

China / Hong Kong Company Guide

Ping An Insurance

Version 4 | Bloomberg: 2318 HK EQUITY | 601318 CH Equity | Reuters: 2318.HKI 601318.SS

Refer to important disclosures at the end of this report

DBS Group Research . Equity

22 Mar 2018

H: BUY

Last Traded Price (H) (21 Mar 2018): HK\$88.30 (HSI : 31,415)
Price Target 12-mth (H): HK\$115 (30% upside) (Prev HK\$100)

A: BUY

Last Traded Price (A) (21 Mar 2018): RMB73.82 (4,061)
Price Target 12-mth (A): RMB87.75 (19% upside)

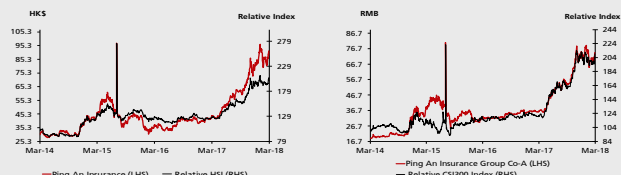
Analyst

Ken SHIH+852 2820 4920 kenshih@db.com

What's New

- Remains optimistic on 2018 "protection" demand, despite hiccup from "Jump-start" sales
- Lengthening asset duration by increasing bond investment to capture benefits from rising rate
- Strong VNB outlook, ample residual margin and high ROEV to secure a higher dividend payout
- Raise earnings by 2%/1% in FY18/19F, fine tune our VNB/EV assumption and raise TP to HK\$115 as we roll over our valuation to FY19F. Reiterate BUY

Price Relative



Forecasts and Valuation(H Shares)

FY Dec (RMBm)	2017A	2018F	2019F	2020F
Net earned premiums	572,990	688,930	847,984	1,034,955
Net investment income	152,101	154,240	178,918	208,553
Net Profit	89,088	93,467	110,991	132,672
EPS (RMB)	4.87	5.11	6.07	7.26
EPS (HK\$)	6.04	6.34	7.53	9.00
EPS Gth (%)	39.4	4.9	18.7	19.5
PE (X)	14.6	13.9	11.7	9.8
DPS (HK\$)	1.86	1.97	2.33	2.79
Net Div Yield (%)	2.1	2.2	2.6	3.2
BV Per Share (HK\$)	32.11	36.59	42.16	48.82
P/Book Value (X)	2.8	2.4	2.1	1.8
P/EV (X)	1.6	1.4	1.2	1.0
ROAE (%)	20.8	18.5	19.1	19.8

Earnings Rev (%)	2	1	NEW
Consensus EPS (RMB)	5.33	6.21	6.99
Other Broker Recs:	B: 24	S: 0	H: 2

Source of all data on this page: Company, DBSV, Thomson Reuters, HKEK

Rosy outlook is intact

Remain optimistic on protection product outlook: We attended Ping An's analyst meeting and left with positive takeaways (Detail Q&A summary on page 2). The insurer remains optimistic on this year's protection-type product demand, as growth potential from the market remains strong with the age of insurance policy purchasers getting younger. Despite slower growth from "Jump-start" sales, the products impacted were mainly saving-type while 1Q17 also represents a high base (FYP +65% y-o-y in 1Q17).

Lengthening asset duration to capture rising rate benefit: In 2017, Ping An's asset duration has reached 7.8 years, vs 7.5 years in 2016. The insurer will continue to lengthen its asset duration by increasing its bond investment to capture the "new money" benefit from rising interest rate. Its net/total investment yield in 2017 reached 5.8%/6.0% (-0.2/+0.7ppts vs 2016), with comprehensive yield coming in at 7.7%, thanks to unrealised gain of Rmb38.7bn (or 7% of equity) for its "available-for-sales" assets by year end. Despite higher market volatility this year, management believes the investment return should at least stay at the 2017 level given stable macro-outlook.

Strong outlook to ensure higher dividend pay-out: With its ongoing focus on protection-type product sales and strong productivity, Ping An believes this will translate into strong VNB growth and residual margin accumulation/release. This is reflected in the insurer's high ROEV of 35.5% for Life and ROE of 20.7% for the group. This will provide a solid foundation for a higher dividend pay-out going forward.

