

EARNINGS REVIEW

**China Pacific Insurance (H) (2601.HK)**

Neutral

Equity Research

**In line with estimates on life, P&C below, stepping up restructuring**

**What surprised us**

CPIC reported 2014 results. Life metrics were largely within expectation, while P&C underwriting worsened. Life: Group embedded value grew 19% yoy, in line with GSe. New business value was Rmb8.7bn, +16% yoy, slightly below GSe of 9bn. But new business margin showed some improvement, especially in 2H14 (FYP margin: 2H14/2014: 35.1%/27.1%, +8.0/5.0pp yoy). We believe this was mainly driven by CPIC Life's consistent focus on quality over quantity and faster agency growth vs bancassurance. Agency headcounts saw healthy 14% growth, with active and high-performing agents outpacing total at 18%. P&C however saw underwriting loss. Combined ratio further worsened 4.3/6.5pp to 104.2%/108.4% in 2014/2H14, while both Ping An and PICC showed improvement. We note that some of the deterioration was driven by one-off impact in reserve changes (c.3% in 2014), but also flagged some strategic missteps in the past (such as less exposure to individual customers vs peers, and less proactive attitude toward innovation and non-auto lines). We believe CPIC is making active changes to address these issues, including the recent restructuring of the P&C business. But we think it will take some time to close the operational gap with peers. As part of CPIC's continued customer-need-driven strategic transitioning, it restructured its life business into individual and group & partnerships, based on different customer types, rather than on distribution channel previously. Financial reporting was changed accordingly to align with the KPI shifts.

**What to do with the stock**

We maintain our Neutral rating on CPIC H/A, and our 12m SOTP based TP of HK\$41.00/Rmb33.21. Risk: Upside: margin improvement, A-share surge; Downside: continued deterioration in P&C underwriting.

**CPIC 2014 results snapshot**

NBV yoy growth	16.3%	EV yoy growth	18.6%	NPAT yoy growth	19.3%
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Source: Company data

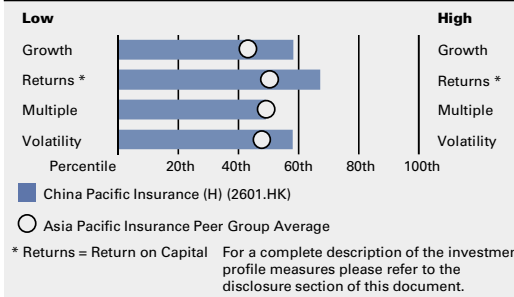
**INVESTMENT LIST MEMBERSHIP**

Neutral

**Coverage View: Neutral**

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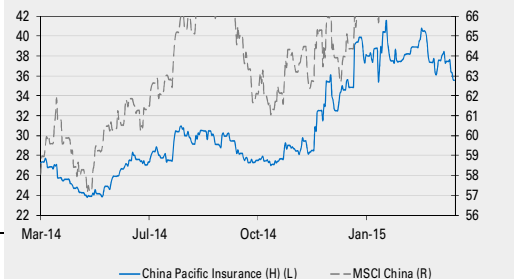
**Investment Profile**



Key data	Current
Price (HK\$)	35.55
12 month price target (HK\$)	41.00
601601.SS Price (Rmb)	32.09
601601.SS 12 month price target (Rmb)	33.21
Market cap (HK\$ mn / US\$ mn)	322,154.1 / 41,547.1
Foreign ownership (%)	--

	12/13	12/14E	12/15E	12/16E
EPS (Rmb)	1.02	1.44	1.61	1.81
EPS growth (%)	73.9	41.2	11.3	12.8
601601.SS EPS (Rmb)	1.02	1.44	1.61	1.81
601601.SS EPS growth (%)	73.9	41.2	11.3	12.8
P/E (X)	21.7	19.7	17.7	15.7
601601.SS P/E (X)	18.1	22.2	20.0	17.7
Dividend yield (%)	1.6	1.6	1.8	2.0
ROE (%)	9.5	12.5	12.6	12.9

**Price performance chart**



Share price performance (%)	3 month	6 month	12 month
Absolute	2.0	30.2	30.5
Rel. to MSCI China	(5.0)	19.3	9.6

Source: Company data, Goldman Sachs Research estimates, FactSet. Price as of 3/27/2015 close.

