# Investor's Newsletter（September 28, 2020）

vol. No.9 in 2020

**CPIC（SH601601，HK02601, LSE CPIC）**

## Stock Data (ending August 31, 2020)

| | |
|---|---|
| Total equity base (in million) | 9, 620 |
| A-share | 6, 845 |
| H-share | 2, 775 |
| Total Cap (in RMB million) | 264, 290 |
| A-share | 195, 111 |
| H-share (in HKD million) | 59, 808 |
| GDR(in USD million) | 2, 379 |
| 6-month highest/lowest | |
| A-share (in RMB) | 33. 80/26. 37 |
| H-share (in HKD) | 26. 25/18. 16 |
| GDR(in USD) | 22. 40/17. 60 |

## IR Calendar

**Investor Relations Department**
Tel: 021-58767282
Fax: 021-68870791
E-MAIL: ir@cpic.com.cn
Add: 15F, 1 Zhongshan Rd. S.
Shanghai, P.R. China, 200010

**Contact: LIU Qing**
Tel:021-33963088
E-MAIL: liuqing-055@cpic.com.cn



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## Premium Income (Unit: in RMB million)

| | January-August | **Changes** | August | **Changes** |
|---|---|---|---|---|
| **P&C** | 100, 870 | 13. 92% | 11, 959 | 18. 45% |
| **Life** | 166, 604 | -1. 74% | 18, 061 | -8. 37% |

# Industry Updates

● **Auto insurance comprehensive reform officially kicked off**

On 19 September, The Guidance on Comprehensive Auto Insurance Reform came into force.

The long-term objective of the reform is to better protect consumer interests, with short-term targets of "lowering prices, expanding coverage and improving quality". (1) Increase protection and limit on sum assured of the compulsory auto insurance: The limit on sum assured of compulsory insurance increases from RMB122,000 to RMB200,000. Introduce a regional floating modifier to the traffic accident factor. The cap of the factor remains unchanged, at 30%, while the floor lowers to -50% from -30%. (2) Expand and improve the scope of coverage and services of third-party insurance: Sum assured of third-party commercial is raised from a range between RMB50,000 and RMB5mn to RMB100,000 and RMB10mn. Previous riders are integrated into vehicle damage insurance without increasing consumer insurance spending, such as vehicle theft, window pane damage, self-combustion, engine flooding, waiver of deductibles, designation of repair shops, and failure in third-party recourse. (3) Optimize the pricing mechanism of third-party insurance premium rates, including enhancing the mechanism for the calculation of industry pure risk premiums, lowering the expense loading reasonably, merging the previous "discretionary channel factor" and "discretionary underwriting factor" into the "discretionary pricing factor", and gradually relaxing limits on the range of the pricing factor. (4)Reform market access and product management: launching the new standardised products for both compulsory and third-party. (5) Push forward reform of infrastructure: introducing in an all-around way the real-name premium payment system, vigourously promoting the use of electronic insurance policies and enhancing the application of new technologies. (6) Strengthen and improve supervision: refine mechanisms of premium rates review and product adjustment.

● **CBIRC releases industry updates for the first 8 months of the year**

On September 25, CBIRC released statistics of the insurance market in the first 8 months of the year. Total primary insurance premiums amounted to RMB3.32 trillion, a growth of 7.15%; claims pay-out reached RMB865.9 billion, up 4.45%; business and management expenses totalled RMB356 billion, an increase of 6.52%; funds under management amounted to RMB20.52 trillion, accounting for 91.88% of industry total assets.

● **Regulator launches campaign to assess and rectify bundled sales of life and health insurance products**

Recently, CBIRC issued a notice on the launch of a campaign to evaluate and rectify bundled sales of life and health insurance products. The effort focuses on 6 areas: improper business philosophies, incompliant bundled sales, unreasonable underwriting rules, irregular sales promotion and advertising, incomplete information disclosure and ineffective company management.

The campaign consists of 2 stages: self-assessment & rectification and regulatory actions, in a bid to rectify irregularities in bundles sales of life and health products and better protect consumer interests.

- **CBIRC issues document on supervision of health management services**

CBIRC recently issued The Circular on Supervising Health Management Services of Health Insurance Companies, which classifies health management services by insurance companies into 7 categories: physical check-up, health counselling, health protection, disease prevention, chronic illness management, hospital visits assistance and rehabilitation. It defines health management service as an intervention into customer's health risk factors so as to prevent diseases, control the progression of diseases and promote recovery. This, according to the document, will lower illness incidence and improve health conditions and in turn reduce health-care spending. It is also stipulated that health management as incorporated into insurance products shall not exceed 20% of the pure risk premium, instead of the previous cap of 10%.

## Company Updates

- **CPIC hosts 2020 Investor Day**

On September 24, CPIC hosted 2020 Investor day.

