BARRON'S INTERVIEW

AIA's Mark Tucker Sets Eyes on China Prize

Five years after its IPO, the CEO of the Asian insurer is set on snaring a bigger share of the Chinese market.

By ISABELLA ZHONG
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Mark Tucker's burning of the midnight oil has helped millions of people across Asia sleep soundly. In the five years since he was parachuted in to float the Asian unit of beleaguered U.S. insurance giant American International Group, Tucker, 58, has transformed AIA Group into the world's second largest life insurer by market cap.

Tucker helped the pan-Asian insurer deliver another solid performance in 2015 as AIA Group (1299.HK) celebrated its fifth birthday as an independent company. While the set of numbers may not have the dazzle of the high octane growth of some of Asia's most popular stocks, they underscore the sure-footed strategy that has made AIA a core holding in many portfolios. Value of new business – which measures the amount of future sales an insurer has locked in – grew 19% year-on-year, while embedded value, or the total value of AIA's business, grew 2.8% to $38.2 billion. A 10% rise in net operating profit underwrote a 39% increase in dividends.

"We are delivering what we said we would," Tucker tells *Barron's Asia* as he sat down for an exclusive interview at AIA's gleaming headquarters in Hong Kong's Central district. Nestled on a swivel chair in a meeting room overlooking Victoria Harbour, the former professional soccer player – and Chelsea supporter – contemplated AIA's game plan for tackling Asia's fast-growing insurance market.

When *Barron's* last caught up with Tucker in 2011, it was a time of new beginnings for the pan-Asian insurer. The company's split from former parent AIG (AIG) and its subsequent shotgun listing in Hong Kong "drew a clear line in the sand" that separated it from the "financial, operational and reputational challenges" that were plaguing the U.S. insurance giant. Upbeat about the growth opportunities underpinned by Asia's rising standards of living, Tucker went on a mission to revitalize AIA.

Tucker has delivered on his goal in spades. AIA's value of new business has more than tripled from $667 million in 2010 to $2.2 billion last year. The business is more profitable thanks to AIA's focus on selling high-margin protection policies through its own army of sales agents. The insurer's VNB margin is now 17 percentage points wider than the 33% it logged in 2010. On the back of the strong top line growth and fatter margins, AIA's net operating profit has almost doubled over the past five years from $1.7 billion to $3.2 billion.

The strong and steady gains in profitability have been reflected in the share price. At its peak last April, AIA's stock had gained almost 200% on its IPO price of HKD19.68 a share, which far outpaced the 17% rise by the Hang Seng Index during the same period. Baring Asset Management investment director William Fong views AIA as "the only real insurance company" in Asia. While other insurers like Ping An Insurance (2318.HK) tend


Mark Tucker, chief executive of AIA Group.

to also operate banks and sell wealth management products, AIA is focused on selling only insurance policies. "They will never sell you a fund," says Fong who has AIA as a top holding in his portfolio. "They just sell you protection, which is very high margin, and therefore they have managed to grow their profit margin every year."

However, fears about the slowing economy in China, which ranks as AIA's third largest market, and weakening Asian currencies have buffeted the insurer's shares in recent months. It also didn't help that China has clamped down on purchases of overseas insurance products as it looked to stem capital outflows. In February, Beijing imposed a $5,000 limit on UnionPay transactions, which are a popular avenue for mainland Chinese households to pay premiums for insurance policies abroad. AIA shares plunged as much as 9.4% on the news. But Tucker argues the actual impact is "not material." "If you look at our customers from China, 75% to 80% are effectively buying policies with less than a $5,000 premium," he points out. The CEO is upbeat about China and expects the country to eventually become AIA's biggest market. Hong Kong, which accounts for a third of the value of new business, is currently AIA's largest market, followed by Thailand.

At around HKD42.45 a share, AIA is down 9% in the year to date. The dip could present a buying opportunity for long-term investors. AIA currently fetches 1.6 times embedded value, which is below a five-year average of 1.7 times. On a price-to-forward earnings basis, the stock has retreated to five-year-average levels around 18 times. The valuations look undemanding given AIA is expected to more than double earnings per share from USD23 cents last year to USD49 cents in 2019, according to consensus analyst estimates from FactSet. Although further weakness in Asian currencies and gyrating financial markets, which underwrote a 10% decline in AIA's net profit last year, could weigh on near-term earnings, the insurer's long-term growth profile appears rock solid. Nomura analyst Shengbo Tang, who has a buy rating on AIA with a HKD60 a share target price, argues AIA's broad geographic footprint – which spans 18 countries – long history, accelerating brand recognition and value-focused strategy makes it a stand-out play on Asia's burgeoning life insurance market.

Life insurance premiums in emerging and developing Asia could average an 11% pace of annual growth over the next five years, with Indonesia, China and India being the three leading markets, according to Reinsurance giant Munich Re (MUV2.DE). Besides a considerably lower coverage ratio compared to developed markets such as Europe and North America, rising levels of income, urbanization and financial savviness are also poised to bolster Asia's appetite for insurance policies.

AIA's rapidly expanding army of sales agents gives it a hefty leg up in capturing the burgeoning demand. "AIA's agency channel is stronger compared to most of its competitors with its emphasis on agent quality rather than quantity," notes Nomura's Tang. It's a fact that Tucker takes a great deal of pride in. The CEO went to great lengths to empower AIA's sales force when he first took the helm in 2010. And the result speaks for itself. "Our Million Dollar Round Table agents in China went up 71%, which is five times since the IPO," Tucker beams. AIA ranks number one globally for the number of agents who have made it into the exclusive club.