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# China Pacific Insurance (H): Summary Financials

Profit model (Rmb mn)	12/13	12/14E	12/15E	12/16E	Balance sheet (Rmb mn)	12/13	12/14E	12/15E	12/16E
<b>Net premiums earned (NEP)</b>	<b>159,625.0</b>	<b>170,659.9</b>	<b>190,756.4</b>	<b>213,799.0</b>	<b>Total investment assets</b>	<b>663,067.0</b>	<b>764,422.1</b>	<b>835,697.5</b>	<b>923,252.7</b>
Risk: Benefits and claims	(135,183.0)	(143,586.5)	(159,659.6)	(178,745.3)	Premiums receivable	7,763.0	12,699.0	14,607.0	16,801.8
Increase in life reserves	--	--	--	--	Deferred policy acquisition costs	0.0	0.0	0.0	0.0
Net commissions expensed	(109.0)	(171.0)	0.0	0.0	Fixed assets	10,542.0	11,548.7	13,284.0	15,280.0
SGA	--	--	--	--	Separate account	0.0	0.0	0.0	0.0
<b>Underwriting profit</b>	<b>(74.0)</b>	<b>(560.6)</b>	<b>1,029.1</b>	<b>1,142.3</b>	Others	42,161.0	47,537.6	54,222.7	61,171.1
Investment income	3,369.0	4,919.9	4,910.4	5,426.3	<b>Total assets</b>	<b>723,533.0</b>	<b>836,207.4</b>	<b>917,811.2</b>	<b>1,016,505.6</b>
Other income	8,619.0	13,106.9	13,460.5	15,318.6	Unearned premium reserves	0.0	0.0	0.0	0.0
<b>Pretax profit</b>	<b>11,914.0</b>	<b>17,466.2</b>	<b>19,400.0</b>	<b>21,887.2</b>	Policyholders' reserves	536,979.0	620,730.5	740,681.8	884,136.9
Tax and minority interest	2,653.0	4,385.6	4,846.8	5,473.0	Separate account	--	--	--	--
<b>Net profit</b>	<b>9,261.0</b>	<b>13,080.5</b>	<b>14,553.2</b>	<b>16,414.2</b>	Other liabilities	--	--	--	--
<b>Factors driving earnings growth (%)</b>	<b>12/13</b>	<b>12/14E</b>	<b>12/15E</b>	<b>12/16E</b>	<b>Total liabilities</b>	<b>624,565.0</b>	<b>726,415.1</b>	<b>796,867.3</b>	<b>882,805.2</b>
Net premiums earned growth	8.0	6.9	11.8	12.1	<b>Total equity</b>	<b>98,968.0</b>	<b>109,792.3</b>	<b>120,943.9</b>	<b>133,700.4</b>
Investment income growth	136.8	46.0	(0.2)	10.5	<b>DuPont analysis (% of avg assets)</b>	<b>12/13</b>	<b>12/14E</b>	<b>12/15E</b>	<b>12/16E</b>
Investment asset growth	7.0	15.3	9.3	10.5	ROAE	9.5	12.5	12.6	12.9
Pretax growth	94.9	46.6	11.1	12.8	x Leverage (X)	13.9	13.4	13.2	13.2
Net profit growth	82.4	41.2	11.3	12.8	ROAA	1.3	1.7	1.7	1.7
<b>Operating ratio for group (%)</b>	<b>12/13</b>	<b>12/14E</b>	<b>12/15E</b>	<b>12/16E</b>	Net earned premiums	22.7	21.9	21.8	22.1
Risk + inv benefits/NEP	(84.7)	(84.1)	(83.7)	(83.6)	Policyholder risk + inv benefit	(19.2)	(18.4)	(18.2)	(18.5)
SG&A + net commission exp./NEP	(0.1)	(0.1)	0.0	0.0	Increase in life reserves	(8.0)	(10.7)	(13.7)	(14.8)
Underwriting profit/NEP	0.0	(0.3)	0.5	0.5	Amortization of DAC	(0.4)	(0.4)	(0.4)	(0.3)
Investment yield (ex cash yield)	0.5	0.7	0.6	0.6	SGA	NM	NM	NM	NM
Pretax margin	7.5	10.2	10.2	10.2	Underwriting profit	0.0	(0.1)	0.1	0.1
Tax rate	21.1	23.8	23.7	23.8	Investment income	0.5	0.6	0.6	0.6
<b>Operating ratios p&amp;c (%)</b>	<b>12/13</b>	<b>12/14E</b>	<b>12/15E</b>	<b>12/16E</b>	Other income	1.2	1.7	1.5	1.6
Net reserves/claims paid	--	--	--	--	Pretax profit	1.7	2.2	2.2	2.3
Net reserves/earned premiums	--	--	--	--	Tax	0.4	0.6	0.6	0.6
Expense ratio	33.9	34.8	34.8	34.8	Net profit	1.3	1.7	1.7	1.7
Loss ratio	66.0	65.7	64.0	64.0	<b>Valuation</b>	<b>12/13</b>	<b>12/14E</b>	<b>12/15E</b>	<b>12/16E</b>
Combined ratio	100.1	100.8	98.7	98.7	P/E basic (X)	21.7	19.7	17.7	15.7
<b>Operating ratios life (%)</b>	<b>12/13</b>	<b>12/14E</b>	<b>12/15E</b>	<b>12/16E</b>	P/B (X)	1.6	1.9	1.7	1.6
Expense ratio	93.7	91.2	91.7	91.5	P/EV (X)	1.4	1.5	1.3	1.2
Pretax margins	7.5	10.2	10.2	10.2	EPS, basic (Rmb)	1.02	1.44	1.61	1.81
Fixed assets/total assets	1.5	1.4	1.4	1.5	BVPS (Rmb)	10.92	12.12	13.35	14.75
					EVPS (Rmb)	15.93	18.88	21.61	24.68
					DPS (Rmb)	0.35	0.47	0.52	0.57
					Dividend yield (%)	1.6	1.6	1.8	2.0
					Dividend payout (%)	42.3	40.2	40.0	38.9

