

**Grading Rationale**

**Asian Life Insurance Company Limited**

**Grading**

Facility/ Instrument	Amount (Rs. In Million)	Grading	Grading Action
Rights Share Issue	754.035273	CARE-NP IPO Grade 3 [IPO Grade Three]	Assigned

*The explanatory notes regarding the Grading symbols of CARE Ratings Nepal Limited (CRNL) are attached as Annexure 1*

CRNL has assigned grading of ‘CARE-NP IPO Grade 3 [IPO Grade Three]’ to the proposed Rights Share Issue of Asian Life Insurance Company Limited (ALIC). ‘CARE-NP IPO Grade 3’ indicates Average Fundamentals. CRNL assigns IPO grades on a scale of Grade 1 to Grade 5, with Grade 1 indicating strong fundamentals and Grade 5 indicating poor fundamentals. CRNL’s IPO grading is an opinion on the fundamentals of the issuer. The grade assigned to any individual issue represents a relative assessment of the ‘fundamentals’ of the issuer. ALIC proposes 60% rights share issue of 7.54035273 million equity shares of face value of Rs.100 each at par aggregating Rs. 754.035273 million.

**Detailed Rationale & Key Grading Drivers**

The grading assigned to the rights share issue of ALIC derives strength from moderate track record with experienced board and management team, diversified and adequate geographical coverage through branches, significant growth in gross premium written, consistent growth in net underwriting profit & healthy combined ratio over the period. The grading further takes into account ALIC’s moderate profitability, low net lapse ratio, moderate assets quality of investment book and increasing investment income, adequate solvency ratio, consistent growth and adequate policyholder/ life insurance fund. The grading, however, is constrained by high portion of claim paid through surrender of policies, concentration in endowment policies, competition from other insurance companies and relatively small market share in the life insurance industry.

Continued promoter support, ability to remain profitable while achieving business growth and maintain adequate solvency position would be the key grading sensitivities.

**Detailed Description of the Key Grading Drivers**

**Key Grading Strength**

***Moderate track record of operations with experienced board and management team***

ALIC started its operation from April 2008 and has been providing its service in life insurance sector for more than 10 years. ALIC has six experienced members on its board lead by Mr.

Deepak Kumar Shrestha, who is chairperson of the company who possesses experience in various Banks & Financial Institutions and Hydropower Sector. The day to day operations of the company are headed by Mr. Rajesh Kumar Shrestha, CEO since August 2012 and has overall work experience of more than two and half decades in Insurance and banking sector. He is assisted by an experienced team across various functions.

***Diversified and adequate geographical coverage through branches***

ALIC has scattered all over the country through its 29 branches (including Head Office) as on July 16, 2018. The branches are spread over all 7 Provinces and cover 24 districts (out of total 77 districts) of Nepal. Till FY17 (refers to period ending mid-July 2017), almost all the business of ALIC is sourced from Individual Agents. During FY18, ALIC has entered into Bancassurance with 8 bank and financial institutions of Nepal from which ALIC is expected to increase and diversify its business source.

***Significant growth in Gross Premium Written and Net Premium Written***

During FY18 (UA), the company's gross premium written (GPW) has increased substantially by nearly 32% to Rs.3,019 Million from Rs.2,294 Million in FY17, backed by 82% growth in first year premiums, which is in line with industry's GPW growth of 32% over the same period. The net premium written (NPW) of ALIC also grew by 32% in FY18 on the back of increase in GPW and high retention of the premium.

***Consistent growth in net underwriting profit and healthy combined ratio over the period, however moderate profitability***

ALIC has depicted consistent growth in Net Underwriting Profit over the period. Net underwriting profit increased substantially by 34% to Rs.2,100 Million during FY18 (UA) over FY17 backed by increase in NPW. During FY18 (UA), the loss ratio (claim ratio) of ALIC has declined to 6.32%; the commission ratio marginally increased to 11.24% resulting from increased Agency Commission Expenses backed by substantial increase on GPW and Expense Ratio marginally declined to 12.41%. On back of these, combined ratio reduced to 29.96% in FY18 as compared to combined ratio of 31.34% during FY17. The same, however, remained healthy.

ALIC reported net profit of Rs.46 Million during FY18 which declined from net profit of Rs.51 Million during FY17, pending actuarial surplus to be transferred from Life Fund for FY18 which is expected to increase PAT for FY18. PAT for the FY17 was declined by 52.25% over FY16 due to Rs. 79 Million provisions which are mainly related to losses on investment (due to market prices of shares falls below its cost price).

***Low Net Lapse Ratio***

Low level of net lapse not only indicates higher renewal premiums but also a strong consumer franchise. Furthermore, it also indicates longer tenure of policy in force which enables the company to recover costs and make profit over the life of the insurance contract. The level of net lapse for ALIC has been low since policies issued three year earlier are renewed with null net lapse and policies issued two year earlier are almost all renewed with 0.91% net lapse ratio during FY17. However, policies issued one year earlier shown high lapse with 13.18% net lapse ratio during FY17.

