In Unearned Premium Reserves	(1,206)	(745)	61.9%	(1,754)	(1,262)	39.0%
NEP	76,274	67,919	12.3%	261,013	262,768	-0.7%
Investment Income	19,065	15,033	26.8%	58,477	50,899	14.9%
Net Fair Value & Forex Gains / Losses	(916)	(647)	41.6%	(1,275)	(729)	74.9%
Other Income	821	627	30.9%	2,289	1,888	21.2%
Total Revenue	95,244	82,932	14.8%	320,504	314,826	1.8%
Insurance Benefits & Claims	(24,883)	(25,042)	-0.6%	(93,274)	(88,571)	5.3%
Increase in Insurance Liabilities	(48,068)	(38,620)	24.5%	(148,136)	(155,550)	-4.8%
Policyholders Dividends (Participating)	1,398	(644)	-317.1%	(1,097)	(6,428)	-82.9%
Underwriting & Policy Acq. Costs	(6,130)	(5,726)	7.1%	(20,699)	(21,069)	-1.8%
G&A Exp.	(5,261)	(4,568)	15.2%	(15,473)	(13,979)	10.7%
Other Expenses (incl. Impairment losses)	(15,911)	(3,899)	308.1%	(34,408)	(9,880)	248.3%
Total Benefits, Claims & Expenses	(98,855)	(78,499)	25.9%	(313,087)	(295,477)	6.0%
Non-operating Profit / Loss	(7)	(23)	-69.6%	(23)	(12)	91.7%
Profit Before Tax	(3,618)	4,410	-182.0%	7,394	19,337	-61.8%
Tax Expenses	1,467	(609)	-340.9%	196	(2,462)	-108.0%
Net Profit	(2,151)	3,801	-156.6%	7,590	16,875	-55.0%
Total Other Comprehensive Income / Loss	844	(24,731)	-103.4%	19,667	(38,072)	-151.7%
Total Comprehensive Income / Loss						
(Net Profit + Other Comp. Income / Loss)	(1,307)	(20,930)	-93.8%	27,257	(21,197)	-228.6%
Operating Ratios			% YoY Chg			% YoY Chg
NEP as % of Total Income	80%	82%	-1.8%	81%	83%	-2.0%
Total Inv't Income as % of Total Income	19%	17%	1.7%	18%	16%	1.9%
Insurance Benefits & Claims as % of NEP	-33%	-37%	4.2%	-36%	-34%	-2.0%
Increase in Insurance Liabilities as % of NEP	-63%	-57%	-6.2%	-57%	-59%	2.4%
Policyholders Dividends (Participating) as % of NEP	2%	-1%	2.8%	0%	-2%	2.0%
Underwriting & Policy Acq. Costs as % of NEP	-8%	-8%	0.4%	-8%	-8%	0.1%
G&A Exp. as % of Total Income	-6%	-6%	0.0%	-5%	-4%	-0.4%
Total Other Comp Inc / Loss as % of Net Profit	-39%	-651%	611.4%	259%	-226%	484.7%

Source: Company, ABCI Securities

China Life: 9M12 investment asset mix

(RMB mn)	9M12	2011	% 9M Chg
Cash Funds	48,067	55,971	-14.1%
Trading Securities	46,263	23,640	95.7%
Policy Loans	38,009	32,321	17.6%
Debt Plan Investments	37,203	28,783	29.3%
Term Deposits	618,823	520,793	18.8%
AFS Fin. Assets	491,540	562,948	-12.7%
HTM Securities	387,377	261,933	47.9%
Long Term Equity	27,022	24,448	10.5%
Total Inv't Assets	1,694,304	1,510,837	12.1%
Gross Inv't Yield	2.17%	3.51%	-1.3%

Source: Company, ABCI Securities

China Life: 9M12 balance sheet snapshot

(RMB mn)	9M12	2011	% 9M Chg
Total Assets	1,783,808	1,583,907	12.6%
Total Liabilities	1,569,729	1,390,519	12.9%
Shareholders Equity	214,079	193,388	10.7%

