Global Insurance Sector

Refer to important disclosures at the end of this report

DBS Group Research . Equity 26 Jan 2024

Prefer P&C insurers amid rate downcycle

- **Expect underwriting performance to continue to recover in 2024**
- **Investment outlook to further improve, driven by higher reinvestment yield**
- **Our stress test suggests China insurers have limited downside and offer attractive dividend yield of 7-9%**
- **Prefer P&C over lifers on better asset/liability position amid rate downcycle. Top picks: Allianz and PICC P&C. We also like AIA for its secular growth potential**

Underwriting performance to continue to recover in 2024. We expect global property and casualty (P&C) insurers to benefit from the alleviation of inflation risk, successful repricing of premiums, and improvements in the combined ratio outlook. Life insurers in the Asia Pacific region may also continue to benefit from the recovery of growth in premiums, driven by the structural demand for health & protection and continuously robust growth from the Mainland China visitors (MCV) segment in HK.

Investment outlook improving on higher reinvestment yield. The recurring investment yield is expected to further improve, driven by the higher reinvestment yield, despite the European Central Bank (ECB) and FED likely cutting benchmark rates in FY24F. P&C insurers are expected to benefit from the rate downcycle, given their positive duration gap. Lifers with low interest rate sensitivity will also show robust investment return. Insurers with strong asset management franchises may also benefit from cyclical demand and an inflow of bond funds.

Our stress test suggests China insurers have limited downside and offer attractive dividend yield of 7-9%. Our stress test suggests China insurers may at most see a 14%-30% downside risk to the current share prices, even under an unlikely extreme and distressed scenario. We hence believe the current share prices have factored in much of the negativity. With the risk-reward looking increasingly attractive and insurers offering dividend yield of 7-9%, we recommend investors gradually accumulate shares upon a further share price pullback.

BUY Allianz, PICC P&C, and AIA. We prefer P&C insurers, such as Allianz (ALV GY) and PICC P&C (2328 HK), over lifers, given their better asset/liability position (i.e., positive duration gap) and lower interest rate sensitivity amid the rate downcycle. We also like AIA (1299 HK) for its secular growth potential and undemanding valuation.

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Recommendation & valuation

Insurance company	Ticker	Rating	Target Price	Potential Return
AIA	1299 HK	BUY	118.00	81.4%
Allianz	ALV GY	BUY	286.00	15.9%
China Life - H	2628 HK	BUY	16.00	70.9%
CPIC - H	2601 HK	BUY	24.00	58.9%
PICC P&C	2328 HK	BUY	12.50	25.6%
Ping An Ins - H	2318 HK	BUY	66.00	90.7%

Source: Thomson Reuters, DBS Bank (Hong Kong) Limited ("DBS HK")

Closing price as of 25 Jan 2024

ed- BM / sa-CS / AH

Prefer P&C insurers amid rate downcycle

Interest rate trends and CPI inflation are restructuring the insurance landscape in 2024 across major markets. Central banks such as the Federal Reserve of the United States (FED), European Central Bank (ECB), and People's Bank of China (PBOC) are expected to cut policy rates in 2024 while average interest rates in the US and Europe currently remain elevated compared to the past low-interest rate era. Meanwhile, the Bank of Japan (BOJ) is ready to put an end to negative rates in 2024. Thanks to the central banks' excellent job in bringing down inflation while avoiding economic recessions, both in the US and Europe, CPI inflation in these two regions is expected to further retreat in 2024, according to DBS macro forecast (Figure 1).

Fig 1. DBS macro forecast

	GDP growth y-o-y (%)		CPI inflation y-o-y (%)		Policy interest rates, eop (%)	
	FY23E	FY24F	FY23E	FY24F	FY23	FY24F
US	2.5	1.5	4.2	2.9	5.5	4.5
Eurozone	0.5	0.2	5.6	2.4	4.5	3.5
Japan	2.0	1.0	3.2	2.0	(0.1)	0.0
China	5.2	4.5	0.2	1.6	3.5	3.4

