October 14, 2020

ICICI Prudential Life Insurance Company Limited: [ICRA]AAA(Stable) assigned to subordinated debt programme

Summary of rating action

Instrument*	Current Rated Amount (Rs. crore)	Rating Action
Subordinated debt programme	1,200.00	[ICRA]AAA(Stable); assigned
Total	**1,200.00**	

**Instrument details are provided in Annexure-1*

Rationale

ICRA has assigned a long-term rating of [ICRA]AAA (pronounced as ICRA triple A) to the subordinated debt programme of ICICI Prudential Life Insurance Company Limited (ICICI Pru). The outlook on the long-term rating is Stable. The rating takes into account the strong support from ICICI Pru's sponsors, ICICI Bank Limited (rated [ICRA]AAA(Stable)) and Prudential Corporation Holdings Limited (rated A2 with a Negative outlook by Moody's), its position as one of the largest private sector life insurers in the country based on new business premium, its strong bancassurance channel, robust underwriting performance with increasing focus on the protection business and comfortable solvency levels.

ICRA notes the slowdown in the company's savings business due to the dominance of the large-ticket unit-linked insurance plan (ULIP) business in its product mix, which is more susceptible to market volatility. ICRA also notes the slowdown in business growth due to the Covid-19-related lockdown. ICICI Pru's ability to comply with regulatory changes while maintaining its growth and profitability targets will remain a key monitorable. Going forward, the increasing focus on improving the protection mix and diversifying into the mass affluent and mass customer segments is expected to reduce the company's vulnerability to weak market conditions. ICRA also notes the impact of the Covid-19 pandemic on the business growth during the lockdown period. In addition, the company is likely to experience higher death claims due to the pandemic.

Key rating drivers and their description

Credit strengths

Strong promoter profiles – ICICI Bank and Prudential Corporation Holdings Limited (Prudential) held 51.37% and 22.11%, respectively, in ICICI Pru as on June 30, 2020. The majority shareholder, ICICI Bank, is one of the largest private sector banks in India with a network of 5,324 branches across the country. It is also the exclusive bancassurance partner of ICICI Pru, which provides the company with a wide reach as well as cost efficiency. ICICI Bank also has a strong brand image and capital market position, which are leveraged by ICICI Pru in terms of a shared brand name. The foreign partner, Prudential (part of Prudential Plc group), is an Asia-led portfolio of businesses focused on structural growth markets.

Leading player in retail segment among private peers with increasing focus on protection products – ICICI Pru is one of the biggest life insurers in the country with a retail weighted received premium (RWRP)[1] market share of 15.8% in the private sector in FY2020. However, this reduced from 17.7% in FY2019, predominantly due to a slowdown in the ULIP

[1] *Calculated as the sum of individual non-single premium and 10% of individual single premium*

business (64.7% of the annual premium equivalent (APE) in FY2020) on account of the volatile market conditions, which impacted the growth in the savings business. This was largely due to the deferral of investments in large-ticket ULIPs by the affluent customer segment as they are more responsive to market developments compared to lower income groups.

ICRA notes ICICI Pru's efforts to diversify its customer base in the mass affluent and mass customer segments. Retail formed 88% of the company's total gross premium in FY2020. The company's RWRP recorded a CAGR of 17.5% during FY2015 to FY2018 although it fell by 4.91% YoY and 6.4% YoY in FY2019 and FY2020, respectively. The company's successful tie-up with ICICI Bank helps it maintain a strong foothold in the retail segment. ICICI Pru is also increasing its focus on protection products (54.6% growth in APE in FY2020). While ICRA notes the capital-intensive nature of protection products in the initial years, the overall profitability is higher in the product life cycle and will help the value of new business (VNB) margin[2] going forward. ICRA expects the recovery in growth to be slow in FY2021 due to the impact of the lockdown.

Strong bancassurance channel – ICICI Pru capitalises the extensive reach of ICICI Bank, which has an exclusive tie-up with the company for the sale of life insurance products. In FY2020, the share of bancassurance distribution was 50.8% (55.8% in FY2019) of the total APE, which predominantly includes contributions from ICICI Bank. Standard Chartered Bank is another significant partner in the bancassurance channel and ICICI Pru has tie-ups with a few other banks as well. The company plans to tap this channel further by activating more bank branches, along with agency and broker channels, to increase its reach in the mass affluent segment. However, the share of bancassurance has been reducing, given the company's strategy of developing a diversified multi-channel distribution architecture. This also mirrors the trend seen in the ULIP mix as the bulk of the business sourced by bancassurance has been ULIP.