Chairman GU Yue and senior management of CPIC P/C made speeches on the theme of "Pursuing high-quality development with value-oriented transformation", focusing on the initiatives, effects and outlook of the company's transformation.

In the Q & A session, management answered questions of common interest from analysts, such as outlook for growth, KPI system, impact of automobile insurance comprehensive reform and company strategies, growth potential of non-auto business, development plan for health insurance, competition from Internet firms, and claims cost reduction from the use of technology.

## Summary of Recent Q&A

**Q: The company's general shareholders' meeting recently elected 3 new directors, and one of them comes from Hillhouse Capital. Is Hillhouse a shareholder? How many shares does it have? Is the**

**stake over 3%?**

A: Hillhouse Capital is a shareholder of the company, represented by Ms. LIANG Hong on the board. Currently the shareholding of Hillhouse does not meet requirement for information disclosure, so we have no further information to share. Besides, under the company' s Articles of Association, apart from shareholders who separately or jointly own over 3% of the company, the board or board nomination and compensation committee can also nominate director candidates. Under SEHK and LSE rules, the HKSCC Nominees Limited is the nominal holder of our H shares, and Citibank is the depositary of GDRs. Currently we have no further information to provide.

In the meantime, as the board lies at the core of corporate governance structure, its decision-making capability is essential to the company' s healthy and sustainable development. We are glad to see that the new board is more professional, diverse and international. In terms of non-executive directors, Ms. LIANG Hong joined the board as a famous economist, which is essential to an insurance company with AuM exceeding 2 trillion yuan. We believe she will play her part in analysis of macro-economic trends, major investment decisions and deployment in new areas. Swiss Re, our GDR cornerstone investor, nominated Mr. John Robert Dacey, its CFO as a director on the board. Given Swiss Re' s experience in insurance business, and in particular in big data, risk pricing and product innovation, Mr. Dacey will surely enhance our insurance expertise. In terms of non-executive independent directors, there is Ms. LIU Xiaodan, who has rich experience in domestic and overseas capital market transactions. Mr. JIANG Xuping, an expert in Internet marketing and management from Tsinghua University, serves as chairman of the newly-established Technological Innovation and Consumer Rights Protection Committee under the board. There is also Mr. Woo Ka Biu, Jackson, a well-known qualified lawyer in the UK, Australia and Hong Kong. His professional background in legal and compliance will improve our risk management capability as a company simultaneously listed in Shanghai, Hong Kong and London.

We are confident that the new board members will contribute to the continued improvement of our governance, paving the way for high-quality development of the company.

**Q: What is management view on the growth potential of the health industry and the steps you will take to seize the opportunity?**

A: We consider the health industry development in 2 dimensions, i.e., outlook for the industry and then what we will do.

In terms of the growth potential, our view is the potential is huge. First, China' s 13th 5-year program defines the Healthy China Initiative as a national strategy, and sets the target of considerably increasing commercial health insurance claims pay-out as a share of total health spending by 2030.

The share in 2018 was only 3%, while in some developed European markets such as Germany and France, it was 10%. Of course, the share in the US is even higher, almost 50%. In comparison, there is still huge space for improvement in China. Second, in January this year, CBIRC issued Opinions on Promoting the Development of Commercial Insurance relating to Social Services, which set the target of RMB2 trillion in premiums for the health insurance market by 2025. The premium income of health insurance in 2019 was RMB706.6bn, and assuming this target, the CAGR in the next 5 years will be 19.7%. In H1, in spite of COVID-19, health insurance held up well and maintained rapid development. Third, government policies provide a window of opportunity for insurance companies to step up investment in health care. China's medical insurance bureau issued Guiding Opinions on Improving Policies of Internet Health Care Prices and Payment of Medical Insurance, which allows Internet care to be covered by medical insurance. Opinions on Deepening Reform of Health Care System by the State Council legalizes doctors' medical practice in multiple hospitals. Moreover, the newly-amended Drug Administration Law of China legalizes drugs sold on-line. These policies provide ample space of development for commercial insurance.

However, there are 3 challenges facing the health insurance business. First is the pressure on business quality. The interests of insurance companies, care providers and customers are not fully aligned. There may even be a conflict of interest. Second is the homogeneity of health insurance products, which may trigger price competitions, instead of differentiation over service. Customers' diverse needs are not met. Third is the absence of health management services. For example, China has 270mn people suffering from blood hyper-tension, 130mn patients of diabetes. However, there are few insurance products or services that can meet the needs of people with such chronic illnesses.

To sum up, the market boasts huge potential but also faces acute problems, which requires breakthroughs on the supply side. Those who can solve the problems will be able to seize the historic opportunities.

