

Research Update

Cathay Life Insurance Co. Ltd. Ratings Affirmed At 'twAA+'; Outlook Stable

September 23, 2019

Overview

- Cathay Life continues to dominate the consolidated credit profile of the Cathay FHC group, contributing a large part of the group's capital and asset base and acting as one of the group's core subsidiaries.
- Cathay Life has a leading market position by total premiums written in Taiwan's life insurance sector, a well-established scale advantage, and very strong control over its distribution channels. We also assess the insurer's capitalization, investment risk exposure, and profitability to be about the domestic average.
- We are affirming our 'twAA+' financial strength and issuer credit ratings on Cathay Life.
- The outlook is stable to reflect our expectation that Cathay Life will maintain its leading market position in Taiwan's life insurance market with stable capitalization over the next one to two years.

Rating Action

Taiwan Ratings Corp. today affirmed its 'twAA+' long-term financial strength and issuer credit ratings on Taiwan-domiciled **Cathay Life Insurance Co. Ltd.** The outlook is stable.

Outlook

The stable outlook reflects our view that Cathay Life will remain the flagship entity and a core member of the **Cathay Financial Holding Co. Ltd.** (Cathay FHC) group and therefore dominate the group credit profile over the next few years. We expect Cathay Life's capital adequacy to remain modest over the period, given the insurer's growth strategy domestically and overseas. Nonetheless, we expect the group to maintain prudent capital management including a supportive dividend policy for Cathay Life.

We also expect Cathay Life to maintain its investment asset allocation strategy, an operating performance consistent with our base-case assumptions of return on average assets of 0.5%-0.6%, and a very strong competitive position in Taiwan's life insurance sector. Moreover, we believe the insurer will maintain its sound risk control mechanism to mitigate volatility in its financial risk profile associated with fluctuations in the capital market and foreign exchange rates.

Downward scenario

We could lower the ratings on Cathay Life if:

- Cathay Life's capital deficiency weakens significantly due to: (1) unexpected financial market volatility with sizable and unrecoverable losses on the insurer's investment portfolio; (2) overly

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aggressive business growth, either organically or via merger and acquisitions, or (3) significantly slower growth of value in-force than our forecast; or

- The effectiveness of Cathay Life's hedging mechanism materially weakens or its hedging policies become more aggressive, resulting in higher foreign exchange risks that could negatively affect the insurer's capitalization.

Upward scenario

We view the likelihood of an upgrade to be remote over the next two years. Such action would require a significant increase in capital to raise our assessment of Cathay Life's capital and earnings to strong. This would also have to be accompanied by the insurer's superior earnings resilience compared with its peers' and stable credit profiles for the other core entities of the Cathay FHC group.

Rationale

We affirmed the ratings on Cathay Life to reflect the insurer's leading market position, well-established franchise from its large operating scale, very strong control over distribution channels, and good underwriting risk control compared with other life insurers domestically. However, we assess Cathay Life's capitalization as fair, at no more than 30% below the 'BBB' confidence level per our capital model. We view this level to be slightly weaker than that of Cathay Life's international peers, albeit in line with the local peer average. This is despite our assessment that Cathay Life has satisfactory capital and earnings, given the insurer's track record of asset and liability risk control, as well as volatility of its domestic equity investments.

Cathay Life's investment leverage and foreign exchange risk exposure are also higher than that of its regional peers'. This which makes the insurer susceptible to global capital market volatility.

Rating Score Snapshot

Business Risk Profile	Strong
Competitive position	Very strong
IICRA	Moderately high
Financial Risk Profile	Satisfactory
Capital and earnings	Satisfactory
Risk exposure	Moderately low
Funding structure	Neutral
Modifiers	
Governance	Neutral
Liquidity	Exceptional
Financial Strength Rating	twAA+

Related Criteria

- General Criteria: Group Rating Methodology - July 01, 2019
- General Criteria: Hybrid Capital: Methodology And Assumptions - July 01, 2019
- Criteria | Insurance | General: Insurers Rating Methodology - July 01, 2019
- Understanding Taiwan Ratings' Rating Definitions, www.taiwanratings.com - June 26, 2018
- Criteria | Insurance | General: Refined Methodology And Assumptions For Analyzing Insurer Capital Adequacy Using The Risk-Based Insurance Capital Model - June 07, 2010
- General Criteria: Principles For Rating Debt Issues Based On Imputed Promises - December 19, 2014
- General Criteria: Use Of CreditWatch And Outlooks - September 14, 2009

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Ratings List

Ratings Affirmed

Cathay Life Insurance Co. Ltd.

Issuer Credit Rating	twAA+/Stable
Financial Strength Rating	twAA+/Stable

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.taiwanratings.com for further information. Complete ratings information is available to subscribers of Rating Research Service at rrs.taiwanratings.com.tw. All ratings affected by this rating action can be found on Taiwan Ratings' public website at www.taiwanratings.com.

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