Source: DBS HK

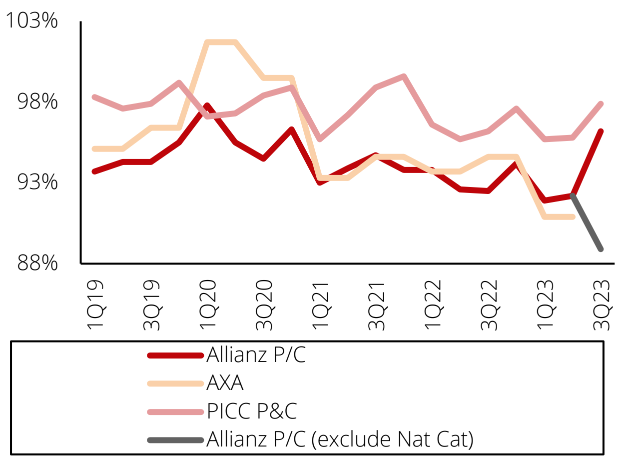
P&C's underwriting profit to ramp up in 2024

In the property and casualty (P&C) segment, we expect the underwriting profit of regional insurers in the developed markets (DMs) that we cover to continue expanding in 2024, mainly due to 1) the successful repricing of premiums, 2) alleviation of inflation risk, and 3) an improving combined ratio outlook (COR). The underwriting profit of China P&C is expected to rise on the back of top-line growth with policy stimuli.

- Insurers' COR benefiting from alleviation of inflation pressure in DMs

The growth momentum of premiums is expected to persist in 2024 across major markets in the US, Europe, and Japan. When increases in pricing take hold, it will more than offset the pressure on insurance demand caused by the economic slowdown, inflation, and rising reinsurance costs. Progress in repricing premiums has been seen among regional P&C insurers, and the trend is expected to continue in 2024, with accelerating repricing in the personal lines and continuation of hard market conditions in the commercial lines. We also expect inflation pressure on claims to further ease in 2024. The DBS economics team forecasts lower CPI inflation in 2024, projecting the CPI to ease to from 4.2%/5.6%/3.2% in FY23F to 3.0%/2.4%/2.0% in FY24F in the US/Eurozone/Japan, respectively. Inflation has the strongest impact on property and auto insurance, the two major lines in the non-life business, due to increasing costs for materials and parts and labour costs. With lower CPI inflation forecasts in 2024, we expect the combined ratios of regional P&C insurers, which have a product mix that leans towards auto and property, to improve with the easing of the upward trend in claims in 2024. Potential losses from natural catastrophes (Nat Cat) will continue to be at the heart of claims dynamics. We believe insurers learnt valuable lessons in 2022 and 2023 and are thus more willing to prepare a solid buffer, through reinsurance arrangements and adequate reserves, to mitigate any impact from Nat Cat risks. In a favourable pricing environment and with the alleviation of inflation risk, we expect the combined ratios and underwriting profits to improve for regional P&C insurers, such as Allianz, AXA (CS FP), and Tokio Marine (8766 JP) in FY24F (Figure 2).

Fig 2. Insurers' combined ratio trend



Source: Company data, DBS HK

- China P&C benefiting from policy initiatives

The growth in premiums of China's P&C insurers will be mainly driven by volume in major sub-segments. The business lines that support the real economy, such as agriculture, accident and health (A&H), and new energy vehicle (NEV) insurance, are expected to deliver double-digit y-o-y growth in FY24F. We expect P&C insurers' COR to remain largely stable in FY24F. Our assumption is conservative, as we assume Nat Cat losses would remain the same as the historically high in 2023, so any lower-than-expected Nat Cat claims will bring an upside to China P&C insurers' COR and underwriting profits. We don't expect the NEV business to be a major concern for China P&C insurers' COR, as NEV auto premiums account for an insignificant portion of total premiums, and large insurers such as PICC P&C and Ping An P&C have already turned profitable or are close to turning profitable with respect to their NEV business. The A&H line is likely to have an upside surprise on a low base effect and as a one-off regulatory impact is to be removed in FY24F, i.e., as the regulator cut the premium rate of lucrative accident products in FY23.

Asia market to lead life and health segment

In the life and health (L&H) segment, the Asia Pacific region will continue to be the engine of growth in terms of premiums worldwide. This is mainly driven by 1) the structural demand for health and protection products, 2) fast accumulating wealth and demand for global asset allocation, and 3) continuously robust growth from the Mainland China visitor (MCV) segment in Hong Kong.

