

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 (JANUARY 2018)
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 amounting NPR 297 million of Gurans Life Insurance Company Limited (GLICL). 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. GLICL has proposed 50% rights issue of 2,970,000 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 to comply with the revised capital requirement for life insurers² rolled out by the Insurance Board of Nepal (the regulator).

The grading factors in the strong ownership profile of the company (as evidenced by >60% stake by individuals and institutions associated with Dugar family³). The grading also factors in an improvement in the premium growth of GLICL in recent years (CAGR 30% over past 5 years ending FY2017⁴) partly aided by the launching of foreign employment (FE) term business in FY2015. The grading also considers an adequate franchise network of the company (64 outlets across the country). The re-insurance contracts including the catastrophic coverage are adequate as per ICRA, and factored in the grading.

However, the grading remains constrained by low policy renewal rates of GLICL over the years which has accentuated in recent years (45% in FY2017 vs. 58% in FY2016 and 71% in FY2015). This remains a concern to the earnings stability and scale growth of the company. The grading is also constrained by the slim margin over regulatory requirements of the solvency profile (solvency ratio of 1.60 times in FY2016⁵ vis-à-vis regulatory minimum of 1.50 times), small scale of operations of the company vis-à-vis peers (ranked 9th in terms of gross premium earnings in FY2017 among the 9 players in the industry); which stems from a limited operating track record (operating since 2008). Although the premium growth remains above industry average in past 5 years, it is aided by recently introduced FE term product. Sustainability of growth and profitability of FE segment remains to be seen, especially in view of declining number of migrant Nepalese workers and an increasing risk cover. The grading also remains constrained by a relatively small life fund (~NPR 3.3 billion as on mid-Oct 2017⁶) which limits the quantum of incremental returns to profit-sharing policyholders as well as shareholders of the company. 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 GPW has grown at a CAGR of 30% during past 5 years (FY2012-FY2017), higher to the industry average of ~25%; albeit on a lower base. GLICL had ventured into FE business in FY2015, which partly aided the improvement in premium growth in recent years. However, first year premium over the period grew at a slow pace (CAGR of 14%), indicating a relatively weak market positioning. Going forward, the ability to underwrite new business is likely to remain a challenge amidst an increased competition in the industry. Policy renewal rates is also in declining trend during past 3 years ending FY2017, which remains a concern. In terms of the distribution channel, GLICL relies heavily on individual agents (and corporate tie ups for FE 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 Individuals associated with Dugar family also have substantial stake in Sunrise Bank Limited (Class A commercial bank)

⁴ Mid-July-17 data are unaudited

⁵ Actuarial valuation of life fund as on FY2017 end is under progress currently

⁶ Mid-Oct-17 data are unaudited

Despite an increase in FE business since FY2015, its proportion in the overall GLICL's portfolio remains low (13% of gross premium in FY2017). GLICL's premium mix is dominated by endowment policies (and its variants) which accounted for ~87% of gross premium during FY2017 (95% in FY2016). Apart from FE business, the company does not have any notable term business. Backed by the FE business taken up in recent years, proportion of new business has improved marginally. Nonetheless, renewal premium accounts for major source of premium earnings for GLICL (58% in FY2017, past 5 years average of 60%). Incremental growth of GLICL will depend on boosting the new business premium and controlling the policy lapse rate. However, achieving the targeted growth rate remains a challenge given the past track record of muted growth in first year premium and increased competition in the industry (particularly in the FE segment). ICRA Nepal takes note of a decline in first year premium of ~7% in FY2017 amid unfavourable business environment, competitive pressures on employees' and agents' retention created by licensing of new LICs, and local election during last quarter of FY2017.