Note: Last actual year may include reported and estimated data.

Source: Company data, Goldman Sachs Research estimates.

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**Exhibit 1: CPIC Group EV grew 19% yoy, in line with GSE. NBV was up 16% to Rmb8.7bn. Combined ratio further worsened 4.3pp to 104.2% in 2014.**  
 CPIC 2014 annual results review

(Rmb mn)	Half year									Full year				
	1H13	2H13	1H14	Actual 2H14	GS Est. 2H14E	Actual vs. GS Est.	HoH	YoY	2013	Actual 2014	GS Est. 2014E	Actual vs. GS Est.	YoY	
<b>Group</b>														
Gross written premiums and policy fees	98,662	78,261	108,413	83,392	84,887	-2%	-23%	7%	176,923	191,805	193,300	-1%	8%	
Net earned premiums	87,745	71,880	95,628	77,263	75,032	3%	-19%	7%	159,625	172,891	170,660	1%	8%	
Net policyholders' benefits and claims	72,497	60,762	74,066	72,518	66,675	9%	-2%	19%	133,259	146,584	140,741	4%	10%	
Interest credited to investment contracts	895	1,029	749	625	2,097	-70%	-17%	-39%	1,924	1,374	2,846	-52%	-29%	
Finance cost	1,271	1,484	1,379	1,774	1,761	1%	29%	20%	2,755	3,153	3,140	0%	14%	
G&A and other expenses	22,239	20,126	25,213	25,403	21,684	17%	1%	26%	42,365	50,616	46,897	8%	19%	
Underwriting profit (9,157)	(11,521)	(5,779)	(23,057)	(17,185)	34%	299%	100%	(20,678)	(28,836)	(22,964)	26%	39%		
Investment income	15,348	15,624	14,138	27,290	24,433	12%	93%	75%	30,972	41,428	38,571	7%	34%	
Pretax profit	6,928	4,986	9,179	5,321	8,286	-36%	-42%	7%	11,914	14,500	17,466	-17%	22%	
Tax	1,382	1,137	2,220	1,035	1,945	-47%	-53%	-9%	2,519	3,255	4,165	-22%	29%	
Net profit attributable to the parent	5,464	3,797	6,848	4,201	6,232	-33%	-39%	11%	9,261	11,049	13,081	-16%	19%	
EPS (Rmb)	0.60	0.42	0.76	0.46	0.69	-32%	-39%	11%	1.02	1.22	1.44	-15%	19%	
DPS (Rmb)	-	0.35	-	0.50	0.47	6%	NM	43%	0.35	0.50	0.47	6%	43%	
Total assets	721,207	723,533	821,391	825,100	836,207	-1%	0%	14%	723,533	825,100	836,207	-1%	14%	
Shareholders' equity	96,306	98,968	106,341	117,131	109,792	7%	10%	18%	98,968	117,131	109,792	7%	18%	
<b>Key ratios</b>														
Death and other benefits / Life premium	25%	37%	37%	47%	38%	10%	0%	11%	29.9%	40.8%	37.0%	4%	11%	
Change in insurance contract liabilities/ life premium	63%	51%	42%	57%	57%	0%	0%	6%	57.9%	48.0%	48.0%	0%	-10%	
Operating expenses / NEP	25%	28%	26%	33%	29%	4%	0%	5%	26.5%	29.3%	27.5%	2%	3%	
