14 May 2020 | Affirmation

Fitch Affirms China Taiping Insurance Group at 'A'; Outlook Stable on Coronavirus Risk Review

Fitch Ratings-Hong Kong-14 May 2020:

Fitch Ratings has affirmed at 'A' (Strong) the Issuer Default Ratings (IDR) of China Taiping Insurance Group Ltd. (TPG), China Taiping Insurance Group (HK) Company Limited (TPG (HK)) and China Taiping Insurance Holdings Company Limited (CTIH). Simultaneously, Fitch has affirmed Taiping Life Insurance Company Limited's (TPL) Insurer Financial Strength (IFS) Rating at 'A+' (Strong) and the IFS Rating of Taiping Reinsurance Company Limited (TPRe) at 'A' (Strong). The Outlook on all the ratings is Stable.

Fitch views TPL and TPRe as TPG's 'Core' and 'Very Important' subsidiaries, respectively. TPL's rating is based on the agency's evaluation of the group's credit profile as a whole, while TPRe's rating reflects its Standalone Credit Profile (SCP).

Key Rating Drivers

The rating actions are based on Fitch's assessment of the impact of the coronavirus pandemic, including its economic impact, under a set of ratings assumptions described below. These assumptions were used by Fitch to develop pro forma financial metrics for TPG, TPL and TPRe that Fitch compared with ratings guidelines defined in its criteria and relative to previously established rating sensitivities for TPG.

TPG's SCP weakened, in terms of capital strength, under Fitch's pro forma analysis. This negative pressure is mitigated by potential government support, which gives the group's IDR the benefit of a one-notch uplift from its SCP. TPG is 90%-owned by China's (A+/Stable) Ministry of Finance, which is likely to extend support to TPG in times of stress. The remaining 10% is held by China's National Council for Social Security Fund.

Under the agency's coronavirus rating-case assumptions, TPG's consolidated capital score on the Fitch Prism Model further declined to the lower end of 'Adequate' level, from its actual position at well into the 'Adequate' at end-2019 (1H19: marginal 'Strong'). The group entity and TPL notably increased their risky assets in 2H19, which include stocks, equity-type funds and long-term equity investments. These investments are sensitive to stock-market shocks and potential impairment losses. TPL's risky-asset exposure exceeded 2.5x of capitalisation at end-2019. The local comprehensive solvency ratio of TPG and TPL was 230% and 227%, respectively, in 4Q19. TPL's solvency ratio remained stable at 222% in 1Q20.

Fitch expects the group's 2020 financial leverage to remain stable, on a consolidated basis, as there are no plans to issue debt at the group standalone level or at key subsidiaries, including at TPL. TPG's consolidated financial leverage ratio was 23% at end-2019 and the agency expects the group's pro forma ratio to remain within Fitch's previously established rating sensitivities. TPG's Fitch Prism Model score and financial leverage ratio are commensurate with IFS 'BBB' rated insurers under the pro forma rating case.

TPG's pro forma financial performance metrics remain intact and are in line with its rating. Fitch views TPL's profitability as 'Strong', with pre-tax return on assets of 2.1% in 2019, averaging at 2.0% during 2017-2019. Nonetheless, the agency sees headwinds in the life insurer's new business growth and investment income amid lower interest rates as a result of the pandemic. TPL's premium fell by 6.2% in 1Q20, from 1Q19. Its new business value reduced by 18.8% yoy in 2019 and the new business margin dropped to 28.4% in 2019, from 36.0% in 2018, as a result.

Fitch expects TPRe's underwriting margin to narrow in 2020 due to more challenging underwriting conditions in the reinsurance sector, despite TPRe's combined ratio remaining commensurate with an IFS 'A' rated reinsurer. From a consolidated perspective, the underwriting performance of TPG's non-life reinsurance business weakened in 2019. The combined ratio rose to 99.3%, from 98.6% in 2018.

Fitch ranks TPG's business profile as 'Favourable' against other insurers in China due to its substantive business franchise and diversified business lines and geographies via its operating subsidiaries in mainland China, Hong Kong and other parts of the world. The diversification of premium sources mitigates potential earning volatility in a single sector. As a result, Fitch scores TPG's business profile at 'a+' under its credit-factor scoring guidelines.

Key Assumptions

Assumptions for Coronavirus Impact (Rating Case):

Fitch used the following key assumptions in support of the pro forma ratings analysis discussed above:

- Decline in key stock market indices by 35% relative to 1 January 2020.

- Increase in the two-year cumulative high-yield bond default rate to 16%, applied to securitised products, including ABS, current non-investment-grade assets, as well as a portion of 'BBB' assets.

- Both upward and downward pressure on interest rates, with spreads widening (including high yield by 400bp), coupled with notable declines in government rates.

- Capital markets access is limited for issuers at senior debt levels of 'BBB' and below.

