



Company Report

New China Life (1336 HK) – Hold Life & Health Insurance Industry Initiation

Key data

H-share price (HK\$)	24.85
Target price (HK\$)	24.85
Upside potential (%)	0.0
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\$m)	88,760
30-day avg vol (HK\$m)	57.2
Major shareholder (%):	
Central Huijin	31.2
Baosteel Group	15.1

Source: Company & Bloomberg

Revenue breakdown in 2011 (%)

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

*Based on 2011 results

Source: Company

Share performance (%)

	Absolute	Relative*
1-mth	9.2	3.7
3-mth	(14.7)	(20.4)
6-mth	(20.4)	(21.4)

*Relative to MSCI China

Source: Bloomberg

1 year price performance



Source: Bloomberg

Analyst

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Cheap for good reasons

New China Life is trading at a low valuation for good reasons. The company disappointed the market by reporting the lowest NBM among peers in 1H12. Also, its premium growth decelerated fast since 1Q12. Lastly, the company's EV is the least sensitive to equity values, and hence a potential recovery of A-share markets. Based on these, we initiate coverage on New China Life with a HOLD recommendation.

With the lowest NBM. New China Life reported its NBM at 23.3% in 1H12. It has improved by only 0.9ppt HoH. Also, its NBM is the lowest among peers. As a result, the company suffered from a YoY decline of 1.4% in VNB. All these undershot the market expectation. Therefore, we hold a negative stance towards its Life underwriting going forward.

EV insensitive to investment upturn. 10% change in equity values will lead to 1.7% change in New China Life's EV in 1H12. This is low compared to 5.4% of China Life, 2.8% of Ping An, 5.5% of China Taiping. In 1H12, New China Life allocated Rmb33.4bn, or 7.4% of investment portfolio, in equity. We expect the insurer to benefit the least from the upcoming recovery of A-share markets.

Trading at a low valuation. New China Life closed at HK\$23.1, 17.5% lower than its H-share IPO price of HK\$28.0. It is trading at 0.90x 2013E PEV and (1.5)x 2013E VNB, much cheaper than the sector average of 1.07x 2013E PEV. We expect New China Life to grow its EVPS by 24.7% YoY in 2012E and 15.7% YoY in 2013E. In spite of several weaknesses in its operations, the stock is trading at a very low valuation.

Initiate coverage with a BUY rating; TP of HK\$24.85. We derive an appraisal value of Rmb62,016 mn for 2013E, also adopting it as TP, or HK\$24.85/ share. The implied valuation of our TP is 0.90x 2013E PEV and (1.5)x 2013E VNB. This represents nil upside potential from the current share price. We initiate coverage of New China Life with a HOLD recommendation.

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

Results and valuation

FY ended Dec 31	2010	2011	2012E	2013E	2014E
Revenue (Rmb mn)	102,709	108,610	123,043	137,935	153,513
Chg (YoY)	39.0	5.7	13.3	12.1	11.3
Net profit (Rmb mn)	2,249	2,799	3,435	4,266	5,145
Chg (YoY)	(15.5)	24.5	22.7	24.2	20.6
EPS (HK\$)	2.23	1.51	1.35	1.71	2.18
PER (x)	11.1	16.4	18.3	14.5	11.4
BPS (HK\$)	6.5	12.3	14.7	16.8	20.2
P/B (x)	3.8	2.0	1.7	1.5	1.2
EVPS (HK\$)	27.9	19.1	23.9	27.6	33.5
PEV (x)	0.9	1.3	1.0	0.9	0.7
VNB (HK\$)	4.71	1.70	1.83	1.83	1.90
VNB (x)	(0.6)	3.4	0.5	(1.5)	(4.6)

Source: Company data, ABCI Securities estimates



Investment Positives

Trading at a low valuation. New China Life closed at HK\$24.85, 11.3% lower than its H-share IPO price of HK\$28.0. It is trading at 0.90x 2013E PEV and (1.5)x 2013E VNB, much cheaper than the sector average of 1.07x 2013E PEV. We expect New China Life to grow its EVPS by 24.7% YoY in 2012E and 15.7% YoY in 2013E. In spite of several weaknesses in its operations, the stock is trading at a very low valuation.