- China lifers gearing up for surging demand for savings

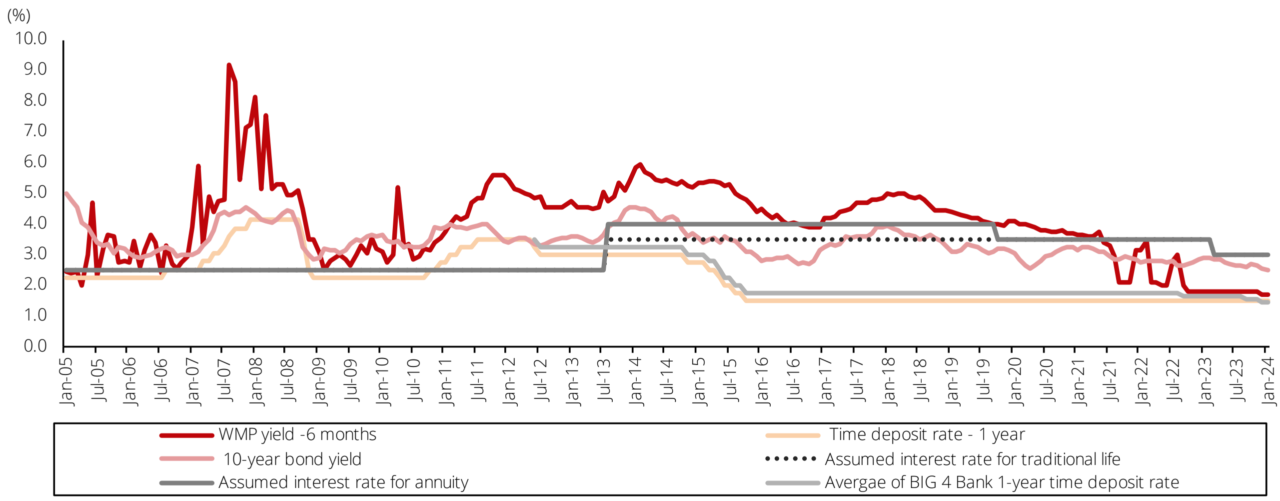
We saw a strong rebound in the value of new business (VNB) among Chinese life insurers in 2023 after the COVID-19 measures were lifted, with y-o-y VNB growth ranging from 14%-41% in 9M23. This was mainly driven by the last-minute sales effect that was a result of the lowering of assumed interest rates and surging demand for savings products, which were benefits felt from the bank lowering its deposit rate and a low base effect. Moving into 2024, we expect China life insurers' VNB to increase by a single digit y-o-y.

Investors are overconcerned about the negative impact of regulatory actions on the growth of premiums. These include 1) the lowering of assumed interest rates, 2) cuts in bancassurance commission fees, and 3) prohibiting insurers from collecting premiums in advance during the open-year sales campaign. During our recent talks with the managements of listed insurers, they maintained a positive tone for their open-year sales campaign and the full-year outlook. This was mainly driven by 1) the strong demand for savings products amid an economic downturn and consumers' reduced risk appetite; 2) the returns of annuity/incremental whole life still being more attractive than bank deposits (Figure 3); and 3) banks facing pressure to grow fee income, which makes them more willing to push for bancassurance products in FY24 (Figure 4).

In the agency channel, we expect the positive VONB growth to be mainly driven by the rising number of resilient, high-productive agents, while the product mix also continues to shift towards savings, given consumer demand. In the bancassurance channel, insurers have already completed renegotiations and signed contracts with the majority of their bank partners. The restrictions on bancassurance sales should be removed going forward, and we maintain our positive views on the bancassurance channel's growth in FY24F. Furthermore, some market leaders with strong bargaining power, such as AIA, also saw an improvement in their VNB margin in 3Q23 due to the lowering of assumed interest rates and cuts in bancassurance fees.

