

October 22, 2021

HDFC Ergo General Insurance Company Limited: [ICRA]AAA(Stable) reaffirmed; and assigned to Rs. 375 crore subordinated debt programme

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Issuer Rating	-	-	[ICRA]AAA(Stable); reaffirmed
Subordinated Debt Programme	504.00	504.00	[ICRA]AAA(Stable); reaffirmed
Subordinated Debt Programme	-	375.00	[ICRA]AAA(Stable); assigned
Total	504.00	879.00	

*Instrument details are provided in Annexure-1

Rationale

The rating takes into account the parentage of HDFC Ergo General Insurance Company Limited (HEGI) with the largest stake (49.98%) held by HDFC Limited (HDFC; rated [ICRA]AAA(Stable)/[ICRA]A1+) and a combined stake of 48.99% held by ERGO International AG and Munich Health as on June 30, 2021. HDFC's largest shareholding, its representation on HEGI's board of directors and the presence of a shared brand name strengthen ICRA's belief that HEGI will receive capital support from the parent company as and when required. ICRA notes the moderation in the solvency profile (1.69 times as on June 30, 2021) amid the Covid-19 pandemic. However, ICRA notes the company's policy and track record of maintaining the solvency buffer above the regulatory minimum and expects capital support from the promoters to maintain the same. The rating also considers HEGI's healthy market share¹ (6.6% in FY2021) with a strong retail franchise and a diversified product portfolio and distribution network.

ICRA notes the moderating underwriting performance amid higher Covid claims, though the net profitability is expected to be supported by the healthy investment income. In the wake of the pandemic, ICRA expects the industry's (including HDFC Ergo) claims ratio to remain at an elevated level in FY2022, particularly in the health and travel insurance segments. The impact of the same on the company's premium growth and underwriting performance amid the changing industry dynamics would remain a key rating monitorable.

The credit rating also factors in the key features of the rated 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
- » In case 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

Key rating drivers and their description

Credit strengths

Strong parentage; experienced management team – Post the completion of the merger of HDFC Ergo Health Insurance (HEHI) with HEGI, HDFC holds a 49.98% stake (as on June 30, 2021) in HEGI while a 48.99% stake is held by ERGO and Munich Health.

¹Excluding Agriculture Insurance Company of India (AIC) and Export Credit Guarantee Corporation of India (ECGC)

The presence of a shared brand name strengthens ICRA's belief that HEGI will receive capital support from its parent companies as and when required. The company receives considerable support from HDFC and Munich Re (parent company of ERGO).

HEGI's operations are handled by a team of senior managers with considerable experience in the general insurance (GI) industry. ICRA expects HDFC to continue to exercise management control and support the business operations of HEGI as and when required. Going forward, the continued importance of the company to the parents and the capital and operational support received would be key rating sensitivities.

HDFC and ERGO have demonstrated their commitment to the business, infusing Rs. 551 crore in HEGI during FY2017-FY2021. ICRA notes that the additional headroom available for raising subordinated debt in the combined entity is Rs. 28 crore as on June 30, 2021. ICRA factors in the continued support from the promoters to keep the capitalisation well above the regulatory requirement. Going forward, the company's ability to keep its solvency levels well above the regulatory minimum while maintaining the growth momentum would remain a key monitorable.

Diversified product portfolio and distribution network – HEGI is the second largest health insurance company and the third largest private GI company with a market share² of 6.6% in FY2021. It has a diversified product profile with the health and personal accident segment forming 35% of the gross direct premium written (GDPW) in FY2021, followed by the motor segment (28%), crop segment (21%), fire (10%) and others (6%).

The company has developed a diversified distribution network, with brokers and direct business each contributing 28% to the total GDPW in FY2021. The commercial line of business is mainly sourced through the broker channel while the crop business is sourced directly by the company. Following its merger with the health insurance arm, which has a higher retail business, the share of agents in the total GDPW grew to 20% in FY2021 from 11% in FY2020; the company had about 1,47,000 agents as on June 30, 2021. The share of bancassurance remained at 13% in FY2021 for HEGI, comprising tie-ups with various banks and non-banking financial companies (NBFCs), including HDFC Bank, Deutsche Bank, SVC Co-operative Bank, Saraswat Bank, Lakshmi Vilas Bank, Federal Bank and L&T Finance Ltd.

Credit challenges

Moderate underwriting performance; profitability impacted by Covid claims – ICRA notes HEGI's consistent overall profitability, supported by investment income. The company reported a net profit of Rs. 592 crore in FY2021 supported by 27% growth in investment income³. The net profitability was also supported by the improvement in the underwriting performance. The combined ratio improved to 103% in FY2021 from 105% in FY2020 because of lower claims in the motor segment, given the lockdown restrictions. This led to lower underwriting losses (Rs. 235 crore in FY2021 compared to Rs. 343 crore in FY2020).

HEGI incurred a net loss of Rs. 36 crore in Q1 FY2022 because of higher underwriting losses of Rs. 324 crore. The combined ratio deteriorated to 125% in Q1 FY2022 due to higher claims in the health segment during the pandemic. HEGI incurred gross Covid claims of Rs. 657 crore in Q1 FY2022 compared to Rs. 615 crore in FY2021. The moderation in the profitability and the increase in the reserving requirement because of higher claims in Q1 FY2022 led to a deterioration in the solvency to 1.69 times as on June 30, 2021 from 1.90 times as on March 31, 2021. ICRA expects the industry's (including HEGI) claims ratio for the health segment to remain at an elevated level in FY2022 during the pandemic. The impact of the same on the underwriting performance and the capitalisation profile would remain a key rating monitorable.

