

National Life Insurance Company Limited

ICRA Nepal assigns [ICRANP] IPO Grade 3 to the proposed rights issue (equity shares) of National Life Insurance Company Limited

INSTRUMENT/FACILITY	ISSUE SIZE	RATING ACTION (NOVEMBER 2017)
Rights Issue (Equity)	NPR 993.647754 million	[ICRANP] IPO Grade 3 (Assigned)

ICRA Nepal has assigned “[ICRANP] IPO Grade 3” indicating **average fundamentals** to the proposed rights issue amounting ~NPR 994 million of National Life Insurance Company Limited (NLICL). ICRA Nepal assigns IPO¹ 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.

NLICL has proposed 60% rights issue of 9,936,477.54 number of equity shares each with face value of NPR 100/-, to be issued to the existing shareholders at par. The proposed issue is being made to comply with the revised capital requirement for life insurers² rolled out by the Insurance Board of Nepal (the regulator).

The grading factors in NLICL’s long track record (operating since 1988), fair market positioning as reflected in ~13% industry share in gross premium written (GPW) in FY2017 and adequate franchise network of the company (99 branches across the country). The grading also factors in NLICL’s steady business growth (CAGR 23% growth in gross premium during FY2014-FY2017), backed by strong growth in first year premium (CAGR 44% over the same period), indicating good competitive positioning. NLICL has strong presence in profitable endowment segment and has sizeable life fund of over NPR 17 billion (as on mid-July 2017). Improvement in fresh premium earnings augurs well for the growth of life fund which has a bearing on incremental prospects of policy holders as well as shareholders of the company. The grading also factors in adequate reinsurance arrangements including catastrophic coverage provision, experienced senior management and established underwriting norms. ICRA Nepal also takes note of the negligible impact of the April 2015 earthquake on NLICL’s solvency and claims paying ability.

However, assigned grading remains constrained by relatively smaller asset size and fund base for its age. Single premium products of NLICL has fared moderately over the years (CAGR growth of 5% during FY2014-FY2017), offsetting the benefits of high growth in instalment based first year premium. This is a drag to incremental shareholders return, which is based on the size and performance of life fund.

NLICL (erstwhile National Life and General Insurance Company (NLGIC) operating in both life and general insurance domain) came into existence as a standalone life insurance company in FY2005, after the non-life business of erstwhile NLGIC’s was spinned-off into separate company. Life insurance business of NLICL has picked up mainly after the separation (in past ~12 years), which partly contributes to relatively smaller asset base, despite the age of the company. The grading is also constrained by high reliance on individual agent for business and lack of fully functional bancassurance channels, which remains a challenge for incremental growth. The grading is also limited by challenging operating environment for life insurers after the recent licensing (in early FY2017) of 10 new life insurance companies (LICs) by the regulator. However, the impact of increased competition is likely to remain lower for old and established players like NLICL as compared to new generation players.

NLICL’s gross premium written (GPW) grew at CAGR 18% during past 5 years (FY2012-FY2017) vs. industry average of 25%. However, the premium growth in recent period has picked up (CAGR growth of 23% during past 3 years), backed by strong growth in instalment based first year premium despite moderate single premium performance contributing in marginal improvement of NLICL’s market share to

¹ Includes rights and further public issue of equity shares

² Minimum paid up capital of NPR 2 billion to be maintained by July 2018 by all life insurers

~13% of industry GPW in FY2017 (~12% in FY2016). During past 3-4 years, term product and single premium endowment product have registered good growth across the industry. NLICL's growth has lagged behind the industry growth due to weak single premium performance. In terms of distribution channel, NLICL relies heavily on individual agents while business sourced from bancassurance remains negligible at present, in line with the current industry scenario.

NLICL's premium mix is dominated by endowment policies (and its variants) which accounted for ~88% of GPW in FY2017 (past 5 years average of 85%). Term segment remains relatively stunted in comparison and comprises mainly of mandatory foreign employment policies. Proportion of new business premium (first year premium *plus* single premium) remains fair vis-à-vis peers (39% in FY2017, past 5 years' average of 36%), supported by recent increase in the proportion of first year premium. Nonetheless, gross premium earnings remained supported by strong renewal premium (~89% in FY2017, past 3 years average of 84%). Although new business premium growth is likely to witness some moderation over next 1-2 years, long term impact is unlikely to be severe for established players like NLICL.