Comfortable capitalisation – ICICI Pru's solvency stood at 205% as on June 30, 2020 (194% as on March 31, 2020) compared to the minimum regulatory requirement of 150%. The solvency ratio is comfortable to support growth at the current level in the medium term. However, ICRA notes the high dividend payout ratio compared to the company's large peers. In case of sustained aggressive growth in the protection business, the capitalisation may be supported by a reduction in the dividend payouts or the raising of subordinated debt, along with internal accruals.

Healthy profitability – The company has been consistent in posting sustainable profits over the past few years. ICICI Pru's return on equity (RoE) was 14.7% in Q1 FY2021 (14.8% in FY2020), down from 15.6% in Q1 FY2020 (16.2% in FY2019). The decline was primarily due to the increase in the net benefits paid in FY2020 because of the higher claims by surrender of policies. Nevertheless, the profitability remains healthy aided by the control of operating expenses (operating expense ratio of 13.9% in Q1 FY2021 and 14.4% in FY2020), low tax outgo and strong persistency levels (13-month persistency of 86.8% and 61-month persistency of 58.7% in FY2020). However, the persistency levels were impacted in Q1 FY2021 due to the Covid-19 pandemic and the volatile capital markets. Further, as the company is in a growth phase, the growth in its profit after tax (PAT) is expected to remain flat in the shorter term due to the strain on underwriting new business, more so for protection products than for savings products.

The VNB margin, which is a better profitability indicator in the life insurance business, improved to 24.4% in Q1 FY2021 and 21.7% in FY2020 from 17.0% in FY2019. This is due to the margin-accretive nature of the expanding protection business. Hence, a decline in profits is not seen as a matter of significant concern while a growth in the VNB would translate into profits in future. The company has provided guidance regarding its intention to double the VNB as of FY2019 over the next 3-4 years. This would require a CAGR of 18.9-26.0% in the VNB during this period. In FY2020, the VNB grew by 20.9% on a YoY basis while it degrew by 35.0% in Q1 FY2021 due to the pandemic and the volatile capital

[2] *VNB/APE*

markets. The company is on track to achieve the targeted VNB though the impact of lower sales in Q1 FY2021 on the VNB growth remains to be seen.

Credit challenges

Ability to grow and maintain profitability in protection business – The company needs higher growth in its protection portfolio for attaining significant value accretion as it already has a lean cost structure. The business has shown strong growth in the last few years though it is expected to moderate in the medium term. The protection business, which formed 15.1% of the APE in FY2020 (26.0% in Q1 FY2021; improved because of significant degrowth in linked business), has low adoption in the country compared to savings. However, improving customer awareness is expected to expand the market. Hence, ICICI Pru's ability to scale up the portfolio to a sizeable proportion in a small market, while maintaining the product pricing and death claims settlement ratio, is a key monitorable.

ULIPs susceptible to capital market movements – ICICI Pru's product mix continues to be dominated by ULIPs, although the same moderated to 64.7% of the APE in FY2020. However, due to the volatile capital markets in March 2020 and Q1 FY2021, the company saw significant degrowth in its linked business, resulting in a decline in the share of ULIP to 43.6% of the APE in Q1 FY2021. This makes the company's operations more vulnerable to the vagaries of the capital market. Although the business has a lower capital requirement, its low-margin nature necessitates an improvement in the persistency levels and cost control. In FY2020 and Q1 FY2021, ICICI Pru continued to see a decrease in new business and lower growth in renewal premium in the ULIP segment. However, ICRA notes that the company has taken steps to diversify into the mass affluent segment, which has relatively stable investment patterns even in volatile market conditions. The existing customer mix largely comprises the affluent segment, with less granularity. The increasing focus on the protection business and foray into other customer segments are expected to reduce the impact of volatile market conditions, going forward. Maintaining growth resilience in a capital market downcycle would be a key point to monitor.

Maintaining profitable growth amid evolving industry challenges and regulations – The insurance industry in India is highly regulated with frequent large-impact regulations. The recent change in tax laws with no tax savings in the new tax regime partly reduces the customer base for the purchase of insurance products. However, the benefits of switching to the new tax regime are low for high salaried individuals. Since ICICI Pru has a relatively higher average ticket size per policy, the actual impact on sales is not expected to be significant.