Underwriting profit / NEP	-10%	-16%	-6%	-30%	-23%	-7%	0%	-14%	-13.0%	-16.7%	-13.5%	-3%	-4%	
Effective tax rate	20%	23%	24%	19%	23%	-4%	0%	-3%	21.1%	22.4%	23.8%	-1%	1%	
ROA	1.6%	1.1%	1.8%	1.0%	1.5%	0%	0%	0%	1.32%	1.43%	1.68%	0%	0%	
ROE	11.4%	7.8%	13.3%	7.5%	11.5%	-4%	0%	0%	9.5%	10.2%	12.5%	-2%	1%	
<b>Life insurance</b>														
Life GWP	56,270	38,831	60,205	38,487	39,740	-3%	-36%	-1%	95,101	98,692	99,945	-1%	4%	
First year life premiums	21,946	11,993	22,277	9,973	11,870	-16%	-55%	-17%	33,939	32,250	34,147	-6%	-5%	
Renewal life premiums	34,324	26,838	37,928	28,514	27,870	2%	-25%	6%	61,162	66,442	65,798	1%	9%	
FYP	21,946	11,993	22,277	9,973	11,870	-16%	-55%	-17%	33,939	32,250	34,147	-6%	-5%	
Individual life	NA	NA	NA	NA	NM	NM	NM	NM	14,379	17,281	NM	NM	20%	
Regular	NA	NA	NA	NA	NM	NM	NM	NM	13,202	16,148	NM	NM	22%	
Single	NA	NA	NA	NA	NM	NM	NM	NM	1,177	1,133	NM	NM	-4%	
Group & Partnerships	NA	NA	NA	NA	NM	NM	NM	NM	19,560	14,969	NM	NM	-23%	
Regular	NA	NA	NA	NA	NM	NM	NM	NM	2,201	1,394	NM	NM	-37%	
Single	NA	NA	NA	NA	NM	NM	NM	NM	17,359	13,575	NM	NM	-22%	
APE	10,873	6,383	12,628	6,385	7,295	-12%	-49%	0%	17,257	19,013	19,923	-5%	10%	
<b>EV and NBV</b>														
Embedded value	139,723	144,378	153,891	171,294	171,061	0%	11%	19%	144,378	171,294	171,061	0%	19%	
New business value in the period	4,254	3,245	5,229	3,496	3,797	-8%	-33%	8%	7,499	8,725	9,026	-3%	16%	
Individual life	NA	NA	NA	NA	NM	NM	NM	NM	6,580	8,069	NM	NM	23%	
Group & Partnerships	NA	NA	NA	NA	NM	NM	NM	NM	919	656	NM	NM	-29%	
NBV breakdown														
Individual life	NA	NA	NA	NA	NM	NM	NM	NM	88%	92%	NM	NM	5%	
Group & Partnerships	NA	NA	NA	NA	NM	NM	NM	NM	12%	8%	NM	NM	-5%	
New business margin - FYP	19.4%	27.1%	23.5%	35.1%	32.0%	3%	12%	8.0%	22.1%	27.1%	26.4%	1%	5.0%	
Individual life	NA	NA	NA	NA	NM	NM	NM	NM	45.8%	46.7%	NM	NM	1%	
Group & Partnerships	NA	NA	NA	NA	NM	NM	NM	NM	4.7%	4.4%	NM	NM	0%	
New business margin - APE	39.1%	50.8%	41.4%	54.8%	52.0%	3%	13%	4%	43.5%	45.9%	45.3%	1%	2%	
Solvency margin ratio	193%	191%	179%	201%	201%	0%	0%	10%	191%	218%	181%	37%	27%	
<b>P&amp;C insurance</b>														
Gross written premiums	42,392	39,430	48,208	44,905	45,147	-1%	-7%	14%	81,822	93,113	93,355	0%	14%	
Net earned premiums	32,624	33,733	36,695	38,962	36,204	8%	6%	16%	66,357	75,657	72,899	4%	14%	
