

August 01, 2022

Star Union Dai-ichi Life Insurance Company Limited: Rating reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Subordinated debt programme	125.00	125.00	[ICRA]AA(Stable); reaffirmed
Total	125.00	125.00	

*Instrument details are provided in Annexure I

Rationale

The rating reaffirmation considers Star Union Dai-ichi Life Insurance Company Limited's (SUD Life) strong promoter profile, which ensures capital, strategic, and operational support as and when required. SUD Life is a joint venture between Bank of India {BOI; rated [ICRA]AA+ (Stable)} holding a 28.96% stake, Union Bank of India {UBI; rated [ICRA]AA+ (Stable)} holding a 25.10% stake and Dai-ichi Life International Holdings LLC (Dai-ichi Life) holding a 45.94% stake as on March 31, 2022. The importance of SUD Life to the promoters is demonstrated by their track record of equity infusion and their continued capital commitment. SUD Life expects a capital infusion of ~Rs. 200 crore through a rights issue from all the promoters as per their current shareholding pattern in Q2 FY2023. This is expected to add ~36 basis points (bps) to the reported solvency ratio of 2.0 times as of March 31, 2022.

The rating also factors in the operational support in terms of access to the extensive branch network (~14,000) of the promoter banks. This enables SUD Life to leverage the bancassurance (banca) channel to source business at a relatively lower cost. SUD Life generates more than 78% of its new business premium (NBP) through the banca channel with its promoter banks. In terms of strategic support, the company leverages the experience of Dai-ichi Life in the life insurance industry for new product approval and reinsurance arrangements, among others.

Despite the significant rise in the net benefits paid mainly due to high Covid claims, the company managed to report a profit after tax in FY2022 driven by its operating efficiency. The profitability was also supported by the recovery from the Dewan Housing Finance Corporation Ltd. (DHFL) bonds, which was entirely provided for in earlier periods. SUD Life does not expect any material Covid claims to be reported in FY2023. ICRA expects the company's return ratios to improve mainly due to the price revision of the loss-making Pradhan Mantri Jeevan Jyoti Bima Yojana (PMJJBY) business, expected lower Covid claims and high operating efficiency.

The rating is partially offset by SUD Life's modest scale of operations with a market share, in terms of NBP, of 0.61% in FY2022. The company's ability to grow the business and improve the return ratios amid rising competition remains a monitorable. Further, the share of the high-margin protection business remained low at 0.7% in FY2022 in individual annual premium equivalent (APE) terms. SUD Life's ability to grow and maintain profitability in the protection business remains a monitorable.

The rating also factors in the key features of the instrument, in line with the applicable guidelines for subordinated debt:

- » Servicing of interest is contingent on the company maintaining a solvency ratio above the levels stipulated by the regulator¹
- » If the interest payouts lead to a net loss or an increase in the net loss, the prior approval of the regulator would be required to service the debt

¹ As per the Insurance Regulatory and Development Authority of India (IRDAI), insurers are required to maintain a minimum solvency ratio of 1.50 times

Key rating drivers and their description

Credit strengths

Strong parentage provides capital, strategic, and operational support – SUD Life is a joint venture between BOI (28.96% as on March 31, 2022), UBI (25.10%) and Dai-ichi Life (45.94%). The company began operations in February 2009 with capital support of Rs. 420 crore from its promoters. The last capital infusion of Rs. 108 crore was in FY2017 in the form of growth capital. SUD Life is expecting a capital infusion of Rs. 200 crore through a rights issue from all the promoters as per their current shareholding pattern in Q2 FY2023. This is expected to support the solvency position and provide headway for the company's aggressive growth plans driven by banca and other channels. ICRA notes that UBI had a 25.1% stake in SUD Life and a 30% stake in IndiaFirst Life Insurance Company Limited (IFLI) as on March 31, 2021. With Bank of Baroda (BOB) buying a 21% stake in IFLI from UBI in Q4 FY2022, the regulatory overhang of a promoter not being allowed to hold more than a 10% stake in more than one insurance company has been resolved. In terms of operational support, SUD Life has access to the wide branch network (~14,000) of the promoter banks. Further, BOI and UBI have sponsored select regional rural banks with more than 1,950 branches, which provides the company with access to rural markets. As a result, SUD Life sources more than 78% of its NBP through the banca channel with its promoter banks.

