

Reliable Nepal Life Insurance Limited

Ratings

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

CARE Ratings Nepal Limited (CRNL) has revised the issuer rating assigned to Reliable Nepal Life Insurance Limited (RNL) to 'CARE-NP BBB+ (Is)' from 'CARE-NP BBB (Is)'. 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 revision in issuer rating of RNL takes into account the improving financial performance of the company in FY22 (Audited, FY refers to the twelve-month period ending mid-July) marked by sustained growth in scale of operations, at a faster pace than the industry, coupled with improvement in net profit post transfer to policyholder's fund owing to increase in both underwriting performance as well as investment income. RNL's profitability continues to be better than most peers with similar capital base and track record resulting in higher distributable profits. Growth in Gross Premium Written (GPW) of RNL has continually outpaced that of the industry over FY20-FY22. The rating also factors in improving solvency profile of the company at the end of FY22, with comfortable cushion from regulatory requirement levels. The rating also takes cognizance of the improved capitalization of the company post successful completion of 100% right issue during 9MFY23 (Unaudited, refers to the nine-month period ending mid-April), which has since led to significant increase in the investments base of the company. The timing of the right issue has been prudent as most of the proceeds from right issue are locked in Fixed Deposits (FD) of longer tenure at relatively higher interest rates amid stressed liquidity in the banking sector, which is likely to benefit RNL's investment yield going forward. The rating also notes the company's plans to meet the minimum paid-up capital requirement as mandated by Insurance Board through Initial Public Offering (IPO) issuances, which is likely to further improve the financial and solvency profile of the company in FY24. Furthermore, the rating continues to derive strength from RNL's experienced board and management team, good asset quality of investment book, adequate reinsurance arrangement along with growing geographical coverage through adequate branch network.

The rating, however, continues to be constrained by RNL's relatively short track record of operations and presence in a highly competitive industry coupled with a modest market share in the life insurance industry. 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 and exposure to regulatory risk. Furthermore, the rating also takes cognizance of slight moderation in GPW of the company in 9MFY23 amid economic slowdown in the country. Although income from insurance business in FY23 could remain stagnant on a year-on-year basis, the company's return indicators are likely to continue to improve supported by favorable product mix, increasing contribution from investments, and rationalization of expenses.

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. The company's ability to complete the proposed IPO within the envisaged timelines will remain a key monitorable aspect.

Detailed description of the key rating drivers

Key Rating Strengths

Experienced board and management team

RNL has seven members on its board chaired by Mr. Udaya Nepali Shrestha. Mr. Shrestha has more than 15 years of experience in different sectors including financial services. Mr. Indra Prasad Sharma, Director, has 13 years of experience in various sectors. The company's management team comprises of seasoned professionals having diversified experience including finance,

banking, and insurance. The day-to-day operations of the company is headed by Chief Executive Officer (CEO) Mr. Narayan Babu Lohani, who has more than 12 years of experience in finance sector and is supported by other experienced management team members.

Adequate geographical coverage through branches

RNL has wide geographical coverage through its 9 branches (including Head Office) and 69 sub-branches as on Mid-April, 2023. The branches are spread over all 7 Provinces of Nepal. Also, it has 28,655 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.

Improving financial risk profile supported by growing scale

There has been sustained growth in RNL's scale of operations over the past few fiscals. During FY22, the company's gross premium written (GPW) increased by 32% year-on-year (industry growth: 15%) to Rs. 4,044 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. 3,829 Mn during FY22 from Rs. 2,888 Mn during FY21 with retention ratio steady at 94% during FY21 and FY22. The first-year premium of RNL increased by 10% (industry growth: 2% decline amid economic slowdown) to Rs. 2,422 Mn during FY22 (FY21: Rs. 2,212 Mn). Also, the renewal premium almost doubled to Rs. 1,541 Mn during FY22 (FY21: Rs. 775 Mn) attributable to increasing concentration towards endowment product policies (74% of NPW contribution towards endowment policies in FY22 as compared to 66% during the previous fiscal year) and policy continuity rate of 88% 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. RNL's net profit post transfer to policyholder fund increased by 39% y-o-y to Rs. 342 Mn during FY22 supported by improvement in net underwriting result to Rs. 1,410 Mn during FY22 (FY21: Rs. 1,071 Mn) coupled with income from investments to Rs. 591 Mn during FY22 (FY21: Rs. 455 Mn).

