

Grading Rationale

Sun Nepal Life Insurance Company Limited

Grading

Particulars	Amount (Rs. In Million)	Grading	Grading Action
Initial Public Offer	600.00	CARE-NP IPO Grade 4 [IPO Grade Four]	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 4’ to the proposed Initial Public Offer (IPO) of Sun Nepal Life Insurance Company Limited (SNLIC). ‘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. SNLIC proposes to issue 6 Mn shares of face value of Rs. 100 each at par aggregating Rs. 600.00 Mn.

Detailed Rationale & Key Grading Drivers

The grading assigned to SNLIC is constrained by short track record of its operation, competition from other insurance companies coupled with relatively small market share in the industry. Further the grading is constrained by lower solvency ratio vis-à-vis the regulatory requirement and concentration in endowment policies. The grading, however, derives strength from strong promoter group, experienced board and management team and moderate financial risk profile with improving combined ratio. Further, grading is supported by SNLIC’s adequate geographical coverage through branches and good asset quality of investment book.

Detailed Description of the Key Grading Drivers

Key Grading Weaknesses

Short track record and competition from other insurance companies coupled with relatively small market share in the life insurance industry

SNLIC started its operation during FY18 and had its first full year of operation only during FY19. Currently, there are 19 life insurance companies operating in Nepal sharing total Rs. 77,066 Million of Gross Premium Written (GPW) as on July 16, 2019; where SNLIC shares only 1.07% of total GPW and ranks 15th Position (out of 19) 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, SNLIC is expected to face high competition to tap the new customers.

Concentration in Endowment policies

SNLIC's business is focused towards endowment segment and its variation with 100% of Net Premium Written (NPW) contribution from these policies during FY18 however decreased to 95.81% during FY19. Term policy contributed 0.06% of NPW during FY19 and Foreign Employment Term Policy contributed 4.12% during FY19.

Low solvency ratio against the regulatory requirement

Being in the initial years of operations, SNLIC has maintained 1.117x solvency ratio during FY18 which is below minimum required ratio of 1.50x. Solvency ratio for FY19 is not yet calculated due to pending actuarial report however is expected to be below minimum required ratio due to higher base of solvency margin required.

Key Grading Strengths

Strong promoter group

SNLIC has been providing its service in life insurance sector since August 2, 2017. As on July 16, 2019, 100% of shares are held by promoter group. The promoter group shares of the company are mostly owned by M/s Om Chao Biro Feed Industries Pvt. Ltd. with 10.71% of total shares followed by Mr. Roshan K.C (7.86%) and M/s Kalika Investment Pvt. Ltd. (6.43%). Institutional investor holds 36.07% of total shares and rest are held by Individuals.

Experienced board and management team

SNLIC has four experienced members on its board led by Mr. Anuj Keyal. Mr. Keyal serves as Director in Keyal group of industries, which is engaged in various industries including manufacturing of steel, feeds and cement. The day to day operations of the company is headed by Mr. Raj Kumar Aryal, CEO having overall work experience of more than 15 years with around one decade of experience in Insurance Board of Nepal. Mr. Aryal holds Master in Law (LLM) and has served as Deputy director discharging functions as Head of the legal division of Insurance Board of Nepal in the past. He is assisted by an experienced team across various functions.

Adequate geographical coverage through branches

SNLIC has presence all over the country through its 21 branches (including Head Office) as on Mid-Dec 2019 along with 56 sub-branches. The branches are spread over all 7 Provinces of Nepal.

Moderate financial risk profile and improving combined ratio

During FY18, company's gross premium written (GPW) was Rs. 297 Mn which increased to Rs. 828 Mn during FY19 (provisional). Net premium written (NPW) increased from Rs. 292 Mn during FY18 with retention ratio of 98.21% to 792 Mn in FY19 with retention ratio of 95.70%. Further, NPW increased to Rs. 241 Mn (Rs. 135 Mn during Q1FY19) during Q1FY20 over Q1FY19. SNLIC reported significant growth in Net Underwriting result (albeit low base) with Rs. 310 Mn during FY19 over Rs. 61 Mn during FY18. Further, underwriting result improved to Rs. 150 Mn (Rs. 62 Mn during Q1FY19) during Q1FY20 over Q1FY19. Despite of improvement in underwriting result, SNLIC reported decrease in net profit during FY19 to Rs. 84 from Rs. 88 Mn during FY18 due to higher transfer of surplus fund to life insurance fund. Further, SNLIC reported net profit of Rs. 35 Mn during Q1FY20 against net profit of Rs. 32 Mn during Q1FY19.

The loss ratio (claim ratio) of SNLIC was at 0.16% during FY18 which increased to 0.41% during FY19. Loss ratio was on lower side due to insignificant claims due to initial year of operations. Further, commission ratio was 23.62% during FY18 due to high commission expenses which decreased to 19.43% during FY19 although increased in absolute amount from Rs. 69 Mn in FY18 to Rs. 150 Mn during FY19. Expense Ratio was 55.16% during FY18 which decreased to 39.90% in FY19. On back of these, combined ratio was 78.94% during FY18 which improved to 59.74% during FY19. Further, combined ratio improved to 43.27% during Q1FY20 due to improvement in commissions ratio and expense ratio.

Goods assets quality of investment book

The company had an investment portfolio of around Rs. 1,570 Mn at the end of FY18 which increased to Rs. 2,072 Mn at the end of FY19 recording a growth of 32%. Further, investment portfolio increased to Rs. 2,192 Mn at the end of Q1FY20 recording a growth of ~6% over FY19. Out of the total investment portfolio, SNLIC has total investment of 93.71% in fixed and interest bearing deposit at different Bank and Financial Institutions as on July 16, 2019, which are readily marketable in nature which lends sufficient liquidity cushion to the company.

As majority of investments of SNLIC are in deposits at different BFIs, investment income of SNLIC comprises of interest income from these investments. Investment income has increased by 14.59% during FY19 to Rs. 207 Million mainly due increase in investment portfolio during FY19. Further, SNLIC

reported investment income of Rs. 49 Mn during Q1FY20 recording a growth of 7.14% over Q1FY19. Average yield on Investment of SNLIC was 11.36% in FY19.

About the Company

Sun Nepal Life Insurance Company Limited (SNLIC) is a life insurance company which obtained license from Insurance Board on August 2, 2017. SNLIC has been offering an extensive range of products as Money Back, Endowment, Whole Life, Term Assurance products etc. through its diversified sales network. SNLIC has branch network of 21 (including head office), 56 sub-branches and 15,838 insurance agents as of Mid-Dec 2019.

SNLIC had an asset base of Rs. 2344 Million as on July 16, 2019. The capital structure of the company comprises of an authorized capital of Rs. 2 Bn out of which Rs. 1.40 Bn is paid up capital from the promoter group and the remaining is proposed to be issued to the public through IPO.

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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.