Underwriting profit	634	(708)	(90)	(3,464)	(471)	636%	3749%	389%	(74)	(3,554)	(561)	534%	4703%	
Pretax profit	2,411	1,204	2,055	(739)	2,705	-127%	-136%	-161%	3,615	1,316	4,760	-72%	-64%	
As % of group pretax profit	35%	24%	22%	-14%	33%	-47%	0%	-38%	30%	9%	27%	-18%	-21%	
Loss ratio	62.2%	69.7%	63.7%	72.0%	67.8%	4%	0%	2%	66.0%	68.0%	65.7%	2%	2%	
Expense ratio (net of reinsurance income)	35.8%	32.2%	36.1%	36.4%	33.5%	3%	0%	4%	33.9%	36.2%	34.8%	1%	2%	
Combined ratio	98.0%	101.9%	99.8%	108.4%	101.3%	7%	0%	7%	99.9%	104.2%	100.5%	4%	4%	
Auto	99.8%	NA	100.0%	NA	NA	NM	NM	NM	99.8%	102.0%	NA	NM	2%	
Non-auto	87.9%	NA	97.5%	NA	NA	NM	NM	NM	98.4%	112.6%	NA	NM	14%	
Commercial property	87.7%	NA	97.6%	NA	NA	NM	NM	NM	102.5%	119.4%	NA	NM	17%	
Liability	93.9%	NA	110.0%	NA	NA	NM	NM	NM	96.6%	122.0%	NA	NM	25%	
Accidental injury	107.3%	NA	105.0%	NA	NA	NM	NM	NM	109.0%	105.0%	NA	NM	-4%	
Cargo	82.5%	NA	83.3%	NA	NA	NM	NM	NM	95.9%	105.0%	NA	NM	9%	
<b>Investments</b>														
Net investment income	15,701	15,345	17,410	19,039	16,848	13%	9%	24%	31,046	36,449	34,258	6%	17%	
Bonds	13,686	14,806	15,857	17,582	15,900	11%	11%	19%	28,492	33,439	31,757	5%	17%	
Equities	2,015	539	1,553	1,457	948	54%	-6%	170%	2,554	3,010	2,501	20%	18%	
Unrealized and realized gains	(353)	279	(3,272)	11,923	7,584	57%	-464%	4173%	(74)	8,651	4,312	101%	-11791%	
Bonds	82	(95)	177	1,187	-	NM	571%	-1349%	(13)	1,364	177	671%	-10592%	
Equities	(435)	374	(3,449)	10,736	7,584	42%	-411%	2771%	(61)	7,287	4,135	76%	-12046%	
Total investment income	15,348	15,624	14,138	30,962	24,433	27%	119%	98%	30,972	45,100	38,571	17%	46%	
Investment yield														
Net yield on bonds	5.02%	5.27%	5.25%	5.39%	4.85%	1%	0%	0%	5.12%	5.45%	5.15%	0%	0%	
Dividend yield on equities	6.14%	1.50%	3.94%	3.57%	2.50%	1%	0%	2%	3.71%	3.87%	3.47%	0%	0%	
Gains on bonds	0.03%	-0.03%	0.06%	0.36%	0.00%	0%	0%	0%	0.00%	0.22%	0.03%	0%	0%	
Gains on equities	-1.33%	1.04%	-8.74%	26.30%	20.00%	6%	35%	25%	-0.09%	9.36%	5.74%	4%	9%	
Net investment yield	4.87%	4.62%	4.89%	5.02%	4.43%	1%	0%	0%	4.80%	5.10%	4.78%	0%	0%	
Overall investment yield	4.76%	4.70%	3.97%	8.16%	6.42%	2%	4%	3%	4.79%	6.31%	5.38%	1%	2%	
Investment assets	661,939	666,799	756,454	761,886	766,288	-1%	1%	14%	666,799	761,886	766,288	-1%	14%	