***Moderate assets quality of investment book and increasing investment income over the period***

The company had an investment portfolio of around Rs. 7,306 Million in FY16 which was increased by 24% to Rs. 9,039 Million in FY17 and the same was further improved by 39% in FY18 to Rs. 12,561 Million. ALIC has complied with guidelines prescribed by regulator for the investments. Out of the total investment portfolio, ALIC has total investment of 82% in fixed and interest bearing deposit at different Bank and Financial Institutions as on July 15, 2017, which are readily marketable in nature lends sufficient liquidity cushion to the company.

The investment income of the company is in increasing trend over the period. Investment income has been increased by 35% during FY17 to Rs.812 Million over FY16 and increased by 45% to Rs.1094 Million during FY18 on back of increase in investment portfolio. Average yield on investment of ALIC was 9.93% in FY17 which was marginally lower than industry yield of 10.20% which shows slight increase with average yield of 10.12% during FY18. Further, the investment portfolio is expected to grow post proposed rights issue and high interest rate prevailing in the banking sector likely to improve the investment yield and income for ALIC.

***Adequate solvency ratio***

ALIC maintained adequate solvency ratio of 2.45 times as on July 15, 2017. Though the solvency ratio was low at 1.53 times & 1.56 times during FY15 and FY16 respectively due to low asset base, the same was marginally above against the minimum regulatory requirement of 1.50 times. Increase in available solvency margin during FY17 led to improvement in solvency ratio of ALIC during FY17.

***Consistent growth and adequate policyholder/ life insurance fund***

ALIC has shown consistent growth in policyholder fund over the period. Policyholder fund increased by 32% to Rs. 7,744 Million during FY16 over FY15; which has further increased by 29% to Rs. 10,000 Million during FY17 and stands at 6th position (out of 9 life insurance companies operated) in terms of fund volume. Further, ALIC's policyholder fund increased to

Rs. 13,130 Million during FY18, pending actuarial valuation, and stands at 6th position (out of 18) in terms of fund volume.

### **Key Grading Weaknesses**

#### ***High portion of claim paid through surrender of policies out of total gross claim paid***

During FY17, ALIC has paid Rs. 180 Million towards gross claim settlement by various reasons. Among which 4,522 number of policies were surrendered (FY16: 3,272) by policyholders on which Rs. 97 Million (FY16: Rs. 50 million) was paid as part of claim settlement for the surrendered policies which constitutes ~54% (FY16: ~42%) of the total gross claim paid. However, the same reduced to ~46% during FY18 with Rs. 87 Million claim settlement through surrender of policies out of total Rs. 189 Million claim paid over the same period.

#### ***Concentration in Endowment policies***

ALIC's business is focused toward endowment segment and its variation. ALIC has not focused on "Foreign Employment Term Policies" segment, in view of high risk associated with the same and the other life insurance companies source large business from the same. A minimal i.e. 0.06% of GPW of ALIC during FY18, was through Micro Term Insurance and remaining was through endowment policies and its variants.

#### ***Competition from other insurance companies and relatively small market share in the life insurance industry***

Currently there are 18 life insurance companies operating in Nepal (9 companies are licensed and started operation after FY17 only) sharing total Rs. 51,008 Million of Gross Premium Written (GPW) as on July 16, 2018; where ALIC shares only 5.90% of total GPW and ranks 5th Position (out of 18). Further, the industry had Rs. 135,702 Million Policyholder's Fund as on July 15, 2017 where ALIC shares 7.27% of total Policyholder's Fund and ranks 6th (position out of 9) reflecting low market share in the industry in comparison to the established life insurance players. Further, due to increase in number of life insurance companies ALIC is expected to face high competition to tap the new customer.

### **About the Company**

Asian Life Insurance Company Limited (ALIC) is a life insurance company, started its operation from April 03, 2008 after registering as Public Limited Company as on November 13, 2007 and received operating license as per Insurance Act 2049 from Insurance Board of Nepal on February 27, 2008. ALIC has established itself as a mid-sized life insurance company in Nepal over the period. The company has been offering an extensive range of Insurance products as Money

Back, Endowment, Whole Life, Joint Life, Term Life, Micro Life Insurance products etc. through its strong and diversified sales network. ALIC has assets base of Rs. 11,201 Million as on July 15, 2017, which has increased to Rs. 14,933 Million as on July 16, 2018.

ALIC rank 6th Position in terms of Gross Premium Written (GPW) with Rs. 2,294 Million during FY17 and has improved its position to 5th with GPW of Rs. 3,019 Million during FY18 among 18 life insurance companies in Nepal. As per the regulations, the Life insurance companies will have to raise its paid-up capital to Rs 2 Billion by mid-July 2018. Paid up capital of ALIC as on mid-July 2018 was Rs.1.26 Billion, after the proposed right share of 60% to its existing shareholders, paid up capital of the company will reach at Rs. 2.01 Billion which is slightly more than regulatory requirement.

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**Annexure 1****CARE Ratings Nepal – IPO Grading Scale**

<b>CARE IPO grade</b>	<b>Definition</b>
CARE-NP IPO Grade 1	Strong fundamentals
CARE-NP IPO Grade 2	Above average fundamentals
CARE-NP IPO Grade 3	Average fundamentals
CARE-NP IPO Grade 4	Below average fundamentals
CARE-NP IPO Grade 5	Poor fundamentals

Note:

Modifiers {"+" (plus)} can be used with the grading symbols 2, 3 and 4. The modifiers reflect the comparative standing within the category.