

IME Life Insurance Company Limited (Revised)

Ratings

Facilities	Amount (Rs. Million)	Rating	Rating Action
Issuer Rating	NA	CARE-NP BBB (Is)	Reaffirmed

CARE Ratings Nepal Limited (CRNL) has reaffirmed rating of 'CARE-NP BBB (Is)' assigned to IME Life Insurance Company Limited (ILIC). Issuers with this rating are considered to offer moderate degree of safety regarding timely servicing of financial obligations, in Nepal. Such issuers carry moderate credit risk.

Detailed Rationale & Key Rating Drivers

The reaffirmation of rating assigned to ILIC continues to derive strength from its strong promoter group, experienced directors and management team, moderate financial risk profile during FY22 (Audited, FY refers to the twelve-month period ending mid-July) along with moderate policy continuation rate. The rating also takes cognizance of the improving trend in the company's moderate solvency ratio in FY22 with further improvement likely in FY23. Furthermore, the rating also derives strength from good asset quality of investment book and adequate reinsurance arrangement along with growing geographical coverage through adequate branch network.

The rating, however, continues to be constrained by ILIC's short track record of operations and presence in a highly competitive industry coupled with a modest market share in the life insurance industry and exposure to regulatory requirement. The rating also factors in deterioration in combined ratio (sum of loss ratio, commission ratio and expense ratio) during FY22 marked by increase in claims ratio.

Going forward, the ability of the company to continue its growth momentum while diversifying the policy segments and maintaining quality of the investment portfolio will be key rating sensitivities. Furthermore, its ability to maintain minimum capital and regulatory solvency ratio at all times will also be key rating sensitivities.

Detailed description of the key rating drivers

Key Rating Strengths

Association with strong promoter group experienced board and management team

ILIC is promoted by IME Group with total holdings of 50.89% as on mid-April 2023. IME Group is an established group in Nepal with cross-sector presence in banking, remittance, hydropower, hospitality among others. The promoter group shares of the company are mostly held by Mr. Chandra Prasad Dhakal with 16.16% of total shares followed by Mr. Hem Raj Dhakal (16.16%) who are associated with IME Group. Other major shareholders include Global IME Bank Limited (14.29%).

ILIC has five experienced members on its board led by Dr. Ram Hari Aryal, Dr. Aryal has overall experience of over 3 decades and also associated with Government of Nepal for over 2 decades in various capacities. The overall operation of the company is managed by Mr. Kabi Phuyal and associated with company in the capacity of Chief Executive Officer (CEO). He has overall experience of ~12 years. He is assisted by an experienced team across various functions.

Moderate financial risk profile supported by growing scale

During FY22, the company's gross premium written (GPW) increased by 27% year-on-year (industry growth: 15%) to Rs. 3,581 Mn. The growth in GPW is attributable to increase in marketing efforts and customer reach with increase in network through insurance agents coupled with increasing insurance awareness in the country. Accordingly, Net premium written (NPW) increased to Rs. 3,423 Mn during FY22 from Rs. 2,735 Mn during FY21 with retention ratio steady at 97% and 96% during FY21 and FY22, respectively. The first-year premium of ILIC decreased by 5% (industry growth: 2% decline amid economic slowdown) to Rs. 1,429 Mn during FY22 (FY21: Rs. 1,511 Mn). However, the renewal premium grew by 67% y-o-y to Rs. 1,991 Mn during FY22 attributable to concentrated endowment product policies (96% of NPW contribution towards endowment

policies) and policy continuity rate of 90% as on mid-July 2022. A healthy level of policy continuity rate indicates higher renewal premiums and longer tenure of policy in force, which would enable the company to recover costs and make profits over the life of the insurance contract.

Despite the increase in scale of operations, however, ILIC reported decline in net underwriting result of Rs. 1,150 Mn during FY22 (FY21: Rs. 1,182 Mn) on account of significant increase in claims related to money back policies. However, with improved income from investments, which increased to Rs. 495 Mn during FY22 from Rs. 363 Mn during FY21, ILIC reported increase in Profit Before tax (PBT) to Rs. 135 Mn during FY22 from Rs. 110 Mn during FY21. The company reported PAT of Rs. 325 Mn during FY22 (FY21: Rs. 296 Mn), mainly on account of deferred tax income of Rs. 190 Mn during FY22.

