April 28, 2023

Cholamandalam MS General 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	100.00	100.00	[ICRA]AA (Stable); reaffirmed
Subordinated debt programme	100.00	-	[ICRA]AA (Stable); reaffirmed and withdrawn
Total	**200.00**	**100.00**	

**Instrument details are provided in Annexure I*

Rationale

The rating factors in Cholamandalam MS General Insurance Company Limited's (CMICL) parentage, with Cholamandalam Financial Holdings Limited (CFHL; part of Murugappa Group) and Mitsui Sumitomo Insurance Company Limited (MSI; rated A1/A3[hyb]/Stable by Moody's) holding equity stakes of 60% and 40%, respectively, and their demonstrated operational, managerial and financial support to CMICL. The rating considers the joint venture partners' representation on CMICL's board of directors and the shared brand name, which further strengthens ICRA's expectation of adequate and timely capital support to the company. The rating also considers the company's established position in the motor segment (5.3% market share in 9M FY2023), improving investment float through a high share of long-term policies driven by the motor third-party (Motor-TP) segment. CMICL's solvency of 2.06x, with an adequate cushion over and above the regulatory requirements, is expected to support the growth in the medium term.

The rating is, however, constrained by the moderate profitability with the underwriting losses largely due to higher management expenses compared to peers. Moreover, the profitability is supported by investment income. The rating also takes into consideration CMICL's concentration in the motor segment, which accounted for 69% of its gross direct premium income (GDPI) in 9M FY2023. Over the medium term, the company's ability to diversify its product mix and improve its underwriting performance and operating efficiency would be critical for improving its earnings profile.

In line with its rating withdrawal policy, ICRA has reaffirmed and withdrawn its rating on CMICL's Rs. 100-crore subordinated debt programme as the same has been fully redeemed and there is no amount outstanding against the rated instrument.

Key rating drivers and their description

Credit strengths

Strong operational, managerial and financial support from shareholders – CMICL is owned by CFHL and MSI, holding 60% and 40% equity stakes, respectively. CFHL is a part of the Murugappa Group, a large business conglomerate with business interests in engineering, fertilisers, abrasives, sugar and financial services among others (key rated entities in the Group include Cholamandalam Investment and Finance Company Limited (rated [ICRA]AA+ (Stable)/[ICRA]A1+) and Tube Investments of India Limited {[ICRA]AA+ (Stable)/[ICRA]A1+)}. MSI, a subsidiary of Japan-based MS&AD Insurance Group Holdings Inc, has a strong global presence in the life and non-life insurance segments. CMICL derives support from the shareholders in the areas of sourcing, underwriting, reinsurance, product development, claims processing and internal controls. It also has adequate board representation with eight directors, of which three are from the Murugappa Group companies and two from the foreign shareholder, while the rest are independent directors.

The capital profile has improved over the last two-three years with a solvency of 2.06x as on December 31, 2022 from the low of 1.58x as on March 31, 2020. The improvement in the solvency was partly due to lower GDPI and lower claims in FY2021 and FY2022 with the impact of the Covid-19 pandemic. Further, despite the higher growth in 9M FY2023, the solvency improved due to the reduction in some of the disallowances in the available solvency margin. ICRA does not expect incremental capital requirement in the medium term for achieving the projected business growth. ICRA, however, expects capital support from the parent companies to be forthcoming, when required.

Established market position in motor segment, aided by wide distribution reach – CMICL benefits from the Murugappa Group's presence in the dealer location through the captive distribution company of the Group, which has ~550 branches in India, mostly in Tier-2/3 cities. The corporate agency channel (includes the captive distribution entities) contributed 33% to the GDPW in 9M FY2023. Other key distribution channels include brokers (40%) and bancassurance (21%). Aided by the recurring business sourced through these channels, the growth in the motor segment, which constitutes 69% of CMICL's business, was higher than the industry average with a market share of 5.3% in 9M FY2023 (4.9% in FY2022). While the share of motor in the product mix is expected to decline on account of diversification of the product line, it is likely to remain the dominant contributor in the medium term.

