NB Insurance Company Limited

ICRA Nepal assigns [ICRANP] IPO Grade 4 to the proposed Equity Shares (Rights Issue) of NB Insurance Company Limited

Instrument/Facility	Issue Size	Rating Action (February 2017)
Rights shares issue	NPR 270 million	[ICRANP] IPO Grade 4 (Assigned)

ICRA Nepal has assigned **"[ICRANP] IPO Grade 4"**, indicating below average fundamentals to the proposed rights issue (equity shares) amounting to NPR 270 million of NB Insurance Company Limited (NBIL). ICRA Nepal assigns IPO grading on a scale of IPO Grade 1 through IPO Grade 5, with grade 1 indicating strong fundamentals and Grade 5 indicating poor fundamentals. For the grading categories 2, 3 and 4, the sign of + (plus) appended to the grading symbols indicate their relative positioning within the grading categories concerned. Thus, the grading of 2+, 3+ and 4+ are one notch higher than 2, 3, and 4 respectively. NBIL is proposing to come out with 1:1 rights issue of 2,700,000 numbers of equity shares of face value NPR 100 each, to be offered to for the existing shareholders at par. The proposed issue is being made to augment the capital base to support future growth plans.

The grading takes into account the improvement in the performance of NBIL after resumption of business in June 2015, under new set of owners and management team. NBIL has suffered from significant erosion in market share/reputation following the charges of financial misappropriation levelled against the erstwhile promoters which led to suspension of NBIL's business operations (between December 2013 and June 2015). ICRA Nepal also notes the change in shareholding pattern of the company following the rights issue in 2016; establishing new promoter group[1] (mainly associated with IME group) as the major shareholders in the company.

The grading also remains constrained by the low possibility of equity holders receiving dividend payments in the medium term (2-3 years) due to the weak financial profile (sizeable accumulated losses of ~NPR 153 million as on mid-October 2016) and weak solvency indicators (mainly due to erosion in net worth over the years) of the company. Although the proposed equity injection will strengthen the capital base to some extent, the company is likely to require further capital injection and/or internal accruals to improve its capitalisation levels. These concerns stand partially mitigated by the strength of the new promoter group, the company's experienced Board of Directors and its senior management team. The grading also factors in the existence of low insurance penetration in Nepal, providing enough space for future growth.

Before the business operations were suspended by the Insurance Board in December 2013, NBIL was a small player with 2% share[2] in industry gross premium written (GPW). Following the resumption of business in June 2015, NBIL regained its share in industry GPW in FY 2015-16; although aided by sizeable aviation portfolio. The premium earnings of NBIL during FY2015-16 (both gross and net) is the highest reported by it during past 5 years.

In terms of portfolio mix, motor segment (89% of net premium earned (NPE) over past 12-18 months) towers over all other segments like engineering (4%), miscellaneous (3%) and fire (2%). Business growth during past 12-18 months remains driven by motor segment, especially the private vehicles. Incrementally, over the short run, the management expects the business to remain driven by motor and fire segments. To that end, NBIL is likely to leverage the market reputation and business network of promoter groups as well as establish bank assurance relation with the players in banking industry. The resumption of almost all the branches closed during the period of turmoil is also likely to support the growth in business, going forward.

Despite reporting profits during FY 2014-15 and FY 2015-16, NBIL is yet to recover the losses accumulated in the past, over the years of dismal performance. The losses remain sizeable vis-à-vis NBIL's current scale of business; despite moderation in recent period (~NPR 153 million in mid-Oct-16 vs NPR 186 million in mid-Jul-15 and NPR 204 million in mid-Jul-14). During FY16, NBIL has reported NPR 28 million in underwriting surplus (combined ratio of 49%) during FY16, its best in the last 5 years, with net profits of NPR 30 million. Incrementally, over next 1-2 years, NBIL plans to adopt a cautious growth

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[1] New promoter group consist of private institutions and individuals associated with IME group. The group bought NBIL's shares auctioned by NB Bank and NCC bank (erstwhile institutional promoters of NBIL). As on mid-Oct 2016, promoters associated with IME group (43% stake), Lomus Pharmaceutical group (5%) and Laxmi Group (7%) together own majority stake in NBIL.

[2] During FY 2012-13.

strategy by focussing on the retail segment. However, limited franchise network remains a constraint in achieving the same. The company's ability to achieve targeted business growth, limit loss ratio and attain scale is likely to improve NBIL's internal accruals and recover the losses.

Supported by capital infusion and internal accruals (albeit modest), NBIL's investment portfolio has grown to NPR 248 million in mid-Oct-16; 47% of which is in the form of equity investments in Nepal Reinsurance Company (with no established dividend track record). Proceeds from proposed rights issue is likely to further boost the investible funds of NBIL. At the same time, improving interest rate environment in the banking sector bodes well for the incremental yield of NBIL; although the sustainability of the same remains to be seen.

NBIL has been maintaining mandatory technical reserves and restricted reserves[3] as prescribed by the regulatory authority (Insurance Board of Nepal). As on mid-Oct-16 these reserves accounted for 94% of net worth of NBIL. NBIL's solvency margin as on mid-Oct-16 stood at ~0.80 times, less than the required minimum of 1 time, mainly due to erosion in net worth over the years. Nonetheless, the same has improved post rights issue in 2016 and is likely to improve further after the proposed rights issue.

Company Profile

Operating since January 2001, NBIL is among the younger players in the non-life insurance industry of Nepal (11th among the 17 non-life insurers[4]). The company has been providing the Non-Life Insurance Service in Fire, Motor, Marine, Aviation, Engineering and Miscellaneous segments. The company's registered office is located in Naxal, Kathmandu and as on mid-Oct-16, it has 19 branches spread across the country for procuring business and providing aftersales services.

NBIL's business was suspended by the Insurance Board between December-13 and June-15, following the revelation of financial irregularities by major promoter group- NB group. The suspension of business resulted in closure of many branch offices, large scale turnover of staffs and loss of market share. Before the malpractices were uncovered leading to business suspension and consequent downfall in business, NBIL accounted for ~2% market share in gross premium among the Nepalese general insurers (FY13). Under the new set of ownership and management, NBIL is looking for revival of business going forward.

NBIL has 80:20 promoter-public shareholding ratios with major shareholding from promoters related to IME group (~43%), Laxmi Group (~7%), Lomus pharmaceutical group (~5%) in addition to institutional promoter holding by Nepal Bangladesh (NB) Bank ~10%. The shareholding of erstwhile NB group shareholders diluted after 80% rights issue in 2016 and currently stands at ~15%. During FY16, NBIL reported a profit after tax of NPR 30 million over assets base of NPR 703 million as on mid-July 2016 vis-à-vis profit after tax of NPR 38 million (mainly backed by one-off dividend income from Nepal Reinsurance Company) over assets base of NPR 429 million on mid-Jul-15. In terms of technology platform, NBIL has implemented "Insure" in its corporate office. The computerized information has been centralized across all the branches.

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[3] Technical reserve includes (reserve towards unpaid claims & unexpired risk); restricted reserves include Insurance reserve and Insurance fund maintained as per regulatory requirement.
[4] Including a government owned company, a foreign joint venture and two branches of Indian general insurer.