Gurans Life Insurance Company Limited

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

INSTRUMENT/FACILITY	ISSUE SIZE	RATING ACTION (FEBRUARY 2019)
Rights Issue (Equity)	NPR 297 million	[ICRANP] IPO Grade 4 (Assigned)

ICRA Nepal has assigned **[ICRANP] IPO Grade 4,** indicating below average fundamentals to the proposed rights issue of NPR 297 million of Gurans Life Insurance Company Limited (GLICL). ICRA Nepal assigns IPO[1] 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. GLICL has proposed the 50% rights issue of 2,970,000 equity shares each with the face value of NPR 100/-, to be issued to the existing shareholders at par. The proposed issue is being made to comply with the revised capital requirement for life insurers[2] rolled out by the Insurance Board of Nepal (the regulator). GLICL's paid up capital after proposed rights issue will reach ~NPR 891 million vs. regulatory minimum requirement of NPR 2,000 million. GLICL is likely to raise another tranche of fresh equity through a further rights issue.

The grading factors in the good ownership profile of the company (as evidenced by >60% stake by individuals and institutions associated with Dugar family[3]). The grading also factors in good growth in premium earnings in recent years (CAGR 30% over past 3 years ending FY2018) partly aided by the growth along foreign employment (FE) term business (which grew by CAGR 96% over the same period). The grading also considers an adequate franchise network of the company (72 outlets across the country) and the relatively unpenetrated insurance market in the country which offers adequate growth potential. The re-insurance contracts share the risk of GLICL with the reinsurers (albeit with low catastrophic loss coverage) and has been factored into the grading.

However, the grading remains constrained by the limited track record (operating since 2008) and small scale of operation of GLICL (smallest among the old nine players in the industry in terms of premium earnings in FY2018 and FY2017). Grading also remains constrained by the moderate premium renewal rates of GLICL (~59% in FY2018) which remains a concern to the earnings stability and scale growth. GLICL has one of the smallest life funds in the endowment product dominated industry which limits the return potential to the profit-sharing policyholders as well as the shareholders. The grading also remains constrained by the moderate solvency profile of the company (solvency ratio of 1.63 times on mid-July 2017 vs. regulatory minimum of 1.5 times). The premium growth rate of GLICL, which was driven by FE policies in the past two to three years could moderate, going forward, given the slowdown in FE premium growth in FY2018. This could affect the future premium earnings and profitability of GLICL. The grading is also constrained by a challenging operating environment for life insurers after the recent licensing (in early FY2017) of 10 new life insurance companies (LICs) by the regulator. GLICL's current paid up capital also remains much lower to the revised regulatory minimum capital. Raising the shortfall within the stipulated timeline also remains a challenge.

GLICL's GPW has grown at a higher-than-industry average growth rate of CAGR ~30% during the past three years ending FY2018 (albeit on a low base), driven by sharp growth along mandatory FE term insurance products. GLICL ventured into FE business in FY2015, which registered high growth till FY2017 before stabilising in FY2018. The first-year premium (for traditional endowment products) over the same period grew at a much lower pace of CAGR ~16%, indicating moderate market positioning in the endowment segment. Given the intensely competitive FE segment and the relatively limited customer

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[1] Includes rights and further public issue of equity shares
[2] Minimum paid up capital of NPR 2 billion to be maintained by July 2019 by all life insurers
[3]Individuals associated with Dugar family also have substantial stake in Sunrise Bank Limited (Class A commercial bank)

base (migrant Nepalese workers), the incremental growth in the segment is expected to remain low, which, coupled with low growth in the first-year premium, could bring down the overall premium growth for GLICL going forward. During FY2018, first year premium of GLICL grew by 17% vs. a 7% decline in FY2017, which remains a comfort. The gradual improvement in insurance awareness is expected to benefit the existing players and new entrants alike. However, GLICL's ability to benefit from it, given its moderate market positioning and increased competition remains to be seen.

In terms of product mix, GLICL remains an endowment-dominated business. Despite high growth in FE business in the past three years, ~89% of the gross premium in FY2018 (~87% in FY2017) was accounted for by traditional endowment products. GLICL's term business is limited entirely to the mandatory FE business. During the past two years ending FY2018, first year premium (traditional endowment) accounted for ~27% of total premium, renewal premium accounted for ~61% of premium and single premium (mostly FE term) accounted for ~12% premium. GLICL's gross premium growth stood at 26% in FY2018 vs. 25% in FY2017. Higher growth in premium despite slowdown in FE business in FY2018 was due to improvement in first year premium growth. First year premium growth of GLICL stood at 17% in FY2018 vs. a 7% decline in FY2017. Going forward, GLICL's premium earnings, scale of operation and financial profile will depend on the company's ability to improve its first-year premium earnings and improve the policy renewal rates. In terms of the distribution channel, GLICL relies heavily on individual agents while bancassurance accounts for minimal proportion of the premium earnings.