Dai-ichi Life was established in 1902 and is one of the major life insurance companies in Japan. Its vast experience in the life insurance industry benefits SUD Life in product approval and reinsurance arrangements, among others, in terms of strategic support. With the relaxation of foreign direct investment (FDI) limits to 74% from 49%, there is scope for further capital support from Dai-ichi Life. ICRA expects that capital support will be forthcoming from the promoters, as and when required, and the company is likely to benefit strategically from its promoter's (Dai-ichi Life) experience along with the leveraging of the huge branch network of its promoters to source business.

Strong solvency position supported by internal accruals; likely to improve further with regulatory changes in PMJJBY business and expected capital infusion – SUD Life's solvency position remained strong with a solvency ratio of 2.00 times as on March 31, 2022 compared to 2.06 times as on March 31, 2021. The company's solvency ratio was better compared to peers and remained above the regulatory requirement of 1.50 times. The strong solvency profile was largely supported by its healthy internal capital generation. Further, SUD Life is anticipating a capital infusion of Rs. 200 crore in Q2 FY2023, which is expected to add ~36 bps to the reported solvency ratio.

SUD Life reported a loss under the PMJJBY scheme in FY2022. With the price revision of the PMJJBY scheme, the company expects to break even in this scheme, which is expected to add ~30 bps to the reported solvency ratio. Further, the solvency requirement for the PMJJBY business was reduced to 0.05% from 0.10% of the sum at risk (Rs. 2 lakh per policy) for the required solvency margin (RSM) calculation. This is expected to add ~10 bps to the company's reported solvency ratio. ICRA believes that SUD Life would remain well capitalised with a strong solvency profile, going forward as well.

Consistent profitability with return ratios expected to improve – The company has been consistently reporting net profits from FY2015. However, SUD Life's gross value of new business (VNB) margin declined marginally due to the rise in the share of the lower VNB margin unit linked insurance plan (ULIP) product (~25% share in terms of individual APE) and the higher repricing of a non-participating (non-par) product. Nevertheless, the company's share of relatively high VNB margin non-par products remained significant at 72.4% in individual APE terms followed by ULIP (24.2%), par (2.7%) and protection (0.7%) in FY2022.

Despite the significant rise in the net benefits paid, the company managed to report a profit after tax in FY2022 driven by the high operating efficiency. The net benefit paid to net premium written (NPW) increased to 42.9% or Rs. 1,680.4 crore in FY2022 from 39.4% or Rs. 1,137.0 crore in FY2021 due to higher PMJJBY and Covid claims. The net Covid claims increased to Rs. 73.7 crore in FY2022 compared from Rs. 8.6 crore in FY2021. However, the Covid claims declined in the last couple of quarters with less than Rs. 2.0 crore reported in Q1 FY2023. The company does not expect any material Covid claims to be reported in FY2023. Moreover, the profitability was supported by the recovery from the DHFL bonds, which was entirely provided for in earlier periods. SUD Life witnessed an improvement in its operating efficiency with lower operating expenses (16.8% in FY2022

from 20.9% in FY2021) driven by the increasing scale and the high share of business sourced from the relatively low-cost banca channel. ICRA expects the company's return ratios to improve mainly due to the price revision of the loss-making PMJBY business and the high operating efficiency.

Credit challenges

Modest scale of operations; ability to maintain return ratios amid rising competition – SUD Life's operations remain modest with a marginal market share, in NBP terms, of 0.61% in FY2022 compared to 0.42% in FY2021. The rise in the market share was driven by the high year-on-year (YoY) growth of 65.5% in the NBP in FY2022, which was above the industry average. However, the company's ability to maintain high business growth with healthy return ratios in the wake of rising competition and ever-evolving regulatory requirements remains a monitorable.

Ability to grow and maintain profitability in protection business – The share of the company's protection business remained marginal at 0.7% in FY2022 in individual APE terms. However, the share of the protection business on a gross premium written basis increased to 15.7% in FY2022 from 7.3% in FY2018. This was largely due to an increase in the group term business, which includes the PMJBY scheme. SUD Life's ability to increase the high-margin individual protection and group credit life businesses among intense competition remains a key rating sensitivity.