Gross benefit paid has grown by CAGR 23% during past 3 years ending FY2017, at par with the growth in premium earnings over the same period. Being the oldest player in the industry, proportion of maturity payments remains the highest (66% of benefits payment, past 3 years average of 58%), followed by death claims (16% in FY2017, past 3 years average of 22%) and surrender payment (9% in FY2017, past 3 years average of 11%) among others. Considering the entry of new players in the industry, the proportion of policy surrenders could increase over medium term for NLICL. Benefit payment ratio (net claims paid/net premium) of NLICL remains slightly higher (33% in FY2017), commensurate with the age of the company. At the same time, NLICL's claims paying ability remains healthy (amount available for claims/ claims paid ratio of ~3 times in FY2017, on relatively large scale of operation).

Net investment income of NLICL for FY2017 stood at NPR 1,285 million corresponding to average yield on investment of ~7.50% (~6.50% in FY2016). The investment portfolio remains compliant with the regulatory guidelines, with ~91% of portfolio, as on mid-July-17 comprised of investments in Government securities, fixed deposits receipt (FDR) with Commercial banks and Development Banks) compared to ~90% in mid-July-16. During past 6-12 months, banking interest rates have begun to harden, following low interest rate regime during FY14-FY16. Given the investment portfolio mix, hardening of interest rates augurs well for the incremental earning profile of the company.

Due to relatively low proportion of term business, NLICL's profitability depends largely on transfer of surplus after actuarial evaluation of the adequacy of life fund. During FY 2016-17, NLICL reported Net Profit of NPR 212 million (before transfer of actuarial surplus from life fund) on a Net Premium of NPR 4,745 million as compared to Net profit of NPR 350 million on a net premium of NPR 3,601 million for FY2016 (corresponding to return on net worth of ~19%). Strong endowment product driven business, growing life fund, relatively lower operating expense ratio and positive investment outlook is likely to support incremental profitability.

On the solvency front, NLICL remains comfortable with solvency ratio of 3.10 times on mid-July 2016³ vis-a-vis a regulatory minimum requirement of 1.5 times. Incremental capital injection plan of the company is likely to further strengthen its solvency position. Similarly, life fund/total investment ratio remains comfortable at ~92% during past 2 years. NLICL has reinsurance agreement (including catastrophic reinsurance agreement) with Hannover Re, Singapore⁴ since inception.

Company Profile

National Life Insurance Company Limited (NLICL), (formerly known as National Life & General Insurance Co. Ltd.), is the first private sector insurance player in Nepal, operating since 1988. The company operated in both life and general insurance segment till 2005; when general insurance business was

³ Solvency ratio for July 2017 is yet to be determined pending actuarial evaluation

⁴ Rated AA- (stable) by Standard & Poor's for financial strength rating.

spinned-off as a separate company, as per regulatory requirement. NLICL's head office is located at Lazimpat in Kathmandu.

NLICL is among the top 3 players in the life insurance industry of Nepal (market share of ~12% in terms of premium earnings during past 3 years ending FY2016). As of mid-July 2017, it is in operation with 99 branches and more than 7,200 active agents spread across the nation for procuring new business and extending after sales services.

NLICL has 65:35 promoter-public shareholdings as on mid-July-2017. Major promoters of the company include Mr. Siddheshwor Kumar Singh (~12% stake), Rastriya Banijya Bank Limited⁵ (~10%), Nepal Investment Bank Limited⁶ (~6%) and Mr. Rana Bahadur Shah (~5%), among others. NLICL reported a profit after tax of NPR 212 million (before transfer from Life Insurance (LI) Fund) during FY 2016-17 over total assets base of NPR 20,555 million on mid-Jul-2016 as compared to profit after tax of NPR 350 million during FY 2015-16 over total assets base of NPR 17,035 million as of mid-Jul-2016. In terms of technology platform, NLICL has implemented "Siddhi Life" in its corporate office and all its branches.

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⁵ Wholly government owned class A commercial Bank.

⁶ Class A commercial Bank, rated A by ICRA Nepal for issuer rating.