During 9MFY23, GPW grew by 22% y-o-y to Rs. 2,986 Mn (industry growth of 2%). Net underwriting result also improved to Rs. 1,162 Mn during 9MFY23 (9MFY22: Rs. 969 Mn) coupled with the increase in income from investments. Consequently, PBT increased to Rs. 182 Mn during 9MFY23 (9MFY22: Rs. 102 Mn).

Adequate geographical coverage through branches and sub-branches

ILIC has wide geographical coverage through its 76 branches as on mid-April, 2023 along with 64 sub-branches. The branches are spread over all 7 Provinces of Nepal covering 71 districts out of 77 districts of Nepal. Also, it has 32,458 insurance agents as of mid-April, 2023 all over Nepal. Adequate no. of branches provides advantage to business growth in terms of marketing, branding and reaching close to customers.

Adequate reserve and reinsurance arrangement

ILIC has entered into reinsurance treaties with Nepal Reinsurance Company Limited (NRIC) where it cedes claim amount of more than NPR. 0.4 Mn per life for the conventional policy and NPR. 0.4 Mn for rider benefits. In case of term policies, 30% of the claim amount is ceded with NRIC. The company only have minor portion concentrated towards term policies till date. ILIC has entered into agreement with Barents Re Reinsurance Company for catastrophic reinsurance where it cedes claim amount of more than Rs. 20 Mn.

Policyholder liabilities of life insurers are impacted by their high sensitivity (due to long tenure) to changes in the mortality rates, medical inflation rates and interest rate movements. Thus, maintaining adequate reserves is critical to meet the liability related to future claims, any unforeseen claim payouts and support the policyholder return, resulting into moderate shareholder's return post-transfer. During FY22, ILIC has transferred Rs. 1,547 Mn to life insurance fund thus life insurance fund increased to Rs. 4,480 Mn at the end of FY22. Also, as per Insurance Board, insurer shall allocate minimum 10% of PAT towards catastrophe reserve. As on FY22, catastrophe reserve of ILIC stood at Rs. 104 Mn (FY21: Rs. 73 Mn).

Improving trend in solvency ratio in FY22

ILIC's solvency ratio including cost of bonus stood moderate at 1.74x during FY22 (2.33x excluding cost of bonus) as compared to 1.53x during FY21 (1.91x excluding cost of bonus) against the minimum requirement of 1.50x. The solvency ratio improved during FY22 on account of increased asset base of the company with the improved business operations. The increased asset base is mainly attributable to increase in the investments of the company, returns of the investments and ploughing back those returns. The ratio is calculated as per the regulatory directive considering regulatory capital requirement of Rs. 2 Bn.

ILIC issued 100% right amounting to Rs. 1.4 Bn during 9MFY23, which has significantly increased asset base of the company. With the increased capital base on collection of right proceeds coupled with proposed IPO issue and accretion of profits, it is expected that ILIC's assets base will increase along with increase in business volume, which is likely to improve solvency ratio of the company. The solvency reflects the availability of capital relative to the quantum of risk underwritten to absorb any unforeseen losses and capacity to underwrite new business. Hence, an increasing trend in solvency risk bodes well from credit perspective.

Good assets quality of investment book

The company had an investment portfolio (inclusive of interest earning deposit in commercial bank, development bank and finance company) of around Rs. 4,452 Mn at the end of FY21 which increased to Rs. 6,168 Mn at the end of FY22 recording a growth of 39%. Further, investment portfolio increased to Rs. 9,198 Mn at the end of 9MFY23 recording a growth of 49% over FY22, backed by the improvement in business operations coupled with 100% right proceeds amounting to Rs. 1.4 Bn during FY23. Out of the total investment portfolio, ILIC has total investment of 77% and 78% in fixed deposit at different Bank and Financial Institutions as on July 16, 2022 and April 13, 2023 respectively which lends sufficient liquidity cushion to the company. During FY22, company had moderate liquidity position with Liquid Assets to Technical Reserve standing at 1.31x (FY21: 1.46x). As majority of investments of ILIC are in deposits at different BFIs, investment income of ILIC comprises of interest income from these investments. Investment income has increased by 36% during FY22 to Rs. 495 Mn (FY21: Rs. 363 Mn) mainly due to increase in investment portfolio during FY22. Further, ILIC reported investment income of Rs. 573 Mn during 9MFY23 recording a growth of 57% over 9MFY22. Average yield on Investment of ILIC was 9.89% in FY22 (FY21: 10.18%)

