

# Bangkok Life Assurance

SET | Reuters | Bloomberg  
BLA | BLA.BK | BLA TB



CG Rating 2009  
n.a. | n.a.

**BUY**

(unchanged)

Price (14 July 2010)

**Bt27**

12-month target price

**Bt36 (+33.3%)**
**Company Update**

## Interest rate rise will benefit life insurers

**A more positive environment for investment side of the business**

The early phase of the interest rate upcycle is the most profitable for insurance companies in terms of investment spread. Given recent bond yield improvements and the Bank of Thailand's decision to raise its policy rate by 25bps yesterday, we believe that BLA's outlook has become more favourable. The negative impact from lower bond yields in 1H10 should partly carry over to 3Q10 but we expect the company to comfortably achieve a 5.25% investment yield this year (vs. 5.45% in 2009), based on an expected 75bps rise in the policy rate. We reiterate our **Buy** call for BLA which we rate as the top pick in the sector.

**BLA and life insurance industry continue to outperform the economy**

BLA continues to leverage off the bancassurance channel and its business grew at a rate of 36% YoY in 5M10 vs. the industry's figure of 15%. In May the company showed a positive growth rate of 18% YoY despite the political unrest. We expect growth to weaken in 2H10 due to seasonal factors and though our 2010F premium growth target of 25% is looking a little conservative, we prefer to leave it unchanged for now.

**2x P/EV multiple seems realistic in our view**

The recent share price movement suggests that the market is comfortable with assigning a 2x P/EV multiple for a high-growth life insurer like BLA. This is fair on a regional basis, in our view, as BLA's EV growth rate is comparable to that of Chinese life insurers which are trading well above a 2x P/EV. One slightly negative issue is a declining New Business Margin due to the bancassurance-centric product mix. But we are not too concerned by this so long as there is rapid raw premium growth.

**Target price raised to Bt36 based on 2011F valuation**

Applying a P/EV multiple of 2x over a 2011F EV of Bt18/share we derived a new target price of Bt36 (previously Bt30). Our TP has an implied new business multiple of 9x which is similar to low-growth European insurers. Risk factors include: 1) more stringent regulatory rules regarding capital/solvency (esp. RBC implementation in 2011); and 2) tougher competition from rival insurers backed by other leading domestic banks.

**CONSOLIDATED FINANCIAL SUMMARY**

Year	2007	2008	2009	2010F	2011F	2012F
Net written premiums	12,296	14,732	19,632	24,497	30,592	37,953
NWP growth (%)	17.8	19.8	33.3	24.8	24.9	24.1
Net profit (Bt, m)	770	752	1,186	1,533	2,025	2,725
Net profit growth (%)	18.0	(2.4)	57.7	29.3	32.1	34.6
EPS (Bt)	0.77	0.75	1.12	1.28	1.69	2.27
EPS growth (%)	18.0	(2.4)	48.9	14.1	32.1	34.6
EV per share (Bt)	10.3	11.1	12.0	14.9	18.3	22.4
BVPS (Bt)	3.1	3.0	6.8	7.1	8.4	10.0
DPS (Bt)	1.00	0.29	0.38	0.51	0.68	0.78
Yield (%)	n.a.	n.a.	1.4	1.9	2.5	2.9

Note : use average price for historical PER, PBV, Yield

**SHARE SUMMARY**
**Price:**

52-week high	Bt28.75
52-week low	Bt13.50
52-week average	Bt21.14

**Stock data:**

Issued shares:	1,200.0m
Par value:	Bt1.0
Market capitalization:	Bt32.4bn
Market capitalization:	US\$1,002.8m
Avg. Daily Turnover:	Bt111.2m
Avg. Daily Turnover:	US\$3.4m
Foreign Limit:	25.0%
Foreign Ownership:	25.0%
Free Float:	28.5%
NVDR:	4.44%
Beta (3 years)	0.70X

**TISCO's forecast vs. consensus**

EPS (Bt)	TISCO	Consensus	% Diff.
2010F	1.28	1.27	0.6
2011F	1.69	1.58	6.9

**Major Shareholders (14/05/10)**

Nippon Life Insurance Co	20.8%
Wattanasophonpanich Co Ltd	13.3%
Bangkok Bank	7.7%
Bangkok Insurance	5.3%
Thai NVDR Co Ltd	4.1%