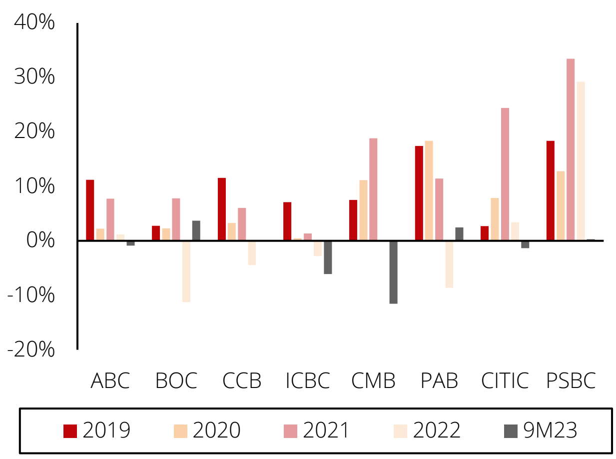
Despite concerns over an economic slowdown and weak consumption sentiment in China, we expect annuity and incremental whole life to drive VNB growth in FY24F. Among life insurers in China, we expect AIA China to lead the VNB growth in FY24F, mainly driven by 1) a solid protection mix and better-than-peer VNB margin; 2) resilient growth in the number of active agents and new recruitments; and 3) increasing VNB contribution from newly expanded territories, with the pace of new expansions being on track (1-2 new provinces per year) and rising agent productivity from the new provinces/cities.

Fig 3. Chinese banks' deposit rate, 10-year bond yield, and assumed interest rate for insurance



Source: Bloomberg, DBS HK

Fig 4. Y-o-y growth (%) in Chinese banks' fee income

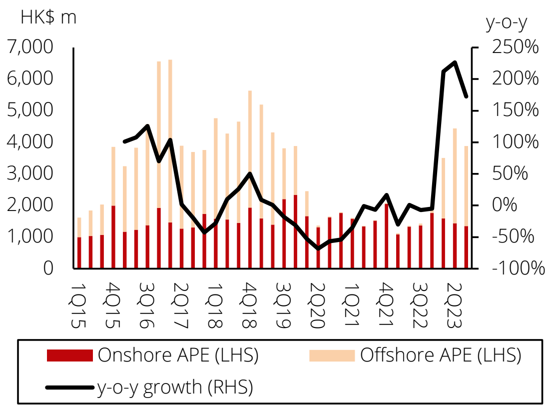


Source: Company data, DBS HK

- MCV remains key driver of HK growth

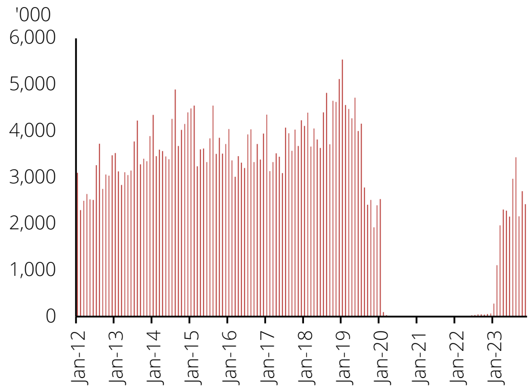
Following the reopening of the HK-China borders, total annualised premium equivalent (APE) rose 91% y-o-y in 9M23, mainly driven by the MCV segment, which saw a 69-fold increase in APE sales, while the domestic market also saw resilient growth during the period (Figure 5). The MCV segment accounted for c.40% of total APE in HK, close to the pre-pandemic level. AIA's and Prudential's (2378 HK) HK VNB outperformed that of other insurers, with its VNBs having doubled and tripled in 1H23, respectively, mainly driven by a higher MCV and protection mix. Looking forward, as the number of MCV arrivals has not yet been capped compared to the peak level seen pre-pandemic (3.3m in Nov 2023 vs. 5.5m in Jan 2019, Figure 6), we expect AIA and Pru HK to still benefit from MCV arrivals edging up, and deliver high double-digit VNB growth in FY24F, mainly supported by 1) a further reactivation of MCV-focused agents after the pandemic, 2) the expectation of a solid protection mix in terms of new business cases, 3) the easing pressure of VNB margin dilution with the ticket size returning to normal, and 4) the expectation of resilient domestic growth.

