P&C Insurers’ Profitability to Remain Under Pressure from Underwriting Losses

Default risk of P&C insurers to stay low thanks to low financial leverage

January 17, 2022

Our outlook remains stable for China’s property & casualty (“P&C”) insurance sector for 2022. We expect insurers’ profitability to remain under pressure due to high claim payments and elevated investment risk. Nevertheless, we expect default risk to remain low in the P&C insurance industry given players’ low financial leverage and lowering credit risk in their insurance business.

Overall premium growth has remained low. We expect the sector’s premium growth to be lower than 2% in 2021. Segments which have enjoyed the highest rate of premium growth are health, casualty and agriculture. In the first nine months of 2021, the premium income of these three segments increased by 26%, 20% and 19% respectively compared with the same period of 2020. Auto insurance premium growth dropped by 9%. This decrease is the main reason for the stagnation of the overall P&C insurance sector’s total premium.

Major insurers have maintained their market share and we expect competition dynamics to remain stable. In the first three quarters of 2021, about 74% of the P&C market share was held by the top 5 insurers, similar to 2020. We believe it is becoming increasingly challenging for small insurers to grow business when overall premium growth has been stagnant.

We have seen increasing diversification in the sector’s product mix. Auto insurance contributed to 56% of the total premium in the first eleven months of 2021. The ratio was 61% in 2020.

Chart 1
Product Mix Witnessed Increasing Diversification
P&C Premium Breakdown by Different Types of Insurance


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We view the decrease of guarantee insurance premium as credit positive because it signals decreasing credit risk in insurers’ insurance business. In the first nine months of 2021, guarantee insurance premium dropped again by 30%. Guarantee insurance has seen high claim payments in recent years. We have seen some extremely high credit risk in small insurers. Taking Anxin P&C Insurance as an example, the company failed to properly provision for certain credit insurance products before 2020, which led to a regulatory breach and dramatic increase of provisioning in 2020. As a result, the company’s reported core solvency ratio deteriorated from 125% as of the end of 2019 to -214% as of the end of 2020.

Chart 2

Different Segments Witnessed Very Different Growth Momentum

YoY Premium Growth of Major Insurance Segments in the First Three Quarters of 2020 and 2021

Source: CBIRC, collected and adjusted by S&P Global (China) Ratings.

The combined ratio of the P&C insurance sector has kept increasing, which exacerbated insurance business losses. We expect the P&C insurance sector’s overall combined ratio to exceed 101% in 2021. The combined ratio is a key measure of insurance business profitability, with figures exceeding 100% indicating underwriting loss. One reason for the increased combined ratio is the comprehensive auto insurance reform initiated by the regulator, which increased claim payments. Another reason for underwriting loss is frequent extreme weather incidents across China in 2021.

Chart 3

The Increase in Combined Ratio will Continue to Compress the Profit Space of P&C Insurers

Combined Ratio of P&C Insurance Sector


With underwriting loss on the insurance business side, investment income has become critically important for the profitability of P&C insurers. We believe their investment performance is vulnerable to elevated capital market volatility, credit risks in their alternative investment portfolios and bond investment portfolios. It remains uncertain how the recent liquidity crunch in the real estate sector will affect insurers’ investment performance.

Therefore, we expect the profitability of the P&C industry to remain under pressure in 2022 due to the high combined ratio and elevated investment risk. We have seen efforts by insurers to reduce their cost and commission expenses to ease earnings pressure, but the effects of such efforts have only proved marginal.

Chart 4

**The Profitability of P&C Insurers is Generally Weaker than Pre-Covid Level**

Combined Ratios and ROE of Top P&C Insurers in the First 3 Quarters of 2019, 2020 and 2021

![Chart showing combined ratios and ROE of top P&C insurers]

Note 1: Annualized ROAE = (Net Income within Q1 to Q3) / ((Total Equity at the beginning of Q1 + Total Equity at the end of Q3)/2) * (4/3).

Note 2: Combined Ratio = Expense Ratio + Claim Ratio + Other Adjustments.

Source: Public Information of Insurance Companies, collected and adjusted by S&P Global (China) Ratings.

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We expect major P&C insurers to maintain strong capitalization, providing a good cushion for profitability pressure in 2022. As of June-end 2021, the P&C insurance sector’s average core solvency ratio was 258%, much higher than the minimum regulatory requirement of 50%. As P&C insurers have actively reduced credit & guarantee insurance business and domestic catastrophe insurance is still in its early stages, the risks of significant solvency erosion are controllable. Capital challenges have been contained to only a few aggressive small insurers.

The implementation of the regulatory solvency framework under Solvency Regulatory Rules II (“Rule II”) should improve the capital management of insurers. In December 2021, CBIRC issued the Solvency Regulatory Rules II (“Rule II”) for insurance companies. The implementation will start in the first quarter of 2022. We believe that Rule II’s adjustments on risk factors, the emphasis on underlying asset quality of the investment portfolios, and a more detailed assessment of the risk management capabilities are all positive for the capital management of the industry.

Hybrid bonds issued by a few smaller, poorly governed players may suffer losses given their very poor capitalization. Tianan Property Insurance was taken over by the regulator in July 2020. Due to significant credit loss of the company’s investment assets, it had to book very large impairment losses, which caused its equity to drop to -36 billion RMB as of the end of June 2020. It issued 5.3 billion RMB in capital supplementary bonds with terms of 5+5 years in October 2015. The company
decided not to exercise its redemption rights for the bonds in 2020, and the bonds stopped accruing interest. Because the company is already insolvent and the bond is subordinated to insurance policy liabilities and other senior liabilities, there is great uncertainty over the payment of this bond in the future.

Nevertheless, we believe the tail risk of the P&C insurance sector has been well contained. Regulators have extended the takeover period of E An P&C Insurance as well as Tianan Property Insurance. In addition, regulators have been focusing on improving corporate governance of insurers and preventing inappropriate behavior of controlling shareholders, efforts which are important to preventing outsized losses among small players. Since overall financial leverage in the industry is low, as of the end of 2021, there were no outstanding bonds issued by sub-investment-grade issuers among the 15 insurers we tested. We believe the industry’s bond default risk is controllable.

Chart 5
**Good Credit Quality of Large P&C Insurers Underpins the Industry’s Overall Stability**

Distribution of Indicative Issuer Credit Quality of 15 Major P&C Insurers and 35 Major Life Insurers by Assets as of End of 2020

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Note 1: Our assessment of indicative issuer credit quality considers the possibility of group or government support in times of stress.

Note 2*: The indicative credit quality distributions expressed in this report are only our indicative views of credit quality derived from a desktop analysis based on public information without interactive review with any particular institution or the full credit rating process such as a rating committee (except for a few cases where we have already assigned public ratings on a company). The opinions expressed herein are not and should not be represented as a credit rating and should not be taken as an indication of a final credit rating of any particular institution.

Note 3: Categories can be adjusted by “+” and “−” except for AAA.

Source: S&P Global (China) Ratings.

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