**PRICE / PRICE RELATIVE**


Source: Reuters

Performance (%)	-1m	-3m	-12m
BLA	5.88	21.62	n.a.
SET	6.50	11.33	40.64

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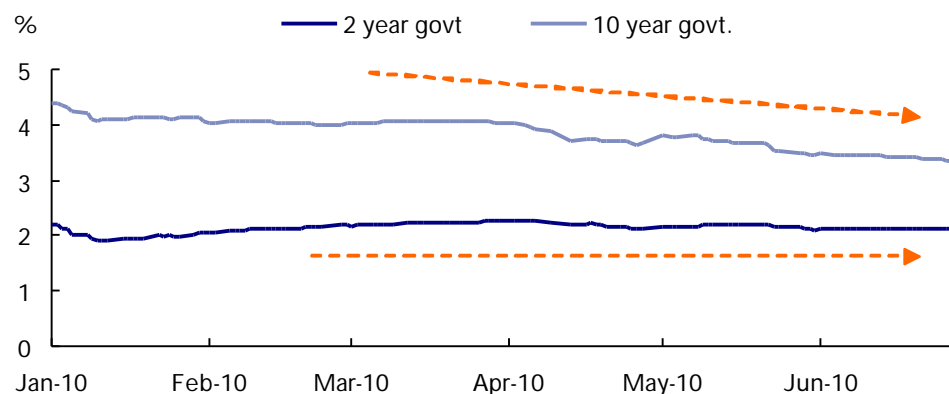
## 2H10F should favour BLA investment spread

### Negative impact of 1H10 bull flattening yield curve twist to partly remain in 3Q10

The macro backdrop in 1H10 was not benign for bond yields and insurers' investment returns. Expectations of a policy rate hike increased in 1Q10 but when this did not materialise, the back end of the yield curve moved lower while the front end remained largely constant. This bull flattening yield curve twist was further mitigated by Thailand's political crisis in 2Q10. This situation would not have been healthy if it was sustained for longer than the past six months. Not only would the investment yield continue to remain depressed but the existing guaranteed businesses (i.e. the bancassurance business) would also start to compress the investment spread.

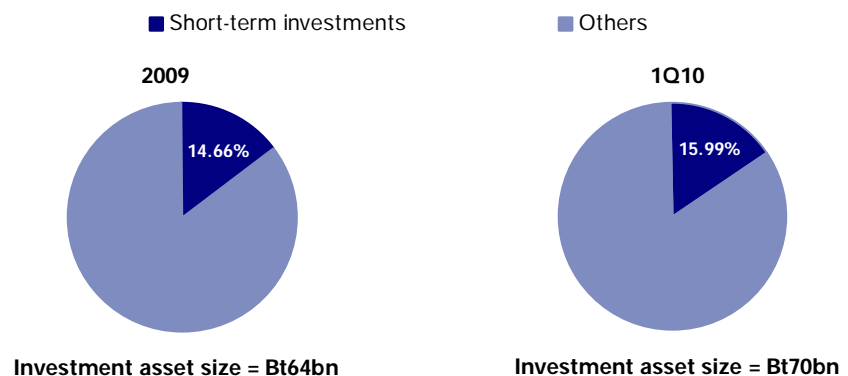
BLA took the usual approach to respond. The investment asset duration was shortened and the proportion of short-term investment assets increased from 14.66% to 15.99%. Though this is less clear on the profit and loss statement since fast premium collection is cycled into a rapidly expanding investment asset base, we expect BLA to continue to endure some short-term pain in 3Q10 as its shorter-dated positions are gradually rolled over. For example, the achieved yield was only 4.61% in 1Q10 vs. 5.32% in 1Q09. Thus the 25bps rise in the BoT's policy rate yesterday would have come as a relief for insurers and the yield on 10-year government bond is now looking better, having jumped 20bps QTD to 3.49%.

**Figure 1. Narrowing of bond spreads seen in 6M10**



Source: Reuters

**Figure 2. BLA responds by shortening investment asset duration**



Sources: BLA, TISCO Research

### **Profitability is most sensitive to rising interest rates**

In general, insurers tend to delay raising rates of return to policyholders until well into the up cycle for interest rates. Therefore BLA's investment spread should widen if, as we expect, the BoT raises its policy rate by 75bps this year. We would expect BLA, to delay raising the rate of return to policyholders until there has been a rise of 100bps in the policy rate. This should happen in early 1H10 and there is likely to be a further delay before it lifts rates on its policies. We therefore expect its investment spread to expand the most in 2H10 and also in 1H11 (for the next 25bps). For each increase of 25bps in the investment spread, we estimate that EPS for 2010F would rise by 10%. Book value would also rise by a respectable, if unexceptional, 1%.

