

Prabhu Mahalaxmi Life Insurance Limited: Rating reaffirmed, removed from Watch with Developing Implications

March 4, 2024

Summary of rating action

Facility/Instrument	Rated Amount	Rating Action
Issuer Rating	NA	[ICRANP-IR] BB+; reaffirmed, removed from Watch with Developing Implications

Rating action

ICRA Nepal has reaffirmed the issuer rating assigned to Prabhu Mahalaxmi Life Insurance Limited (PML) (erstwhile Prabhu Life Insurance Limited) at [ICRANP-IR] BB+ (pronounced ICRA NP Issuer Rating double B plus). Issuers with this rating are considered to have moderate risk of default regarding timely servicing of financial obligations. The rating is only an opinion on the general creditworthiness of the rated entity and not specific to any particular debt instrument. The sign of + (plus) or – (minus) appended to the rating symbols indicate their relative position within the rating categories concerned.

The rating has been removed from watch with developing implications (denoted by &).

Rationale

The rating action positively factors in the successful conclusion of the recent merger which has increased the scale of operations as well as increased the paid-up capital closer to the regulatory minimum requirement. The rating also takes into consideration, PML's good ownership profile, adequate quality of investment vis-à-vis policyholder liability, good investment returns and the company's adequate reinsurance arrangements, including catastrophic provisions. Going forward, PML's strong franchise network (137 network points across the country as of mid-October 2023), its adequate solvency profile coupled with experienced management team augur well for future business growth. Low penetration of the insurance sector in Nepal also offers growth potential to the new players like PML.

However, the rating remains constrained by PML's limited track record (operating since December 2017). As such, the management's ability to sustain its financial and operational numbers over a longer timeframe remains untested. Given the highly fragmented industry and resulting competition, the company's ability to scale up and gain market share remains to be seen and the company's profitability is likely to remain modest in the interim. ICRA Nepal also notes the uptick in the surrender claims of the company in the recent years leading to moderate policy renewals rate of ~60%¹ in terms of premium earnings in FY2023. The ability of the company to improve policy renewal rate and implement adequate underwriting controls to control the policy discontinuation rate going forward, will remain a key monitorable. In addition to the policy continuation, the company's ability to generate adequate fresh business amid high industry competition and moderate to weak economic outlook over the near to medium term will also remain a key monitorable as it will have a bearing on the long-term profitability and liquidity.

ICRA Nepal take note of the recent reduction in future bonus provisioning requirement by the regulator. With effect from FY2023, LICs are required to maintain complete provision against the vested bonuses and 50% provision against future bonuses as against 100% provision requirement for future bonuses in the past². PML has maintained provision for all vested bonuses and ~46% provision for future bonuses till mid-July 2022³ which is largely adequate vis a vis regulatory

¹ This year's renewal premiums, RP / (last year's FYP + RP)

² Valuation directive 2020; Annexure IV- Guidelines on Actuarial Valuation 5 and 10 (e), released in August 2020

³ The date of latest actuarial valuation report

requirement. Compliance with the future bonus provisioning norms as well as revised paid-up capital norms (expected to be met through equity-raising programme) will also remain among the key monitorable.

Key rating drivers

Strengths

Increased institutional ownership post-merger – The recent merger has increased the institutional ownership in the merged entity (PML). Post merger, PML has ~30% from banks and financial institutions (including ~7% held by Nepal Investment Mega Bank Ltd. ([ICRANP-IR] A@), ~5% by Prabhu Bank Limited ([ICRANP-IR] BBB-@), ~7% by Jyoti Bikash Bank Ltd. ([ICRANP-IR] BB@ and ~4.5% by Shangrila Development Bank Limited ([ICRANP-IR] BB@) among others). Increased institutional ownership remains a positive from governance standpoint.

Post merger growth in scale and capital - Erstwhile Prabhu Life Insurance Limited (PLI) merged with erstwhile Mahalaxmi Life Insurance Limited (MLIL) and started merged operations under the name of Prabhu Mahalaxmi Life Insurance Limited in mid-July 2023. With the acquisition, the share capital of the company has now increased to NPR 4,296 million as against the regulatory minimum of NPR 5 billion. The company plans fresh equity infusion in order to comply with the regulatory minimum capital requirement. Nonetheless, its ability to complete the fund-raising process and ensure the revised minimum regulatory capital requirement of NPR 5 billion within the regulatory timeline will remain a monitorable from compliance perspective. Increased operational scale post-merger is also expected to bring in economies of scale to the company going forward.