Liquidity position: Strong

SUD Life reported liquid assets of Rs. 11,063 crore (calculated as liquid investments², adjusted for haircuts and cash & bank balance) as on March 31, 2022. In FY2021, the actual benefits/claims paid were Rs. 1,680 crore, amounting to 15.0% of the policy and linked liabilities as on March 31, 2021 (policy and linked liabilities were Rs. 11,188 crore as of March 31, 2021). The nearest debt repayment is the Rs. 9.7-crore coupon payment for the subordinated debt programme, which is due on November 24, 2022. The principal of the subordinated debt programme of Rs. 125 crore is due on November 24, 2031. However, SUD Life has a call option, which is exercisable five years from the date of allotment on November 24, 2026 and at the end of every year thereafter before the redemption date. ICRA does not foresee any liquidity risk in the near term.

Rating sensitivities

Positive factors – The rating could be revised if there is a change in the credit profile of the promoters or a substantial and sustained improvement in the company's market share and profitability, leading to an improvement in its financial risk profile.

Negative factors – The outlook or the rating could be revised if there is a weakening in the credit profile of the promoters, a significant change in the company's shareholding or in its linkages with the parents. Pressure could also arise if the company's solvency ratio deteriorates to less than 1.60 times on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Issuer Rating Methodology for Life Insurance Companies Methodology for Rating Hybrid Debt Instruments Issued by Insurance Companies Impact of Parent or Group Support on an Issuer's Credit Rating
Parent/Group support	Parent/Investor: BOI, UBI and Dai-ichi Life International Holdings LLC ICRA factors in the company's strong promoter profile comprising Dai-ichi Life (equity stake of 45.94%), BOI (28.96%) and UBI (25.10%). The rating also factors in the track record of capital and strategic support from the promoters along with operational support from the parent banks.
Consolidation/Standalone	The rating is based on the standalone financial statements of the issuer.

² Excluding linked investments

About the company

SUD Life is a joint venture between BOI (28.96% as on March 31, 2022), UBI (25.10%) and Dai-ichi Life (45.94%). The company was incorporated in September 2007 and began operations in February 2009. BOI and UBI are public sector banks with established track records. Established in 1902, Dai-ichi Life is one of the major life insurance companies in Japan.

SUD Life's life insurance business consists of the Participating Life (Individual), Non-participating Life (Individual and Group), Annuity (Individual and Group), Pension Individual, Health Individual and Unit Linked Life (Individual & Group) and Pension segments. SUD Life operates through a network of ~14,000 bank branches catering to more than 9.2 million customers.

Key financial indicators (audited)

Star Union Dai-ichi Life Insurance Company Limited	FY2020	FY2021	FY2022
Gross direct premium	2,314	2,999	4,137
Income from investment and fees	383	1,459	1,243
Total operating expenses*	598	625	695
PAT	59	65	23
Total net worth	657	720	736
Total policyholders' + shareholders' investments@	7,096	9,135	11,825
Total expense ratio (including commission expense)	25.9%	20.9%	16.8%
Return on equity	9.0%	9.1%	3.1%
13th month persistency ratio^	74.6%	74.0%	72.7%
61st month persistency ratio^	32.2%	32.1%	30.8%
Regulatory solvency ratio (times)	2.40	2.06	2.00

Source: Company, ICRA Research; Amount in Rs. crore

* Total operating expenses include commission expenses and provision for diminution in value of investments

@ Investments exclude linked investments

^ The 13th and 61st month persistency ratios for FY2021 and FY2022 are based on regular premium/limited premium payments under individual category while the data for FY2019 and FY2020 are on original premium basis

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

Instrument	Type	Current Rating (FY2023)		Chronology of Rating History for the Past 3 Years			
		Amount Rated (Rs. crore)	Amount Outstanding as of Jul 26, 2022 (Rs. crore)	Date & Rating in FY2023	Date & Rating in FY2022	Date & Rating in FY2021	Date & Rating in FY2020
				Aug 01, 2022	Aug 03, 2021	-	-
1 Subordinated debt programme	Long term	125.0	125.0	[ICRA]AA(Stable)	[ICRA]AA(Stable)	-	-

Complexity level of the rated instruments

Instrument	Complexity Indicator
Subordinated Debt Programme	Moderately Complex

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analysing an entity's financial, business, industry risks or

complexity related to the structural, transactional or legal aspects. Details on the complexity levels of the instruments are available on ICRA's website: www.icra.in

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
INE503V08016	Subordinated debt programme	Nov-24-2021	7.75%	Nov-24-2031*	125.00	[ICRA]AA(Stable)

Source: Company, ICRA Research

* The company has a call option, which is exercisable five years from the date of allotment on November 24, 2026 and at the end of every year thereafter before the redemption date

Annexure II: List of entities considered for consolidated analysis: Not applicable

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Branches



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