Canara HSBC Oriental Bank of Commerce Life Insurance Company Limited

April 01, 2022

Ratings

Facilities/Instruments	Rating[1]	Rating Action
Issuer rating*	CARE AAA (Is); Stable [Triple A (Issuer Rating); Outlook: Stable]	Reaffirmed
Total Instrument		

Details of instruments/facilities in Annexure-1
*The rating is subject to the company maintaining overall gearing not exceeding 0.2x.

Detailed Rationale & Key Rating Drivers

The issuer rating of Canara HSBC Oriental Bank of Commerce Life Insurance Company Ltd factors in strong parentage marked by high degree of support, synergies and brand linkages from its promoters enjoyed by the company, experienced management, high solvency ratio and consistent persistency ratios.

The rating also derives strength from strong liquidity position with individual positive mismatches in all the time buckets as per asset liability mismatch (ALM) statement as on December 31, 2021, track record of controlled operating costs and profitable operations, strong systems and processes and growth prospects for the insurance industry. These rating strengths are, however, partially offset by the company's modest market position (around 2% share in the private life insurance segment).

Rating Sensitivities

Going forward, the continued support of the shareholders, maintenance of solvency sufficiently above the regulatory requirement, the ability to increase premium written and profitability will be the key rating sensitivities.

Negative Factors- Factors that could lead to negative rating action/downgrade:

- Any material changes in the shareholding pattern leading to expectation of diminished shareholder support and/or impact on the bancassurance partnerships
- Weakness in the capitalization profile with solvency going below 2 times
- Moderation in premium written, persistency, operating expenses resulting in impact on the underwriting profitability

Detailed description of the key rating drivers

Key Rating Strengths

Strong shareholders with high degree of synergies and brand linkage with the company

The company is a joint venture between Canara Bank, HSBC Insurance (Asia Pacific) Holdings Limited, and Punjab National Bank (PNB) and the shareholders hold 51%, 26% and 23% stake, respectively, in the company as on December 31, 2021. On August 20, 2019, the Government of India (GoI) announced amalgamation of 10 public sector banks into four entities. Of these, Oriental Bank of Commerce (OBC) and United Bank of India (UBI) amalgamated into PNB. Consequently, with effect from April 1, 2020, OBC's share was transferred to PNB and now PNB holds 23% of the shareholding of the company. End December 2021, PNB also held 30% in another insurance company, namely, PNB MetLife. However, as per the extant guidelines, one promoter cannot hold more than 10% in two insurance companies, and PNB had applied to IRDAI seeking forbearance from reducing its stake in the company upon merger but there has been no update on the same till date. Additionally, Syndicate Bank merged into Canara Bank. The completion of bank amalgamation process has allowed the company access to a significantly larger customer base and strong branch network of two of the largest public sector banks.

Experienced board members and management team

The overall operations of company are governed by a 13-member Board of Directors, which includes representatives of the key shareholders, viz., Canara Bank, PNB and HSBC Holdings. Furthermore, the company has an experienced management team headed by Mr Anuj Mathur, who is the Chief Executive Officer of the company. He is ably supported by a team of experienced professionals who have considerable experience in the insurance sector.

Strong solvency position

The company's solvency declined to 2.74x at end December 2021 compared with 2.89x at end-December 2020; however, continues to remain strong. The decline was driven by net losses incurred by the company in 9MFY22 due to high claim pay-out ratio caused by the second Covid wave. With moderation in claim ratio in the subsequent quarters and consequent improvement in the profitability indicators, solvency position is expected to improve in the near term.
End-December 2021, the available solvency margin (ASM) stood at Rs.1,746 crore as against the required solvency margin (RSM) of Rs.638 crore. The solvency ratio for the company is largely driven by the shareholder's fund given its track record of profitable operations over the past nine years starting FY13 (refers to the period April 1 to March 31). In addition, the company has taken re-insurance for covering risk beyond a threshold limit and to cover for catastrophic risks, which not only helps in avoiding high claims but also helps in conserving the capital. The capital requirement (RSM) of the company is, however, increasing with declining share of linked products (31% of the net earned premium in 9MFY22 as against 58% in FY18) which

[1]Complete definition of the ratings assigned are available at www.careedge.in and other CARE Ratings Ltd.'s publications

are relatively less capital intensive as much of the risk is borne by the investors. Going forward, with the increasing share of non-linked traditional products, the ability of the company to maintain healthy solvency would be crucial and will be a key rating sensitive.