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

ILIC started its operation during FY18 and had its first full year of operation only during FY20. As on Mid-April, 2023 there were 17 life insurance companies operating in Nepal sharing total Rs. 100,799 Mn of Gross Premium Written (GPW); where ILIC shares only 2.96% of total NPW and ranked 11th Position (out of 19) reflecting modest market share in the industry in comparison to the established life insurance players. However, ILIC stood in 3rd position (out of 10 new companies licensed and started operation after FY17). Further, due to a relatively high number of life insurance companies present in Nepal, ILIC is expected to face high competition to tap new customers leading to a challenging market dynamic to increase material market share. Also, large scale increases the insurer's capacity to absorb any abrupt high-claim pay-outs caused by any external shocks, compared to relatively smaller peers.

Deterioration in combined ratio marked by increase in claims ratio

The loss ratio (claims ratio) of ILIC increased to 30.37% during FY22 from 16.77 % during FY21. Loss ratio was on higher side on account of increase in partial maturity claims on anticipated endowment policies (money back policies). However, commission ratio decreased to 16.23% in FY22 from 18.46% in FY21 and Expense Ratio decreased to 19.51% in FY22 from 22.72 % in FY21 (against the regulatory requirement of 30%) mainly on account of economies of scale and rationalization of management expenses. Combined ratio thus deteriorated to 66.11% in FY22 from 57.95% during FY21 on account of significant increase in loss ratio although offset somehow by decrease in commission and expense ratio. However, combined ratio improved to 57.32% during 9MFY23 mainly due to improvement in commission ratio and expense ratio. The management expects that with the company's decision to discontinue the annual money back policies, loss ratio is expected to decrease going forward.

Exposure to Regulatory Risk

The insurance industry is regulated by Insurance Board. Being a highly regulated industry, the government's rules for the insurance industry play a key role in the company's performance besides the demand and supply trend. Furthermore, the industry dynamics like the demand for products, per capita income levels, competitive pressure, interest rate dynamics, and investment opportunities in the industry determine the business and financial profile of insurers in the industry. Overall insurance penetration (percentage of population covered by insurance excluding term, micro term and Foreign Employment Term Policies (FET)) was 17.43% as on mid-April, 2023, thus reflecting low insurance reach in Nepal and high growth potential in upcoming years. Also, The Insurance Board has mandated all life insurance companies to maintain minimum paid-up capital

of Rs. 5 Bn by mid- July 2023. The paid-up capital of the company stood at Rs. 2.8 Bn as on Mid-April, 2023. ILIC is likely to meet this requirement through public issuances. Timely collection of Initial Public Offer (IPO) proceeds will be key monitorable aspect.

About the Company

IME Life Insurance Company Limited (ILIC) is a life insurance company registered at Office of Company Registrar under the Company Act 2006 on October 1, 2008 and has obtained license from Insurance Board on July 4, 2017. ILIC had an asset base of Rs. 7,079 Mn as on July 16, 2022. The paid-up capital of the company stood at Rs. 2,800 Mn as on Mid-April, 2023.

Brief financial performance of IME Life Insurance Company Limited (ILIC) during last 3 years is given below:

Particulars	(Rs. In Million)		
	FY20 (A)	FY21 (A)	FY22(A)
Total Gross Premium	1,414	2,822	3,581
Net Premium Earned	1,358	2,811	3,392
Income from Investment	268	363	495
Profit before Tax (PBT)	106	110	135
Profit after Tax (PAT)	199	296	325
Investments	2,922	4,452	6,168
Return on Total Assets (%)	6.49	6.75	5.29
Solvency ratio (times)*	1.32	1.53	1.74

A: Audited

*Solvency ratio including cost of bonus

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