Theoretically, a 75bps increase in the policy rate without an insurer response could be negative for the attractiveness of insurance policies at the margin, with potentially more surrenders and lapses. However, since BLA's average premium value per new policy was only Bt23,000 in 2009 (the average for the industry was Bt20,000) the incentive in the form of a tax deductible allowance would be more than enough to offset the policyholder's reduced spread return (relative to saving deposits, bonds etc.). Note that the average premium per new bancassurance policy written in 2009 was also below the Bt100,000 tax deductibility allowance limit at Bt60,000.

### **More importantly, it is also positive on the embedded value basis**

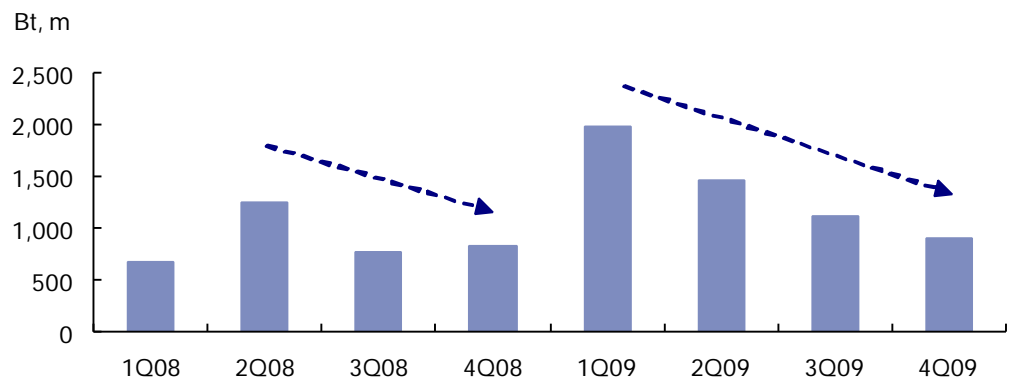
There are two effects from the rising yield due to increases in the policy rate. Firstly, investment returns should rise along with the rate rise, though higher interest rates would also mean that the risk discount rate used to discount back future cash flows would also need to rise, leading to a lower present value. The former effect generally exerts a greater influence and there should be a positive effect on embedded value. Under exceptional circumstances such as when liabilities are interest-insensitive (e.g. pure protection products, equity unit linked policies), the calculated embedded value could fall. However, if the market is saturated with contract guarantees i.e. bancassurance products and insurers tend to have net liabilities duration, as is Thailand's case, the effect on embedded value is positive.

Our sensitivity calculation shows that for each 25bps increase in return on investment, our 2010F EV forecast would grow by an estimated 5.6-7%. This is slightly below the company's guidance of 5.9% at the end of 2009, since we believe that the growing proportion of bancassurance policies is bringing down the blended margin.

### **Quantifying yield movements through the P&L account**

Though we prefer to look at insurers on the embedded value basis as life insurance is a super-long insurance product, many investors still prefer to look at the shorter-term P&L account to gauge profitability.

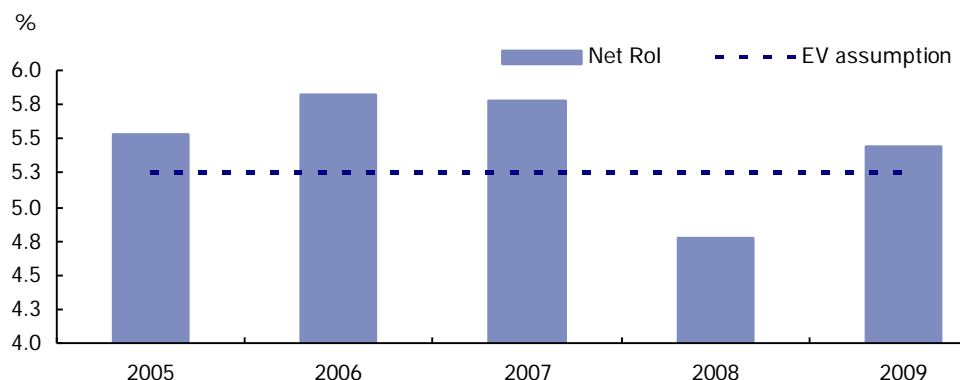
We forecast net profit growth of 29% YoY to Bt1.53bn for 2010. This was revised down from Bt1.7bn previously due to an anticipated slowdown in premium sales because of the political upheaval. The delayed rise in the policy rate and its smaller magnitude i.e. a projected rise of 75bps this year rather than +100bps, also weighed on our earnings call.