Source: Company, ABCI Securities



China Life: Embedded Value

(Rmb mn)	2009	2010	2011	2012E	2013E	1H12
Embedded value						
Adjusted net worth	159,948	144,655	110,266	128,817	145,755	136,286
Value of in-force	149,387	183,008	215,608	252,330	278,651	232,639
Cost of solvency margin	(24,106)	(29,564)	(33,020)	(32,614)	(34,571)	(34,598)
Embedded value	285,229	298,099	292,854	348,533	389,836	334,326
Vnb (long term)	17,713	19,839	20,199	20,399	20,855	12,494
Multiplier	10	9	9	10	10	
New business value (long term)	175,344	179,381	187,849	197,817	208,354	
Appraisal value	460,573	477,480	480,703	546,351	598,189	
EV movement analysis						
Opening embedded value	240,088	285,229	298,099	292,854	348,533	292,854
Expected return						
- SHF's	7,580	8,797	7,650	6,065	7,085	4,944
- In-force	13,519	16,433	20,131	23,717	27,756	9,234
Value of new business (VNB)	17,713	19,839	20,199	20,399	20,855	12,494
Inv't r var + Mkt val adj	15,307	(11,234)	(40,839)	12,000	(5,500)	19,429
Capital raising & dividends	(6,500)	(19,785)	(11,306)	(6,501)	(6,894)	(6,501)
OpEx var, model chg & others	(2,478)	(1,180)	(1,080)	-	(2,000)	1,872
Closing embedded value	285,229	298,099	292,854	348,533	389,836	334,326
EVPS (HK\$)	11.45	12.57	12.61	15.17	17.24	14.55
AVPS (HK\$)	18.49	20.13	20.71	23.78	26.45	
PEV implied	1.61	1.60	1.64	1.57	1.53	
VNB (HK\$)	0.71	0.84	0.87	0.89	0.92	
VNB implied (x)	9.90	9.04	9.30	9.70	9.99	
EV contributions 1 (%)						
Expected return on beg EV	9%	9%	9%	10%	10%	10%
IRV + MVA contribution to beg EV	6%	-4%	-14%	4%	-2%	13%
VNB contribution to beg EV	7%	7%	7%	7%	6%	9%
VNB contribution to beg VIF	14%	13%	11%	9%	8%	
EVPS (HK\$) growth	19%	10%	0%	20%	14%	
EV contributions 2 (%)						
Beginning EV	84%	96%	102%	84%	89%	88%
Expected return						
- SHF's	3%	3%	3%	2%	2%	1%
- In-force	5%	6%	7%	7%	7%	3%
Inv't r var + mkt val adj	5%	-4%	-14%	3%	-1%	6%
Value of new business (VNB)	6%	7%	7%	6%	5%	4%
Capital raising & dividends	-2%	-7%	-4%	-2%	-2%	-2%
OpEx var, model chg & others	-1%	0%	0%	0%	-1%	1%
Ending EV	100%	100%	100%	100%	100%	100%

