Investor's Newsletter（July 20, 2017） Vol. No. 7 in 2017

CPIC（SH601601, HK02601）

Stock Data (ending Jun 30, 2017)

Total equity base (in million)	9,062
A-share	6,287
H-share	2,775
Total Cap（in RMB million）	289,769
A-share	212,941
H-share（in HKD million）	88,523
6-mth highest/lowest	
A-share (in RMB)	33.87/25.66
H-share (in HKD)	32.25/27.05

Investor Relations Calendar

August 29, 2017

CPIC Interim Results Announcement

Shanghai

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Premium Income (Unit: in RMB million)

	Jan. to Jun.	Changes	June	Changes
P&C	52,556	6.90%	9,415	22.54%
Life	110,551	34.43%	16,805	23.82%

Company Updates

- **CPIC hosts Investor Day in Yinchuan**

CPIC hosted an investor day on the topic of "Drivers of Sustainable Value Growth of Life Insurance Business" in Yinchuan of Ningxia on June 26.

During his opening speech, Board Secretary MA Xin reviewed the achievements of CPIC's customer-oriented transformation in four respects, i.e, channel mix improvement, growth of value per customer on the back of product innovation, customer recognition as a result of enhanced experience, mid-and-back-office support for front-end with increased use of new technologies. Mr. ZHANG Yuanhan, Group Chief Actuary, and Ms. CHEN Xiujuan, Life Chief Actuary, made consecutive presentations on drivers of life insurance value growth, mix of profit sources and product strategies. Mr. Zhang reviewed the value growth of CPIC Life over the past decade since CPIC's listing, and shared his insights on profit mix as well as pricing strategies. Ms. Chen focused on the development of long-term protection business, followed by an outlook of the company's product strategy in the context of new regulations.

During the Q & A session, analysts and investors interacted with company management on CPIC's mid-and-long-term strategy, shareholder dividend policy, profit mix of life insurance, the release of residual margin, solvency management, outlook of NBV margin and improvement of agency productivity.

- **CPIC kicked off preparation for new IFRS implementation**

On June 19, CPIC Group held a preparatory meeting for new IFRS implementation. A project team across the Group and its subsidiaries was set up, responsible for the preparation over the next 2 years, covering rule interpretation, impact analysis, plan formulation and IT system revamping.

The implementation of IFRS 9 and IFRS 17 will have profound impact on insurers' financial reporting, with far-reaching consequences for their business operation such as product strategy, investment strategy, asset liability management, budget indicators and performance evaluation.

Briefing

Q & A for 2017 Investor Day

1. **What is the amount of amortized residual margin annually? How do you choose the carrier of amortization?**

Profit consists of the release of residual margin and risk margin, and the return on net asset. The return on net asset has been stable over the years, ranging from 60 to 70 billion annually. Residual margin constitutes the bulk of profit, while risk margin has a much smaller share. We disclosed accounting profits over the years excluding impact of discount rate curve movement, which rose from 2.4 billion in 2011 to 14.9 billion in 2016, with an annual compound growth of 44%, driven largely by amortization of residual margin.

The amortization of residual margin will stretch over the entire insurance period. The choice of carriers for the amortization is based on regulations of the Ministry of Finance and CIRC in 2009, considering service types (protection or savings), and is "locked up" for the entire amortization period. The method of amortization may not be comparable across different insurers.

2. **Your analysis of first-year solvency on new business is very clear. But what about the capital requirement for the same business into the second year? Does the required capital on your VIF go up over the years?**

The first-year required capital for new business for Q1 2017 was 12.7 billion, while the actual capital amounted to 31.6 billion, meaning a margin of 18.9 billion. Given the time difference between first-year actual capital and accounting profits, the same business will generate sufficient actual capital in the 2nd policy year. Of course, it is difficult to make a breakdown. We would recommend looking at the overall solvency. Currently, there is a healthy matching between required capital and actual capital on our in-force business, and the solvency margin ratios as of Q1 2017 slightly improved from the end of 2016.

3. **How do you define long-term protection (LTP) business?**

Our LTP business includes whole life, term life, and long-term A/H. Anxingbao's base policy offers personal accident cover, and considering consumers expectations, also features return of premiums via an endowment rider. Overall, the product provides high level of protection and is therefore included in the LTP business. Chaonengbao and Aiwuyou both combined health cover with endowment, which are primarily protection products. In short, the definition is based on the level of protection of products, irrespective of whether it's a traditional or participating product. For example, the Jin product series, also defined as LTP business, is a combination of a participating base policy and a non-par rider of critical illnesses. Savings products consist of endowment, annuity and participating products such as Dongfanghong and Xingfu Xiangban, which offer cash policy-holder dividend.

