

Analyst: Paul Sham
CHINA LIFE INSURANCE COMPANY LIMITED (中國人壽)

Sector	: Insurance
HKSE Code	: 02628
Market Price	: HK\$22.25 (29/08/2014)
Shares Issued	: 7,441m (H shares)
Mkt. Cap.	: HK\$165,562m (H shares)
52 weeks Hi/ Lo	: HK\$24.42 / HK\$16.76
HSI / HSCEI	: 24,742.06 / 10,963.59 (29/08/2014)
Main Business	: Life insurance businesses

Chairman : Mr. Yang Mingsheng

SUMMARY OF THE INTERIM RESULTS FOR THE SIX MONTHS ENDED 30TH JUNE 2014
Interim Results Highlights

	1H2014	1H2013	
	<u>RMB million</u>	<u>RMB million</u>	<u>Change</u>
Gross written premiums	197,250	203,251	-3.0%
Net earned premiums	193,775	200,844	-3.5%
Net investment income (recurring)	45,075	40,103	+12.4%
Net realized/unrealized gain/(loss) from investments	279	4,840	-94.2%
Other revenues	1,852	1,761	+5.2%
Total revenues	240,981	247,548	-2.7%
Total policy benefits & expenses	(220,176)	(228,967)	-3.8%
Share of results of associates	2,041	1,576	+29.5%
Profit before taxation	22,864	20,157	+13.4%
Profit attributable to shareholders	18,407	16,198	+13.6%
Basic EPS (RMB)	0.65	0.57	+14.0%
Interim DPS (RMB)	0	0	+0.0%

- The 1H14 net profit of China Life Insurance ("China Life") grew 13.6% y-o-y to RMB18,407m, better than market estimate of HK\$16,925m. The double-digit earnings growth was attributable to a decline in policy benefits & expenses, which more than offset the sluggish performance in net earned premiums and the flattish investment income.
- China Life's gross written premiums fell 3.0% y-o-y, mainly due to the 12.9% y-o-y fall in premium earned through bancassurance channel. Agency insurance channel registered a flattish y-o-y growth of 0.7% as China Life focused on value creation instead of volume growth by adjusting its product mix.
- China Life's Embedded Value (EV) increased by 14.1% h-o-h to RMB390,367m, driven by higher expected return on its investment portfolio of RMB17,665m (+5.2% h-o-h on EV), value of new business (VNB) of RMB13,459mn (+3.9%), investment experience variance of RMB9,649m (+2.8%) and market value adjustment of RMB14,703m (+4.3%), which more than offset the 2.5% decline in EV due to dividend payment of RMB8,479m.
- Basic EPS was RMB0.65, up 14.0% y-o-y. As usual, China Life did not declare any interim dividend.

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- Breakdown of first-year premiums by distribution channel

	1H14 RMB million	1H13 RMB million	Change
Agency Channel - first-year premium	21,710	19,522	+11.2%
Value of new business	13,118	11,527	+13.8%
Margin	60.4%	59.0%	
Bancassurance Channel - first-year premium	53,583	58,409	-8.3%
Value of new business	207	794	-73.9%
Margin	0.4%	1.4%	
Group insurance & other Channel - first-year premium	1,360	1,981	-31.3%
Value of new business	134	268	-50.0%
Margin	9.9%	13.5%	
Total first-year premium	76,653	79,912	-4.1%
Value of New Business	13,459	12,589	+6.9%
Margin	17.6%	15.8%	+1.8ppts

- China Life's **first-year premium** fell 4.1% in 1H14 to RMB76,653m, dragged by the negative first-year premium growth in both bancassurance and group insurance products. In respect of value creation, China Life's VNB rose 6.9% y-o-y to RMB13,459m on the back of 1.8ppts-expansion on product margin. Agency business was again the key growth driver, with the agency VNB growing 13.8% y-o-y in 1H14 and contributing 97.5% of overall VNB generation. In contrast, bancassurance was the key drag in VNB. VNB of bancassurance plunged 73.9% y-o-y to RMB207m only in 1H14, despite its first-year premium fell only moderately by 8.3%. The gap between the decline in VNB and first-year premium translated into a significant drop in the new business margin of bancassurance, which dropped to 0.39% only in 1H14, from an already low level of 1.36% in 1H13.
- Overall **investment income** was the largely unchanged y-o-y in 1H14 but the gross investment yield fell from 4.96% for 1H13 to 4.78% for 1H14 as a result of enlarged investment portfolio. China Life's net investment income (mainly from debt securities and bank deposits) grew 12.4% y-o-y amid expansion of its bond portfolio. Nevertheless, equity return was lowered to RMB279m, down 94.2% y-o-y in 1H14, as China Life reported a net loss of RMB267m on its financial assets in 1H14, compared with a gain of RMB3,922m a year ago. China Life's equity investment allocations also declined to 5.3% (from 7.5% at end-2013), showing reduced reliance on A-shares market.

Outlook & Prospects

- Value creation trailed peers** Similar to other insurers, China Life focuses on value creation instead of volume growth in the recent years. Nevertheless, its progress of transformation lagged behind peers as its VNB grew at 6.9% in 1H14, slower than CPIC's 22.9% and Ping An's 16.7%. The underperformance of China Life was attributable to its heavy reliance on bancassurance products, which are low-margin in nature, to maintain its market shares. With an 8.3% y-o-y decline in bancassurance premium in 1H14, China Life's market share shrank notably from 30.4% at end-2013 to 25.7% only at end-1H14. We believe China Life may take a few years to optimize its product mix and expect its market share will shrink further. China Life's VNB growth will continue to trail peers as bancassurance still contributes substantial premiums to China Life as a whole.

- **Solvency should not be a concern** China Life's solvency margin stood at 241% in 1H14, up from 226% at end-2013. The capital adequacy position suggested a minimal need for China Life to raise capital in the near term. In addition, given China Life's current balance of sub-debt of RMB68 billion or 28% of its net assets (vs 50%, the maximum sub-debt level allowed by CIRC for each insurer), China Life can further issue sub-debt of around RMB53 billion, which could improve its solvency ratio by an additional 67% in due course.
- **Lacking cross-selling model** Since the Chinese insurance industry broadens its product offerings, there is greater opportunity for cross-selling such as telemarketing sales of P&C products and credit cards to life customers, offering banking services to existing customers and upselling bancassurance customers with higher-margin individual life protection products. Unlike Ping An which has its own banking platform to cross-sell products, the monotonous business model puts China Life at a disadvantage to capture all these opportunities. This also partly explains why China Life continued losing market share in the recent years.
- **Valuation** Share prices of China Life have been range-bounded for the past 3 years and are currently trading at 1.27x FY14E P/EV, a discount to CPIC's 1.43x. However, since China Life is still struggling to improve its agency business and lacks exposure on property & casualty insurance, China Life should be a less preferred play in the sector. As such, we prefer CPIC in the life insurance sector for its better agency distribution channel.

Recommendation: *Prefer CPIC*

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