Gross benefit paid (claims) ratio of GLICL has remained higher in FY2017 and FY2018 (12% and 15% respectively) vs. previous two years' average of ~5%. Increased ratio is on account of benefits paid under the structured moneyback plans. Despite the introduction of FE term business about three years ago, there has not been any sharp rise in the death claims for GLICL, which remains a comfort. Nonetheless, the rising death cover under FE policies and the declining number of insurable populations in the FE segment remains a threat to the long-term sustainability of FE business. GLICL's ability to pay its claims remains comfortable despite some moderation in recent years (amount available for claims/ claims paid ratio of ~7 times in past two years ending FY2018 vs. ~17 times in FY2016. The decline is caused by a relatively large benefit payment made under the structured moneyback plans in the past two years.

Net investment income of GLICL for FY2018 stood at NPR 463 million on an investment portfolio base of NPR ~NPR 4.8 billion, corresponding to an average yield on investment of ~11% (vs. ~8% in FY2017). The recent increase in the banking sector interest rates on deposits has benefitted large institutional depositors like GLICL. Since >90% of the total investment are concentrated in banking sector deposits, higher interest rates are likely to support the investment earnings and profitability of GLICL. The investment portfolio of GLICL is compliant with the regulatory guidelines, with ~93% of the investment portfolio concentrated in the FDRs with different categories of banks and financial institutions (~92% in FY2017).

Due to a sizeable endowment business, GLICL's profitability depends upon the transfer of the surplus after actuarial evaluation of the adequacy of the life fund. During FY2018, GLICL reported a net profit of NPR ~38 million (before transfer of actuarial surplus from life fund) on a net premium written of ~NPR1,448 million vs net profit of ~NPR 73 million in FY2017 on net premium written of NPR 1,129 million (corresponding to the return on equity of ~4% and ~9% respectively in FY2018 and FY2017). Over the short run, increased earnings on investment are likely to support the profitability to some extent. However long-term profitability will depend on the company's ability to scale up its operation and asset base by increasing the market share. Moreover, return indicators over the next two to three years are likely to remain diluted, given the sizeable equity injection plan of the management over the next six to eight months.

On the solvency front, GLICL's solvency margin remains slim (solvency ratio of 1.63 times in mid-July 2017[4] vs. ~1.60 times on mid-July 2016) yet adequate vis-a-vis a regulatory minimum requirement of 1.5 times. The incremental capital injection plan of the company is likely to comfort its solvency position to

[4] Solvency ratio for July 2017 is yet to be determined pending actuarial evaluation

some extent. Similarly, life fund/total investment ratio stood comfortable at 87% on mid-July 2018 vs. 80% on mid-July-2017.

For FY2019, GLICL has the reinsurance agreement for traditional life policies, FE policies and catastrophic losses with Nepal Reinsurance Company Limited. While the regular treaty adequately covers the risk for GLICL, the coverage in case of catastrophic losses remains on the lower side, which remains a concern.

Analytical approach: For arriving at the ratings, ICRA Nepal has applied its rating methodology as indicated below.

Links to applicable criteria:
IPO Grading Methodology

Company Profile
Gurans Life Insurance Company Limited (GLICL) is the sixth life insurance company to be licensed by the Insurance Board of Nepal (insurance sector regulator). GLICL commenced its business after receiving licence from the board in March 2008.

GLICL is the smallest player in terms of gross premium earnings among the nine old players in the life-insurance industry[5] with ~3% market share in industry gross premium earnings during the past two years ending FY2018. As of mid-January 2019, it is in operation with 72 outlets and it had ~2,500 active agents[6] during H1 FY2019, spread across the nation for procuring new business and extending after sales services.

GLICL has 70:30 promoter-public shareholdings as on mid-October 2018. GLICL reported a profit-after-tax of ~NPR 38 million (before transfer of actuarial surplus from life fund) during FY2018 over a total assets base of NPR 5,450 million on mid-July 2018 as compared to NPR 73 million during FY2016-17 over total assets base of NPR 4,205 million on mid-July 2017. During H1 FY2019, GLICL reported a net profit of NPR 41 million over an asset base of NPR 6,202 million on mid-January 2018. On the technology platform, GLICL has implemented the 'I Solutions' software in its corporate office and its branches.

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[5] Excluding the 10 new players that were licensed recently in FY2017
[6] Out of total registered agents of 19,600.

helping ICRA Nepal in areas such as the rating process and methodologies, analytical software, research, training, and technical and analytical skill augmentation.

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