Raise TP to HK\$115. Reiterate BUY. We revise up our earnings by 2%/1% in FY18/19F and fine tune our VNB/EV assumption. We now expect VNB to grow 23%/25% y-o-y and Life's EV to grow 17%/19% in FY18/19F, respectively. By also rolling over our valuation base to FY19F, we raise our TP to HK\$115. With 28% share price upside, we reiterate our BUY call on Ping An.

Valuation:

Our TP is based on SOP valuation, using 2.2x P/EV for Ping An Life, 1.0x P/BV for Ping An P&C, Ping An Bank and all other businesses, a total of HK\$16.2/ share for Ping An's fintech unit and a 15% conglomerate discount.

Key Risks to Our View:

Increasing market competition, reversal in interest rate upcycle, rising volatility in both China's bond and equity markets, policy risks, and slower-than-expected China economy.

At A Glance

Issued Capital - H shares (m shs)	7,448
- Non H shrs (m shs)	10,833
H shs as a % of Total	41
Total Mkt Cap (HK\$m/US\$m)	1,650,173 / 210,433
Major Shareholders (%)	
Shenzhen Investment Holdings Limited	5.28
Major H Shareholders (%)	
Charoen Pokphand Group Co. Ltd	30.96
UBS Group AG	26.15
JPMorgan Chase & Co.	17.15
BlackRock, Inc.	5.33
Citigroup Inc.	5.08
3m Avg. Daily Val. (US\$m)	676.4
ICB Industry: Financials / Life Insurance	



ed- CK/ sa- CS /AH

WHAT'S NEW

Summary of Q&As raised during the meeting:

Dividend payout trend?

Dividend payout increased from 22% to 31% in FY17. The payout should be based on the net profit attributable to shareholders of the parent company. Management has confidence in its capital adequacy level, which should ensure the sustainability of such a payout ratio going forward.

Residual margin release trend?

The residual margin release depends on a number of factors, including product types and pattern of release. The amortisation rate should usually be about 10-20%.

Business outlook?

Management sees that there is potential for the younger generation to purchase insurance products. Plus, the insurance industry is highly supported by the Chinese government. Contribution from saving-type products will continue to be lower while protection type will increase. It has also noted that there is a high-base effect in 1Q18 given that VONB rose 60% y-o-y in 1Q17 (strong open-start sales)

Going forward, the fin-tech business will have bigger contribution to the Ping An group and will also provide synergies to Ping An's existing business (e.g. cross-selling).

Investment strategy in 2018?

The company increased the asset duration to 7.8 years from 7.5 years by allocating more to long-term fixed income investments. It will continue to lengthen the duration of the investment portfolio and invest in quality stocks with reasonable dividend yields.

Growth in 2H17 looks sluggish (+5% h-o-h). What is the agency growth trend?

The company usually conducts its hiring in second or third quarter. Management sees room for an increase in agency force in the industry (double-digit growth in the next five years). Its agency monthly income reached RMB6,250 while a team leader can make as much as RMB18,000.

Impact from adoption of IFRS17 and implemented C-ROSS?

Management believes the updated C-ROSS will incentivise insurance companies to sell more protection products. And it does not expect significant impact from the adoption of IFRS17.

Products sold on tele and Internet channels?

Management mentioned that the products sold on tele and Internet channels are basically simpler version of the products sold through other channels. As these are also long-term and regular-pay protection products, the VONB margin is not much different.

Reason for favourable operating variance of RMB 8.9bn?

This is caused by more favourable surrender rate, death rate and claims trends, as the assumptions made by Ping An are quite conservative.

What is the reason for an increase in liability reserve for Life business?

The liability reserve for life & health products has reached Rmb32bn, vs Rmb15bn in 1H17 and Rmb29bn in 2016. The 11% y-o-y increase was mainly due to 1) the 750-day MA of 10-year government bond yield curve was still declined during 1H17 to 3Q17, and 2) downward adjustment in composite premium to fully reserve for legacy high-interest rate book. Ping An did not change any assumption regarding "Life table".

Reason for increase in P&C's combine ratio?

Ping An P&C's ROE has consistently hovered at the 20%-23% level, thus its profitability is strong. The slightly higher combined ratio y-o-y was mainly due to its guarantee insurance business, where its cooperation with Puhui to provide credit insurance contributed more business and the combined ratio was moderately higher. Nonetheless, the overall combined ratio for its guarantee business came in at 88.6%, which is still very healthy.

