

Grading Rationale

United Insurance Company (Nepal) Limited

Rating/ Grading

Facility/ Instrument	Amount (Rs. In Million)	Rating/ Grading	Rating Action
Rights Share Issue	725.76	CARE-NP IPO Grade 4 [IPO Grade Four]	Reaffirmed

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

CRNL has reaffirmed grading of ‘CARE-NP IPO Grade 4 [IPO Grade Four]’ to the proposed Rights Share Issue of United Insurance Company (Nepal) Limited (UIC). ‘CARE-NP IPO Grade 4’ indicates Below 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. UIC proposes 240% rights share issue of 7.2576 million (Mn) equity shares of face value of Rs.100 each at par aggregating Rs.725.76 Mn.

Detailed Rationale & Key Grading Drivers

The grading assigned to the rights share issue of UIC is constrained by substantial decline in gross premium written, net underwriting profit and PAT during FY18 (refers to 12 month period ended mid-July 2018) and H1FY19 (refers to 6 month period ended mid-January 2019) impacting combined ratio. Further, the grading is constrained by UIC’s concentration in motor segment, albeit some diluting over the period, competition from other insurance companies and relatively small market share in the non-life insurance industry in Nepal. The grading, however, derives strength from long track record and strong promoter group, experienced board and management team, improved investment income, good asset quality of investment book and healthy solvency ratio. The grading also factors in the Supreme Court order which held the action taken by Insurance Board of Nepal to halt fire business and negative reserve and surplus recovered substantially over the period.

Detailed Description of the Key Grading Drivers

Key Grading Weaknesses

Substantial decline in Gross Premium Written, net underwriting profit and PAT during FY18 and H1FY19 impacting Combined Ratio

During FY18, the company's gross premium written (GPW) declined by ~23% from Rs.619 Mn in FY17 to Rs.477 Mn in FY18 while the net premium written (NPW) decreased by ~27% to Rs.273 Mn in FY18. Further, the GPW and NPW declined by ~14% and ~10% respectively during H1FY19 vis-à-vis H1FY18. Net Underwriting Profit of UIC declined to Rs.169 Mn during FY18 from Rs.224 Mn during FY17, owing to decline in NPW and high net claims incurred during FY18. UIC reported net underwriting loss of Rs.3 Mn during H1FY19 as compared to net underwriting profit of Rs.34 Mn during H1FY18. UIC reported net profit of Rs.168 Mn during FY18, vis-à-vis PAT of Rs. 257 Mn during FY17. The net profit declined by 57% to Rs.17 Mn during H1FY19 as compared to Rs.41 Mn during H1FY18. High competition in the insurance sector, establishment of new company with limited market size, and frequent changes in management team to some extent has led to decline in overall financial performance of the UIC during FY18 and H1FY19. On the back of increase in the loss ratio (claim ratio) of UIC to 8.55 %, decline in the commission ratio to 8.63% (FY17: 9.91%) and increase in the expense ratio to 49.39% (FY17: 44.22%) during FY18, the combined ratio moderated to 49.30% in FY18 as compared to 33.85% during FY17. Further, the combined ratio deteriorated sharply to 102.36% during H1FY19 due to high net claims incurred during the said period.

Concentration in motor segment, albeit diluting over the period

Motor segment comprised 79.49% (51,460 policies) of total policies in force of 64,734, followed by fire segment (9.88%) as on July 16, 2018. Motor segment proportion reduced to 74.19% (24,083 policies) of total policies during H1FY19; whereas, the proportion of fire segment increased to 11.97% (3,887 policies) during the same period. Further, the motor segment contributed ~84% of Net Premium Earned (NPE) followed by fire (~9%) and other segments during FY18. Total NPE declined marginally by 1.34% during FY18 to Rs.333 Mn from Rs.338 Mn during FY17.

Competition from other insurance companies and relatively small market share in the non-life insurance industry

Currently there are 20 non-life insurance companies (including three newly licensed companies during Q4FY18) operating in Nepal, with a combined GPW of Rs.24417 Mn during FY18. UIC's share of the total GPW was only 1.95% and ranked 17th, reflecting low market share in the industry. Further, due to increase in number of non-life insurance companies UIC is facing high competition to tap the new customers.

Key Grading Strength

Supreme Court order held the action taken by Insurance Board of Nepal to stop fire business

Insurance Board (IB) via notice dt. March 12, 2018 directed UIC to stop its Fire Insurance Business and the same was validated by Patan Appellate Court (now Patan High Court) dt. November 28, 2017. Against which UIC had made appeal at the Supreme Court of Nepal. The court had issued interim verdict as on July 06, 2018 to hold the decision of IB and Patan High Court till the finalization of the case from Supreme Court. Accordingly UIC had informed IB regarding decision of Supreme Court via letter dated July 10, 2018 and had resumed the fire insurance business.