Liquidity position: Strong

The company had a liquidity buffer of Rs. 1,49,377 crore (calculated as liquid investments, adjusted for haircuts and stressed investments and cash & bank balance) as of June 30, 2020. In FY2020, actual benefits/claims paid stood at Rs. 19,377 crore, amounting to 12.8% of the policy and linked liabilities as on March 31, 2019 (policy and linked liabilities were Rs. 1,44,254 crore as of March 2020). ICICI Pru has no outstanding subordinated debt. ICRA does not foresee any liquidity risk in the near term.

Rating sensitivities

Positive triggers – Not applicable

Negative triggers – The rating could be revised if there is a deterioration in the credit risk profile of the parent company, ICICI Bank, a change in the parentage or a decline in the strategic importance of ICICI Pru to its promoter companies or a decline in the expectation of support from the promoters. Pressure could also arise if the company's solvency ratio deteriorates to less than 1.70 times on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	ICRA Policy on Rating Hybrid Instruments Issued by Insurance Companies
Parent/Group Support	Parent/Investor: ICICI Bank The rating considers the financial and management support received by ICICI Pru from its parent in the form of senior management and board representation. The rating also factors in the company's strong ability to leverage ICICI Bank's wide branch network for the distribution of insurance policies. ICRA notes the shared brand name and past capital support from the promoters, indicating implicit support from the parent.
Consolidation	For arriving at the rating, ICRA has used the consolidated financials of ICICI Pru. As on March 31, 2020, the company had one subsidiary, which is listed in Annexure-2.

About the company

ICICI Prudential Life Insurance Company Limited (ICICI Pru) is a joint venture between ICICI Bank, which is one of India's largest private sector banks in India and Prudential Corporation Holdings Limited (Prudential) – a leading international financial services group. ICICI Bank and Prudential held 51.37% and 22.11%, respectively, in ICICI Pru as on June 30, 2020, while the rest is publicly held. Incorporated in July 2000, the company provides life insurance, pensions and health insurance to individuals and groups. The products are offered under the participating, non-participating, non-participating variable and unit-linked lines of business. These are distributed through individual agents, corporate agents, banks, brokers, the company's proprietary sales force and its website. It has a national presence comprising ~517 branches and over 1.90 lakh agents as on March 31, 2020.

Key financial indicators (audited; consolidated)

	FY2019	FY2020	Q1 FY2021
Gross Direct Premium	30,930	33,431	5,747
Income from Investments and Fees	10,948	(11,773)	13,218
Total Expense including Commission	4,199	4,737	769
Benefits Paid	14,259	19,377	2,596
Net Change in Valuation of Liability in Respect of Life Policies / Increase in Reserves	21,159	(4,859)	14,928
PAT	1,139	1,067	287
Total Net Worth	7,042	7,213	7,788
Total Policyholders' + Shareholders' Investments (excluding assets held to cover linked liabilities)	48,057	54,167	58,255
Assets Held to Cover Linked Liabilities	1,10,946	97,085	1,10,251
Expense Ratio (opex / NPW)	13.7%	14.4%	13.9%
Commissions Ratio (commissions / NPW)	5.2%	4.8%	3.7%
Return on Equity	16.2%	14.8%	14.7%
13th Month Persistency Ratio	86.2%	86.8%	84.3%
61st Month Persistency Ratio	58.1%	58.7%	58.5%
Regulatory Solvency Ratio	2.15	1.94	2.05

Source: ICICI Pru public disclosure, ICRA research; Amounts in Rs. crore

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2021)				Rating History for the Past 3 Years		
		Type	Amount Rated	Amount Outstanding	14-Oct-20	FY2020	FY2019	FY2018
						NA	NA	NA
1	Subordinated Debt Programme	Long Term	1,200.00	-	[ICRA]AAA(Stable)	**NA**	**NA**	**NA**

Amount in Rs. crore

Complexity level of the rated instrument

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website www.icra.in

Annexure-1: Instrument details

ISIN	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
Not Yet Placed	Subordinated Debt Programme	NA	NA	NA	NA	[ICRA]AAA(Stable); assigned

Source: ICICI Pru

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
ICICI Prudential Pension Funds Management Company Limited	100%	Full consolidation

Source: ICICI Pru

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About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

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.

For more information, visit www.icra.in

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