DBS Target price

Ping An business entities	Estimated fair value (HK\$)/share	% of total	Multiple	
Ping An Life EV per share	42.6			
P/EV (x)	2.2		2.2	In-line with peer's 5 year average
Ping An Life fair value	95.9	71%		
Ping An P&C BVPS	6.3			
P/B (x)	1.0		1	
Ping An P&C fair value	6.3	5%		
Ping An Bank BVPS	9.8			
P/B (x)	1.0		1	
Ping An Bank fair value	9.8	7%		
Ping An Trust BVPS	1.7			
P/B (x)	1.0		1	
Ping An Trust fair value	1.7	1%		
Ping An Securities BVPS	1.7			
P/B (x)	1.0		1	
Ping An Securities fair value	1.7	1%		
Others BVPS	3.7			
P/B (x)	1.0		1	
Other business fair value	3.7	3%		
Ping An Fintech platforms fair value	16.2	12%	13.79	
Sub-total	135.3			
Conglomerate discount @15%	15%			
Ping An fair value - H share	115.0			
Share price (as of Mar 21, 2018)	89.5			
% of upside/(downside)	28%			
Ping An fair value - A share	100.9			
Share price (as of Mar 21, 2018)	69.0			
% of upside/(downside)	46%			
				FY19F
Implied FY19F PB (Group)	3.4			1,111,145
Implied FY19F P/EV (Group)	1.9			

Source: Company, DBS Vickers

CRITICAL FACTORS TO WATCH

Critical Factors

Sensitive to china government bond yield

An increase in the 750-day moving average would lower the insurance reserve assessment. This is also positive for insurer's reinvestment yield under a rising yield environment. We believe China's tightening stance is favourable for life insurers like Ping An.

First-year premium(FYP) / Value of New Business (VoNB)

Ping An's first-year premium, reaching RMB171,547m or +26% y-o-y, comprised agency channel (71%), bancassurance (4%), tele and Internet (8%) and group (17%) in FY17. Ping An is shifting its focus to value with agency channel increasing by 35% to RMB122bn and bancassurance decreasing by 34% to RMB7bn given more lucrative new business margin from agency channel (50%) than bancassurance channel (10%).

The value of new business reached RMB67bn, increasing by 32% y-o-y in FY17. Agency, tele and Internet and bancassurance channels contributed 90%, 8% and 1% respectively. Steering away from bancassurance to agency is positive for its new business value. The group's embedded value reached RMB825bn, increasing by 29% compared with the end of 2016.

Agency growth and productivity

In FY17, the group's exclusive individual agency sales force reached 1.386m, increasing by 25% y-o-y. The agency productivity, measured in first-year-premium per agent, reached RMB8,373, increasing by 7% y-o-y. This is an improvement with 13 / 25 months' persistency rate increasing by 0.4% / 1.5% y-o-y to 91.8% / 88.0%.

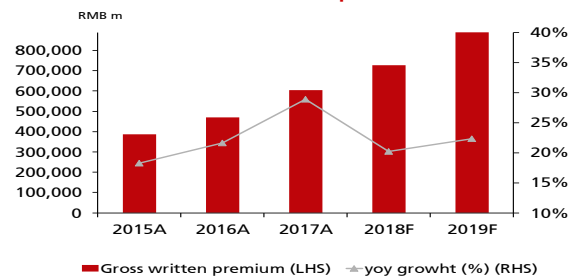
Investment Performance

Ping An achieved net investment yield of 5.8% in FY17, 0.2% lower than the corresponding period of 2016. Fixed-income investments (term deposits, bonds and other fixed income investments) represented 69% of its investment portfolio. Thus, with a sizeable fixed income portfolio, we believe the group's reinvestment yield will benefit under a rising interest rate environment.

