

January 24, 2023

HDFC Ergo General Insurance Company Limited: Rating reaffirmed/assigned

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	-	300.00	[ICRA]AAA (Stable); assigned
Subordinated debt programme	375.00	375.00	[ICRA]AAA (Stable); reaffirmed
Subordinated debt programme	80.00	80.00	[ICRA]AAA (Stable); reaffirmed
Subordinated debt programme	74.00	74.00	[ICRA]AAA (Stable); reaffirmed
Subordinated debt programme	80.00	-	[ICRA]AAA (Stable); reaffirmed and withdrawn
Total	609.00	829.00	

*Instrument details are provided in Annexure I

Rationale

The rating considers the parentage of HDFC ERGO General Insurance Company Limited (HDFC ERGO) with the largest stake (49.98%) held by HDFC Limited (HDFC; rated [ICRA]AAA (Stable)/[ICRA]A1+) and a stake of 48.99% held by ERGO International AG (ERGO) as on September 30, 2022. The rating derives comfort from HDFC's large shareholding and its representation on HDFC ERGO's board of directors. Further, the presence of a shared brand name strengthens ICRA's belief that HDFC ERGO will receive capital support from both promoters as and when required. The rating also considers HDFC ERGO's healthy market share¹ (6.9% in H1 FY2023) with a strong retail franchise and a diversified product portfolio and distribution network.

While the solvency had reduced to 164% as on March 31, 2022, it improved to 178% as on September 30, 2022 compared to the minimum regulatory requirement of 150%. The solvency profile was supported by steady internal accruals and stable required solvency margin {RSM; +0.9% year-to-date (YTD)} and lower risk retention in H1 FY2023, especially in the corporate segment. 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.

In April 2022, HDFC had announced a scheme of amalgamation, whereby it would amalgamate with and into HDFC Bank Limited (HDFC Bank) subject to regulatory approvals. The amalgamation (HDFC and HDFC Bank) of the promoter entity and regulatory clarity on its stake in HDFC ERGO will remain key monitorables.

HDFC ERGO's profitability remains moderate with underwriting losses, supported by investment income. With the severity of Covid-19 infections receding, ICRA expects the company's net loss ratio in the health & personal accident segment to improve in FY2023.

ICRA has reaffirmed and withdrawn the rating outstanding of [ICRA]AAA (Stable) on the Rs. 80-crore subordinated debt programme as the company redeemed the rated bonds by exercising a call option and there is no amount outstanding against the same. The rating has been withdrawn in accordance with ICRA's policy on the withdrawal of credit ratings.

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

Key rating drivers and their description

Credit strengths

Strong parentage; experienced management team – HDFC is the largest shareholder in HDFC ERGO with a 49.98% stake as on September 30, 2022 followed by ERGO International AG (48.99%). The balance (1.03%) is held by the employees of the company. HDFC's stake was diluted from 50.56% as on March 31, 2021 due to the Reserve Bank of India's (RBI) direction to reduce its stake in HDFC ERGO to 50% or below. HDFC is a leading housing finance institution operating for more than 40 years in India. With a presence in banking, insurance and asset management, the HDFC Group is an important part of the Indian financial services sector. The shared brand name with HDFC and ERGO strengthens ICRA's belief that HDFC ERGO will receive capital support from its parent companies as and when required. HDFC ERGO's operations are handled by a team of senior managers with considerable experience in the general insurance (GI) industry.

In April 2022, HDFC announced a scheme of amalgamation, whereby it would amalgamate with and into HDFC Bank subject to regulatory approvals. HDFC Bank is the largest private bank in India. ICRA notes that as and when HDFC ERGO becomes a subsidiary of HDFC Bank (subject to regulatory approvals), any further capital infusion will require the RBI's approval. HDFC ERGO's capital-raising ability will be limited to a rights issue, an increase in the stake of other existing investors or the entry of new investors through a preferential allotment or a qualified institutional placement.

Diversified product portfolio and distribution network – HDFC ERGO is the second largest private GI company with a market share² of 6.9% in H1 FY2023. It has a diversified product profile with the health & personal accident segment forming 32.2% of the gross direct premium written (GDPI) in H1 FY2023, followed by the motor segment (25.5%), crop (21.5%), fire (12.5%), and others (8.3%). ICRA notes that the company has a considerable presence in the crop segment with a 20-24% share in the GDPI in the last few years.

HDFC ERGO has a diversified distribution network, with brokers and direct business contributing 32.9% and 31.4%, respectively, to the total GDPI in H1 FY2023. 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 GDPI grew to 17.6% in H1 FY2023 from 11.3% in FY2020. HDFC ERGO has one of the largest agency networks in the industry with an agent base of 1,35,830 as on September 30, 2022. It has tie-ups with various banks and non-banking financial companies (NBFCs), including HDFC Bank, Deutsche Bank, SVC Co-operative Bank, Saraswat Bank, Federal Bank and L&T Finance Ltd.

Credit challenges

Profitability impacted by underwriting losses – HDFC ERGO reported underwriting losses of Rs. 227.2 crore in H1 FY2023 (Rs. 567.8 crore in FY2022 and Rs. 235.0 crore in FY2021). It reported underwriting losses despite the retention ratio being lower than peers at ~51%. ICRA notes that the underwriting losses in FY2021 and FY2022 were partly due to the high share of the health & personal accident business in the GDPI, which was impacted due to Covid claims. The combined ratio improved to 103.5% in H1 FY2023 from 107.5% in FY2022 with the waning of the impact of Covid-19 as the claims ratio declined to 79.2% in H1 FY2023 from 84.0% in FY2022.