We have completed the formulation of a top-level design for health-related business in the next 5 years, which has recently been approved by the board. The plan is also referred to as Strategy One Two Four Three. To be specific, we will focus on 3 customer segments, namely, individuals, firms and governments, foster capabilities in 4 areas, i.e., products, services, operation and risk control, put in place support of 2 kinds of resources, that is, big data and health sector equity investment funds, and manage and coordinate the process through a health business development commission. We are committed to becoming a leading domestic provider of comprehensive health-related services. And we plan to achieve 3 targets. First is to build, via deployment in insurance + service, an ecosystem for health management with aligned interests between insurers, care providers and customers. Second, effectively support product innovation and risk control through big data collection, analytics and applications and foster our big data capabilities. Third is to sharpen the competitive edge in the number and quality of health care and big data professionals.

Based on the top-level design, we will leverage 3 strengths. One is our strength as an insurance group, with 141mn customers, a huge customer base. Our P/C subsidiary participated in many government-sponsored programs and accumulated rich experience in serving government clients. Our life operation provides protection and service to large numbers of individual customers. Our health insurance subsidiary has fostered capabilities in specialized products and professional services. In big data, we will leverage the overall strength of the group and increase the penetration of group customers by health insurance and health services. Another strength is the integration of commercial insurance customers, which is a new growth engine. We can provide tailor-made health management to different customer segments, such as healthy people, those with chronic diseases and special customer segments, based on integration of care, drugs and insurance. And this one-stop integrated solution can enhance customer experience in an all-around way. Then we will make full use of our strength in long-term funds, which is our moat. Through the establishment of health equity investment funds, we will make extensive investments in medical appliances and health management, with varying degrees of capital intensity, so as to cover the whole value chain of health management, medical treatment and recovery.

We will bring into full play market-based mechanisms, which is the key to the success of the plan and the capacity-building in various areas. Three factors are particularly important: resources, people and technology. We will pool resources in medical service, technology and capital and deliver a win-win situation based on collaboration and sharing. We will introduce market-oriented mechanisms so that we can get multiple parties on board and things can be done by the right people. Technology will change the way we serve customers, cultivating a competitive edge.

In a nutshell, we will move steadily, and step by step, with innovative mechanisms and institutions, towards our target so that health-related business can become a new growth engine of CPIC.

**Q: You recently announced your plan to establish CPIC Fintech, and could you elaborate on its business model and strategic positioning?**

A: The rationale of CPIC Fintech is as follows. First is to embrace industry trends and dynamics. Fintech has become a key driver of the insurance market, and a key driver of business development instead of only a supportive factor. Second, in terms of regulatory supportive policies, last year PBoC issued The Development Program of Financial Technology between 2019 and 2021, which explicitly encourages licensed financial institutions to establish fin-tech subsidiaries according to laws and regulations.

The establishment of the subsidiary will stimulate dynamism in 3 ways. First, setting up a market-oriented entity will improve organizational vitality and boost productivity. Second, the establishment of a market-based incentive and performance evaluation system will better motivate talent. Third, a better allocation of data as a key production factor will make data a more dynamic contributor.

**Q: What is the impact of the automobile insurance comprehensive reform and your coping measures?**

A： The reform is intended first to protect consumer rights and second to pressurize insurance companies to enhance operational efficiency and centralisation so as to provide more diverse, better products and services with more competitive prices. The standard premium will be lowered considerably, with adjustment of discretionary factors for both compulsory and third-party. Overall, this will lead to a steep fall in premiums, in line with the CBIRC targets of “lowering prices, expanding coverage and enhancing quality”.

As for its impact, loss ratio will go up a lot. As per requirements of CBIRC, the expected loss ratio will reach 75%, 10 percentage points higher than before, with the expected expense ratio going down by 10 percentage points, benefiting consumers. In the past week since the implementation of the reform, there was indeed a big drop in commercial auto insurance premiums, with a slight decrease in compulsory premiums. Overall, premiums and premium adequacy both came down. At the same time, expense ratio also fell, which offset lower premiums. In the long term, the situation will gradually stabilise.

The reform has just been kicked off, and it is difficult to tell how long this transitioning period will last. But essentially we believe capacity-building in the following areas will be very helpful: first is capability to reach customers directly, which is the common focus of insurance companies, i.e., the share of customers from direct channels; second is capability in centralised operations. The expense loading was lowered from 35% to 25%, and this requires an all-around enhancement of centralised operation; third is capability in customer service, which is the key differentiator going forward.

We have been pushing forward transformation initiatives centering on these 3 priorities. There is a project on distribution channels, seeking to enhance our direct access to customers. The project on the operational side focuses on centralisation and specialisation, which, among others, include digital underwriting. By enhancing centralized operation, we can offer more competitive products. The innovative UBI product we launched in Hong

Kong, known as Lichengbao, was based on a high level of centralisation. Once we get regulatory approval, we will roll it out in mainland China. There is also a project on "CPIC Service", striving to provide comprehensive service to customers, both standard and personalized, along the insurance value chain.