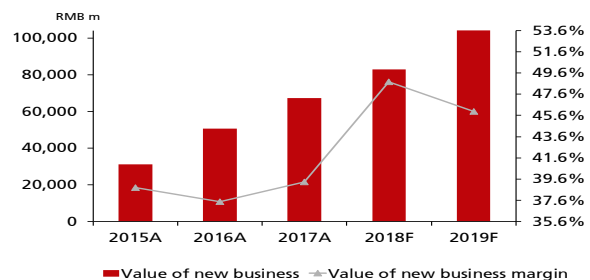
Income from associate (Ping An Bank)

Ping An Bank continued its transformation into a smart retail bank centred on social media + app + tele. The bank, 58% owned by Ping An, is a consolidated banking subsidiary. Profit attributable to Ping An was RMB13.5bn (+4.6% y-o-y), equivalent to 15% of the group's net profit in FY17.

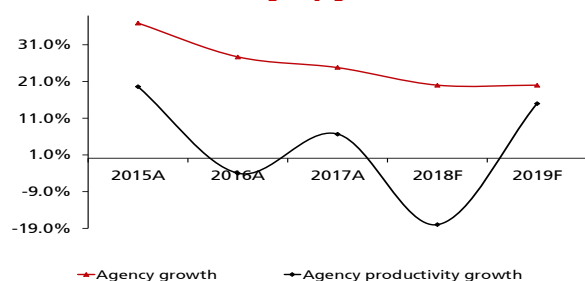
Gross written premiums



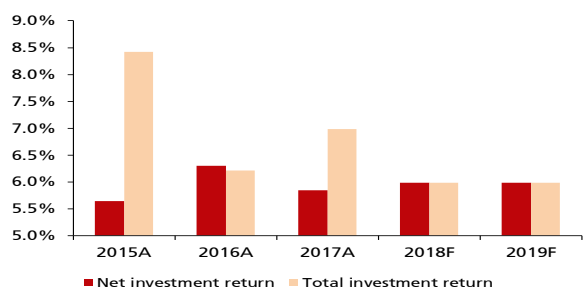
Value of new business



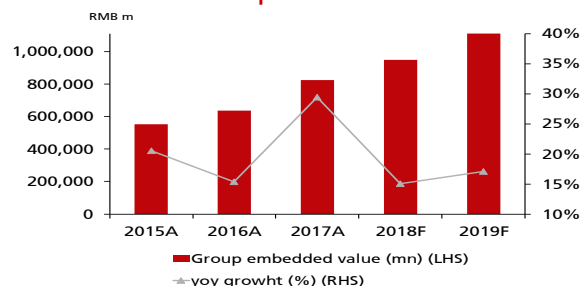
Agency growth



Net Investment return



Group embedded value



Source: Company, DBS Vickers

Balance Sheet:

Ping An's core and comprehensive solvency ratios stood at 209% and 215% in FY17, 8ppts and 5ppt higher than end of 2016. The leverage (Total Asset / Total Equity) stood at 11.0x in the FY17, decreasing marginally from 11.5x in FY16.

Share Price Drivers:

Sensitive to China government bond yield: An increase in the 750-day moving average would lower the insurance reserve assessment. This is also positive for insurer's reinvestment yield under a rising yield environment. We believe China's tightening stance is favourable for life insurers.

Value of new business: The share price performance is linked to the group's ability to deliver value of new business growth. Any change in product mix or channel that is favourable for the value of the new business is positive for the value of new business growth.

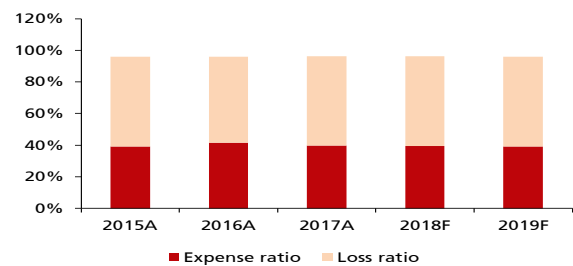
Key Risks:

Any substantial decline in China's government bond yields would require higher reserves. More intense pricing competition would affect new business margins. Asset-quality deterioration in banking operations. Rising A/H share volatility. Slower-than-expected China economic growth.

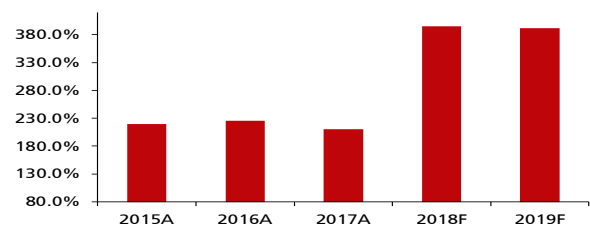
Company Background

Ping An Insurance was established in May 1988 as the first joint-stock insurance company in China. It was listed on the HKEX and SHEX in June 2004 and March 2007 respectively. Ping An is a conglomerate involved in life insurance, P&C, banks, trust and securities. At end-2017, its total assets and equity reached RMB6.5tr and RMB473bn respectively.