While the underwriting losses are offset by investment income, considering the company's lower retention ratio, the surplus for investment is lower. As a result, the company's profitability is moderate compared to peers (return on equity (RoE) of 14.0% and 18.2% in FY2022 and FY2021, respectively). The moderation in the profitability and the increase in the reserving requirement because of higher Covid claims in the last couple of years led to a moderation in the solvency to 164% as on March 31, 2022. Since then, the solvency has improved and it stood at 178% as on September 30, 2022. Further, HDFC ERGO has

² Excluding AIC and ECGC

headroom for raising additional sub-debt of ~Rs. 536 crore³, which could boost the solvency to ~204% on a proforma basis. It also has the option to reduce the dividend payout (Rs. 231.7 crore in FY2022 or 11 basis points (bps) of the reported solvency as on March 31, 2022). ICRA notes that the dividend payout is relatively higher than peers.

Liquidity position: Strong

The company's net premium was Rs. 7,107 crore in FY2022 in relation to the maximum net claims paid of Rs. 4,903 crore in the last few years. It had investments in Central/state government securities, accounting for 37% of the total investments or Rs. 7,429 crore as on September 30, 2022, which further supports the liquidity position to meet the claims of policyholders. HDFC ERGO's shareholders' investment of Rs. 4,059 crore remains strong in relation to sub-debt outstanding of Rs. 529 crore as on September 30, 2022.

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 HDFC ERGO 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	Rating Methodology for General Insurance Companies Impact of Parent or Group Support on an Issuer's Credit Rating Policy on Withdrawal of Credit Ratings
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 (HDFC ERGO) is a joint venture between HDFC Limited, India's premier housing finance institution (49.98% stake as on September 30, 2022) and ERGO International AG (48.99% stake), while the balance is held by the employees of HDFC ERGO. 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. HDFC ERGO has a presence across the country with 207 branch offices as on September 30, 2022.

³As per the revised regulation, whereby the threshold limit has been increased to 50% from 25% of the paid-up capital & share premium, subject to 50% of the company's net worth

Key financial indicators

HDFC Ergo General Insurance Company Limited	FY2021	FY2022	H1 FY2022	H1 FY2023
Gross direct premium	12,295	13,498	6,525	8,002
Total underwriting surplus / (shortfall)	(235)	(568)	(403)	(227)
Total investment + Trading income	1,152	1,297	629	694
PAT	592	500	153	321
Total net worth*	3,254	3,577	3,491	3,870
Total technical reserves	10,430	11,536	11,096	12,976
Total investment portfolio	16,643	18,397	17,155	19,874
Total assets	19,319	21,290	20,489	23,377
Return on equity	18.2%	14.0%	8.8%	16.6%
Gearing (times)	0.15	0.15	0.14	0.14
Combined ratio	103.2%	107.5%	113.0%	103.5%
Regulatory solvency ratio (times)	1.90	1.64	1.71	1.78

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

* Total net worth includes share capital, reserves & surplus and fair value change account; The figures for FY2021 and FY2022 are audited while H1 FY2022 and H1 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 (FY2023)				Chronology of Rating History for the Past 3 Years			
		Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating in FY2023		Date & Rating in FY2022	Date & Rating in FY2021	Date & Rating in FY2020
					Jan 24, 2023	Sep 07, 2022	Oct 22, 2021	Feb 02, 2021	Jan 30, 2020
1	Issuer Rating	Long term	-	-	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	-
2	Subordinated debt programme	Long term	74.00	74.00	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	-
3	Subordinated debt programme	Long term	375.00	375.00	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	-	-
4	Subordinated debt programme	Long term	80.00	80.00	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	-	-	-
5	Subordinated debt programme	Long term	300.00	-	[ICRA]AAA (Stable)	-	-	-	-
6	Subordinated debt programme	Long term	80.00	-	[ICRA]AAA (Stable); reaffirmed and withdrawn	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	-
7	Subordinated debt programme	Long term	-	-	-	[ICRA]AAA (Stable); reaffirmed and withdrawn	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)

Complexity level of the rated instruments

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: [Click Here](#)

Annexure I: 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); reaffirmed and withdrawn
INE092V08028	Subordinated debt programme	Sep 18, 2018	10.25%	Sep 18, 2028*	74.00	[ICRA]AAA (Stable)
INE225R08022	Subordinated debt programme	Sep 19, 2022	7.72%	Sep 19, 2032*	80.00	[ICRA]AAA (Stable)
INE225R08014	Subordinated debt programme	Nov 09, 2021	7.10%	Nov 09, 2031*	375.00	[ICRA]AAA (Stable)
Not yet placed	Subordinated debt programme	NA	NA	NA	300.00	[ICRA]AAA (Stable)
NA	Issuer Rating	NA	NA	NA	NA	[ICRA]AAA (Stable)

Source: Company; *The company has a call option, which is exercisable five years from the date of allotment

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 regulator⁴
- » 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 – Not applicable

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

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