Potential entry to MSCI China-H Index. New China Life A-share was included into MSCI China A Index in May. Also, the stock was included in FTSE China Index upon its IPO in Dec 2011. Currently, New China Life is trading at a market cap of US\$3.0bn and H-share free float market cap of US\$1.0. This is compared to US\$2.6bn and US\$1.2bn of China Taiping. China Taiping is currently a constituent of MSCI China, with about 0.3% weighting. As a result, we believe there is a genuine chance for New China Life to be included into MSCI China H Index. This will in turn attract more passive institutional fund flow to the stock.

High EV operating margins. In 2011, New China Life's EV operating margins was 31.1% 15.9%, higher than 15.9% of China Life, 23.6% of Ping An and 29.7% of Taiping Life. Given the low base effect, we expect New China Life to outgrow its peers in EV in the future.

Investment Concerns

With the lowest NBM. Investors put high hope on New China Life for its margin improvement and VNB growth in early 2012. However, the company failed to deliver up to market expectation on these fronts in 1H12. In fact, New China Life reported its NBM 23.3% in 1H12. It has improved by only 0.9ppt HoH, in spite of a higher contribution from long term regular premium sales. Also, its NBM is the lowest among peers. Its peers averaged 35.5% ion NBM during the same half. As a result, the company suffered from a YoY decline of 1.4% in VNB. Therefore, we are not optimistic of the Life underwriting of New China Life going forward.

Volume weakening. The total premium growth has started to decelerate for New China Life since 2Q12. Total premiums grew 5.8% YoY in 8M12, compared with 16.0% YoY in 3M12. FYP dropped by 6.6% in 1H12. We expect further deceleration for its premium growth in 2H12.

EV insensitive to investment upturn. Per the company disclosure, 10% change in equity values will lead to 1.7% change in New China Life's EV in 1H12. This is low compared to 5.4% of China Life, 2.8% of Ping An, 5.5% of China Taiping. In 1H12, New China Life allocated Rmb33.4bn, or 7.4% of investment portfolio, in equity. We expect the insurer to benefit the least from the upcoming recovery of A-share markets.



Valuation & Recommendation

We forecast high-teens EV Growth. New China Life reported group EV of Rmb48,991 mn in 2011 and Rmb56,149 mn in 1H12. In 2012E, we expect the company to report investment return variance of Rmb2,600 mn, due to slightly improved capital markets in China, compared to 2011. Besides, we forecast VNB of Rmb4,630 mn in 2012E and Rmb4,570 mn in 2013E, on the back of weak NBM's averaging 24.3%. As such, we forecast the EV to reach Rmb60,536 mn in 2012E, up 23.6% YoY, and Rmb68,933 mn in 2013E, up 13.9% YoY.

Expecting earnings growth. Based on a net premium growth of 6.0% YoY and gross investment yield of 4.3%, we estimate China Life to report net earnings of Rmb4,266 mn in 2013E, up 24.2% YoY from Rmb3,435 mn in 2012E. Our earnings forecast is in-line with consensus of Rmb4,250 mn.

TP and recommendation. Based on the aforementioned assumptions, we derive an appraisal value of Rmb62,016 mn for New China Life in 2013E and also adopt it as our target price. It is equivalent to HK\$24.85/ share. We forecast 2013E EVPS and VNB of HK\$27.62 and HK\$1.83, respectively. The implied valuation of our TP is 0.90x 2013E PEV and (1.5)x 2013E VNB. This represents nil upside potential from the current share price. We initiate coverage of New China Life with a HOLD recommendation.



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
Persistence 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 - share price & valuation

		NEW CHINA LIFE	
		2011	2012E
Share Price (HK\$)	Hi	28.10	36.28
	Lo	23.41	21.55
	Av	24.90	29.04
PEV(X)	Hi	1.47 x	1.52 x
	Lo	1.22 x	0.90 x
	Av	1.30 x	1.22 x
EVPS YoY Growth (%)		-31%	25%
VNB(X)	Hi	5.26 x	6.80 x
	Lo	2.51 x	(1.27x)
	Av	3.38 x	2.84 x
VNB YoY Growth (%)		-64%	7%