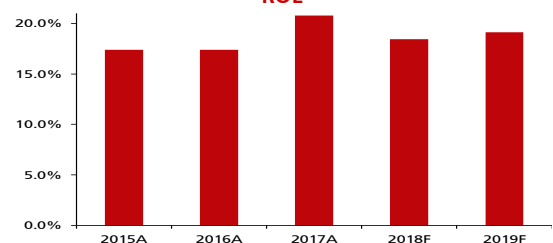
Expense/Loss/Combined ratio



Solvency ratio



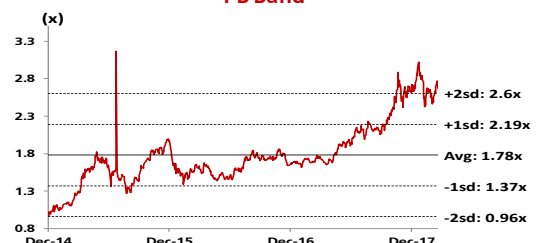
ROE



PEV Band



PB Band



Source: Company, DBS Vickers

Key Assumptions

FY Dec	2016A	2017A	2018F	2019F	2020F
Gross written premium growth	21.6	28.9	20.2	22.3	21.7
Agency growth	27.7	24.8	20.0	20.0	10.0
Agency productivity growth	(4.0)	6.7	(18.0)	15.0	5.0
Expense ratio	41.6	39.7	39.5	39.3	39.3
Loss ratio	54.4	56.6	56.8	56.8	56.8
Combined ratio	96.0	96.2	96.3	96.1	96.1
VNB margin	37.4	39.3	48.7	45.9	46.8
Net investment return	6.3	5.8	6.0	6.0	6.0
Total investment return	6.2	7.0	6.0	6.0	6.0
EV growth	15.3	29.4	15.0	17.1	16.9
Solvency ratio	225.9	210.0	394.7	391.3	370.1

Source: Company, DBS Vickers

Income Statement (RMB m)

FY Dec	2016A	2017A	2018F	2019F	2020F
Gross written premiums	469,555	605,035	727,180	889,239	1,082,628
Net earned premium	441,620	572,990	688,930	847,984	1,034,955
Investment income	116,675	152,101	154,240	178,918	208,553
Other operating income	158,864	195,133	150,809	175,258	195,099
Total income	717,159	920,224	993,978	1,202,161	1,438,607
Benefits and claims	(324,814)	(427,243)	(486,999)	(595,627)	(727,694)
Underwriting and policy acquisition costs	(78,684)	(114,587)	(94,230)	(117,669)	(145,577)
Finance cost	(12,144)	(11,167)	(9,853)	(13,125)	(13,125)
Other expenses	(922,895)	(1,159,856)	(1,251,374)	(1,506,693)	(1,789,275)
Total expenses	(1,338,537)	(1,712,853)	(1,842,457)	(2,233,114)	(2,675,671)
Share of profit of associated and JVs	(1,370)	7,145	0	0	0
Profit before tax	94,411	134,740	145,500	171,207	201,542
Income tax expense	(22,043)	(34,762)	(41,710)	(48,490)	(55,615)
Minority interest	(9,974)	(10,890)	(10,323)	(11,726)	(13,256)
Preferred dividend	0	0	0	0	0
Net income attributable to shareholders	62,394	89,088	93,467	110,991	132,672

Source: Company, DBS Vickers

Balance Sheet(RMB m)

FY Dec	2016A	2017A	2018F	2019F	2020F
Total Investment	1,971,798	2,385,502	2,767,182	3,209,931	3,723,521
Property, plant and equipment	40,143	47,067	47,067	47,067	47,067
Other assets	3,564,962	4,060,506	4,193,185	4,395,029	4,659,387
Total assets	5,576,903	6,493,075	7,007,434	7,652,027	8,429,975
Net life reserves - traditional	1,625,473	1,932,969	2,255,924	2,671,129	3,191,711
Net life reserves - investment contracts	44,930	50,309	56,471	64,891	75,875
Other Liabilities	3,420,039	3,921,880	4,030,752	4,157,979	4,292,839
Total liabilities	5,090,442	5,905,158	6,343,148	6,893,999	7,560,426
Shareholder's equity	383,449	473,351	539,397	621,413	719,678
Minority interest	103,012	114,566	124,889	136,615	149,871
Total equity	486,461	587,917	664,286	758,029	869,549