**Figure 3. First Year Premium ‘seasonality’**

Source: TISCO Research

We maintain our forecast of 25% premium growth YoY even though 5M10 growth rate was higher at 36%, as first year premiums have consistently demonstrated seasonal weakness in the latter half of the year due to the tendency of bank employees to be less aggressive in promoting fee income products after reaching their performance targets. This is unchanged from our previous expectation despite changes to our interest rate forecast, since growth is still predominantly based on a starting point of low market penetration rather than the insurance policy's attractiveness versus other investment opportunities. We forecast first year premium written growth of 30% which should add a new business value of c.Bt1.60.

On the investment side, the total asset base should expand by c.27% YoY to Bt80bn. We expect BLA to be hurt by lower bond yields in 1H10 and by position adjustments into investment assets with shorter duration. Our estimate of a 5.35% investment yield is below the 5.45% that was achieved in 2009. Nonetheless the 5.35% figure should not threaten our EV-based valuation given that our 2010F assumption for RoI is 5.25%.

**Figure 4. RoI assumption is realistic (and conservative)**

Source: BLA

**Raising target price to Bt36 on 2011F valuation**

We derived a new target share price of Bt36 (previously Bt30) by applying a P/EV multiple of 2.0x over a 2011F EV of Bt18.30 (with Bt0.30 rounding down). Assuming a new business value of c.Bt2.10 per share, our price target suggests a new business multiple of 9x which is in line with the multiples for mature European insurers.

Potential risks include: 1) more stringent regulatory rules covering capital/solvency ratios especially after RBC implementation in 2011; and 2) tougher competition from rival insurers that are backed by other leading Thai banks.

## CONSOLIDATED INCOME STATEMENT (Bt, m)

	Year Ended December 31,				
	2008	2009	2010F	2011F	2012F
Net premiums written	14,732	19,632	24,497	30,592	37,953
Net investment income	2,430	2,760	3,886	4,955	6,386
Gains on investments in securities	(359)	236	50	50	50
Other income	26	26	28	32	37
Total revenue	16,829	22,654	28,461	35,629	44,427
Life policy reserve increase	7,670	11,666	14,943	18,661	23,152
Benefit payments	4,926	5,437	7,055	8,935	11,236
Commissions	1,985	2,502	2,940	3,671	4,554
Other underwriting expenses	262	349	430	525	639
Personnel expenses	490	551	612	672	732
Premises and equipment expenses	108	121	123	125	127
Other operating expenses	360	451	466	540	621
Total expenses	15,801	21,077	26,568	33,129	41,062
Income tax	277	392	360	475	639
Extraordinary items	0	0	0	0	0
<b>Net Profit</b>	<b>752</b>	<b>1,186</b>	<b>1,533</b>	<b>2,025</b>	<b>2,725</b>

## KEY FINANCIAL RATIOS (%)

	Year Ended December 31,				
	2008	2009	2010F	2011F	2012F
Premium receivable (days)	27.1	21.0	18.5	17.6	16.7
Gross profit margin (%)	14.5	12.8	10.2	9.8	9.4
Net profit margin (%)	4.5	5.2	5.4	5.7	6.1
Return on investment (%)	4.9	5.6	5.6	5.6	5.7
Cost to insurance income ratio (%)	21.8	20.1	18.6	18.0	17.6
Underwriting profit margin (%)	(0.8)	(1.6)	(3.6)	(3.9)	(4.3)
Investment-net expense margin (%)	7.0	8.0	7.7	8.2	8.9
Return on equity (%)	49.5	23.1	19.5	21.8	24.7
Return on asset (%)	3.1	2.0	2.0	2.1	2.2
Asset turnover (x)	0.7	0.4	0.4	0.4	0.4
Policy reserve to equity ratio (x)	13.9	7.4	8.0	8.7	9.2
Policy reserve to asset ratio (%)	0.8	0.8	0.8	0.8	0.8
Book value per share (Bt)	3.0	6.0	7.1	8.4	10.0
Earnings per share (Bt)	0.8	1.0	1.3	1.7	2.3