Source: Bloomberg, Company data, ABCI Securities

New China Life: Embedded Value

(Rmb mn)	2010	2011	2012E	2013E	1H12
Embedded value					
Adjusted net worth	6,400	21,966	27,501	29,766	26,348
Value of in-force	29,866	36,818	44,004	51,231	40,257
Cost of solvency margin	(8,181)	(9,793)	(10,968)	(12,065)	(10,456)
Embedded value	28,085	48,991	60,536	68,933	56,149
Vnb (long term)	4,741	4,360	4,630	4,570	2,419
Multiplier	(2)	(1)	(2)	(2)	
New business value (long term)	(9,515)	(5,297)	(7,802)	(6,917)	
Appraisal value	18,570	43,694	52,734	62,016	
EV movement analysis					
Opening embedded value	20,333	28,383	49,290	60,536	48,991
Expected return					
- SHF's	300	333	1,142	1,430	535
- In-force	2,654	3,525	4,234	5,060	1,895
Value of new business (VNB)	5,095	4,681	4,971	4,906	2,419
Inv't r var + Mkt val adj	(203)	(11,894)	2,600	(2,000)	2,539
Capital raising & dividends	-	25,621	(500)	-	(221)
OpEx var, model chg & others	204	(1,359)	(1,200)	(1,000)	(9)
Closing embedded value	28,383	49,290	60,536	68,933	56,149
EVPS (HK\$)	27.89	19.14	23.87	27.62	22.16
AVPS (HK\$)	18.44	17.07	20.79	24.85	
PEV implied	0.66	0.89	0.87	0.90	
VNB (HK\$)	4.71	1.70	1.83	1.83	
VNB implied (x)	(2.01)	(1.21)	(1.69)	(1.51)	
EV contributions 1 (%)					
Expected return on beg EV		14%	11%	11%	5%
IRV + MVA contribution to beg EV		-42%	5%	-3%	5%
VNB contribution to beg EV		17%	10%	8%	5%
VNB contribution to beg VIF		16%	14%	11%	6%
EVPS (HK\$) growth		-31%	25%	16%	
EV contributions 2 (%)					
Beginning EV	72%	58%	81%	88%	87%
Expected return					
- SHF's	1%	1%	2%	2%	
- In-force	9%	7%	7%	7%	4%
Inv't r var + mkt val adj	-1%	-24%	4%	-3%	5%
Value of new business (VNB)	18%	9%	8%	7%	4%
Capital raising & dividends	0%	52%	-1%	0%	0%
OpEx var, model chg & others	1%	-3%	-2%	-1%	0%
Ending EV	100%	100%	100%	100%	100%