Consistent performance over the years

The company's gross earned premium (GEP) grew y-o-y by 29.8% and by three-year compounded annual growth rate (CAGR) of 22.5% for FY21. Although the y-o-y growth moderated to 13.5% in 9MFY22, the 50.2% increase in first-year non-single-premium during same period reflects growth momentum through renewal premiums over the medium term. The impact of the closure of bancassurance tie-up with PNB, as it plans to divest its stake in the company to meet regulatory requirements, will be offset by increased business from other channels.

The company has been moving towards traditional products with the share of linked plans going down and constituted 31% of the net earned premium (NEP) for 9MFY22 down from 58% end FY18. On the other hand, the cumulative share of non-linked products (par, non-par, variable) has been on a rise and stood at 69% for 9MFY22. Of the non-linked products, the share of plain vanilla product, i.e., non-participating and non-linked plans has been rising since these plans assure fixed sum, are completely insulated from market risks, are available at low cost to the customers and have a longer tail. As a result, the share of non-par, non-linked has risen to 50% for 9MFY22 as against 16% for FY18.

The company reported net loss / NEP of -3.7% in 9MFY22 against 1.9% in FY21. The losses are due to high claim pay-out during Q1FY22 in which the mortality rates increased on account of the fatal COVID second wave (Net claims / NPE of 50.2% in 9MFY22 against 40.9% in FY21). However, with no adverse impact of COVID third wave, the mortality rates have improved. Also, the premium rates have been increased for different products. Thereby, the management expects to cover the loss and achieve breakeven in FY22. The profitability will improve over the medium term but will remain below historical levels owing to change in the product composition toward non-linked-non-participating products, which have higher expense ratio.

Low operating costs

The company operates on the bancassurance model and has an exclusive access to the network of its promoters. The operating costs for the company are low as the company benefits from the bancassurance model (~67% of new business generated in 9MFY22) with exclusive agreement with the promoters, as the operational expenses incurred, and commissions paid are relatively less under the said model. Furthermore, the infrastructure and operational expenses are lower as bank branches are used as distribution centres.

The expense ratio is low at 17.5% in FY21, improved from 19.3% in FY20 and was at 18.4% in 9MFY22. The overall expense ratio has remained range bound in past four years despite the increase in commission ratio (commission / net premium earned ratio) to 5.7% in 9MFY22 from 4.6% in FY18. The increase in commission expense is owing to the changing product mix (towards traditional and non-PAR products which entail higher commission as against the linked products as the former tend to be long-tailed products and are more profitable in the long run. Also, commissions are capped by IRDAI for ULIP products.

Healthy persistency ratio

The persistency ratios of the company are healthy and have been improving over the years, which not only indicates higher renewal premiums but also a strong consumer franchise. Furthermore, it also indicates longer tenure of policy in force which enables the company to recover costs and make profit over the life of the insurance contract. The company has been investing in technology and reach, to reach out to its customers to maintain a high persistency ratio. For FY21, the one-year persistency (measured on 13th month) stood at 80.4% (77.9% in FY18), while the fifth year (measured on 61st month) stood at an improved 53.6% (43.3% in FY18), thereby indicating improvement in retention ratios.

Good asset quality and liquidity of investment book

Overall, the company's asset quality remains strong with company investing its funds in accordance with the regulatory norms prescribed by IRDAI and the investment policy as approved by the Board of the company. The company's non-linked funds (investments supporting both the non-linked policy portfolio and the shareholders' funds) are largely invested in fixed-income securities ensuring less risk and better liquidity. As on December 31, 2021, the company had total funds (shareholders plus policyholder's) of Rs.25,240 crore. The non-linked investments of Rs.12,244 crore was largely invested in government securities (57%) and AAA rated corporate securities (35%). The linked investments of Rs.12,996 crore was largely in equities (70%), government securities (18%), and AAA rated corporate securities (8%). Also, investment risk of the company is relatively lower due to high share of ULIPs/Linked Pensions (31% of NWP in 9MFY22) and participating policies (19%) in its product mix wherein the investment risk is borne by the investor. A substantial portion of the company's investments are readily marketable, thereby extending it ample liquidity support. The asset quality of the company is good with nil net non-performing assets (NNPAs) in the investment book as on December 2021.

Adequate Systems and Controls

The major risks for the company are strategic risks (product, people, channel and regulatory risks), insurance risks (mortality, discontinuity, expense risks), operational risks (fraud, business continuity, process/system failure risks) and investment market risk (credit, equity, interest rate risk). The company, to mitigate these risks, undertakes regular assessment of the risks and has also put in place control mechanisms. The company has an internal audit department to ensure that proper and adequate systems and procedures are in place and being followed. Concurrent audit of investment operations is conducted by an independent firm, in line with IRDAI regulations. Also, peer review of actuarial assumptions is conducted by an independent third party.

