

Insurance - China

Potential cut of guaranteed rates from 3.5% and 3.0%

Industry Overview

Potential cut of guaranteed rates from 3.5% to 3.0%

China domestic media reported that China regulators are going to cut China insurers' guaranteed rates from 3.5% to 3.0%. The news has been in the market from the beginning of this year and we think the cut is highly likely as the current guaranteed rates at 3.5%, which was cut from 4.025% in 2017, are much higher than market rates, such as benchmark deposit rates and 10yr treasury bill rates, and the adjustment is necessary to lower insurers' interest rate risks in the future.

What are guaranteed rates?

Guaranteed rates are actually assumed interest rates and are important for insurers' pricing. The rates are not only for "saving" products, like annuities, but also other products, from critical illness to health insurance. As insurers set guaranteed rates, they calculate premium based on the rates and policyholders can, likely, regard the rates as the return they could receive. Higher guaranteed rates mean both lower premium and better return, which are good for policyholders, but could lead to risks on insurers if actual market rates get lower in the future. On the contrary, lower guaranteed rates will lead to higher premium and lower return for policyholders, but lower risks on insurers. To cut guaranteed rates from 3.5% and 3.0% will likely lead to 5-15% increase of premium, depending on product types and duration.

Impact on sales: good for 2Q, bad for 3Q

As products with 3.5% guaranteed rates are still in the market, we may see another round of "last call" in 2Q23, i.e., potential customers rush to buy the 3.5% products before the products are sold out. Usually, such kind of purchase could boost near-term sales, leading to better premium/VNB (Value of New Business) growth in 2Q23, but at the cost of weaker sales in 3Q23. The typical example was the sharp decline of critical illness products sales in 2Q21 when the old products were terminated in 1Q21.

Long-term risks are lower

Not only Mainland China insurers, insurers in Japan and Taiwan also suffered from the impact of interest rate cuts and huge losses. If China stays in the low interest rate environment for longer time, 3.5% guaranteed rates will undoubtedly give insurers higher risks than 3.0%. Even at 3.0%, we think insurance products could still be attractive than the current return from bank wealth management products which no longer provide guarantee to principle and return.

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