

August 03, 2021

Star Union Dai-ichi Life Insurance Company Limited: [ICRA]AA(Stable) assigned

Summary of rating action

Instrument*	Current Rated Amount (Rs. crore)	Rating Action
Subordinated Debt Programme	125.00	[ICRA]AA(Stable); assigned
Total	125.00	

*Instrument details are provided in Annexure-1

Rationale

The assigned rating takes into account Star Union Dai-ichi Life Insurance Company Limited's (SUD Life) strong promoter profile, which enables capital, strategic, and operational support as and when required. SUD Life is a joint venture between Bank of India {BOI; rated MAA+ (Stable)} holding a 28.96% stake, Union Bank of India {UBI; rated [ICRA]AA+(hyb) (Negative)} holding a 25.10% stake and Dai-ichi Life International Holdings LLC (Dai-ichi Life) holding a 45.94% stake as on March 31, 2021. The importance of SUD Life to the promoters is demonstrated by their track record of equity infusion and their continued capital commitment. The rating also factors in the operational support in terms of access to the extensive branch network (~14,300) of the promoter banks. This enables SUD Life to leverage the bancassurance (banca) channel to source business at a relatively lower cost. The amalgamation of UBI, Andhra Bank and Corporation Bank provided SUD Life with access to ~6,700 additional branches to distribute its insurance products. SUD Life generates ~98-99% of its new business premium (NBP) through the banca channel with its promoter banks. In terms of strategic support, the company leverages the vast experience of Dai-ichi Life in the life insurance industry for new product approval and reinsurance arrangements, among others.

The rating considers the consistent net profits reported by the company from FY2015 with a net profit of Rs. 65.4 crore (return on equity (RoE) of 9.1%) in FY2021 compared to Rs. 59.2 crore (RoE of 9.0%) in FY2020. Supported by internal accruals, the company's solvency position remains strong and above peers at 2.06 times as on March 31, 2021 compared to the regulatory requirement of 1.50 times. However, SUD Life witnessed net Covid-19 claims of ~Rs. 40 crore (5.6% of net worth as on March 31, 2021) from 752 claims in Q1 FY2022 compared to ~Rs. 11 crore from 253 claims in FY2021. The impact of the Covid-19 pandemic on the company's profitability with increasing death claims would be a key monitorable.

The rating is partially offset by SUD Life's modest scale of operations with a market share of 0.80% in FY2021 in annualised premium equivalent (APE) terms. The company's ability to grow the business and maintain the return ratios amid rising competition remains a monitorable. Further, the share of the high-margin protection business remained low at 0.9% in FY2021 in individual APE terms while the loss-making portfolio of the Pradhan Mantri Jeevan Jyoti Bima Yojana (PMJJBY; 50% reinsured in FY2022) business is increasing as it is sourced from banks. However, the company plans to leverage its high customer base under the PMJJBY scheme to cross-sell other profitable products. Also, 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, 2021), UBI (25.10%) and Dai-ichi Life (45.94%). The company was incorporated in September 2007 and 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 as growth capital. As on April 1, 2020, Andhra Bank and Corporation Bank amalgamated with UBI, which increased UBI's branch network by ~6,700 branches. In terms of operational support, SUD Life has access to the wide branch network (~14,300) 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 ~98-99% of its NBP through the banca channel with its promoter banks. Due to the amalgamation of the banks, UBI held a stake in SUD Life and IndiaFirst Life Insurance Company Limited (IFLI) of 25.1% and 30%, respectively, as on March 31, 2021. However, as per IRDAI regulations, a promoter is not allowed to hold more than a 10.0% stake in more than one insurance company. UBI is expected to pare down its stake in IFLI to less than 10.0% by March 2022.

Dai-ichi Life, which was established in 1902, is the second largest life insurance company in Japan and one of the top 10 life insurers globally. Dai-ichi Life's 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%, the scope for further capital support in SUD Life by Dai-ichi Life has opened up. 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 promoters' (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 – SUD Life's solvency position remained strong with a solvency ratio of 2.06 times as on March 31, 2021 compared to 2.40 times as on March 31, 2020. The company's solvency ratio was better compared to peers without any subordinated debt raise and remained above the regulatory requirement of 1.50 times. The strong solvency profile was largely supported by its healthy internal capital generation with RoE of 9.1% in FY2021. As per management, SUD Life expects business growth at a compound annual growth rate (CAGR) of ~25% in the next three years. However, it does not expect any capital requirement to achieve this growth, which will be funded through internal capital generation. The management is planning to raise Rs. 125 crore of subordinated debt, which is expected to improve the solvency ratio by around 0.28 times. ICRA believes that SUD Life would remain well capitalised with a strong solvency profile, going forward as well.