Fig 5. HK onshore/offshore APE sales trend



Source: HKIA, DBS HK

Fig 6. MCV inbound visitor number trend

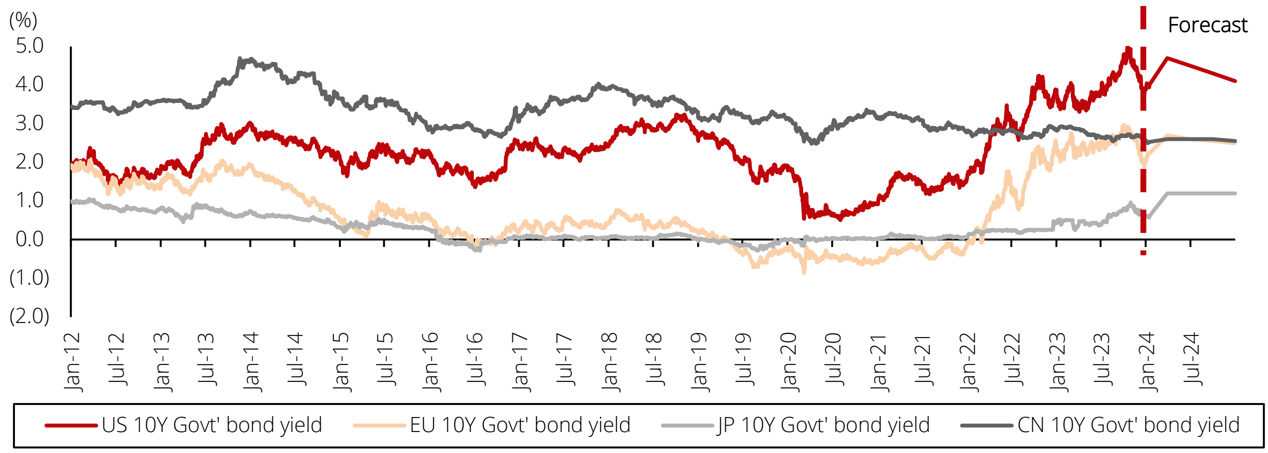


Source: CEIC, DBS HK

- Life growth muted in developed markets

In developed markets, elevated rates are expected to support growth in premiums by providing more attractive returns to policyholders, while being partially offset by competition from bank deposits and other alternative choices, such as money market funds. We are more positive about life demand in the EU (Allianz/AIA) and Japan (Tokio Marine) than in the US due to less choice for alternative investments that offer higher returns in the former two markets.

Fig 7. 10-year govt bond yields in major markets

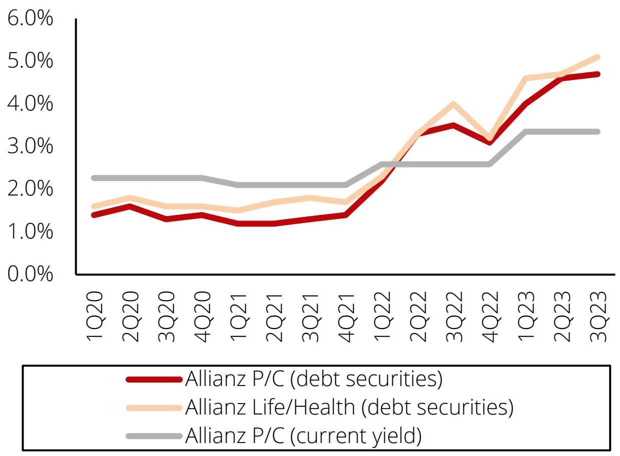


Source: Bloomberg Financial L.P., DBS HK

Recurring yield to further improve

Following multi-year lows or negative interest rates in major developed countries, 10-year government bond yields are expected to stay elevated in 2024 compared to the past 10-year average (est. 4.4%/2.6%/1.2%, on average, in US/EU/JP in 2024 vs. past 10-year average of 2.3%/0.5%/0.2%, respectively), despite the expectation of 100bps in policy rate cuts by the FED and ECB in 2024 (Figure 7). We hence expect a continued improvement in insurers' recurring yield, driven by higher reinvestment yield. Using Allianz as a case in point, Allianz P&C's current yield rose from 2.59% by end-2022 to 3.35% by end-3Q23, while its reinvestment yield has surged to 4.7% for debt securities, surpassing the current yield by 130bps, suggesting room for growth in recurring yield (Figure 8).

Fig 8. Allianz's current yield vs. reinvestment yield



Source: Company data, DBS HK

We believe rate cuts are more positive for P&C insurers than lifers, given the former's positive duration gap, although lifers with low interest rate sensitivity will also show robust investment return. Regional insurers, including Allianz, AIA, and Manulife, are less sensitive to interest rate movements due to their effective asset/liability hedging strategies, while China insurers are typically more sensitive to interest rate movements, given their larger duration gap between assets and liabilities (Figure 9).

