

Himalayan General Insurance Company Limited

ICRA Nepal assigns [ICRANP] IPO Grade 3 to the proposed rights issue (equity shares) of Himalayan General Insurance Company Limited

INSTRUMENT/FACILITY	ISSUE SIZE	RATING ACTION (MAY 2017)
Rights Issue (Equity shares)	NPR 642 million	[ICRANP] IPO Grade 3 (Assigned)

ICRA Nepal has assigned “[ICRANP] IPO Grade 3”, indicating average fundamentals to the proposed rights issue amounting to NPR 642 million of Himalayan General Insurance Company Limited (HGI). 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. HGI has proposed 166.67% rights issue of 6,420,000 numbers of equity shares of face value NPR 100 each, to be issued to the existing shareholders at par. The proposed rights issue is being made to increase its capital base in line with the revised minimum paid up capital requirement for general insurers² as prescribed by the Insurance Board of Nepal.

The assigned grading factors in HGI’s long track record, tested underwriting norms, steady clientele comprising of reputed businesses³, adequate underwriting and overall profitability and experienced management team. The grading also factors adequate reinsurance arrangements, including catastrophic provisions, which helped HGI maintain its claims paying ability, solvency position and profitability profile⁴ in the aftermath of the April 2015 earthquake.

However, the grading is constrained by low business growth vis-à-vis industry average (past 5 years CAGR⁵ growth of 15% in GPW⁶ and 4% in NPW⁷ vs. industry average growth of 21% and 19% respectively), high concentration among top accounts (top 10 clients accounted for 63% of GPW in FY16) along with high dependence on institutional clients (85% of GPW during past 2 years) which remains a concern to the stability of earning profile. HGI premium cession to reinsurers remains the highest in the industry due to high proportion of large ticket sum insured. This affects its net premium earnings and profit levels compared to its gross premium written. Low premium retention emanates from low proportion of retail business, which is partly aided by HGI’s moderate franchise network of 11 branches as on mid-Jan-2017. The grading is also constrained by likely dilution in returns indicators of HGI with proposed capital injection; despite adequate profitability profile as of now (return on net worth of ~19% as on mid-Jul-16). The grading is further constrained by lack of institutional promoters, moderate yield on investment and stiff competition from other players in the general insurance industry of Nepal.

In the aftermath of April 2015 earthquake, HGI was exposed to a total earthquake related claims of ~NPR 5 billion; concentrated among few large accounts (top 5 earthquake claims accounted for >75% of total claims). Most of these large accounts were facultatively reinsured with only small portion of risk retained by HGI. Additionally, the catastrophic loss coverage under reinsurance treaty also cushioned the earthquake losses. As a result, the impact of earthquake related claims in the financials of HGI remained low. Of the total claims of ~NPR 5 billion, ~99.5% was recovered through the reinsurers including ~85% recovery under facultative reinsurance arrangements. HGI retained a total loss of ~NPR 15 million in its account towards earthquake related claims. Out of the total earthquake claims of NPR 5 billion, ~NPR 1 billion remains payable as on mid-Jan 2017 mainly due to pending final surveyor report. HGI’s retention out of the claims payable is likely to be negligible (~NPR 0.3 million).

HGI is among the medium sized players in the general insurance industry in terms of premium earnings with ~7% share in industry gross premium written (GPW) in FY16. However, the premium earnings are

¹ Includes rights and further public issue of equity shares

² Minimum paid up capital of NPR 1 billion to be maintained by July 2018 by all general insurers.

³ Major clients include the projects with foreign direct investments

⁴ Combined ratio for the company is better than Industry (~59% during FY14-FY16 Vs. industry average of ~84%).

⁵ Compounded annual growth rate

⁶ Gross premium written

⁷ Net premium written



highly concentrated among top accounts most of which are facultatively reinsured by HGI, retaining a small portion of the premium (and risk). During FY12-FY16, average premium retention ratio for HGI stood at ~26%, much lower than industry average of ~51%. As a result, HGI has a modest ~3% share in industry NPW in FY16. During FY12-FY16, HGI's premium growth rate has lagged the industry average eroding the market share of the company. Management plans to boost the volume of premium earned and retained by focussing on geographical expansion and retail business is likely to be challenged by the competitive industry scenario.

