

Asian Life Insurance Company Limited

ICRA Nepal assigns [ICRANP] IPO Grade 4+ to the proposed rights issue (equity shares) of Asian Life Insurance Company Limited

INSTRUMENT/FACILITY	ISSUE SIZE	RATING ACTION (OCTOBER 2017)
Rights Issue (Equity)	NPR 402.79662 million	[ICRANP] IPO Grade 4+ (Assigned)

ICRA Nepal has assigned “[ICRANP] IPO Grade 4+” indicating below average fundamentals to the proposed rights issue amounting NPR 402.79662 million of Asian Life Insurance Company Limited (ALICL). ICRA Nepal assigns IPO¹ grading on a scale of IPO Grade 1 through IPO Grade 5, with Grade 1 indicating strong fundamentals and Grade 5 indicating poor fundamentals. For the grading categories 2, 3 and 4, the sign of + (plus) appended to the grading symbols indicate their relative positioning within the grading categories concerned. Thus, the grading of 2+, 3+ and 4+ are one notch higher than 2, 3, and 4 respectively. ALICL has proposed 50% rights issue of 4,027,966.2 number of equity shares each with face value of NPR 100/-, to be issued to the existing shareholders at par. The proposed issue is being made in order to comply with the revised capital requirement for life insurers² rolled out by the Insurance Board of Nepal (the regulator).

The grading considers ALICL’s relatively moderate operating track record, moderate market positioning as reflected in ~6% share in industry gross premium written (GPW) over past 2-3 years and adequate franchise network of the company (23 branches and 72 sub-branches) across the country. The grading also factors in ALICL’s strong presence in profitable endowment segment and sizeable life fund of over NPR 10 billion built over relatively short time; which augurs well for incremental returns to policyholders as well as shareholders of the company. The grading also factors in adequate reinsurance arrangements including catastrophic coverage provision, experienced senior management and conservative underwriting norms. ICRA Nepal also takes note of the negligible impact of the April 2015 earthquake on ALICL’s solvency and claims paying ability.

However, the grading is constrained by slim solvency margin of the company. Solvency profile of ALICL deteriorated after FY2013 due to factors like de-growth in fresh premium earnings (in FY2012 and FY2013)³ and declining yield on investments that lowered new business surplus. Solvency margin improved marginally in FY2016 due to recent improvement in new business premium which remains a positive. However, despite improvement, solvency margin of ALICL as on mid-July 2016 stood at 1.56 times, marginally above regulatory minimum of 1.5 times. The assigned grading also remains constrained by lower premium growth rate compared to industry, moderate profitability profile of the company resulted from lower actuarial surplus transferred from life fund during past 2-3 years ending FY2016⁴, absence of institutional promoters and challenging operating environment for life insurers after the recent licensing (in mid- 2017) of 10 new life insurance companies (LICs) by the regulator.

ALICL’s GPW has grown at CAGR 19% during past 4 years (FY2013-FY2017), much below the industry average of 28%. Nonetheless, following weak growth in FY2012 and FY2013, ALICL’s GPW growth has improved enabling the company to maintain its market share of ~6% in the industry GPW. Moreover, during past 4 years, ALICL’s fresh premium has grown at CAGR 27% which remains a positive from incremental business growth perspective. During past 3-4 years, term product and single premium endowment product have registered good growth across the industry. Due to absence of these products in ALICL’s portfolio initially, ALICL’s growth lagged the industry average. In terms of distribution channel, ALICL relies heavily on individual agents while business sourced from bancassurance remains negligible at present.

ALICL’s premium mix is entirely comprised of endowment policies (and its variants) during past 5 years. The company does not have outstanding term business as on mid-July 2017 (except for negligible amount of recently introduced micro-term business). Due to weak term and single premium endowment business,

¹ Includes rights and further public issue of equity shares

² Minimum paid up capital of NPR 2 billion to be maintained by July 2018 by all life insurers

³ ALICL’s business was temporarily suspended by the regulator in 2012 and 2013, over dividend distribution issues.

⁴ Actuarial valuation of life fund as on FY2017 end is under progress currently.

proportion of new business premium (first year premium *plus* single premium) remains moderate vis-à-vis peers (average of 27% during past 2 years). Nonetheless, gross premium earnings remained supported by strong renewal premium (~86% renewal rate in past 3 years). First year premium reported a decline of ~8% in FY2017 amid unfavourable business environment and competitive pressures on employees' retention created by licensing of new LICs and local election during last quarter of FY2017 among other things.