RNL has transferred surplus of Rs. 299 Mn from policyholder's fund to shareholders fund (Rs. 33.7 Mn transferred in FY21). In the past, RNL transferred certain funds from shareholders' fund to policyholders' fund in order to maintain the insurance contract liabilities. However, the scenario is different in FY21 and FY22. This led to increase in the distributable profit of the company.

During 9MFY23, the GPW decreased to Rs. 2,741 Mn (9MFY22: Rs. 2,990 Mn) mainly on account of company's decision not to continue higher claims and not profitable micro term policies segment. However, RNL net profit increased to Rs. 285 Mn during 9MFY23 (9MFY22: Rs. 210 Mn) mainly due to increase in investment income by 62% y-o-y to Rs. 654 Mn during 9MFY23 (9MFY22: Rs. 403 Mn).

Adequate reserve and reinsurance arrangement

RNL has entered into reinsurance treaties with Nepal Reinsurance Company Limited and Himalayan Reinsurance Limited where it cedes 20% of claim amount (10% of claim amount is ceded to each reinsurer) due to compulsory re-insurance mandated by GoN. Also, RNL has entered into an agreement with Hannover Reuck SE on the surplus basis with the retention limit of Rs. 0.5 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, RNL has transferred Rs. 1,644 Mn to life insurance fund thus life insurance fund increased to Rs. 4,638 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 RNL stood at Rs. 88 Mn (FY21: Rs. 57 Mn).

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. 7,229 Mn at the end of FY22 which increased from Rs. 5,251 Mn at the end of FY21 recording a growth of 38%. Further, investment portfolio increased to Rs. 10,266 Mn at the end of 9MFY23 recording a growth of 42% 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, RNL has total investment of 75% and 80% 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 1.33x (FY21: 1.48x).

As majority of investments of RNL are in deposits at different BFIs, investment income of RNL comprises of interest income from these investments. Investment income has increased by 30% during FY22 to Rs. 591 Mn (FY21: Rs. 455 Mn) mainly due to increase in investment portfolio during FY22. Further, RNL reported investment income of Rs. 654 Mn during 9MFY23 recording a growth of 62% over 9MFY22. Average yield on Investment of RNL was 9.65% in FY22 (FY21: 10.38%)

Improving solvency profile

RNL's solvency ratio including cost of bonus improved and stood at 2.16x during FY22 (2.68x excluding cost of bonus) as compared to 1.85x during FY21 (2.20x 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.

RNL 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 RNL'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.

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

RNL started its operation during FY18 and had its first full year of operation only during FY19. 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 RNL shares only 2.72% of total NPW and ranked 13th Position (out of 19) reflecting modest market share in the industry in comparison to the established life insurance players. RNL stood in 6th 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, RNL 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 (claim ratio) of RNL increased to 24.49% during FY22 from 18.49 % during FY21. Loss ratio was on higher side mainly on account of increase in partial maturity claims on anticipated endowment policies coupled with death claims related to term policies. The uptick in death claims were majorly related to micro-term policies. Further, commission ratio decreased to

16.01% in FY22 from 16.91% in FY21 and Expense Ratio decreased to 20.57% in FY22 from 22.36 % 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 61.06% in FY22 from 57.76% 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 56.13% during 9MFY23 mainly due to improvement in commission ratio and expense ratio. With the company's decision not to continue micro term policies with low premiums and high claims experience, the increase in loss ratio due to uptick in death claims is expected to moderate somehow.

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. RNL 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

Reliable Nepal Life Insurance Limited (RNL) is a life insurance company registered at Office of Company Registrar under the Company Act 2006 on December 04, 2007 and has obtained license from Insurance Board on August 02, 2017. RNL has network of 9 branches (including head office), 69 sub branches and 28,655 insurance agents as of Mid-April, 2023. RNL had an asset base of Rs. 11,856 Mn as of Mid-April 2023. The paid-up capital of the company stood at Rs. 2,800 Mn as on Mid-April, 2023.

Brief financial performance of Reliable Nepal Life Insurance Limited (RNL) during last 3 years is given below:

(Rs. In Million)

Particulars	FY20 (A)	FY21 (A)	FY22 (A)
Total Gross Premium	1,622	3,072	4,044
Net Premium Earned	1,439	2,535	3,622
Income from Investment	330	455	591
Profit before Tax (PBT)	235	245	340
Profit after Tax (PAT)	236	247	342
Investments	3,622	5,251	7,229
Return on Total Assets (%)	6.76	4.89	4.75
Solvency ratio (times)*	1.65	1.85	2.16

A: Audited

*Solvency ratio including cost of bonus

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About CARE Ratings:

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