Canara HSBC Oriental Bank of Commerce Life Insurance Company Ltd

March 31, 2021

Ratings

Type of Rating	Rating[1]	Rating Action
Issuer Rating*	**CARE AAA (Is); Stable (Triple A (Issuer Rating); Outlook: Stable)**	**Assigned**

Details in Annexure-1

**The rating is subject to the company maintaining overall gearing not exceeding 0.2x (expected level as on March 31, 2022).*

Detailed Rationale & Key Rating Drivers

The issuer rating of **CARE AAA (Is); Stable** assigned to Canara HSBC Oriental Bank of Commerce Life Insurance Company Ltd factors in strong parentage marked by high degree of support, synergies and brand linkages enjoyed by the company, experienced management, high solvency ratio at 2.89 times as on Dec-20 and consistent improvement in persistency ratios with 13th month persistency at 79.80% and 61st month persistency at 54.40% as on December 31, 2020.

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 Sep-20, controlled operating costs with adjusted combined ratio at 94% end March-20, profitable operations with return on total assets (RoTA) at 0.69% end March-20, strong systems & processes and growth prospects for the insurance industry. These rating strengths are however offset by the company's modest market position (~2% share in the individual 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

- Any material change 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 & 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 March 31, 2020. On 20th August 2019, the Government of India (GoI), announced amalgamation of ten 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 1st April 2020, OBC's share was transferred to PNB and now PNB holds 23% of the shareholding of the company. End December 2020, 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 an access to a significantly larger customer base and strong branch network of two of the largest public sector banks.

The shareholders are also actively involved in the business having extended financial, technological, infrastructural and managerial support to the company. The company is strategically important for the shareholders as demonstrated by the high degree of brand and operational linkages. The company is the captive insurer of Canara Bank, HSBC and PNB and operates primarily on bancassurance model which contribute significant percentage of the individual premium written by the company. Once the open architecture gets implemented, the company will have access to a network of over 21,000 branches (as on December 31, 2020) of these banks. Any further change in the shareholding pattern due to IRDAI guidelines and subsequent impact on the operations of company would be a key monitorable.

[1]*Complete definition of the ratings assigned are available at www.careratings.com and other CARE publications*

Experienced board members and management team

The overall operations of company are governed by a 14 members Board of Directors which includes representatives of the key shareholders viz. Canara Bank, PNB and HSBC Holdings. Further, 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 stood at 3.65 times as on March 31, 2020 that came down to 3.12 times as on Sept-20 and further to 2.89 times as on December 31, 2020, though still well above the prescribed limit of 1.50 times as stipulated by IRDAI. End Dec 2020, the Available Solvency Margin (ASM) stood at Rs.1,462 crore as against the Required Solvency Margin (RSM) of Rs.506 crore. The solvency ratio for the company is largely driven by the shareholder's fund given its track record of profitable operations over the last 8 years. In addition, the company has taken re-insurance for covering risk beyond a threshold limit and also to cover for catastrophic risks which not only helps in avoiding high claims but also help in conserving capital. The capital requirement (RSM) of the company however is increasing with declining share of linked products (40% of annual premium in FY20 as against 48% in FY18) which 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.

Low operating costs

The company operates on the bancassurance model and has an exclusive access to network of over 21,000 bank branches (10,925 domestic branches of PNB and 10,491 branches of Canara Bank as on December 31, 2020) of its 3 corporate agents. Post the amalgamation of Canara Bank with Syndicate bank and of PNB with OBC and UBI, the consolidated branch network to which the company has access to, has risen substantially. The operating costs for the company are low as the company benefits from the bancassurance model with exclusive agreement with the promoters, as the operational expenses incurred and commissions paid are relatively less under the said model. Further, the infrastructure and operational expenses are lower as bank branches are used as distribution centers.

The company has low total expense ratio of 19.3% in FY20 as against 17.2% in FY 19. This is owing to the Bancassurance model. The overall expense ratio has remained range bound in last three years in despite the increase in commission ratio (Commission/Net Premium Earned ratio) by 41 bp Y-o-Y to 5.77% end FY 20. The increase in commission expense is owing the changing product mix (towards traditional and Non-PAR products which entail higher commission as against linked products as former tend to be long tailed products and are more profitable in the long run. Also, commissions are capped by IRDAI for ULIP products.