4. **Further to the comparison of the share of the investment spread between high pricing interest rate product and low pricing rate product, could you give us more color on the mix of the new business value in terms of investment margin, mortality and expense gains?**

First, under current Chinese GAAP and EV regime, profit release is based on comprehensive margin (residual margin+ risk margin) which covers a range of factors, and can hardly be attributed to one particular source or factor. Second, variance analysis is more important, i.e, the difference between expected profit and actual experience. The variance is a reflection of both changes of the environment and the soundness of assumptions, hence a better measure of business performance. Third, China's vast insurance market can accommodate product diversity, leading to difference in profit sources across insurance companies. A market big enough with diverse customer needs is central to profit. There are not yet widely accepted methods for profit source analysis in the industry. As an international norm, the share of investment spread on long-term non-unit-linked products is over 50%.

5. **You delivered fast improvement in NBV margin over the past decade. Any indication on how much the margin can improve in the future?**

China's insurance market still boasts huge potential, with protection business low in penetration and relatively high in NBV margin. We believe that given rising demand for risk protection, and the regulator's focus on protection, our NBV margin will continue to improve.

6. **Overseas investors like your "pure player" strategy. What is your**

strategy in the next 3-5 years, given the election of a chairman?

On June 9th the new Board of Directors of CPIC was elected, and its chairman, Mr. KONG Qingwei also got the qualifications approval from CIRC recently. After joining CPIC, Mr. Kong articulated his thinking about the company's future strategy. First is adhering to the key value proposition of insurance. CPIC will continue to tap the huge potential of China's insurance market and has no intention to diversify. This strategy has been consistent, well aligned with the regulator's priorities and helped us overcome challenges of economic cycles over the past decade since our IPO. Second is to forestall major risks. Third is innovation and transformation. The company will put forward its 2nd program of transformation, an extension of the 1st 5-year customer-oriented transformation initiative.

7. **Under C-ROSS, LTP business helps to boost solvency. Do you consider further increasing the pay-out ratio to improve your capital efficiency?**

The company is committed to providing sustainable and stable returns to its shareholders. Since our IPO, DPS has been on the rise steadily, being 0.3 between 2007 and 2009, 0.35 between 2010 and 2012, and higher than 0.4 between 2013 and 2015. The dividend for 2016 was 0.7, with a pay-out ratio of 52.6%, much higher than the average 31% for Shanghai-listed firms. Besides, the dividend policy is also part of our capital planning strategy. We will consider other factors like business development and solvency when setting the dividend level.

8. **Under C-ROSS, most insurance companies' solvency improved. Yet there may be more volatility. What is your internal target range of the solvency margin ratios?**

Under C-ROSS, both our actual capital and required capital have been different. Currently we boast strong solvency margin ratios. The required capital is composed of market risk, insurance risk and credit risk, with market risk accounting for 70%, consisting of equity risk and asset liability mismatch. Solvency margin ratios are closely linked to a company's risk appetite. We set 2 extra thresholds on top of the 150% of the required capital by CIRC, and split the actual capital for market risk, insurance risk and credit risk. Under the rolling stress testing scenarios, 200% level will be defined as "comfortable". A big variable is accounting profits which are heavily impacted by capital market volatility. Of course, given different investment strategy and business diversification effect, insurers with similar business volume may face quite different reserve requirements.

9. Your agency channel productivity seems less than that of your peers. Any plan or thinking to drive productivity gains?

In a way our agent productivity is not entirely comparable with that of our peers. First, our average pay duration is more than 8 years, which means smaller annual premium. Second, our product portfolio focuses on protection business, which has a smaller average policy size. Anxingbao, for example, averages about 2,000 per policy. Generally speaking, our productivity is aligned with the company's product strategy, and delivered sustained improvement in 2016 amid fast head-count growth. That being said, we are committed to further productivity gains via, among others, enhanced "infrastructure management" of the sales force, such as attendance, retention and improvement in agents' skills in both new customer acquisition and up-sell.

10. Any concrete plans for the promotion of the tax-deferred pension business? By your estimate, what is the potential of the business?

It is possible that the tax-deferred pension scheme will be rolled out by the end of the year. The product will be attractive, given under-supply of old-age cover by private insurance. In the context of China's demographic shift and increasing demand for protection against survival, old-age, illnesses, death and disability, this type of product holds great promise. In product design, it may take the form of universal products, combining accumulation of funds on the part of insurers and sharing of profits and risks between insurers and customers, similar to the tax-advantaged health insurance product.