Credit challenges

Moderate profitability – CMICL's profitability remained moderate with a return on equity (RoE) of 7.3% in 9M FY2023 (3.9% in FY2022). While the company has been reporting underwriting losses, the net profitability is supported by investment income. The profitability was adversely impacted in FY2022 as the company fully provided the prepaid expenses balance of Rs. 326 crore (as on April 01, 2021) in FY2022 related to the acquisition cost of long-term policies. Despite this, the overall profitability was supported by the sizeable release of prior period provisions in the Motor-TP segment (Rs. 442 crore in FY2022). This also supported the lower loss ratio in the Motor-TP segment in FY2022. The company's overall loss ratio increased to 75.2% in 9M FY2023 (65.1% in FY2022) with a higher loss ratio in the motor segment as vehicle movement normalised after the lockdowns in the preceding years.

The management expenses ratio continues to remain high (~37% of net premium written in FY2023) with the increase in the share of multi-year policies, where expenses are upfronted but premium income is amortised over the policy life. Premium income from multi-year polices accounted for ~11% of GDPI in 9M FY2023. CMICL's overall combined ratio was weak at 111.4% in 9M FY2023 (111.0% in FY2022). While an increase in multi-year policies results in elevated expenses in the first year, it improves the investment float and associated investment income. The company's investment leverage[1] stood at 6.6 times, as on December 31, 2022, higher than peers, and its net profitability is largely supported by investment income.

Given the recent revision in the regulatory guidelines for expenses, the company plans to reduce its expense ratio[2] to the specified regulatory level of 30% in the next three-year timeframe. This will be supported by the changes in the product mix as CMICL plans to re-enter certain bulk business segments, like the crop segment, and increase the share of commercial business, which has a lower acquisition cost. The impact of this regulatory change on profitability will remain a key monitorable.

CMICL had contingent liabilities of Rs. 410 crore as on December 31, 2022, for which it has deposited Rs. 70 crore with the Income Tax (I-T) Department. ICRA takes cognizance of the relatively high level of contingent liabilities (~20% of net worth as on December 31, 2022), though the same has declined from ~29% as on March 31, 2022 with the resolution of some of the liabilities. The contingent liability is due to the income tax demand pertaining to the incurred but not reported (IBNR) reserve. These matters are currently pending before the tax authorities. The crystallisation of such liabilities would further constrain the profitability and solvency and would be a key rating monitorable.

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[1] *Investment leverage = (Total investment – sub-debt)/Net worth)*

[2] *Management expenses + Direct claims paid as a % of GDPI*

Limited presence in product segments, barring motor – CMICL faces stiff competition from private as well as public sector general insurance companies in India. While its market share in the motor segment stood at 5.3% in 9M FY2023, its presence in other segments remained limited. CMICL is consciously looking to improve its presence in segments such as small and medium enterprises (through fire and property insurance products), health and personal accident among others. Further, within motor, the company has diversified into two-wheelers and private cars (21% and 36%, respectively, of the motor segment GDPI in 9M FY2023). Within commercial vehicles (CVs), CMICL has increased the share of insurance business from lower tonnage CVs (3,500 cc CV plying within town limits) and businesses like construction equipment, tractor, school buses, which typically have lower loss ratios. CMICL's ability to grow its market share in other segments and improve its profitability amid rising competition is to be seen.

High share of long-tail business exposes the company to reserving risks – The major risk faced by an insurance company is the underwriting of business at an adequate premium pricing. The uncertainty regarding the extent of claims is relatively higher in the Motor-TP segment, which is long-tail in nature and accounted for 43-47% of CMICL's total GDPI in the last few years. While the company's loss reserving for the long-tail business has been prudent in the past, however given the high share of long-tail business, the adequacy of the existing provisions for future claims in long-tail businesses remains a key risk and could adversely impact future profitability and capital if the claims turn out to be higher than the existing provisions.

Liquidity position: Strong

The company's net premium was Rs. 3,572 crore in FY2022 in relation to the maximum net claims paid of Rs. 1,874 crore in the last few years. For 9M FY2023, the net premium stood at Rs. 3,289 crore against net claims paid of Rs. 1,340 crore. CMICL had investments in Central/state government securities, accounting for 66% of the total investments or Rs. 9,290 crore as on December 31, 2022, further supporting the liquidity to meet the claims of policyholders. The company's shareholders' investment of Rs. 1,768 crore remains strong in relation to Rs. 100-crore sub-debt outstanding as on December 31, 2022.