High share of crop insurance, making the business vulnerable to the vagaries of the weather – HEGI continues to underwrite a significant proportion of the crop business. The gross direct premium (GDP) in the crop business contributed 21% to the overall GDPW in FY2021. While HEGI has a decade of experience in this business and a significant portion of the business (82%)

²Excluding Agriculture Insurance Company of India (AIC) and Export Credit Guarantee Corporation of India (ECGC)

³Excluding Profit on Sale and Terrorism Pool investment income

is reinsured, ICRA notes that the claims in this segment remain contingent on climatic conditions, which are unpredictable, thus posing a risk. The net claims ratio in the crop segment was 78% in FY2021 (87% in FY2020).

Liquidity position: Strong

The company had estimated liquid assets of Rs. 13,515 crore (sum of total investments less haircuts estimated by ICRA, plus cash and bank balances plus net due from insurance companies) as of June 30, 2021, against which it had total liability of Rs. 11,000 crore (total technical reserve plus debt due in the next one year). Gross claims paid, including reinsurance accepted in FY2021, stood at Rs. 6,232 crore, accounting for 59% of the liquid assets as on March 31, 2020. Moreover, the business generated in FY2022 would provide liquidity cushion. ICRA does not foresee any liquidity risk for the company in the near to medium term.

Rating sensitivities

Positive factors – Not applicable

Negative factors – The rating or outlook could be revised if there is a downward revision in the ratings of the promoter company (HDFC) or a decline in the strategic importance of HEGI to its promoter companies or a decline in the expectation of support from the promoters. In addition, a decline in the company's solvency ratio to less than 1.70 times on a sustained basis could lead to a rating downgrade.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	General Insurance Rating Approach - Hybrid Instruments Issued by Insurance Companies Implicit Parent or Group Support
Parent/Group Support	Parent/Investor: HDFC Limited ICRA factors in the implied support of the parent entity, HDFC Limited, and takes comfort from the experience of the management team in the insurance business. The capital ownership structure and shared branding provide comfort.
Consolidation/Standalone	Standalone

About the company

HDFC ERGO General Insurance Company Limited (HEGI) is a joint venture between HDFC Limited, India's premier housing finance institution (49.98% stake as on June 30, 2021) and ERGO International AG and Munich Health (combined stake of 48.99% as on June 30, 2021), while the balance is held by the employees of HEGI. The company offers a complete range of general insurance products including crop, motor, health, travel, home and personal accident insurance in the retail space and customised products like property, marine and liability insurance in the corporate space. HEGI has a presence across the country with 203 branch offices as on June 30, 2021.

Key financial indicators (audited)

HDFC Ergo	FY2019	FY2020	FY2021	Q1 FY2021	Q1 FY2022
Gross Direct Premium	8,613	9,630	12,295	1,984	2,386
Total Underwriting Surplus / (Shortfall)	(78)	(343)	(235)	71	(324)
Total Investment + Trading Income	732	878	1,140	274	297
PAT	383	327	592	235	(36)
Total Net Worth ⁴	1,955	2,768	3,254	3,045	3,268
Total Technical Reserves	6,400	8,983	10,430	9,252	11,000
Total Investment Portfolio	9,104	13,577	16,643	14,323	17,162
Total Assets	11,529	17,060	19,319	16,590	19,229
Return on Equity (%) ⁵	19.6%	11.8%	18.2%	30.9%	(4.3%)
Gearing (times)	0.18	0.15	0.15	0.17	0.15
Combined Ratio (%)	98.7%	105.3%	103.2%	103.5%	124.9%
Regulatory Solvency Ratio (times)	1.75	1.78	1.90	1.95	1.69

Source: Company, ICRA Research; All ratios as per ICRA calculations; Amount in Rs. crore

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years

Current Rating (FY2022)					Chronology of Rating History for the Past 3 Years		
Instrument	Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating in FY2022	Date & Rating in FY2021	Date & Rating in FY2020	Date & Rating in FY2019
				Oct 22, 2021	Feb 02, 2021	Jan 30, 2020	Dec 21, 2018
1 Issuer Rating	Long Term	-	-	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	-	-
2 Subordinated Debt Programme	Long Term	350.00	350.00	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)
3 Subordinated Debt Programme	Long Term	154.00	154.00	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	-	-
4 Subordinated Debt Programme	Long Term	375.00	375.00	[ICRA]AAA (Stable)	-	-	-

Complexity level of the rated instrument

Instrument	Complexity Indicator
Subordinated Debt Programme	Moderately Complex
Issuer Rating	Not Applicable

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

⁴Including fair value change account and reserve on amalgamation

⁵Calculated on closing net worth

Annexure-1: Instrument details

ISIN	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
INE092V08010	Subordinated debt programme	Sep 18, 2017	8.40%	Sep 17, 2027	80.00	[ICRA]AAA(Stable)
INE392I08011	Subordinated debt programme	Nov 09, 2016	7.60%	Nov 09, 2026	350.00	[ICRA]AAA(Stable)
INE092V08028	Subordinated debt programme	Sep 18, 2018	10.25%	Sep 18, 2028	74.00	[ICRA]AAA(Stable)
Not Yet Placed	Subordinated debt programme	NA	NA	NA	375.00	[ICRA]AAA(Stable)
NA	Issuer rating	NA	NA	NA	NA	[ICRA]AAA(Stable)

Source: Company

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
Not Applicable	Not Applicable	Not Applicable

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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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