Tucker points out that in China, where rivals such as Ping An and China Life (2628.HK) have more than a million agents on their rosters, AIA's sales force is bringing in "the highest quality business." "98% of our business in China is regular premium, not single, big lump sum," he says. The focus on quality means profit margins for AIA's agency sales, which account for around 70% of the value of new business growth, are much higher than for other distribution channels such as bancassurance. In turn, AIA's compensation model ensures that its high-performing agents are aptly rewarded and

poachers are kept at bay. "Our agents are paid a multiple of the industry average, given their productivity" says Tucker. Duly rewarding hard work also helps AIA to attract fresh talent although the insurer is "very selective" about new recruits so as to maintain the high quality of its sales force.

Besides growing in size, Asia's life insurance market is also going through a demographic shift. Countries such as China, South Korea and Singapore have a greying population, which will lead to higher mortality rates – and claims – in coming years, while urbanization is driving an increase in the incidence of chronic diseases such as cancer and diabetes. Because of its protection-heavy product mix, AIA's business is more sensitive to shifts in mortality and morbidity rates compared to rivals, notes Nomura's Tang. But Tucker is hitting back at Asia's rising morbidity rates by helping customers to live healthier lifestyles. "Traditional insurance has been the case where you die or get injured and we paid," he says. "Now, we want to help you to live a longer, better and healthier life." With its new AIA Vitality program, the insurer gives discounts on premiums and other rewards such as movie tickets to customers who exercise and eat healthily. Also, "you are monitored very carefully," says Tucker. "You can't just eat fast food all the time and get bigger and bigger because you have to go for check-ups."

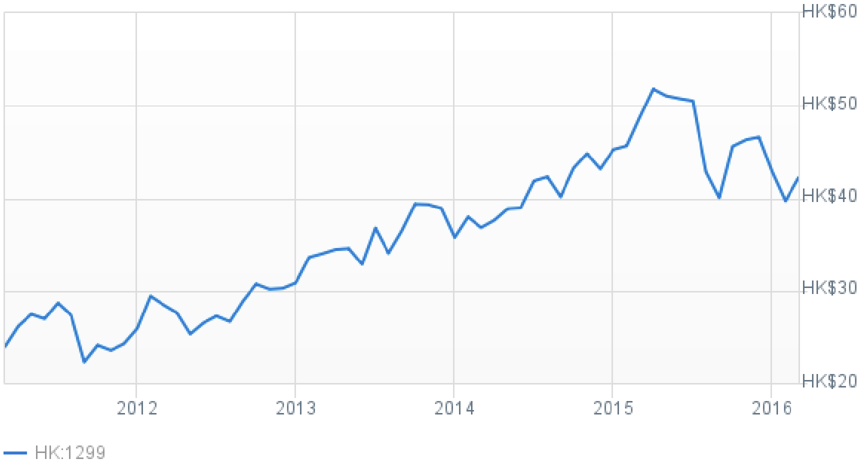
While mortality may be more difficult to modulate than morbidity, AIA is well equipped to navigate changes. The insurer's century-long history and customer base of more than 45 million allows it to generate mortality tables that Tucker says are more insightful than government versions. AIA is also known for being conservative with the assumptions it inputs into pricing models, which include estimates of mortality, as well as morbidity and surrender rates. Tucker tells *Barron's Asia* that positive deviations between actual numbers and assumptions have boosted the insurer's profits by more than $750 million in the past five years. "My view is that we need to be prudent and thoughtful and act as stewards of the business because our job is to ensure the company is here in 100 years' time," the insurance industry veteran says.

The prudence is also visible on the balance sheet. AIA's solvency ratio – a measure of the soundness of an insurer's balance sheet – is a sturdy 4.3 times, which is much higher than rival Prudential's (PRU.UK) 2.5 times and puts the Hong Kong-based insurer in good standing to weather what could be the arrival of tougher solvency rules in Asia in coming years. AIA is also conservative with how it invests the billions of premiums it collects each year. Although a fall in the value of its stock holdings took a $370 million bite out of the AIA's net profits last year, the insurer's investment portfolio contains mostly bonds and is less exposed to stocks than that of Chinese rivals. Nomura's Tang estimates a 10% decline in Asia stocks would leave a 2% dent in AIA's earnings, which is lower than the 3.3% for Ping An and the 5.5% for New China Life (1336.HK). The increasing availability of long-dated bonds in Asia is also offsetting mismatches between the duration of policies and the investments needed to fund them. "If you look at Thailand as an example, the longest bond you could buy was 30 or 60 days post the 1997 Asia financial crisis," says Tucker. "You can now buy 50 year durations."

AIA's financial discipline means it has also been less active in acquisitions compared to rivals despite it having ample financial capacity due to strong cash flows and low debt levels. "When investment banks tell you something is strategic, it often means the financials are not very good," laughs Tucker. That said though, the CEO spies acquisition opportunities in some markets, especially given recent falls in stock valuations, but was tight-lipped about which. Nonetheless, AIA's main focus will be organic growth. "We have a very wide footprint across 18 markets," says Tucker. "We want to get deeper in each of these markets and broader in products, distribution and customers in each of them."

Sure-Footed

AIA Group Ltd.



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