Adequate solvency and good quality of investment – PML's regulatory solvency ratio of 2.08 times as of mid-July 2022 remained adequate against the regulatory minimum of 1.5 times. The solvency profile is likely to improve going forward with the increased capital base and company's capital raising plans (through rights issue).

The company has a sizeable investment portfolio of NPR 12,382 million as of mid-January 2024 which is dominated by FDRs and debentures of class-A banks (collectively accounting for ~82% of investment portfolio). PML reported overall investment (including policy loan) yield of ~9.75% during H1FY2024 despite the recent softening of interest rates, given the long-term placement in fixed income securities in the past. Likewise, new investment directive (rolled out by the regulator in December 2022) has widened the investment avenues for the LICs. Although PML's ability to generate returns from those avenues remains untested, it nonetheless reflects positively on the company's future return prospects.

Adequate reinsurance arrangement – The company has adequate reinsurance support for regular life policies (from Nepal Reinsurance Limited - rated AA- by ICRA Nepal and Himalayan Reinsurance Limited-rated A- by ICRA Nepal) as well as adequate coverage against catastrophic risk (from Hannover Reuck SE-rated A+ (Superior) by AM Best and Himalayan Reinsurance Limited). Good quality of counterparty reinsurer remains a positive from the company's ability to maintain solvency during high-loss event.

Challenges

Limited track record of operation – PML has a limited operating track record of around six years (the company commenced operation from December 2017) in the Nepalese market. Although the company's scale has grown post-merger, the company still has a relatively modest market share of ~3% in the industry with the combined⁴ GPW of ~NPR 3,657 million in FY2023.

⁴ Of erstwhile PLI and MLIL

Regulatory change regarding policy holder bonuses could affect near term profit and growth prospect – The regulatory provision requires all LICs to maintain a complete provision of the vested bonus and 50% provision on future policyholder bonuses. As of mid-July 2022, the company provided for all the vested bonuses and approximately 46% of the future bonus, which lags the regulatory requirement. Though the requirement for future bonus has been reduced to 50%⁵ from 100%⁶ in the past, future bonus provisioning requirement is nonetheless likely to moderate the Nepalese LICs' ability to declare the returns to policy holders as well as their shareholders, which could have an impact on business growth.

High expense ratio affecting profitability – PML's returns indicators remained subdued, given the initial stage of operations, high acquisition cost associated with the insurance business in initial years and lower actuarial surplus from the insurance contract liabilities so far. As the company has a sizeable endowment business, its future profitability profile will remain dependent on the future actuarial transfers to the shareholder's account.

For FY2023⁷, PML reported a net profit of NPR 187 million (PBT of ~NPR 184 million) on a net premium of NPR 1,906 million corresponding to a return on net worth (average), RoNW of ~5% (~7% in H1 FY2024) before the actuarial valuation. Further, relatively higher operating expense ratio (total management expense of ~22% of GPW in FY2023) on a small scale of operation remains a setback to the profitability. However, the scale growth following recent merger is likely to improve the economies of scale and control the expense ratio to some extent.

Analytical approach: For arriving at the grading, ICRA Nepal has applied its issuer rating methodology as indicated below.

Links to applicable criteria

[Issuer Rating Methodology](#)

Link to last rating rationale:

[Rationale - Prabhu Life Insurance Limited \(August 16, 2022\)](#)

Company Profile

Prabhu Mahalaxmi Life Insurance Limited (PML) is a public limited life insurance company (LIC). Erstwhile Prahbu Life Insurance Limited (PLI) was renamed to PML after the merger with erstwhile Mahalaxmi Life Insurance Limited (MLIL) in July 2023 at a share swap ratio of 1:1. Erstwhile PLI was operating since December 2017 while MLIL was in operation since January 2019. Post merger PML has a promoter: public shareholding ratio of ~85:15. PML's head office is in Kamaladi, Kathmandu and the company operates with ~137 branches as of mid-January 2024.