Gross benefit paid (claims) ratio of GLICL has remained moderate (3-5% of net premium earnings during FY2013-FY2016) before rising to 13% in FY2017 (mainly due to benefits paid under the structured money-back plans). Despite the introduction of FE term business about 3 years ago, there has not been any sharp rise in the death claims for GLICL which remains a comfort. Nonetheless, rising death cover under FE policies and a declining number of insurable population in FE segment remains a threat to the long-term sustainability of the business. At the same time, with the entry of new players, FE segment is likely to witness increase competition which is also likely to affect the incremental growth under this segment. Nonetheless, GLICL's claims paying ability remains comfortable despite some moderation in recent years (amount available for claims/ claims paid ratio of ~7 times in FY2017 (~17 times in FY2016); sharp decline caused by sizeable amount paid under structured money back plans during FY2017.

Net investment income of GLICL for FY2017 stood at NPR 256 million corresponding to average yield on investment of ~8%. The investment portfolio remains compliant with the regulatory guidelines, with ~92% of portfolio, (comprising investments in Government securities, fixed deposits receipt (FDR) (with Commercial banks and Development Banks) and debentures of commercial banks) as on mid July 2017 compared to ~95% in mid-July-2016. Since mid FY2017, banking interest rates have begun to harden, following a period of rising liquidity and softer rates (during FY2014-FY2016). Since, >90% of the total investment of GLICL is concentrated in domestic financial institution's FDRs, the hardening of interest rates augurs well for the incremental earning profile of the company.

Due to a sizeable endowment business, GLICL's profitability depends upon transfer of the surplus after actuarial evaluation of the adequacy of life fund. During FY2017, GLICL reported net profit of ~NPR 57 million (before transfer of actuarial surplus from life fund pending actuarial evaluation) on a Net Premium of NPR 1,127 million, as compared to a net profit of NPR 75 million on a net premium of NPR 925 million for FY2016 (corresponding to return on net worth of ~7% in FY2017, against 10% in FY2016). At the same time, a small life fund, relatively high operating expense ratio limits the profitability prospect of the company. Short term profitability is likely to be driven by incremental performance of FE segment while long term profitability will depend on the company's ability to improve its market positioning in the traditional business arena as well as management's ability to introduce product innovation. Moreover, return indicators over next 2-3 years are likely to remain diluted given sizeable equity injection plan of the management over next 6-8 months.

On the solvency front, GLICL's solvency margin remains slim (solvency ratio of 1.60 times on mid-July 2016⁷) yet adequate 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 comfortable at 80% on mid-July-2017 vs. 80% in mid-July-2016.

⁷ Solvency ratio for July 2017 is yet to be determined pending actuarial evaluation

GLICL has a reinsurance agreement for traditional life policies with SCOR Global Life Re, Singapore⁸ since inception. GLICL changed its reinsurer for FE business and catastrophic loss cover to Nepal Reinsurance Company from FY2017 (previously done with SCOR).

Company Profile

Gurans Life Insurance Company Limited (GLICL) is the 6th life insurance company to be licensed by Insurance Board of Nepal (insurance sector regulator). GLICL commenced its business after receiving license from the board in March 2008.

GLICL is the smallest player in the industry with ~3% market share (9th rank in terms of gross premium in FY2017 among the 9-players universe). As of mid-Oct 2017, it is in operation with 64 outlets and ~3,900 active agents⁹ spread across the nation for procuring new business and extending after sales services.

GLICL has 70:30 promoter-public shareholdings as on mid-Oct-2017. GLICL reported a profit after tax of NPR 57 million (before the transfer of actuarial surplus from life fund pending actuarial evaluation) during FY 2016-17 over total assets base of NPR 4,198 million on mid-Jul-2017 as compared to profit after tax of NPR 75 million during FY 2015-16 over total assets base of NPR 3,195 million as of mid-Jul-2016. During Q1FY2017-18, GLICL has reported net profit of NPR 27 million over asset base of NPR 4,371 million on mid-Oct 2017. In terms of technology platform, GLICL has implemented “Siddhi Life” software in its corporate office and all its branches.

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⁸ Rated Aa3 (stable) by Moody’s for financial strength rating.

⁹ Out of total registered agents of ~17,000.