Consistent profitability with healthy return ratios – The efficient use of capital resulted in the company consistently reporting profits from FY2015. SUD Life's high value of new business (VNB) margin of more than 35% in the last few years was mainly supported by its product mix with the company consciously selling more non-participating (non-par) policies, which typically have higher margins compared to participating (PAR) and unit-linked insurance plan (ULIP) policies. As a result, the share of non-par products remained high at 74.7% in individual APE terms followed by ULIP (19.8%), PAR (4.6%) and protection (0.9%) in FY2021. The company had a high customer base of ~7 million under the PMJJBY scheme in FY2021, which is typically a loss-making portfolio. Its ability to leverage the PMJJBY customers to cross-sell other profitable products would be monitored.

SUD Life's profitability improved on the back of lower operating expenses (20.9% in FY2021 from 28.7% in FY2017). SUD Life's operating efficiency improved driven by the increasing scale and the high share of business sourced from the low-cost banca channel. The net benefit paid to net premium written (NPW) declined consistently to 39.4% in FY2021 from 76.3% in FY2017 supported by lower claims and healthy NPW growth. SUD Life reported net Covid claims of ~Rs. 40 crore (752 cases) or 5.6% of net worth as on March 31, 2021 in Q1 FY2022 compared to net Covid claims of ~Rs. 11 crore (253 cases) in FY2021. The impact of the pandemic on the company's profitability with rising death claims would be a key monitorable.

Improving persistency ratio – The company witnessed an improvement in the persistency ratio across all cohorts in FY2021. The 13th month persistency ratio increased to 78.1% in FY2021 from 74.6% in FY2020. The improvement was mainly driven by

the use of analytics, direct debit mandate, dedicated collection teams and key performance indicators for the sales team to improve persistency along with sourcing NBP. SUD Life's persistency levels largely remain in line with peers. The management expects that the 13th month persistency ratio will increase to ~80.0% in FY2022 with a 2-3% improvement in the 25th to 61st month cohorts in FY2022.

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 0.42% in FY2021 compared to 0.30% in FY2020. The rise in the market share was driven by the high YoY growth of 51% in the NBP in FY2021, 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 company's share of the protection business remained marginal at 0.9% in FY2021 in individual APE terms. However, the share of the protection business on a gross premium written basis increased to 13.7% in FY2021 from 7.7% in FY2017. The rise in the protection business' share was largely due to an increase in the group term business, which includes the PMJJBY scheme. The amalgamation of Andhra Bank and Corporation Bank with UBI as on April 1, 2020 provided the company with access to their huge customer base. SUD Life plans to cross-sell other profitable products to these customers (~7 million) to turn them into a profitable portfolio; this remains a monitorable. The company's ability to increase the high-margin individual protection and group credit life business among intense competition remains a key rating sensitivity.

Liquidity position: Strong

SUD Life reported liquid assets of Rs. 8,616 crore (calculated as liquid investments², adjusted for haircuts and cash & bank balance) as on March 31, 2021. In FY2021, the actual benefits/claims paid were Rs. 1,137 crore, amounting to 13.1% of the policy and linked liabilities as on March 31, 2020 (policy and linked liabilities were Rs. 8,694 crore as of March 31, 2020). SUD Life has no outstanding subordinated debt. 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 in case of a revision in the ratings of the parent companies, 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.

² Excluding linked investments

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 and UBI ICRA factors in the company's strong promoter profile comprising BOI (equity stake of 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.

About the company

SUD Life is a joint venture between BOI (28.96% as on March 31, 2021), 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 the second largest life insurance company in Japan and one of the top 10 life insurers globally.

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 ~14,300 bank branches catering to more than 9.2 million customers.