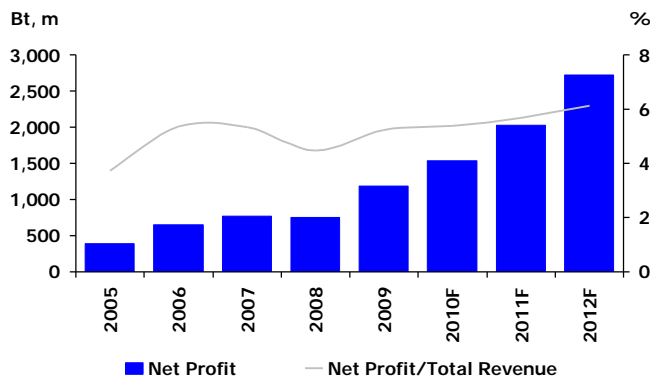
## CONSOLIDATED QUARTERLY RESULTS (Bt, m)

	1Q09	2Q09	3Q09	4Q09	1Q10
Net premiums written	4,722	4,701	4,872	5,337	6,849
Net investment income	635	688	742	695	773
Gains on investments in securities	125	41	58	12	87
Other income	7	6	6	8	7
Total revenue	5,490	5,435	5,677	6,052	7,716
Life policy reserve increase	2,434	2,822	3,133	3,278	4,287
Benefit payments	1,201	1,363	1,399	1,475	1,563
Commissions	671	603	553	675	898
Other underwriting expenses	127	66	86	69	126
Personnel expenses	136	139	135	141	143
Premises and equipment expenses	29	29	30	32	32
Other operating expenses	118	107	106	120	120
Total expenses	4,717	5,129	5,441	5,791	7,171
Income tax	217	73	22	79	104
Extraordinary items	0.00	0.00	0.00	0.00	0.00
<b>Net Profit</b>	<b>556</b>	<b>233</b>	<b>214</b>	<b>182</b>	<b>441</b>
Net profit margin (%)	10.1	4.3	3.8	3.0	5.7
Return on investment (%)	5.5	5.7	5.5	4.6	4.7
Underwriting profit margin (%)	6.1	(3.2)	(6.1)	(3.0)	(0.4)

## CONSOLIDATED BALANCE SHEET (Bt, m)

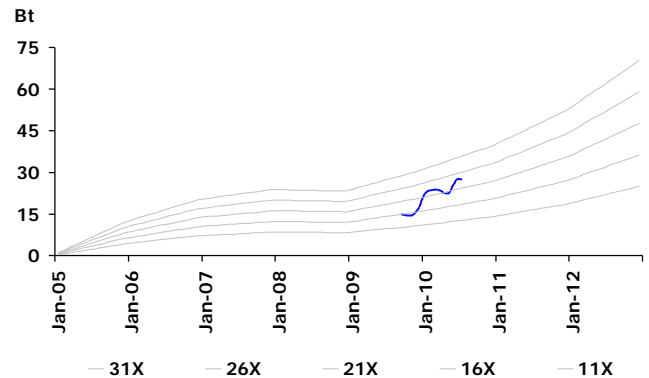
	As of December 31,				
	2008	2009	2010F	2011F	2012F
Bonds	28,449	42,951	78,840	99,537	124,711
Notes	4,058	4,696	60	75	95
Stocks	3,594	4,446	57	71	89
Debentures	7,423	7,764	99	125	156
Total investment in securities	44,858	62,141	79,084	99,845	125,097
Allowance for doubtful accounts	(3)	(3)	(3)	(3)	(3)
Loans net allowance	1,798	1,904	2,154	2,439	2,762
Cash and deposits	2,382	1,718	2,102	2,516	3,567
Other assets	2,443	2,576	3,133	3,713	4,439
<b>Total assets</b>	<b>51,482</b>	<b>68,339</b>	<b>86,473</b>	<b>108,513</b>	<b>135,865</b>
Life policy reserve	41,892	53,558	68,501	87,162	110,314
Unpaid policy benefits	3,984	4,680	6,508	8,280	10,480
Other	2,587	2,870	2,953	3,001	3,055
<b>Total liabilities</b>	<b>48,463</b>	<b>61,108</b>	<b>77,962</b>	<b>98,444</b>	<b>123,849</b>
Surplus on revaluation of investments	316	1,033	1,200	1,300	1,300
<b>Total shareholder's equity</b>	<b>3,019</b>	<b>7,232</b>	<b>8,512</b>	<b>10,069</b>	<b>12,017</b>