Rating sensitivities

Positive factors – The outlook or the rating could be revised if there is an improvement in the credit profile of the parents and a sustained improvement in CMICL's profitability along with an improvement in its market share.

Negative factors – The outlook or the rating could be revised in case of a material deterioration in the credit risk profile of the parents or a decline in the strategic importance of CMICL or in the expectation of support from the promoters or a change in the parentage. In addition, a decline in the company's solvency ratio below 1.60x on a sustained basis could lead to a rating downgrade.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	ICRA Policy on Withdrawal of Credit Ratings General insurance Implicit parent or group support
Parent/Group support	Parent/Investor: Murugappa Group and MSI The rating factors in the high likelihood of support from the Murugappa Group and MSI, given the shared brand name and representation on the board.
Consolidation/Standalone	The rating is based on the standalone financial statements of the issuer.

About the company

Cholamandalam MS General Insurance Company Limited (CMICL) is a joint venture between CFHL (part of the Murugappa Group) and MSI, which raised its stake in CMICL to 40% in FY2016 (from 26%) after the regulator allowed maximum foreign ownership of 49% in domestic insurance companies. CMICL offers a wide range of products, including motor, accident, engineering, health, liability, marine, property, travel and rural insurance, and caters to individuals as well as corporates. The company has a network of over 153 branches across the country, with its head office in Chennai.

Key financial indicators

	FY2021	FY2022	9M FY2022	9M FY2023
Gross direct premium income	4,388	4,824	3,442	4,389
Total underwriting surplus / (shortfall)	(287)	(433)	(315)	(475)
Total investment + Trading income	804	799	605	657
PAT	282	77	62	116
Total net worth[3]	1,885	1,962	1,946	2,078
Total technical reserves	8,824	9,501	9,212	10,609
Total investment portfolio	11,061	12,534	12,042	14,016
Total assets	12,509	13,716	13,315	15,340
Return on equity (%)	14.7%	3.9%	4.2%	7.3%
Gearing (times)	0.05	0.05	0.05	0.05
Combined ratio*	107.3%	111.0%	113.0%	111.4%
Regulatory solvency ratio (times)	2.08	1.95	1.86	2.06

Source: Company, ICRA Research; All ratios as per ICRA's calculations; Amount in Rs. crore
** Combined ratio – (net claims incurred/net premium earned) + (management expenses + net commission expenses)/net premium written)*
The figures for FY2021 and FY2022 are audited while those for 9M FY2022 and 9M FY2023 are unaudited

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2024)				Chronology of Rating History for the Past 3 Years		
		Type	Amount Rated (Rs. crore)	Amount Outstanding as on Apr 28, 2023 (Rs. crore)	Date & Rating in FY2024	Date & Rating in FY2023	Date & Rating in FY2022	Date & Rating in FY2021
					Apr 28, 2023	May 23, 2022	Sep 08, 2021	Sep 17, 2020
1	Subordinated debt programme	Long Term	100.00	-	[ICRA]AA (Stable); withdrawn	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)
2	Subordinated debt programme	Long Term	100.00	100.00	[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

[3] *Excluding fair value change account*

complexity related to the structural, transactional or legal aspects. Details on the complexity levels of the instruments are available on ICRA's website: [Click Here]

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
INE439H08012	**Subordinated debt programme**	May 25, 2017	8.75%	May 25, 2027^	100.00	[ICRA]AA (Stable); withdrawn
INE439H08020	**Subordinated debt programme**	June 02, 2022	8.47%	June 02, 2032*	100.00	[ICRA]AA (Stable)

*Source: Company; *Call option exercisable at the end of five years from deemed date of allotment and every coupon payment thereafter; ^As on May 25, 2022, CMICL exercised Call option.*

Key features of rated debt instrument

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 regulator[4]

» If the interest payouts lead to a net loss or an increase in the net loss, prior approval of the regulator would be required to service the debt

Annexure II: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
Not Applicable	Not Applicable	Not Applicable

[4] *As per IRDAI regulations, insurers are required to maintain a minimum solvency ratio of 150%*

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Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.

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