Key financial indicators (audited)

Star Union Dai-ichi Life Insurance Company Limited	FY2019	FY2020	FY2021
Gross Direct Premium	1,994	2,314	2,999
Income from Investment and Fees	713	383	1,459
Total Operating Expenses*	483	598	625
PAT	102	59	65
Total Net Worth	600	657	720
Total Policyholders' + Shareholders' Investments [@]	5,310	7,096	9,135
Total Expense Ratio (including commission expense)	24.2%	25.9%	20.9%
Return on Equity	16.9%	9.0%	9.1%
13th Month Persistency Ratio	74.2%	74.6%	78.1%
61st Month Persistency Ratio	53.1%	32.2%	43.1%
Regulatory Solvency Ratio (times)	2.53	2.40	2.06

Note: Amount in Rs. crore; All calculations are as per ICRA research

Source: Company, ICRA research

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

[@] Investments exclude linked investments

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2022)				Chronology of Rating History for the Past 3 Years		
		Type	Amount Rated (Rs. crore)	Amount Outstanding as of Jul 28, 2021 (Rs. crore)	Date & Rating in FY2022	Date & Rating in FY2021	Date & Rating in FY2020	Date & Rating in FY2019
1	Subordinated debt programme	Long term	125.0	-	Aug 03, 2021 [ICRA]AA(Stable); assigned	-	-	-

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-1: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Subordinated debt programme	NA	NA	NA	125.00^	[ICRA]AA(Stable)

^ Unplaced

Source: Company

Annexure-2: List of entities considered for consolidated analysis: Not applicable

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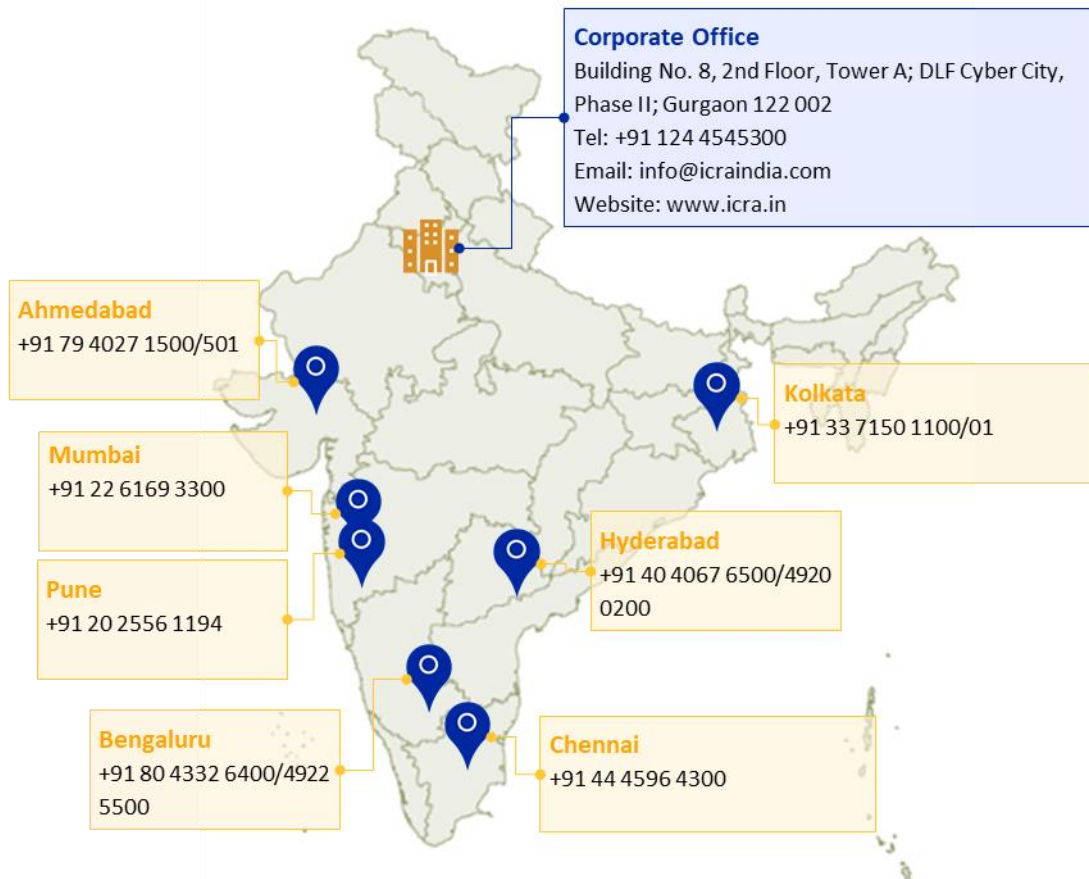
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