Canara HSBC Oriental Bank of Commerce Life Insurance Company Ltd

March 2, 2020

Ratings

Facilities	**Amount (Rs. crore)**	**Rating[1]**	**Rating Action**
Claims Paying Ability/Financial Strength	-	**CARE AAA (In) (Triple A Insurance)**	**Reaffirmed**

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers
The rating continues to factor in the strong parentage of Canara HSBC Oriental Bank of Commerce Life Insurance Company Ltd (CHOICe) with high degree of support, synergies & brand linkage enjoyed by the company, experienced management, high persistency ratios, apart from strong solvency and liquidity position. The rating also takes cognizance of controlled operating costs, profitable operations, strong systems & processes and growth prospects for the insurance industry. However, CHOICE has a 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. Also, any impact of the merger of the PSU Banks (Syndicate Bank with Canara Bank and Oriental Bank of Commerce with Punjab National Bank) on the shareholding of CHOICE and any its impact on the operations of CHOICe (if any) given the significance of OBC as an important Bancassurance partner, will be crucial.

Negative factors
- Any material change in the shareholding pattern and impact on the bancassurance partnerships
- Weakness in the capitalization profile with solvency going below 200%
- Moderation in premium written, persistency, operating expenses resulting in impact on the profitability

Detailed description of the key rating drivers
Key Rating Strengths
Strong shareholders with high degree of synergies & brand linkage with the company although impact of the PSU bank merger on the shareholding and operations needs to be seen
The shareholders (Canara Bank, HSBC, OBC Bank) hold 51%, 26% and 23% stake respectively in the company and 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 OBC Bank and operates primarily on Bancassurance model which contribute significant percentage of the individual premium written by CHOICe. This agreement gives the company access to around 115 million customers and a network of over 10,000 branches of these banks.

Ministry of Finance (MoF), Government of India (GoI) announced amalgamation of public sector banks on August 30, 2019. Under the amalgamation process, Punjab National Bank (PNB) will act as an anchor bank and will take over Oriental Bank of Commerce (OBC: CARE A+; under credit watch with developing implications) and United Bank of India (UBI: CARE A+; under credit watch with developing implications). The Boards of all three banks have given in-principle approval for the amalgamation. On completion of amalgamation, PNB will be the second largest public sector bank in terms of asset size. However, PNB has a 30% holding in PNB Metlife and upon merger of OBC, will get the 23% holding of OBC in CHOICe whereas as per the extant guidelines one promoter cannot hold more than 10% in two insurance companies. Consequently, PNB has applied to IRDAI seeking forbearance from reducing its stake in CHOICe upon merger. Additionally, Syndicate Bank (rated CARE AA; under credit watch with developing implications) would be merging into Canara Bank, thereby giving access to the large customer base and branch network of Syndicate Bank to CHOICe.

Thus, the impact due to change in shareholding on the operations of CHOICe particularly the bancassurance partnership will be a key monitorable.

Experienced management

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

CHOICe management team is currently headed by Mr Anuj Mathur who is Chief Executive Officer of the company. He is ably supported by a team of experienced professionals. The overall operations of CHOICe are governed by a 13 member Board of Directors which includes representatives of the key shareholders viz. Canara Bank, OBC and HSBC Holdings.

Strong solvency position

CHOICe's solvency ratio computed as per IRDAI norms is 382% as on Sept 30, 2019 and this margin is well above the prescribed limit of 150% by IRDAI. The Available Solvency Margin (ASM) is Rs.1336 crore as against the Required Solvency Margin (RSM) of 349 crore. CHOICe's solvency ratio is also largely driven by the shareholder's fund given its track record of profitable operations over the last 7 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 CHOICe however is increasing with declining share of linked products (40% of AUM as on Mar-19 as against 48% as on Mar-18 and 77% as on Mar-17) which are relatively less capital intensive as much of the risk is borne by the investors. Ability of CHOICe to maintain healthy solvency would be crucial.

Low operating costs

The company benefits from the bancassurance model with exclusive agreement with the promoters, as the operational expenses incurred and commissions paid are less. Also, the infrastructure and operational expenses are lower as bank branches are used as distribution centers.

Consistent performance over the last seven years

CHOICe registered a 13% growth in APE (Annual Premium Equivalent excluding employee benefit) from Rs.859.2 crore during FY18 to Rs.974.8 crore in FY19. Overall Gross Written Premium (GWP) increased by 26% during FY19 to Rs.3491 crore (PY Rs.2781 crore). The growth in premium written was largely driven by the growth in premium for traditional products (Non-Linked products), the share of which increased from 51% in FY18 to 58% in FY18 in the first year premium as the company has been introducing new products in the non-linked category as well as expanding its presence in the Tier-II,III and IV markets. Also, the renewal rate increased resulting in increase in renewal premium during FY19.