PML reported a profit after tax of ~NPR 187 million in FY2023 on a total asset base of ~NPR 13,203 million as of mid-July 2023 compared to a profit after tax of NPR 131 million in FY2022 on a total asset base of NPR 6,305 million. The company garnered a profit of ~NPR 176 million during H1 FY2024 on a total asset base of NPR 14,636 million as of mid-January 2024.

⁵ Circular issued by the regulator to LICs -dated December 8, 2022.

⁶ Valuation directive 2020; Annexure IV- Guidelines on Actuarial Valuation 5 and 10 (e), released by the regulator in August 2020

⁷ Revenue figures of PLI only. Impact of revenue statement of erstwhile MLIL directly adjusted to balance sheet of merged entity.

Key financial indicators:

Amount in NPR million	MLIL		PLI	PML	
Amount in NPR million	FY2022 (Audited)	FY2023 (Provisional)	FY2022 (Audited)	FY2023 ⁸ (Provisional)	6M FY2024 (Provisional)
Number of months in operation	12	12	12	12	6
First year premium (FYP)	721	504	1,422	564	371
Renewal premium (RP)	736	1,100	946	1,416	1,634
Single premium (SP)	170	-	60	72	33
Total gross premium (TGP)	1,626	1,605	2,429	2,052	2,038
Net premium	1,564	1,551	2,313	1,906	1,999
Premium on endowment policies	1,349	1,453	2,175	1,951	1,916
% share of endowment in total premium	83%	91%	90%	95%	94%
Premium on term policies	278	151	254	101	122
% share in total premium	17%	9%	10%	5%	6%
Total management expenses			503	450	-
Management expenses as a % of gross premium			21%	22%	
Total investment (including policy loans)	4,359	4,986	5,414	11,321	13,425
Yield on investment	9.56%	10.91%	8.37%	6.87%	9.75%
Life fund	2,420	3,512	3,294	7,283	8,517
Profit after tax	51	98	131	187	176
Return on equity	3%	5%	5.26%	5.00%	6.94%
Solvency margin	1.37		2.08		

For further details please contact:

Analyst Contacts:

Mr. Sailesh Subedi (Tel No. +977-1-4519910/20)
sailesh@icranepal.com

Ms. Kushum Bhattarai (Tel No. +977-1-4519910/20)
kushum@icranepal.com

Relationship Contacts:

Ms. Barsha Shrestha, (Tel. No. +977-1-4519910/20)
barsha@icranepal.com

About ICRA Nepal Limited:

ICRA Nepal Limited, the first credit rating agency of Nepal, is a subsidiary of ICRA Limited (ICRA) of India. It was licensed by the Securities Board of Nepal (SEBON) on October 3, 2012. ICRA Nepal is supported by ICRA Limited through a technical

⁸ Revenue figures of PLI only. Impact of revenue statement of erstwhile MLIL directly adjusted to balance sheet of merged entity.



support services agreement, which envisages ICRA helping ICRA Nepal in areas such as the rating process and methodologies, analytical software, research, training, and technical and analytical skill augmentation.

Our parent company, ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment information and credit rating agency. Today, ICRA and its subsidiaries together form the ICRA Group of Companies.

For more information, visit www.icranepal.com

ICRA Nepal Limited,

Sunrise Bizz Park, 6th Floor, Dillibazar, Kathmandu, Nepal.

Phone: +977 1 4519910/20

Email: info@icranepal.com

Web: www.icranepal.com

All Rights Reserved.

Contents may be used freely with due acknowledgement to ICRA Nepal.

ICRA Nepal ratings should not be treated as recommendation to buy, sell or hold the rated debt instruments. The ICRA Nepal ratings are subject to a process of surveillance which may lead to a revision in ratings. Please visit our website (www.icranepal.com) or contact ICRA Nepal office for the latest information on ICRA Nepal ratings outstanding. All information contained herein has been obtained by ICRA Nepal from sources believed by it to be accurate and reliable. Although reasonable care has been taken to ensure that the information herein is true, such information is provided 'as is' without any warranty of any kind, and ICRA Nepal in particular, makes no representation or warranty, express or implied, as to the accuracy, timeliness or completeness of any such information. All information contained herein must be construed solely as statements of opinion and ICRA Nepal shall not be liable for any losses incurred by users from any use of this publication or its contents.