Source: Company data, ABCI Securities estimates



New China Life Financial Statements

Profit & loss (Rmb mn)						Operating ratios (%)					
	2010	2011	2012E	2013E	2014E		2010	2011	2012E	2013E	2014E
GWP & policy fees	91,956	95,151	106,569	117,226	128,949	Gross written premium growth	40.6%	3.5%	12.0%	10.0%	10.0%
(-) Premiums to reinsurers	32	584	213	234	258	Net earned premium growth	40.5%	4.1%	11.5%	10.0%	10.0%
NWP & policy fees	91,988	95,735	106,782	117,460	129,207	Claims/benefits - % of NEP	90.9%	91.1%	92.8%	93.5%	94.5%
Chg. in unearned premium res.	(128)	(71)	(107)	(117)	(129)	Div to PH & net inc. in PH res. % of NEP	0.8%	0.7%	1.0%	1.0%	1.0%
NEP & policy fees	91,860	95,664	106,675	117,343	129,077	Ttl. claim/PH benefits to NEP	91.8%	91.7%	93.8%	94.5%	95.5%
Investment income	10,521	12,754	16,194	20,411	24,245	Claims/benefits - % of total revenue	81.4%	80.2%	80.5%	79.5%	79.5%
Other income	328	192	173	181	191	Net inc. in PH res. - % of total revenue	0.8%	0.6%	0.9%	0.9%	0.8%
Total revenue	102,709	108,610	123,043	137,935	153,513	Ttl. claim/PH benefits to total revenue	82.2%	80.8%	81.3%	80.4%	80.3%
Insurance benefits & claims	(83,611)	(87,151)	(98,995)	(109,716)	(121,978)	Commission cost ratio	7.9%	7.6%	7.0%	7.2%	7.2%
Investment contract benefits	(772)	(635)	(1,067)	(1,173)	(1,291)	General & admin. cost ratio	9.2%	9.6%	8.5%	8.5%	8.5%
Total Claims / PH Benefits	(84,383)	(87,786)	(100,062)	(110,889)	(123,269)	Other exp. & stat. levy ratio	0.2%	0.2%	0.2%	0.2%	0.2%
Commission and brokerage expenses	(7,252)	(7,317)	(7,467)	(8,449)	(9,294)	Operating expense ratio	17.2%	17.5%	15.7%	15.9%	15.9%
Administrative expenses	(8,410)	(9,229)	(9,067)	(9,974)	(10,972)	New investment yield	3.8%	4.1%	4.3%	4.2%	4.1%
Other expenses	(147)	(199)	(213)	(235)	(258)	Gross investment yield	4.3%	3.8%	3.8%	3.9%	3.9%
Total Operating Expenses	(15,809)	(16,745)	(16,748)	(18,658)	(20,523)	Solvency ratio	35.0%	155.9%	179.9%	162.8%	149.6%
Finance Expenses	(263)	(806)	(2,417)	(2,701)	(2,860)						
Associate / JV - Profits / Losses	1	2	2	2	2						
Net profit before tax	2,255	3,275	3,818	5,690	6,863	Balance sheet (Rmb mn)					
Tax expense	(5)	(475)	(382)	(1,422)	(1,716)		2010	2011	2012E	2013E	2014E
Net profit after tax	2,250	2,800	3,436	4,267	5,147	Cash	27,368	21,095	28,624	39,867	46,896
Minority interest	1	1	1	2	2	Investments	265,498	352,861	448,436	529,666	623,052
NP to NCI shareholders	2,249	2,799	3,435	4,266	5,145	PP&E / Investment Properties	3,435	4,735	4,972	5,220	5,481
						Reinsurance Assets	4,535	4,202	4,415	4,650	4,907
						Premium Receivables	979	1,395	1,443	1,617	1,778
						Other assets	2,751	2,483	3,889	3,722	6,735
						Total Assets	304,566	386,771	491,779	584,742	688,851
Financial summary						Long-term insurance contracts liabilities	233,821	292,818	379,762	472,239	571,755
	2010	2011	2012E	2013E	2014E	Short-term insurance contracts liabilities	804	996	1,114	1,225	1,347
EPS (HK\$)	2.23	1.51	1.35	1.71	2.18	Investment contracts	19,912	19,001	20,068	21,241	22,532
<i>EPS growth (%)</i>	-11.7%	-32.2%	-10.4%	26.2%	27.4%	Borrowings (Sub-debt)	0	5,073	15,214	17,000	18,000
PER (x)	11.1	16.4	18.3	14.5	11.4	Financial assets under repo agreement	24,712	32,481	33,089	25,361	21,449
PBV (x)	3.81	2.03	1.69	1.48	1.23	Unearned premiums	390	504	522	584	643
PEV (x)	0.89	1.30	1.04	0.90	0.74	Other Liabilities	18,354	4,585	4,763	5,076	5,462
VNB multiple (x)	(0.65)	3.35	0.54	(1.51)	(4.55)	Total liabilities	297,993	355,458	454,530	542,726	641,187
Dividend per share (HK\$)	0.00	0.00	0.00	0.00	0.00	Net assets	6,573	31,313	37,249	42,016	47,663
Yield (%)	0.0%	0.0%	0.0%	0.0%	0.0%	Minority interests	6	7	9	11	13
Payout ratio (%)	0.0%	0.0%	0.0%	0.0%	0.0%	Net equity to shareholders	6,567	31,306	37,240	42,005	47,650
Return on equity (%)	41.6%	14.8%	10.0%	10.8%	11.5%						
Return on assets (%)	0.9%	0.8%	0.8%	0.8%	0.8%						
Tax rate (%)	0.2%	14.5%	10.0%	25.0%	25.0%						

Source: Company data, ABCI Securities estimates



Disclosures

Analyst Certification

I, Chan Wing Fu (Francis Chan), being the person primarily responsible for the content of this research report, in whole or in part, hereby certify that all of the views expressed in this report accurately reflect my personal view about the subject company or companies and its or their securities. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed in this report. I and/or my associates have no financial interests in relation to the listed company (ies) covered in this report, and I and/or my associates do not serve as officer(s) of the listed company (ies) covered in this report.

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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