Growing Peacefully – A Look at Ping An

2318 HK / 601318 SS

Grow with China's domestic savings

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“Time is the friend of the wonderful company, the enemy of the mediocre.”

-Warren Buffett

Executive summary

- Ping An is an insurance giant in China, giving exposure to rising wealth management needs in China
- Investment policies are sensible, forward-looking but not too aggressive
- Optionality: Exposure to online lending, online insurance, apps to adapt to new modes of business
- International exposure is limited

Fertile ground

- China's middle income and high income class has a rising need for savings products. Banks pay 1.75% for a 1-year Term Deposit, while inflation is ~2.0% in recent years
- China's equity and bond markets could provide GDP-like returns of over 6%, and insurance could be a route to deliver that to policyholders, minus fees and expenses

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Special aspects of China

- P2P market has just started being regulated. Wild Wild West.
- Partnership model for new ventures limits risk in some areas:
  - Tencent, Alibaba are P2P venture partners in Lufax
  - Didi Kuaidi combined forces against Uber China

Ping An – A Peaceful Giant

- Fortune #96; Forbes #32. Assets base of USD 0.7 trn (2015)
- Individual customers: over 109 mn
- New customers in 2015: 30mn
- Written premiums in 2015:
  - RMB 300bn in Life (~USD 46bn)
  - RMB 160 bn in P&C (~USD 25bn)
- 8% total investment yield of funds at group level (2015)
- 5.8% net investment yield
- Combined ratio of 95.6% in Property & Casualty
- Bank Net Interest Margin : 2.8%, achieved with a cost-income ratio of 31%

Scope of business

- Revenue segments (2015) :
  - 50% of revenues: Life
  - 25%: Banking
  - 20%: Property and Casualty
- New Age businesses:
  - P2P: owns 43% of Lufax: 3.6mn active/ total 18mn+ users.
  - Zhong An: First online-only insurance.
  - Health Cloud: 30mn app users
  - Real Estate: Haofang is a portal (7mn users; 51 cities)
  - Payments: YiWallet (25mn users)

Shareholder dynamics

- ~32% owned by Foreign Investor No.1 : CP Group (Thailand) (bought from HSBC)
- Non-executive Directors: 5
- Executive Directors: 6
- Independent Directors on board: 6
- Chairman is an Executive: Founder and CEO MA Mingzhe
- Wall Street Journal reports stake by family (Wen Jiabao's)
- JP MorganChase: 9.1%
- Blackrock: 4.9%

Catalysts

- Lufax IPO in 2016. Valuation (Jan 2016): USD 18.5bn
- Business Trends:
  - Bank deposit rates unattractive for long-term savings
  - Online P2P lending is poised for explosive growth
  - Insurance companies may dominate domestic capital allocation in the years to come

Ways to express a view

- 2318 HK:
  - Shares trading at HKD (1.6 price to book). Good quality business at a fair price.
- 601318 SS
  - Shares trading in RMB (Shanghai Listing)
- Bonds available for both domestic (Chinese) investors and overseas institutions
- First USD bonds: January 2016

Data as of 01 April 2016

FAQ

- Exposure to China recession?
  - Possibly. This is a through-the-cycle investment. A slowing economy will still see positive nominal GDP growth
- Exposure to property crash?
  - Yes. Exposure will be through corporate bond portfolio and real estate loans. Financing exposure is 28% of total. This can cause a deep-drawdown in net asset value. A well-managed insurance company could make good long-term investments in a crisis (distressed debt). Group is reducing exposure to real estate financing
- Demographic challenges?
  - Repeal of the one-child policy will increase spending per household. However impact may be limited due to families choosing not to have a second child for economic reasons.

Appendix: Ratios and data

- **Ping An (HK)**
- Ticker: 2318 HK Equity on Bloomberg
- Founded: 1988
- Head office: Shenzhen, China
- Employees: (31-December-2015) 275,011
- Market cap (01-April-2016): 674.6 bn (USD 87.05bn at HKD 7.75 per USD)
- Price per share: 36.05 HKD
- Price to book: 1.64x
- Loss Ratio: 56.7%
- Expense Ratio: 38.9%
- Combined ratio (TTM): 95.6%
- Shares outstanding: 7,447.6 million
- Free float: 63%
- Dividend yield: 1.5% trailing 12 months
- Auditor: PricewaterhouseCoopers

Data is from Bloomberg (01 April 2016)

Appendix: Ratios and data

- **Ping An (Shanghai)**
- Ticker: 601318 SS Equity on Bloomberg
- Founded: 1988
- Head office: Shenzhen, China
- Market cap (01-April-2016): RMB 570bn (USD 87.7bn @ 6.5RMB per USD)
- Price per share: RMB 31.92
- Price to book: 1.75x
- Combined ratio (TTM): 95.6%
- Shares outstanding: 10,832 million
- Free float: 78.4%
- Dividend yield: 1.35% trailing 12 months
- Auditor: PricewaterhouseCoopers

Data is from Bloomberg (04 April 2016)

Appendix: Insurance key ratios

- Loss ratio: what you expect to lose due to the risk you have accepted
- Expense ratio: your cost of running the business (salaries, commissions, rent, travel, etc..)
- Combined ratio: add the loss ratio and expense ratio. Ideally should be below 100%. Insurance industry can survive with combined ratios over 100% too, as timing of claim can be quite different from premium paying period, allowing investment income from the premia collected (float) to be earned and kept. Such income may or may not be shared with policyholder, depending on policy.