Fig 9. Insurers' sensitivity analysis

		Allianz	AXA*	AIA	Prudential*	Manulife
S/h equity						
Interest rate	+50bps	-1%	2%	0%	-1%	0%
	-50bps	1%	-2%	0%	-1%	0%

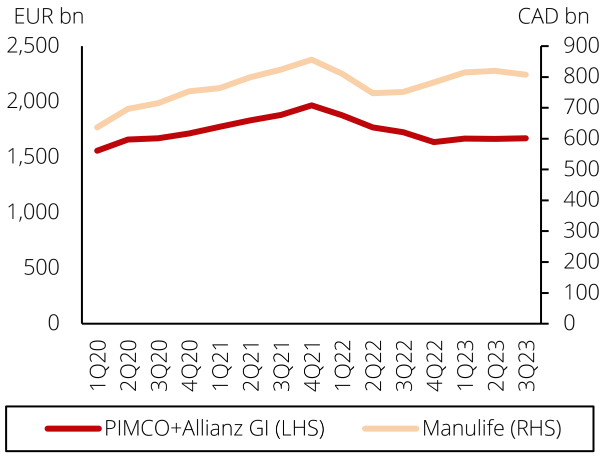
		Ping An L&H	China Life	CPIC Life*	Taiping Life*	PICC L&H
Embedded value						
Investment return and	+50bps	8%	7%	8%	7%	8%
risk discount rate	-50bps	-8%	-7%	-8%	-8%	-8%

Note: AXA, Prudential, CPIC, and Taiping based on 2022 data; otherwise, based on 1H23 data

Source: Company data, DBS HK

Insurers with a strong asset management arm (such as Allianz GI and PIMCO of Allianz) are also likely to benefit from an inflow of funds with the expectations of rate cuts by the ECB and FED in the EU and US (Figure 10), respectively. With early indications of reflation success, the Bank of Japan (BOJ) is expected to exit the negative policy-balance rate, from -0.1% to reach 0% in 2024, which may lead to the appreciation of the yen against the USD. We remain cautious about Tokio Marine's profit in FY24F, as 60% of it is contributed from overseas assets (mainly in the US) and it is thus more impacted by any appreciation of the yen against the USD.

Fig 10. Asset management fund in/outflow trend

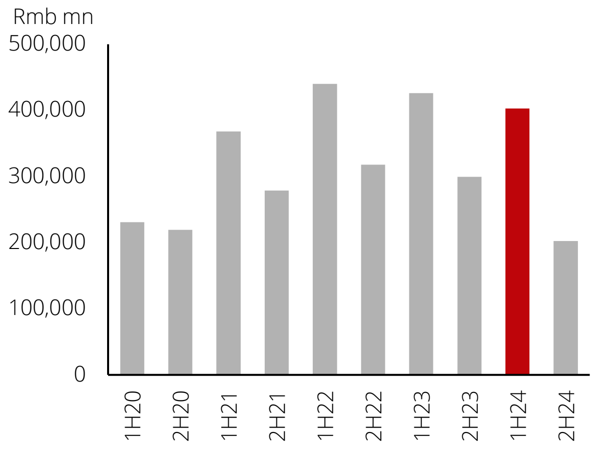


Source: Company data, DBS HK

Limited downside to China insurers due to property exposure

The property risk in China may still be a key overhang in the near term for Chinese lifers, as 1H24 may still see another peak of offshore bond repayment cycle for Chinese developers; and so far, there's still no "firm and effective" policy being rolled out to support the property market (Figure 11). Sentiment wise, we think any negative news – i.e., should developers default on their payments or should the policy stimulus fail to boost the economy – may still affect insurers' share prices.

Fig 11. Developers' offshore bond repayment cycle



Source: CRIC, DBS HK

We conducted a stress test on the potential impairment of China insurers' property, where we assume their property exposure would be impaired by 5%-50% across estimated asset classes related to the property sector and LGFV exposure. Under an extreme, distressed scenario, we assume 1) debt, equities, NSAs would be impaired by 50%; 2) mortgage and developer loans would be impaired by 5% and 30%, respectively; c) estimated LGFV exposure would be impaired by 5%; and d) assets within the "real estate subsidiaries" would be impaired by 50%, except for investment properties, which would be impaired by 25%. We further apply a 0.8x P/B ratio to the post-impairment fair value to reflect the weak sentiment towards China insurers. We hence estimate Ping An, China Life and CPIC to have further 14%-30% downside compared to their current market capitalization. As the likelihood of such an extreme, distressed scenario occurring is close to zero, it would be more meaningful to consider a scenario somewhere in the middle that reflects investors' concerns over economic slowdown and property downturn. We hence believe much of the negatives have already been priced in. (Please find out more details in our report on stress testing China insurers' impairment on their property exposure, "How much of the negatives are priced in?").