- Impairment of alternative investments and loans by 7.8%.

- Decline in value of investment property by 7.8%.

- A COVID-19 infection rate of 5% and a mortality rate (as a percentage of infected) of 1%.

- A negative effect on the industry-level accident year loss ratio from COVID-19-related claims at 3.5 percentage points (pp), partially offset by a favourable effect from the auto line averaging 1.5pp.

RATING SENSITIVITIES

The ratings remain sensitive to any material change in Fitch's rating-case assumptions with respect the coronavirus pandemic. Periodic updates to our assumptions are possible given the rapid pace of changes in government actions in response to the pandemic, and the pace with which new information is available on the medical aspects of the outbreak. A discussion of how ratings would be expected to be impacted under a set of stress case assumptions is included at the end of this section to help frame sensitivities to a severe downside scenario.

Factors that could, individually or collectively, lead to negative rating action/downgrade:

- A significant change in shareholding that results in the Ministry of Finance losing its controlling interest in TPG and CTIH, or a downgrade of China's Long-Term Local-Currency IDR (A+/Stable)

- Diminishing perceived significance of TPG in China's insurance sector, in Fitch's view

Factors that could, individually or collectively, lead to lowering the SCP:

- A material adverse change in Fitch's ratings assumptions with respect to the impact of the coronavirus outbreak.

- TPG failing to maintain its Fitch Prism Model score at a level well into 'Strong' and consolidated financial leverage ratio above 35% consistently

- Pre-tax return on assets falling below 1.0% and deterioration in underwriting profitability of the group's property and casualty and reinsurance operations, with a combined ratio persistently above 100%.

Factors that could, individually or collectively, lead to positive rating action/upgrade:

- An upgrade of China's sovereign rating

Factors that could, individually or collectively, lead to a raise in the SCP:

- TPG's ability to improve its Fitch Prism Model score to marginal 'Strong' will reduce the negative view on its SCP

- A material positive change in Fitch's ratings assumptions with respect to the pandemic impact

- Positive rating action that is prefaced by Fitch's ability to reliably forecast the impact of the pandemic on the financial profile of China's insurance industry and TPG

- TPG's Fitch Prism Model score at 'Very Strong' and the consolidated financial leverage ratio below 20% on a sustained basis

- The group's return on equity consistently exceeding 12%.

Stress Case Sensitivity Analysis

Fitch's stress case assumes the following: a 60% stock market decline; two-year cumulative default rate of 22%, high-yield bond spreads widening by 600bp and more prolonged declines in government rates, heightened pressure on capital-market access, impairment of alternative investments and loans by 16.5%, a decline in the value of investment property by 16.5%, a COVID-19 infection rate of 15% and mortality rate of 0.75%; and an adverse non-life industry-level loss ratio impact of 7pp for COVID-19 claims, partially offset by a favourable 2pp for the motor line.

- The implied rating impact under the stress case would be in line with China's sovereign rating.

Best/Worst Case Rating Scenario

International scale credit ratings of Financial Institutions issuers have a best-case rating upgrade scenario (defined as the 99th percentile of rating transitions, measured in a positive direction) of three notches over a three-year rating horizon; and a worst-case rating downgrade scenario (defined as the 99th percentile of rating transitions, measured in a negative direction) of four notches over three years. The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Best- and worst-case scenario credit ratings are based on historical performance. For more information about the methodology used to determine sector-specific best- and worst-case scenario credit ratings, visit https://www.fitchratings.com/site/re/10111579.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING
The principal sources of information used in the analysis are described in the Applicable Criteria.

China Taiping Insurance Group Ltd.; Long Term Issuer Default Rating; Affirmed; A; RO:Sta
China Taiping Insurance Group (HK) Company Limited; Long Term Issuer Default Rating; Affirmed; A; RO:Sta
China Taiping Insurance Holdings Company Limited; Long Term Issuer Default Rating; Affirmed; A; RO:Sta
Taiping Life Insurance Company Limited; Insurer Financial Strength; Affirmed; A+; RO:Sta
Taiping Reinsurance Company Limited; Insurer Financial Strength; Affirmed; A; RO:Sta
China Taiping Capital Limited
----senior unsecured; Long Term Rating; Affirmed; A-
China Taiping New Horizon Limited
----senior unsecured; Long Term Rating; Affirmed; A-

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Additional information is available on www.fitchratings.com

Applicable Criteria
Insurance Rating Criteria (pub. 02 Mar 2020) (including rating assumption sensitivity)

Applicable Model
Numbers in parentheses accompanying applicable model(s) contain hyperlinks to criteria providing description of model(s).
Prism Factor-Based Capital Model, v1.7.1 (1)

Additional Disclosures
Dodd-Frank Rating Information Disclosure Form
Solicitation Status
Endorsement Status
Endorsement Policy
