

# SKFH First Quarter 2016 Results Conference Call

*May 19, 2016, 4:30 p.m. (Taipei)*

## INTRODUCTION

**Stan Lee:**

Good afternoon, ladies and gentlemen.

Welcome again for joining the Shin Kong Financial 2016 First Quarter analyst call. Before we start, I would like to introduce my colleagues who are with me today.

- First of all, we are happy to have Vice Chairman Victor Hsu of the Financial Holding Company to review the first quarter results with us.
- We are also joined by Simon Dai, Director of Deloitte Actuarial and Insurance Solutions. Simon has been working with us closely over the past few months in reviewing our EV work, and he is here to help us answer any question you may have.
- Also in the room are Executive Senior Vice President Sunny Hsu; Han-Wei Lin, the appointed actuary of Shin Kong Life and leader of our EV work; Isabella and Amber, members of the IR team.

The presentation we are about to go through was sent out 2 hours ago. You may also download it from our website or participate through webcast. If you do not have the presentation, please let us know now.

Your lines will be muted when we are presenting. If you are cut off, please dial back in or call Amber at 886 956 \*\*\* \*\* for assistance.

If you have no question, we will start by asking Vice Chairman Victor Hsu to give us a group level update for the first quarter 2016. Vice Chairman Hsu ...

## PRESENTATION

**Victor Hsu:**

Page 4 Thank you, Stan. Good afternoon, ladies and gentlemen. Please turn to page 4.

Due to continuously strengthening and limiting exposure to equity portfolio, SKFH recorded a consolidated after-tax loss of NT\$2.56bn for the first quarter 2016; consolidated comprehensive loss was NT\$1.42bn. Book value per

share as of the end of March was NT\$10.68.

Core business of each subsidiary remained solid during this quarter.

For Shin Kong Life, FYPE amounted to NT\$9.39bn, up 21.6% year-on-year, driven by promotion of interest-sensitive whole life products. Annualized cost of liabilities decreased at a steady pace from 4.51% for 2015 to 4.48%.

Interest income grew 17.4% year-on-year to NT\$17.14bn, due to incremental allocation to overseas fixed incomes. Recurring yield before hedging increased 22 bps year-on-year to 3.59%.

For Shin Kong Bank, driven by well-controlled funding cost and optimized deposit and loan structure, net interest income reached NT\$2.62bn, up 5.4% year-on-year. Consolidated after-tax profit was NT\$1.07bn. On the asset quality side, NPL ratio remained low at 0.19%, and coverage ratio was 681.13%. Both are better than industry average.

Life insurance EV per share of SKFH was NT\$21.1. EV of Shin Kong Life was NT\$215.7bn, including property unrealized gains of NT\$72.6bn. Although total FYP for 2015 declined 13.3% year-on-year, V1NB was only down by 6% to NT\$16.8bn, and VNB margin rose to 22.1%.

I will now hand it back to Stan who will take you through the results of the financial holding company and Shin Kong Life.

**Stan Lee:**

Page 6 Thank you, Vice Chairman Hsu. Please turn to Page 6.

Affected by market turbulence in January, SKFH recorded an after-tax loss of NT\$2.61bn for the first quarter 2016. At the subsidiary level, Shin King Life's after-tax loss was NT\$3.66bn, and Shin Kong Bank's after-tax profit was NT\$1.07bn.

Page 10 Page 10 – FYP decreased 26.4% year-on-year to NT\$21.0bn, primarily constrained by our strategy to avoid selling interest-sensitive annuities and limit sales of whole life policies with survival benefit. However, FYPE increased 21.6% year-on-year to NT\$9.39bn.

In order to improve cost of liabilities, Shin Kong Life will continue to promote interest-sensitive whole life products. Annualized cost of liabilities declined to 4.48%, 3 bps lower compared to 2015.

Low interest rate sentiment has triggered market demand for savings products. Shin Kong Life has also been actively promoting bancassurance business together with Shin Kong Bank. FYP momentum is expected to pick

up and further drive down cost of liabilities.

Page 13 Page 13 gives an overall view of our investment portfolio. Annualized investment return for the first quarter 2016 was 2.72%, which was adversely affected by market volatility. Breakdown of investment returns for different asset classes were: real estate 3.3%, mortgage and corporate loans 2.2%, policy loans 5.8%, overseas investment 3.5%, domestic securities 0.02%, and cash 0.4%.

Page 14 Page 14 shows our portfolio of overseas fixed incomes. At the end of the first quarter, corporate bonds comprised the largest portion, representing 56.1% of the total, followed by international bonds at 23.0%.

Shin Kong Life held international bonds of NT\$265.3bn with average yield before hedging of 4.5%, which after hedging is still higher than domestic bonds. The position is expected to reach NT\$300bn by the end of the second quarter 2016. Portfolio reallocation allowed interest income for the first quarter 2016 to increase NT\$2.54bn, 17.4% higher year-on-year.