Consistent performance over the years

In the last five years till FY 20, the company's gross premium written (GPW) has grown at a compounded annual growth rate (CAGR) of 19% to reach Rs 3,943 crore end FY 20. During FY20, the Gross Written Premium (GWP) of the company increased 13% y-o-y to Rs.3,943 crore as on March 31, 2020. The growth in GPW was at a slower pace in FY 20, growing at an annual rate of 13% Y-o-Y as against 26% Y-o-Y growth registered a year before that. This was underpinned by impact of covid and subsequent lockdown that was imposed on March 25, 2020 that adversely impacted new business in quarter ending March 2020. For half year ended Sept 2020, the GPW stood at Rs 2,184 crore, up 22% Y-o-Y.

The company has been moving towards traditional products with the share of linked plans going down and constituted 34% of NPW end H1FY21 down from 65% end FY 17. On the other hand, the cumulative share of non-linked products (Par, non-par, variable) has been on a rise and stood at 66% end H1FY 21. 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 customers and have a longer tail. As a result, the share of non-par, non-linked has risen to 37% end H1FY21 as against 20% end FY 17.

The company has been reporting profits for the past eight years. End FY 20, the company reported a PAT of Rs 105 crore, down 36% Y-o-Y driven by higher premium income though partially offset by higher provisions. The adjusted combined operating ratio (as a percentage of net premium and investment income) of the company was comfortable at 93.8% in FY20 driven by claim Payout (including change in valuation of liability) (69%), Operating Expenses (18%) and commission payout ratio (8%).

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 so as to maintain a high persistency ratio. End Dec 2020, the one year persistency (measured on 13th month) stood at 79.8% while the fifth year (measured on 61st month) stood at an improved 54.4% 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 March 31, 2020, the company had total funds (shareholder's plus policyholder's) of Rs 15,374 crore, of which 32% are in government securities and another 26% in AAA rated corporate bonds.

Of the controlled funds of Rs 7,218 crore, 49% were invested in Government bonds, 43% in AAA rated securities, 4% in AA/AA+ rated securities, 3% in money market instruments and balance 2% in equity share. Investments of Rs 8,155 crore that were supporting linked policies were approximately 55% in equities, 18% in Govt. Securities, 13% in money market instruments and balance 14% in corporate bonds. Also, investment risk of the company is relatively lower due to higher share of ULIPs/Linked Pensions (46% of NWP in FY20) and 27% of participating policies in its product mix (combined share has been 70-80% over the last 5 years) wherein the investment risk is borne by the investor. A substantial portion of company's investments are readily marketable thereby extending it ample liquidity support. The asset quality of the company is good with Nil Net NPAs in investment book as on Dec-20.

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, in order 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.

In order 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 with reinsurers for mitigating the risk. Also, in order 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.15,374 crore as on March-20, marginally up from Rs. 14,854 crore as on March-19. Further, 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 individual weighted premium income) end FY 20 among 23 private life insurers.

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

Applicable Criteria

Criteria on assigning 'outlook' and 'credit watch' to Credit Ratings
CARE's Policy on Default Recognition
Financial Ratios – Insurance Sector
Rating Methodology - Insurance Sector
Rating Methodology: Notching by factoring linkages in Ratings
CARE's Issuer Rating

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 has an exclusive access to around 115 million customers and a network of over 21,000 bank branches of its 3 partner banks. The Company has also tied up with two Rural Regional Banks (RRBs), Dhanlaxmi Bank and with 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 assets under management as on March 31, 2020 were Rs.15,374 crore.

Brief Financials (Rs. crore)	FY19 (A)	FY20 (A)
Net Premium Earned	3,450	3,889
PAT	165	105
Total Assets	15,090	15,542
ROTA (%)	1.18	0.69
Solvency Ratio	3.93	3.65
Assets under Management (AUM)	14,854	15,374

A: Audited

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	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 2020-2021	Date(s) & Rating(s) assigned in 2019-2020	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018
1.	Issuer Rating-Issuer Ratings	Issuer rat	0.00	CARE AAA (Is); Stable	-	-	-	-

Annexure-3: Detailed explanation of covenants of the rated instrument / facilities: NA

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

Sr. No.	Name of the Instrument	Complexity Level
1.	Issuer Rating-Issuer Ratings	Simple

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

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