Gross benefit paid has grown by CAGR 30% during past 3 years ending FY2017, slightly higher than the growth rate of premium earnings. Over the period, proportion of surrender payment remains the highest (44% of gross benefits paid during past 3 years), followed by death claims (23%), scheduled payments⁵ (21%) and others. Proportion of policy surrender has increased during past 3-4 years from ~22% of gross claims in FY14 to 54% in FY2017. Considering the entry of new players in the industry, the proportion of policy surrenders could increase over medium term for ALICL. Nonetheless, due to low track record, benefit payment ratio (net claims paid/net premium) of ALICL remains low at ~7% over past 3 years. At the same time, ALICL's claims paying ability remains healthy (amount available for claims/ claims paid ratio of ~15 times in FY2017, albeit on small scale).

Net investment income of ALICL for FY2017 stood at NPR 809 million corresponding to average yield on investment of ~9.5%⁶. The investment portfolio remains compliant with the regulatory guidelines, with 88% of portfolio, as on mid-July-17 (comprising investments in Government securities, fixed deposits receipt (FDR) (with Commercial banks and Development Banks) and debentures of commercial banks) compared to ~87% in mid-July-16. During past 6-12 months, banking interest rates have begun to harden, following a period of rising liquidity and softer rates during FY14-FY16. Since, ~80% of the total investment of ALICL is concentrated in domestic financial institution FDRs, hardening of interest rates augurs well for the incremental earning profile of the company.

Due to absence of term business, ALICL's profitability depends entirely on transfer of surplus after actuarial evaluation of the adequacy of life fund. During FY 2016-17, ALICL reported Net Profit of ~NPR 4.80⁷ million (before transfer of actuarial surplus from life fund) on a Net Premium of NPR 2,279 million as compared to Net profit of NPR 106 million on a net premium of NPR 1,999 million for FY16 (corresponding to return on net worth of ~11%). Strong endowment product driven business, growing life fund, relatively lower operating expense ratio remain positive for incremental profitability. However, ability of ALICL to achieve targeted business growth amid increased competition in the industry remains a challenge. Moreover, incremental return indicators are likely to remain diluted given sizeable equity injection plan of the management.

On the solvency front, ALICL solvency ratio remains 1.56 times on July 2016⁸ vis-a-vis a regulatory minimum requirement of 1.5 times. Incremental capital injection plan of the company is likely to comfort its solvency position to some extent. Similarly, life fund/total investment ratio stood slightly higher at 112% on July-17 vs. 106% in July-16. ALICL has reinsurance agreement (including catastrophic reinsurance agreement) with SCOR Re, Singapore⁹ since inception.

Company Profile

Asian Life Insurance Company Limited (ALICL) is the 5th life insurance company to be licensed by Beema Samiti (Insurance Board, Nepal). ALICL was licensed in 27th February 2008 and started commercial operation from 3rd April 2008.

ALICL is among the smaller players in the industry with ~6% market share (in 9 players universe) in industry gross premium earnings during past 2 years. As of mid-July 2017, it is in operation with 95 outlets (23

⁵ annuities/pension payment

⁶ Including capital gain, excluding capital gain, the yield stood at ~7%.

⁷ Before transfer from life insurance fund due to pending actuary valuation

⁸ Solvency ratio for July 2017 is yet to be determined pending actuarial evaluation

⁹ Rated Aa3 (stable) by Moody's for financial strength rating.

policy issuing branches and 72 sub-branches) and ~9,400 active agents spread across the nation for procuring new business and extending after sales services.

ALICL has ~70:30 promoter-public shareholdings as on mid-July-2017. ALICL reported a profit after tax of NPR 4.76 million (*before transfer from Life Insurance Fund*) during FY 2016-17 over total assets base of NPR 11,307 million on mid-Jul-2017 as compared to profit after tax of NPR 106 million during FY 2015-16 over total assets base of NPR 8,952 million as of mid-Jul-2016. In terms of technology platform, ALICL has implemented “Soham Life” in its corporate office and all its branches

October 2017

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