We see the following potential events becoming positive signals for the market, which will help drive an improvement in investment sentiment. These include 1) the confirmed announcement of the 3rd Plenary Meeting of the 20th Central Committee to outline how Chinese leadership plans to manage the structural slowdown and boost domestic consumption, 2) effective policy stimulus to bolster the slumping property market, and 3) the end of another offshore bond repayment peak cycle for developers, which will likely be seen by end 1H24.

With the risk-reward looking increasingly attractive at the current level and China insurers expected to offer a dividend yield of 7-9%, we suggest that investors gradually accumulate shares upon further share price pullbacks.

Prefer P&C insurers over lifers on better asset/liability positive amid rate downcycle

Overall, we prefer P&C insurers over lifers amid the expected global interest rate downcycle ahead, as lower interest rates are generally a tailwind for P&C insurers, given their shorter liability duration and net positive asset-liability duration gap compared to life insurers. Other positive drivers include the improving combined ratio outlook and further room for the improvement of recurring investment yield. We also see insurers with strong asset management franchises, such as PIMCO/Allianz, benefitting from the cyclical demand for bond investment, given the peaking of the rate cycle and hence the potential inflow of funds.

Our top picks include Allianz (ALV GY, BUY) and PICC P&C (2328 HK, BUY). We also like AIA (1299 HK, BUY) for its secular growth potential in the China and Asia Pacific life insurance space, with an undemanding valuation.