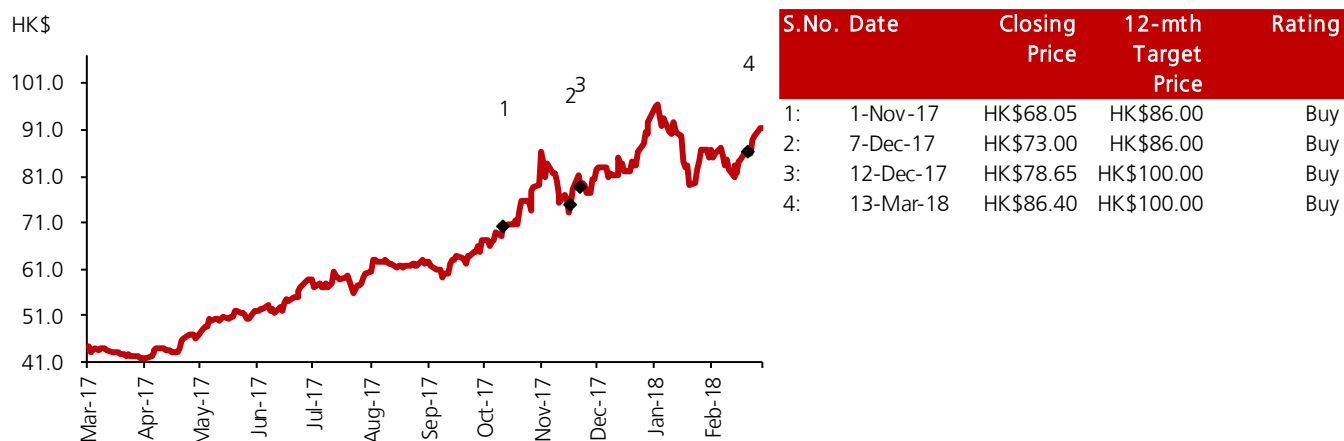
Source: Company, DBS Vickers

Key Financials & Ratios

FY Dec	2016A	2017A	2018F	2019F	2020F
Du Pont analysis (%)					
Net profit / premium income	13.8	15.2	13.2	12.7	12.5
Premium income / total asset	8.1	9.0	10.1	11.4	12.6
Total asset / total equity	11	11	11	10	10
Return on equity	17.4	20.8	18.5	19.1	19.8
Embedded value(RMB m)					
Book value	383,449	473,351	539,397	621,413	719,678
Adjusted items	23,891	39,362	39,525	39,719	39,940
Adjusted book value	407,340	512,713	578,922	661,132	759,618
Value-in-force	230,362	312,459	370,321	450,013	539,623
Adjustment (if any)	0	0	0	0	0
Group embedded value	637,702	825,172	949,243	1,111,145	1,299,241
Per share analysis(RMB)					
EPS	3.50	4.87	5.11	6.07	7.26
BPS	20.98	25.89	29.51	33.99	39.37
DPS	0.75	1.50	1.59	1.88	2.25
EVPS	34.88	45.14	51.93	60.78	71.07
Capital Strength (%)					
Leverage ratio	11	11	11	10	10
Solvency ratio	225.9	210.0	394.7	391.3	370.1