To reduce the risk on account of fraud, the company has put in place various parameters for writing the risks (as per the Underwriting Policy). The company has also entered into treaty agreements and facultative agreements with reinsurers for mitigating the risk. Also, to mitigate the investment risks, the company follows the investment limits as defined under the IRDAI guidelines and has defined internal guidelines allocation of limits w.r.t. maximum exposure in a single entity/group' bonds/equity.

Key Rating Weaknesses
Moderate scale of operations
The company started its operations in 2007 and has moderate scale of operations with an investment book of Rs.25,240 crore at end-December 2021. Furthermore, the market standing of the company also remains moderate, with it being the 10th-largest private life insurance player with a market share of about 2.3% (based on gross written premium) end FY21 among 23 private life insurers. Further, the company has moderate geographical diversification with Karnataka contribution 30.8% of new business generated in FY21 followed by Maharashtra (13.0%).

Analytical approach: Standalone; expecting continuous support from promoters given shareholding, brand linkage, business synergies, and management & operational linkages.

Applicable Criteria
Policy on default recognition
Factoring Linkages Parent Sub JV Group
Financial Ratios - Insurance Sector
Issuer Rating
Rating Outlook and Credit Watch
Rating Methodology – Insurance Sector

About the Company
CANARA HSBC OBC Life Insurance Company Limited was incorporated on September 25, 2007, is licensed by IRDAI Insurance Regulatory & Development Authority of India) to carry out life insurance business in India. The company commenced operations in June 2008. It is a joint venture of Canara Bank (51%), HSBC Insurance (Asia Pacific) Holdings Ltd (26%) and Punjab National bank (23%).
It is engaged in the business of life insurance and pension. The business spans across individual and group products. The company operates on a bancassurance model, and it generated 80% of GWP in 9MFY22 from its three partner banks. The company has also tied up with two rural regional banks (RRBs), Dhanlaxmi Bank and with Non-Banking Financial Companies (NBFCs), including CanFin Homes for distribution of its products. The company also distributes its products through direct channel, viz., direct distribution and digital platform. The total investments as on December 31, 2021, were Rs.25,240 crore.

Brief Financials (Rs. crore)	31-03-2020 (A)	31-03-2021 (A)	9MFY22 (UA)
Net Premium Earned	3889	5026	3868
PAT	105	95	-69*
Total Assets	15,946	22,586	25,986
Investments	15,374	21,871	25,240
Net NPA (%)	0.00	0.00	0.00
ROTA (%)	0.7	0.5	-0.4*

A: Audited; UA: Unaudited; *Includes surplus of Rs 75.48 crore to be included in P&L post statutory-audit.

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

Rating History for last three years: Please refer Annexure-2

Covenants of rated instrument / facility: Detailed explanation of covenants of the rated instruments/facilities is given in Annexure-3

Complexity level of various instruments rated for this company: Annexure 4

Annexure-1: Details of Instruments / Facilities

Name of the Instrument	ISIN	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Issuer Rating-Issuer Ratings		-	-	-	0.00	CARE AAA (Is); Stable

Annexure-2: Rating History of last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating history			
		Type	Amount Outstanding (Rs. crore)	Rating	Date(s) & Rating(s) assigned in 2021-2022	Date(s) & Rating(s) assigned in 2020-2021	Date(s) & Rating(s) assigned in 2019-2020	Date(s) & Rating(s) assigned in 2018-2019
1	Issuer Rating-Issuer Ratings	Issuer rat	0.00	CARE AAA (Is); Stable	-	1)CARE AAA (Is); Stable (31-Mar-21)	-	-

* Long Term / Short Term

Annexure-3: Detailed explanation of covenants of the rated instrument / facilities: Not available

Annexure 4: Complexity level of various instruments rated for this company

Sr. No	Name of instrument	Complexity level
1	Issuer Rating-Issuer Ratings	Simple

Annexure 5: Bank Lender Details for this Company
To view the lender wise details of bank facilities please **click here**

Note on complexity levels of the rated instrument: CARE Ratings Ltd. has classified instruments rated by it on the basis of complexity. Investors/market intermediaries/regulators or others are welcome to write to care@careedge.in for any clarifications.

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About CARE Ratings Limited:
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With an established track record of rating companies over almost three decades, we follow a robust and transparent rating process that leverages our domain and analytical expertise backed by the methodologies congruent with the international best practices. CARE Ratings Limited has had a pivotal role to play in developing bank debt and capital market instruments including CPs, corporate bonds and debentures, and structured credit.

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