Fig 12. Peers' comparison table

		Price	DBS	TP	Mkt Cap	PBV (x)		PEV* (x)		Div Yield (%)		ROE (%)	
Coverage	Ticker	(LC)	rating	(HK$)	(US$ m)	FY24F	FY25F	FY24F	FY25F	FY24F	FY25F	FY24F	FY25F
H-share insurers													
AIA	1299 HK	65.05	BUY	118.00	88,954	1.9	1.8	1.3	1.2	2.7%	2.9%	13.5%	13.8%
China Life - H	2628 HK	9.36	BUY	16.00	82,519	0.6	0.5	0.2	0.1	7.2%	7.9%	12.6%	13.1%
CPIC - H	2601 HK	15.10	BUY	24.00	25,529	0.5	0.5	0.3	0.3	8.5%	9.6%	13.7%	14.0%
Manulife	945 HK	168.00	BUY	182.00	38,724	1.0	1.0	0.8	0.7	5.4%	5.0%	11.5%	12.1%
PICC Group - H	1339 HK	2.54	HOLD	2.80	25,702	0.4	0.3	0.3	0.3	10.5%	11.5%	8.4%	8.5%
PICC P&C	2328 HK	9.95	BUY	12.50	26,953	0.8	0.7	n.a.	n.a.	6.2%	7.0%	12.4%	12.8%
Ping An Ins - H	2318 HK	34.60	BUY	66.00	88,863	0.5	0.5	0.5	0.5	9.1%	9.9%	13.6%	13.8%
China Taiping	966 HK	6.72	BUY	9.50	2,779	0.2	0.2	0.1	0.1	8.2%	9.6%	6.2%	6.3%
ZhongAn	6060 HK	13.96	BUY	27.00	2,446	1.0	1.0	n.a.	n.a.	0.0%	0.0%	1.8%	2.9%
Prudential	2378 HK	82.50	BUY	130.00	28,293	1.4	1.3	0.6	0.6	2.1%	2.3%	13.1%	13.0%
Average						**0.8**	**0.8**	**0.5**	**0.5**	**6.0%**	**6.6%**	**10.7%**	**11.0%**
A-share insurers													
China Life - A	601628 CH	28.69	HOLD	27.68	82,520	2.1	2.0	0.6	0.5	2.0%	2.2%	12.6%	13.1%
CPIC - A	601601 CH	24.77	HOLD	24.62	25,530	1.0	0.9	0.5	0.5	4.5%	5.0%	13.7%	14.0%
Ping An Ins - A	601318 CH	41.15	BUY	52.74	88,864	0.7	0.7	0.7	0.6	6.6%	7.2%	11.5%	12.1%
PICC Group - A	601319 CH	5.10	HOLD	5.51	25,703	0.9	0.8	1.6	1.5	4.5%	4.9%	8.4%	8.5%
Average						**1.2**	**1.1**	**0.9**	**0.8**	**4.4%**	**4.8%**	**11.6%**	**11.9%**
Regional Insurers													
Sun Life Financial	SLF CN	69.11	NR	NA	29,727	1.8	1.6	n.a.	n.a.	4.6%	4.9%	17.6%	17.3%
Great-West Lifeco	GWO CN	44.10	NR	NA	30,133	1.7	1.6	n.a.	n.a.	4.9%	5.1%	16.3%	16.5%
AXA	CS FP	30.75	BUY	35.00	75,451	1.4	1.3	2.3	2.0	6.5%	6.9%	17.0%	16.6%
Allianz SE	ALV GY	246.85	BUY	286.00	104,356	1.6	1.5	2.0	1.9	5.3%	5.6%	16.8%	16.6%
Legal & General Gp	LGEN LN	2.53	NR	NA	18,993	2.5	2.4	n.a.	n.a.	8.4%	8.9%	28.7%	29.2%
Aviva PLC	AV/ LN	4.34	NR	NA	15,066	1.2	1.2	n.a.	n.a.	8.1%	8.6%	12.7%	11.8%
Average						**1.7**	**1.6**	**2.1**	**2.0**	**6.3%**	**6.7%**	**18.2%**	**18.0%**
Japan & Korea insurers													
Samsung Life	032830 KS	63,800	NR	NA	9,257	0.3	0.2	0.2	0.2	6.4%	6.9%	4.8%	4.9%
Hanwha Life	088350 KS	2,690	NR	NA	1,728	0.1	0.2	n.a.	n.a.	7.3%	8.4%	4.6%	4.8%
Tongyang Life	082640 KS	4,470	NR	NA	536	0.2	0.2	n.a.	n.a.	9.8%	10.0%	5.6%	6.3%
Japan Post Insuranc	7181 JP	2,172	NR	NA	6,942	0.3	0.3	n.a.	n.a.	4.3%	4.4%	3.5%	3.2%
Dai-ichi Life Holding	8750 JP	2,361	NR	NA	21,102	0.7	0.6	0.3	0.2	3.7%	3.8%	9.0%	8.8%
Average						**0.3**	**0.3**	**0.2**	**0.2**	**6.3%**	**6.7%**	**5.5%**	**5.6%**
Other Asian insurers													
Cathay FHC	2882 TT	44.35	NR	NA	20,656	0.9	0.8	n.a.	n.a.	3.5%	3.8%	10.2%	10.2%
Fubon FHC	2881 TT	64.60	NR	NA	26,495	1.1	1.0	n.a.	n.a.	3.4%	3.7%	11.2%	11.1%
Shin Kong FHC	2888 TT	8.57	NR	NA	4,199	n.a.	n.a.	n.a.	n.a.	1.8%	2.3%	n.a.	n.a.
Bangkok Life	BLA TB	19.00	NR	NA	922	0.6	0.6	n.a.	n.a.	4.2%	4.8%	8.8%	9.5%
BAO Viet Holdings	BVH VN	40,700	NR	NA	1,232	1.3	1.3	n.a.	n.a.	2.3%	2.5%	8.0%	8.8%
ICICI Prudential Life	IPRU IN	486.30	NR	NA	8,302	6.4	6.1	1.5	1.3	0.4%	0.4%	11.5%	12.7%
Tokio Marine	8766 JP	3820.00	HOLD	3,800.00	51,790	1.8	1.7	n.a.	n.a.	3.2%	3.7%	14.8%	13.7%
Average						**1.0**	**0.9**	**n.a.**	**n.a.**	**3.0%**	**3.4%**	**9.5%**	**9.9%**

Note: BBG or Visible Alpha consensus used for non-rated (NR) stocks

Closing price as of 25 Jan 2024

Source: Company data, Bloomberg Finance L.P., DBS HK

DBS HK recommendations are based on an 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 share price catalysts within this time frame)

**Share price appreciation + dividends*

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