### Net profit



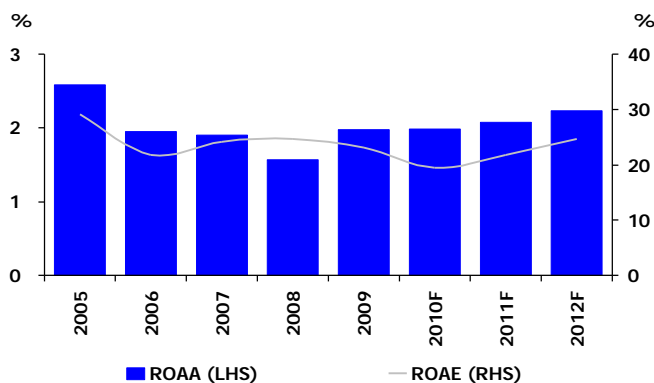
Sources : Company data, TISCO Research

### PE Band



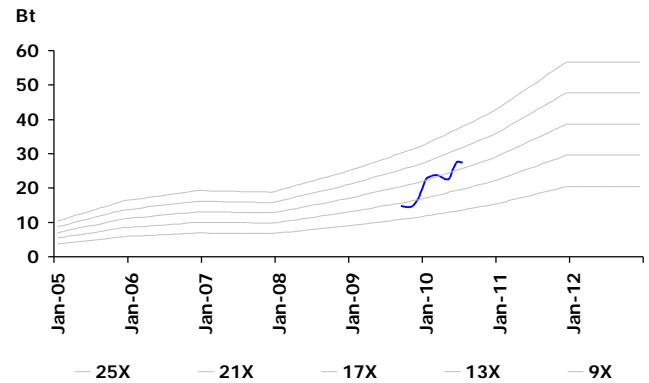
Sources : Company data, TISCO Research

### ROAA, ROAE



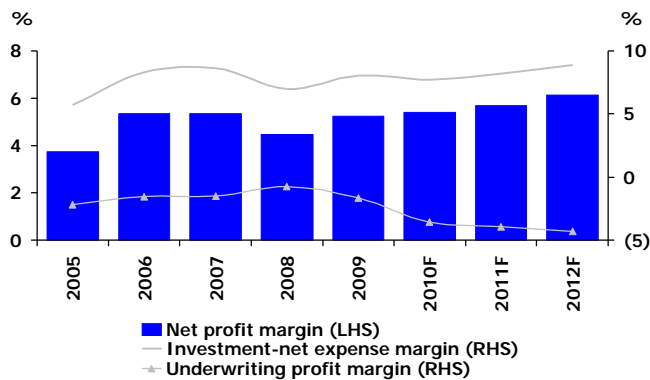
Sources : Company data, TISCO Research

### PE (forward) Band



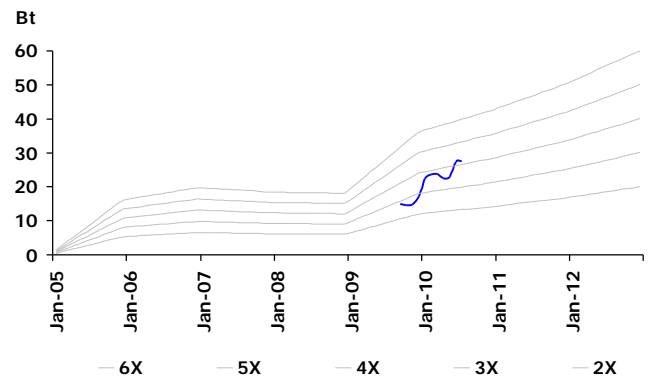
Sources : Company data, TISCO Research

### Underwriting profitability



Sources : Company data, TISCO Research

### PBV Band



Sources : Company data, TISCO Research

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Corporate Governance Report  
of Thai Listed Companies 2009

Score Range	Level	Description
90 - 100	5	Excellent
80 - 89	4	Very Good
70 - 79	3	Good
60 - 69	2	Satisfactory
50 - 59	1	Pass
< 50 or not rated	n.a.	n.a.

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The survey result is as of the date appearing in the Corporate Governance Report of Thai Listed Companies. As a result, the survey result may be changed after that date. TISCO Securities Company Limited does not confirm nor certify the accuracy of such survey result.

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