Source: Company, DBS Vickers

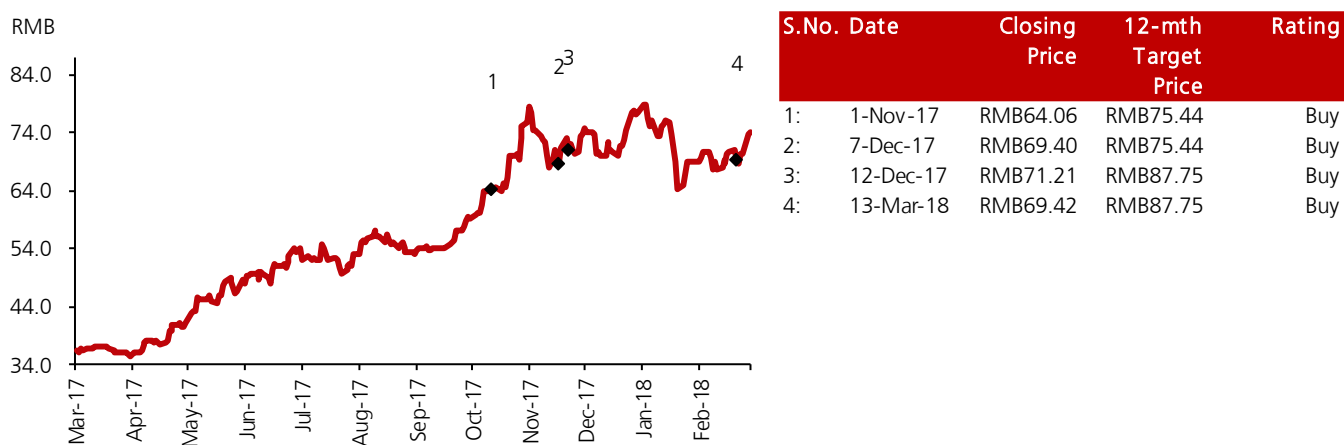
H Share - Target Price & Ratings History



Source: DBS Vickers

Analyst: Ken SHIH

A Share - Target Price & Ratings History



Source: DBS Vickers

Analyst: Ken SHIH

DBSVHK recommendations are based on Absolute Total Return* Rating system, defined as follows:

STRONG BUY (>20% total return over the next 3 months, with identifiable share price catalysts within this time frame)

BUY (>15% total return over the next 12 months for small caps, >10% for large caps)

HOLD (-10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps)

FULLY VALUED (negative total return i.e. > -10% over the next 12 months)

SELL (negative total return of > -20% over the next 3 months, with identifiable catalysts within this time frame)

Share price appreciation + dividends

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Sources for all charts and tables are DBS Vickers unless otherwise specified.

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DBS Vickers (Hong Kong) Limited18th Floor Man Yee building, 68 Des Voeux Road Central, Central, Hong Kong

Tel: (852) 2820-4888, Fax: (852) 2868-1523

Company Regn. No. 31758

DBS Regional Research Offices

HONG KONG

DBS Vickers (Hong Kong) Ltd

Contact: Carol Wu

18th Floor Man Yee Building

68 Des Voeux Road Central

Central, Hong Kong

Tel: 852 2820 4888

Fax: 852 2863 1523

e-mail: dbsvhk@dbs.com

Participant of the Stock Exchange of Hong Kong Ltd

MALAYSIA

AllianceDBS Research Sdn Bhd

Contact: Wong Ming Tek (128540 U)

19th Floor, Menara Multi-Purpose,

Capital Square,

8 Jalan Munshi Abdullah 50100

Kuala Lumpur, Malaysia.

Tel.: 603 2604 3333

Fax: 603 2604 3921

e-mail: general@alliancedbs.com

SINGAPORE

DBS Bank Ltd

Contact: Janice Chua

12 Marina Boulevard,

Marina Bay Financial Centre Tower 3

Singapore 018982

Tel: 65 6878 8888

Fax: 65 65353 418

e-mail: equityresearch@dbs.com

Company Regn. No. 196800306E

INDONESIA

PT DBS Vickers Sekuritas (Indonesia)

Contact: Maynard Priajaya Arif

DBS Bank Tower

Ciputra World 1, 32/F

Jl. Prof. Dr. Satrio Kav. 3-5

Jakarta 12940, Indonesia

Tel: 62 21 3003 4900

Fax: 6221 3003 4943

e-mail: research@id.dbsvickers.com

THAILAND

DBS Vickers Securities (Thailand) Co Ltd

Contact: Chanpen Sirithanarattanukul

989 Siam Piwat Tower Building,

9th, 14th-15th Floor

Rama 1 Road, Pathumwan,

Bangkok Thailand 10330

Tel. 66 2 857 7831

Fax: 66 2 658 1269

e-mail: research@th.dbs.com

Company Regn. No 0105539127012

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