11. Recently CIRC imposed restrictions on fast return products and universal life as riders. What is its impact on your product strategy for the jump-start campaign next year?

There is a mismatch between consumers' strong demand for protection and the relatively short supply of such products on the market. We are working on products for next year's jump-start campaign, which may consist of upgrading the existing products and development of new products to diversify our offerings. Of course, all products will comply with the latest regulatory requirements. Tentatively, the new products could be designed as participating insurance.

12. **Under C-ROSS, will a large share of protection business translate into an equally big share of insurance risk in capital requirement?**

The insurance risk will have a relatively small share, similar to credit risk, even for companies with a high proportion of protection business. Insurance risk is composed largely of morbidity, mortality and expense rate, and therefore is mostly manageable. On the other hand, the market risk is still the most important risk and has the biggest share of the required capital for life insurers, given the mismatch in duration of assets and liabilities.

13. **With the issue of document No.134 by CIRC, do you have specific plans for the development of new products and withdrawal of existing products?**

The company will implement its product plan steadily in the run-up to October 1, when the new regulations, document No. 134 will come into force. Certain products will be withdrawn gradually by October 1, and the product of fast return of premiums will be withdrawn before June 30th. We target a top-line growth in line with the market, and will not seek to drive sales through hype about product termination or withdrawal.

14. **Your PPT shows on slide 17 that the product with higher pricing interest rate has higher NBV margin. Why? Is it because its a traditional product while the one with a lower rate a participating product?**

The two products are slightly different in NBV margin, being 27.3% and 24.3% respectively. The difference mainly stems from the impact of discounting and reserving under C-ROSS EV system. Yet there is no substantial difference for customers or insurers as they are the same in premiums.

Through the example we mainly want to highlight their difference in the share of investment spread and sensitivity to interest rate risk. The share of investment spread is 41% for the product with a higher pricing rate, while the share is 71% for the one with a lower pricing rate. Yet their exposure to interest rate risk is similar, being 5.7% and 5.8% respectively. Of course, different products may show different results. Participating insurance will have a smaller share of investment spread and therefore, less exposure to interest rate risk. For the purpose of comparison, both products in the example are traditional.

Regulatory Updates

- **News report on China's 5th National Financial Work Conference (excerpt)**

China's National Financial Work Conference was held in Beijing from July 14th to July 15th. XI Jinping, President, General Secretary of CPC Central Committee and Chairman of CPC Military Committee delivered an important speech. Mr. Xi points out that the financial services industry forms part of a nation's core competitiveness, and financial security is an important part of national security, with the financial system an important component of the infrastructure of China's social and economic development. It's imperative to strengthen the stewardship of the sector by the Chinese Communist Party, pursue progress amid stability, adhere to the industry's inherent development patterns, and give priority to the 3 central tasks of serving the real economy, manage financial risks and deepen financial reform. To this end, efforts will be enhanced to intensify regulations, improve governance of financial institutions, deepen the financial system, accelerate the shift of mode of development, enhance the rule of law in the financial services sector, ensure financial security and promote the virtuous cycle of real economy and the financial market.

Xi outlines 4 principles for China's financial market: first, **return to the basics**, i.e., serving the needs of real economy; second, **improve mix**, namely, optimize the financial market, product line-up and financial institutions; third, **enhance regulation** to fend off major financial risks; fourth, **uphold market orientation** so that market will play a decisive role in financial resources allocation.

XI Jinping reiterates that serving the development of the real economy is the primary duty of financial services, and is the reason the industry came into being in the first place. Returning to this basic value proposition is the long-term solution for mitigating financial risk. He calls for formulation of new development philosophies, i.e., giving priority to quality and efficiency, and focusing more on the supply side restructuring and optimization to facilitate shift of growth drivers. Capital market financing will be higher on the agenda. China will put in place a multi-tiered capital market with strong financing capabilities, sound infrastructure, effective supervision and effective protection of investors' legitimate rights and interests. The mix of bank-intermediated financing needs improving, with efforts to push for strategic transformation of major SOE banks, and further development of small-and-medium-sized banks and private-owned financial institutions. Insurance industry will be encouraged to fulfill its key mandate of providing long-term risk management and protection. An inclusive financial services system will be built to improve access to financial services of micro-enterprises, farmers and people in remote places. The financial sector shall play a more important role in targeted poverty alleviation and China's environment protection. Efforts will also be made to help financial institutions to lower operational costs, streamline business procedures to control the funding costs for the real economy.