HGI's portfolio mix is dominated by the motor segment (74% of Net premium earned (NPE) during FY14-FY16), followed by miscellaneous⁸ (19%) and Fire (5%); with negligible contribution from other segments. All major segments of HGI has generated underwriting surplus during each of past 5 years ending FY16. Overall underwriting surplus of HGI has grown by 28% during FY12-FY16, backed by decline in claims ratio (from 59% in FY12 to 31% in FY16) and commission expense ratio⁹. Low premium retention and high management expense ratio (on small base) remains a challenge to underwriting performance. Source wise, business from direct customers accounted for ~75% of GPW during FY14-FY16 while only ~25% was sourced through individual/ corporate agents. Similarly, during FY14-FY16, ~85% of GPW was accounted for by institutional clients, reflecting on the weak retail presence of HGI.

Underwriting surplus of HGI in FY16 has reported healthy growth (NPR 144 million in FY16 vs 44 million in FY15). Combined ratio of the company in FY16 stood at 35%, improving from 81% in FY15, backed by moderation in claims ratio and commission expense ratio. However, it was partly offset by stagnant premium level and increase in net worth (from retention in profit accruals). As a result, return on net worth of HGI in FY16 stood at ~19% vis-a-vis ~25% in FY15.

Profitability of HGI remains supported by its investment income (average yield of ~5% over past 12-18 months over a portfolio of NPR 787 million in mid-January 2017). Investment yield was significantly benefitted during FY15 due to one-off dividend income from Nepal Reinsurance. Rising interest rate environment and proceeds collected from the proposed IPO could boost HGI's investment income and prevent dilution of return for the shareholders to some extent. However, it will depend on the sustainability of the increased interest rates. Investment portfolio of HGI is by and large in compliance with the guidelines prescribed by the regulator, with major concentration in Government securities and Banks fixed deposits. HGI has been maintaining the mandatory technical reserves and restricted reserves¹⁰ as prescribed by the regulatory authority (Insurance Board of Nepal). As on mid-Jan-17 the said reserves accounted for 77% of HGI's net worth. HGI's solvency margin on mid-Jul-16, calculated as per regulatory directive, stood at ~3 times vis-a-vis a regulatory minimum of 1.0x times.

Company Profile

Operating since December 1993, Himalayan General Insurance Company Limited (HGI) is among the oldest players in the non-life insurance industry¹¹ of Nepal. HGI is a medium sized player in the non-life insurance segment with market share of ~7% in terms of gross premium and ~3% in terms of net premium in FY16. As of January 2017, the total network of the company comprises of 11 branches spread across 10 districts and employs 108 staffs for procuring business and extending after sales services.

The paid-up capital and the net worth of the company as of mid-Jan 2017 is NPR 385 million with net worth of NPR 745 million. As on mid-Jan 2017, HGI has 51:49 promoter public shareholding with maximum individual shareholding of 13.80%. Major shareholders of the company include Mahendra Krishna Shrestha (13.80%)¹², Subarna Krishna Shrestha (12.20%), Bikram Krishna Shrestha (11.87%), Vinod Krishna Shrestha (11.86%) and Raj Krishna Shrestha (11.70%).

HGI reported profit after tax (PAT) of NPR 131 million during FY16 over an asset base of NPR 1,377 million as on mid-July 2016 as compared to a PAT of NPR 142 million in FY15 over an asset base of

⁸ Includes All Risk policies, personal accidents, group medical policies, bankers' blanket indemnity, among others.

⁹ Agency commission was capped at 5% of GPW by the Insurance Board with effect from April 2015.

¹⁰ Technical reserve includes (reserve towards unpaid claims & unexpired risk); restricted reserves include Insurance reserve and Insurance fund appropriated from annual profits.

¹¹ Industry comprises of 17 non-life insurers.

¹² Mr. Mahendra Krishna Shrestha and family control ~60% stake in HGI as on mid-Jan 2017.



~NPR1,774 million in FY2014-15. During H1FY17¹³, the company has reported PAT of NPR is NPR 40 million over an asset base of NPR 1,423 million. In terms of technology platform, HGI has implemented “Gaps Go” in its corporate office. The computerized information has been centralized across all the branches.

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¹³ As per unaudited financials