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Chinese Insurers Could Face Higher Risks As They Venture Overseas

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HONG KONG (Standard & Poor's) Nov. 2, 2015--The recent cuts in interest rates in China are likely to encourage the country's insurers to seek overseas investments. However, such investments will increase the risks for these insurers. That's according to a report, titled "China Credit Spotlight: China Credit Spotlight: Risks For Chinese Insurers Could Rise As Higher Yields Lure Them Overseas," that Standard & Poor's Ratings Services published today.

"We believe the lifting of restrictions on investments will help Chinese insurers reduce the geographic concentration of their investment portfolios and have greater flexibility to manage investment risks and boost returns," said Standard & Poor's credit analyst Eunice Tan. "But they may not be fully equipped to manage risks in the shift in their asset allocation toward countries and asset classes that they are less well-versed with."

We expect the investment overseas and in shadow-banking-type instruments (such as local debt schemes, trust plans, and wealth management products) to have a limited impact on the credit profiles of rated Chinese insurers. That's because the allocation is small relative to their capital bases.

China's cooling economy and falling interest rates will likely lead to slower growth in new business for Chinese insurers and increase claim liability reserves on their existing business, the report notes. Moreover, high competition is likely to reduce underwriting margins and drag down

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profitability. Consequently, these companies are likely to focus more on investment returns.

We believe the liberalization of products and investment guidelines indicates the increasing maturity of China's insurance sector. Insurers now have more flexibility to adjust the guaranteed rate of return for products and choose more investment options.

"We expect the evolving insurance landscape in China to spur insurers to have full control to decide on their preferred investment and business profile," said Ms. Tan. We believe companies with stronger or sophisticated risk management controls can achieve good risk-adjusted returns and outperform peers. On the other hand, insurers with aggressive expansion strategies in less familiar businesses could be exposed to higher risks.

Standard & Poor's does not expect Chinese insurers to significantly raise their guaranteed returns despite the regulator lifting the ceiling. China's slowing economy, falling interest rates, and volatility in the domestic equity market will likely dissuade insurers from guaranteeing higher returns.