Page 16 Page 16 – Annualized hedging cost for the first quarter 2016 was 0.73%, and foreign currency volatility reserve was NT\$6.19bn. Hedging ratio was 81.3%, including CS, NDF, and naturally-hedged forex policies position. The mid- to long-term target of hedging ratio ranges from 65% to 90% under stringent risk management. CS and NDF accounted for 72% and 28%, respectively, of traditional hedges.

I will now hand over to Isabella who will take you through the results of Shin Kong Bank.

### **Isabella Wang:**

Page 19 Thank you, Stan. Please turn to Page 19.

Shin Kong Bank generated an after-tax profit of NT\$1.07bn for the first quarter 2016, with net interest income up 5.4% year-on-year. The increase in net interest income benefited from prudently controlled funding cost.

On the capital adequacy front, BIS and Tier 1 ratio have improved to 12.9%, and 9.8%, respectively.

Page 21 Page 21 – Total loan size declined 2.2% year-to-date to NT\$477.06bn. However, from the second quarter onwards, both corporate and consumer loans are expected to grow gradually.

Shin Kong Bank will actively participate in overseas syndicated loans to enhance loan-to-deposit ratio and maintain a stable net interest margin.

In addition, credit quality of SME loans was closely monitored and mainly supported by credit guarantee funds or fully collateralized.

Page 22 Page 22 – Driven by the optimized deposit and loan structure, net interest spread increased 4 bps quarter-on-quarter to 1.98%, and net interest margin remained at the same level as the previous quarter at 1.48%.

Looking forward, Shin Kong Bank will pay attention to both funding cost and loan yields to keep net interest margin stable in the current low interest rate environment.

Page 24 Page 24 – Wealth management income for the first quarter 2016 was NT\$408mn, with fee income from bancassurance increasing 29.0% year-on-year to NT\$285mn. Wealth management income for April grew substantially to around NT\$200mn. The positive growth momentum is expected to extend into May and further contribute to wealth management business. Also, an internal research team has been established to work with financial planners in providing clients with timely market updates and sound financial advice.

Page 25 Page 25 – New NPL generated in the first quarter was NT\$377mn, which mainly came from corporate loans. The situation is expected to improve in the second half along with economy recovery. NPL ratio remained low at 0.19% and coverage ratio was 681.13%.

I will now turn over to Han-Wei to talk about the update on EV/AV.

### **Han-Wei Lin:**

Page 27 Thank you, Isabella. Please turn to page 27.

In 2015, the earning rate of VIF goes from 4.05% to 5.10% in 30 years for TWD products and 4.32% to 6.09% for USD products. The Equivalent investment yield is 4.46%, 11bps lower than the 2014 rolling over to 2015 yield, 4.57%. For VNB, the earning rate goes from 4.06% to 5.10% and 4.25% to 5.68% in 30 years for TWD and USD products, respectively. Our EV, as a result, decreases 10% mainly due to decrease in the Adjusted NAV and increase in the COC, which includes regulatory change of the additional charge percentage of previous year's C3 risk for traditional products from 10% to 30%. VNB also decreases 6% due to volume decrease. However, our VNB margin increases from 20.2% to 22.1% in 2015.

Page 28 Page 28 – Under the base case scenario, risk discount rate remains at 10.5%. Our EV, at the end of 2015, was NT\$215.7bn. VNB of 2015 was NT\$16.8bn. AV's for 5 years of NB and 20 years of NB were NT\$273.8bn and NT\$349.8bn accordingly. We also provide the sensitivity tests of investment return and risk

discount rate for your reference.

- Page 29 Page 29 – Statutory Net Worth decreased from NT\$69.5bn to NT\$64.3bn in 2015. The biggest impact came from Unrealized Gains on Available-for-Sale Financial Assets, which deducted NT\$4.7bn from Statutory Net Worth.
- Page 30 Page 30 – For adjusted NAV, the shareholder value at the end of 2015 was \$64.3bn. Unrealized Gains on property added NT\$72.6bn. Special reserves of Unrealized Gains on Property added NT\$21.2bn. Foreign exchange volatility reserve and others added another NT\$6.7bn.
- Page 31 Page 31 – VIF grew from NT\$111.7bn to NT\$121.4bn in 2015. Lower investment return counted the most impact from the assumption changes. VIF grew mainly from the new business issued, which added NT\$23.2bn to VIF.
- Page 32 Page 32 – VNB decreased from NT\$17.8bn to NT\$16.8bn in 2015. The decrease of sales volume deducted NT\$2.3bn from VNB. However, better Product Mix brought VNB up a little bit and increased VNB margin to 22.1%.
- That wraps up our results presentation. Moderator, please start the Q&A session.

## Q&A SESSION

### *Disclaimer:*

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