Source: Company data, Goldman Sachs Global Investment Research

# Disclosure Appendix

## Reg AC

We, Mancy Sun and Ning Ma, hereby certify that all of the views expressed in this report accurately reflect our personal views about the subject company or companies and its or their securities. We also certify that no part of our compensation was, is or will be, directly or indirectly, related to the specific recommendations or views expressed in this report.

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The Goldman Sachs Investment Profile provides investment context for a security by comparing key attributes of that security to its peer group and market. The four key attributes depicted are: growth, returns, multiple and volatility. Growth, returns and multiple are indexed based on composites of several methodologies to determine the stocks percentile ranking within the region's coverage universe.

The precise calculation of each metric may vary depending on the fiscal year, industry and region but the standard approach is as follows:

**Growth** is a composite of next year's estimate over current year's estimate, e.g. EPS, EBITDA, Revenue. **Return** is a year one prospective aggregate of various return on capital measures, e.g. CROCI, ROACE, and ROE. **Multiple** is a composite of one-year forward valuation ratios, e.g. P/E, dividend yield, EV/FCF, EV/EBITDA, EV/DACF, Price/Book. **Volatility** is measured as trailing twelve-month volatility adjusted for dividends.

## Quantum

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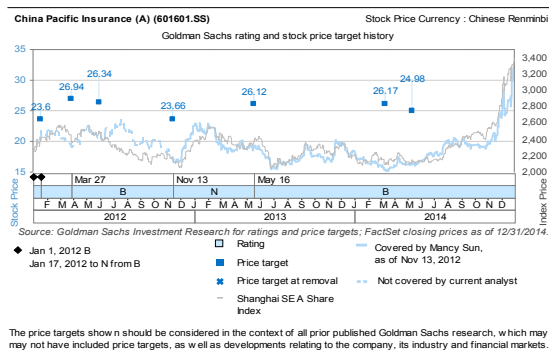
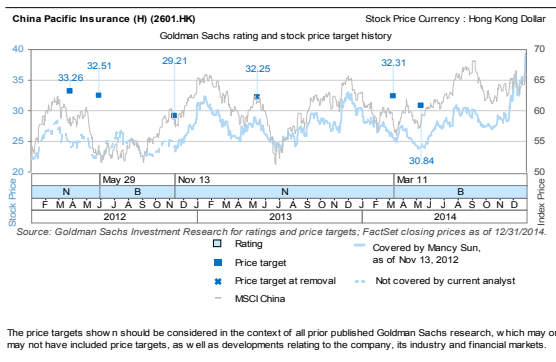
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