Source: Company data, ABCI Securities estimates



China Life Financial Statements

Profit & loss (Rmb mn)						Operating ratios (%)					
	2010	2011	2012E	2013E	2014E		2010	2011	2012E	2013E	2014E
GWP & policy fees	318,229	318,252	314,338	333,198	353,190	Gross written premium growth	15.3%	0.0%	-1.2%	6.0%	6.0%
(-) Premiums to reinsurers	177	232	280	431	457	Net earned premium growth	15.6%	0.1%	-2.3%	6.0%	6.0%
NWP & policy fees	318,052	318,020	314,058	332,767	352,733	Claims/benefits - of NEP	25.1%	34.3%	36.5%	31.5%	31.5%
Chg. in unearned premium res.	(36)	(256)	3,169	3,278	3,475	Div to PH & net inc. in PH res. of NEP	62.8%	57.1%	57.8%	60.5%	60.5%
NEP & policy fees	318,088	318,276	310,889	329,489	349,258	Ttl. claim/PH benefits to NEP	87.9%	91.3%	94.3%	92.0%	92.0%
Investment income	64,993	49,851	56,409	80,418	91,277	Claims/benefits - of total revenue	20.7%	29.4%	30.7%	25.1%	24.8%
Other income	2,757	2,772	3,039	3,190	3,350	Net inc. in PH res. - of total revenue	51.7%	49.0%	48.5%	48.3%	47.6%
Total revenue	385,838	370,899	370,337	413,098	443,885	Ttl. claim/PH benefits to total revenue	72.5%	78.4%	79.2%	73.4%	72.4%
Claims, surrenders, annuities/maturities	(95,151)	(117,294)	(120,846)	(121,911)	(129,226)	Commission cost ratio	0.0%	0.0%	0.0%	0.0%	0.0%
Div. & int. to PH & net inc. in PH res.	(199,655)	(181,579)	(179,703)	(199,341)	(211,301)	General & admin. cost ratio	6.4%	6.8%	8.0%	6.8%	6.8%
Ttl. claims/PH benefits	(294,806)	(298,873)	(300,550)	(321,252)	(340,527)	Other exp. & stat. levy ratio	1.3%	1.5%	1.8%	1.6%	1.6%
Commission expenses	0	0	0	0	0	Operating expense ratio	7.7%	8.3%	9.8%	8.4%	8.4%
U/W & policy acq. expense	(27,256)	(27,434)	(26,553)	(30,012)	(31,813)	Gross investment yield	5.2%	3.5%	3.5%	4.3%	4.3%
General & administrative expense	(20,285)	(21,549)	(24,951)	(22,444)	(23,790)	Solvency ratio	212.0%	170.1%	211.7%	197.4%	189.2%
Other expense	(4,254)	(4,743)	(5,625)	(5,291)	(5,609)						
Total expenses	(51,795)	(53,726)	(57,130)	(57,747)	(61,212)						
Net profit before tax	39,237	18,300	12,657	34,099	42,147	Balance sheet (Rmb mn)					
Associate/JV - Profits/losses	1,771	2,213	2,669	2,936	3,230		2010	2011	2012E	2013E	2014E
Tax expense	(7,197)	(2,022)	(2,134)	(7,407)	(9,075)	Cash	47,854	55,985	92,797	105,509	119,282
Net profit after tax	33,811	18,491	13,193	29,628	36,301	Investments	1,288,391	1,438,984	1,653,190	1,879,657	2,125,024
Minority interest	(185)	(160)	(141)	(296)	(363)	Receivables	7,274	8,253	15,974	17,611	19,416
NP to China Life shareholders	33,626	18,331	13,052	29,332	35,938	Deferred acquisition costs	0	0	0	0	0
						Fixed assets	18,946	20,231	20,321	20,321	20,321
						Other assets	48,114	60,454	72,010	72,010	72,010
						Total assets	1,410,579	1,583,907	1,854,292	2,095,108	2,356,053
Financial summary						Policyholder benefits	1,070,963	1,245,741	1,426,145	1,640,313	1,867,331
	2010	2011	2012E	2013E	2014E	Policyholder deposits	70,171	69,797	68,051	71,346	74,839
EPS (HK\$)	1.42	0.79	0.57	1.30	1.68	Unearned premiums	1,880	3,719	5,363	8,641	12,116
<i>EPS growth (%)</i>	7.4%	-44.3%	-28.1%	128.4%	29.4%	Claim reserves	0	0	0	0	0
PER (x)	15.9	28.6	39.7	17.4	13.4	Payables	8,275	3,719	2,879	3,174	3,500
PBV (x)	2.56	2.73	2.45	2.21	1.89	Repo	22,660	13,000	42,529	42,529	42,529
PEV (x)	1.79	1.79	1.49	1.31	1.11	Borrowings	0	29,990	57,982	57,982	57,982
VNB multiple (x)	11.93	11.42	8.32	5.76	2.20	Statutory insurance fund	194	146	192	192	192
Dividend per share (HK\$)	0.48	0.28	0.30	0.30	0.30	Other liabilities	25,961	24,407	37,312	38,358	39,475
Yield (%)	2.9%	1.7%	1.8%	1.8%	1.8%	Total liabilities	1,200,104	1,390,519	1,640,454	1,862,536	2,097,963
Payout ratio (%)	33.6%	35.5%	52.8%	23.1%	17.9%	Net assets	210,475	193,388	213,838	232,572	258,090
Return on equity (%)	15.9%	9.1%	6.4%	13.1%	14.6%	Minority interests	1,765	1,858	1,948	2,244	2,607
Return on assets (%)	2.6%	1.2%	0.8%	1.5%	1.6%	Net equity to shareholders	208,710	191,530	211,890	230,328	255,483
Tax rate (%)	17.6%	9.9%	13.9%	20.0%	20.0%						

Source: Company data, ABCI Securities estimates



Disclosures

Analyst Certification

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Definition of equity rating

Rating	Definition
Buy	Stock return \geq Market return rate
Hold	Market return $- 6\% \leq$ Stock return $<$ Market return rate
Sell	Stock return $<$ Market return $- 6\%$

Stock return is defined as the expected % change of share price plus gross dividend yield over the next 12 months

Market return: 5-year average market return rate from 2007-2011

Time horizon of share price target: 12-month

Definition of share price risk

Rating	Definition
Very high	$2.6 \leq$ 180 day volatility/180 day benchmark index volatility
High	$1.5 \leq$ 180 day volatility/180 day benchmark index volatility $<$ 2.6
Medium	$1.0 \leq$ 180 day volatility/180 day benchmark index volatility $<$ 1.5
Low	180 day volatility/180 day benchmark index volatility $<$ 1.0

We measure share price risk by its volatility relative to volatility of benchmark index.

Benchmark index: Hang Seng Index.

Volatility is calculated from the standard deviation of day to day logarithmic historic price change. The 180-day price volatility equals the annualized standard deviation of the relative price change for the 180 most recent trading days closing price.

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