CHOICe reported a PAT of Rs.165 crore during FY19 (as against Rs.168 crore in FY18) with it being the 7th year of profitable operations. FY19, was the first year wherein CHOICE saw positive accumulated profits. Its adjusted combined operating ratio was comfortable at 94-97% in FY18-FY19 driven by claim Payout (79-82% of Net Premium and Investment Income), Operating Expenses (13-15% of Net Premium) and commission payout ratio (4.5-5.5% of Net premium). The profitability was also lower during FY19, due to provision of Rs.42.57 crore (out of total provision of Rs.55 crore) provided towards the exposure towards IL&FS group from the shareholders account during FY19.

During H1FY20, CHOICe, has written net premium of Rs.1795 crore and reported PAT of Rs.58 crore (including surplus in policy holder's account pending transfer to Shareholder's account) as against net premium of Rs.1464 crore and PAT of Rs.56 crore during H1FY19. This was largely due to a provision of Rs.45 crore effected from the shareholders' account during H1FY20 (balance 50% provision against the IL&FS exposure) as against Rs.18.65 crore during H1FY19.

Consequently, with the improvement in profitability and changing product mix with increasing share of traditional products, the Value of New Business Margins and Embedded Value of CHOICe, has also increased.

Persistency ratio

The persistency ratios of CHOICe 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. Below are the persistency ratios for last 3-4 years:

Persistency Ratio (%)	**FY17**	**FY18**	**FY19**	**H1FY20**
For 13th Months	78.1	77.9	80.9	80.8
For 25th Months	64.1	69.2	68.8	71.4
For 37th Months	56.0	59.1	63.5	61.5
For 49th Months	52.3	53.4	55.8	59.6
For 61st Months	42.2	43.3	46.0	48.1

Good Asset Quality and liquidity of Investment book; exposure to IL&FS group fully provided for as of Sept-19

The company's 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, 2019, 50% of the these funds were invested in Government bonds, 43% in AAA rated securities, 2% in AA/AA+ rated securities, 3% in money market instruments and balance 2% in equity shares as on Mar-19. Investments supporting linked policies were approximately 65% in equities, 14% in Govt. Securities, 9% in money market instruments and balance 12% in corporate bonds. Also, investment risk of CHOICE is relatively lower due to higher share of ULIPs/Linked Pensions (51% of GWP in FY19) and 24% 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 CHOICE's investments are readily marketable thereby extending it ample liquidity support.

As on Sept 30, 2019, CHOICe had Nil Net NPAs having completely fully provided for its exposure of Rs.125 crore in IL&FS and IL&FS Financial Services Ltd.

Adequate Systems and Controls

The major risks for CHOICE 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). CHOICe, in order to mitigate these risks undertakes regular assessment of the risk 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, CHOICe has put in place various parameters for writing the risks (as per the Underwriting Policy). CHOICe has also entered into treaty agreements with reinsurers for mitigating the risk. Also, in order to mitigate the investment risks, CHOICe 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 scale of the operations of CHOICe is small. As on Mar-19, it had an investment book of Rs.14,854 crore (P.Y. Rs. 12,688 crore) with over 9 lac individuals covered. The market standing of CHOICe also remains moderate, it being the 10th largest private sector player with around 2% share of overall First Year Individual Premium written by Private sector players.

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

Applicable Criteria

Rating Methodology: Insurance Companies
Rating Methodology: Consolidation and Factoring Linkages in Ratings
Financial Ratios – Insurance Sector

About the Company

CHOICe is a joint venture of Canara Bank (51%), HSBC Insurance (Asia Pacific) Holdings Ltd (26%) and Oriental Bank of Commerce (23%). CHOICe, 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 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 10,000 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 Sept 30, 2019 were Rs.15,794 crore.

Brief Financials (Rs. crore)	FY18 (A)	FY19 (A)
Gross Premium Earned	2,781	3,491
Net Premium Earned	2,752	3,450
PAT	168	165
Total Assets	12,810	15,090
ROTA (%)	1.39	1.18
Solvency Ratio (%)	382	393
Assets under Management (AUM)	12,688	14,854

A: Audited

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
Claims Paying Ability	NA	NA	NA	NA	CARE AAA (In)

NA: Not Applicable

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 2018-2019	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018	Date(s) & Rating(s) assigned in 2016-2017
1.	Claims Paying Ability	Insurer ratings	-	CARE AAA (In)	-	1) CARE AAA (In) (31-Dec-18)	1) CARE AAA (In) (24-Oct-17)	1) CARE AAA (In) (18-Oct-16)

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

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