Long track record and strong promoter group

UIC has been providing its services in non-life insurance sector for around 24 years. As on July 15, 2017, 60% of shares are held by promoter group and remaining 40% is held by the general public. The promoter group shares are mostly owned by Chaudhary Group and N.E. group. Chaudhary Group P Ltd is a part of CG Group which is a multi-national conglomerate headquartered in Nepal. It has diversified business interests including financial services, FMCG, automobile dealerships, education, hospitality, energy, consumer electronics, real estate etc. Mr. Binod Chaudhary is the Chairman of CG Group, with networth of USD 1.52 Billion as per Forbes Magazine as on May 24, 2018. N.E. Group is an Industrial and Trading House with wide range of business activities.

Experienced Board and Management team

UIC has eight experienced members on its board lead by Mr. Uday Krishna Upadhyay, Chairman. Mr. Upadhyay has more than thirty years' of work experience in various Banks and Financial Institutions. The day to day operations of the company are headed by Acting CEO Mr.

Ramesh Kumar Bhattarai, who have overall work experience of around two decades in Insurance sector. Mr. Bhattarai holds Master in Business Administration degree. He is assisted by an experienced team across various functions.

Negative reserve and surplus recovered substantially over the period

UIC had negative reserve & surplus of Rs.50 Mn as at the end of FY17. The same has improved to positive balance with Rs.33 Mn as at the end of FY18 with accretion of PAT of Rs.168 Mn. Reserve & surplus fund had further improved to Rs. 44 Mn as at the end of H1FY19.

Improved Investment Income

The investment income of the company was volatile over the period. Investment income has increased sharply by ~66% during FY18 to Rs.66 Mn majorly benefited by increased interest income from fixed and other deposits due to high interest rates prevailing in FY18. Average yield on Investments of UIC improved to 9.21% during FY18 as compared to 6.66% during FY17. Investment income further improved by ~8% to Rs.26 Mn during H1FY19 as against Rs.24 Mn during H1FY18.

Good assets quality of investment book

The company had an investment portfolio of around Rs.757 Mn during FY17 and the same declined by ~12% during FY18 to Rs.668 Mn, mainly due to withdrawal from Bank Deposits, however, the same again increased by 4% to Rs.695 Mn during H1FY19. UIC has complied with guidelines prescribed by the regulator and out of the total investment portfolio, UIC has total investments of 70% in fixed and interest bearing deposit at different Banks and Financial Institutions as on January 14, 2019, which are readily marketable in nature lends sufficient liquidity cushion to the company.

Healthy solvency ratio

UIC's solvency margin improved to 3.12x as on July 16, 2018 (UA) as against the 2.20x as on July 15, 2017 because of decrease in the provisions for outstanding claim (Rs. 441 Mn at the end of FY17 and Rs. 194 Mn at the end of FY18) and decrease in the provisions for unexpired risk reserve (Rs. 199 Mn at the end of FY17 and Rs. 139 Mn at the end of FY18).

About the Company

United Insurance Co. (Nepal) Limited (UIC) is a General (Non-life) insurance company. The company has started its operation from December 1, 1993. The company is promoted by leading

industrialists and reputed trading and commercial houses of Nepal. The company has been offering a range of general insurance covers for businesses & individuals and has a comprehensive range of general insurance products for Fire, Marine, Motor, Engineering, Agriculture and Aviation etc. UIC has branch network of 30 (including head office) and 137 insurance agents as on Mid-January 2019. UIC has assets base of Rs. 1,270 Mn as on July 16, 2018.

Analyst Contact

Mr. Giri Raj Kandel

giriraj.kandel@careratingsnepal.com

Tel No.: Tel No.: +977-01-4232610

Relationship Contact

Mr. Sajan Goyal

sajan.goyal@careratingsnepal.com

Tel No.: 9818832909/+977-01-4233436

DISCLAIMER

CRNL's IPO grading is a onetime assessment and the analysis draws heavily from the information provided by the issuer as well as information obtained from sources believed by CRNL to be accurate and reliable. However, CRNL does not guarantee the accuracy, adequacy or completeness of any information and is not responsible for any errors or omissions or for the results obtained from the use of such information. CRNL's IPO grading does not take cognizance of the price of the security and it is not a recommendation to buy, sell or hold shares/securities. It is also not a comment on the offer price or the listed price of the scrip. It does not imply that CRNL performs an audit function or forensic exercise to detect fraud. It is also not a forecast of the future market performance and the earnings prospects of the issuer; also it does not indicate compliance/violation of various statutory requirements. CRNL shall not be liable for any losses incurred by users from any use of the IPO grading.

Annexure 1

CARE Ratings Nepal – IPO Grading Scale

CARE IPO grade	Definition
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.