RATING REPORT

Pakistan Reinsurance Company Limited

REPORT DATE:
December 19, 2019

RATING ANALYSTS:
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RATING DETAILS		
	Latest Rating	**Initial Rating**
Rating Category	**Long-Term**	**Long-term**
IFS	AA	AA
Rating Date	*December 19, 2019*	*October 12, 2018*
Rating Outlook	Stable	Stable

COMPANY INFORMATION	
Incorporated in 2000	**External auditors:** BDO Ebrahim & Co., Chartered Accountants
Public Limited Company	**Chairman of the Board:** Mr. Shahab Khawaja
Key Shareholder(s):	**Chief Executive Officer:** Mr. Mushtaq Ahmed Mahar (on deputation)
Secretary Ministry Of Commerce – 44.88%	
State Life Insurance Corporation – 24.41%	
PRCL Employees Empowerment Trust – 6.12%	
General Public – 13.26%	

APPLICABLE METHODOLOGY(IES)
VIS Entity Rating Criteria : General Insurance (November 2019) ***http://www.vis.com.pk/kc-meth.aspx***

OVERVIEW OF THE INSTITUTION

Pakistan Reinsurance Company Limited (PRCL) was incorporated as a public limited entity in March 2000. Majority shareholding of company lies with Government of Pakistan. It operates through its head office in Karachi and North Zonal Office in Lahore.

RATING RATIONALE

The rating draws comfort from the strong sponsorship of Government of Pakistan, directly and indirectly controlling 75% share. The assigned rating derives strength from improved underwriting performance of PRCL along with stable investment income. Sound capitalization indicators, high solvency level along with robust liquidity profile of the company remain key rating drivers. Leverage indicators of the company continue to remain within manageable levels.

Key Rating Drivers

Business volumes have remained a function of the growth in the insurance industry; the company focused aggressively on building its facultative business

By virtue of being the sole reinsurer in Pakistan, all insurance companies must offer at least 35% of their business to PRCL under treaty arrangements, whereby the company enjoys discretion for first right of refusal. Given the aggressive stance of the management over the past three years, PRCL negotiated higher shares in treaty arrangements with various insurance players. While PRCL's treaty business increased as a result of this strategy during 2018, facultative business grew at a faster pace. In FY18, proportion of facultative business improved to 78.1% vis-à-vis 58.1% in the previous corresponding period. Given the nature of facultative business, management was able to have a greater control on its underwriting operations vis-à-vis when writing business under treaties. The company posted total gross premium of Rs. 10.7b (FY17: Rs. 8.0b) during the outgoing year with growth in premiums for PRCL (33.4%) outpacing an industry growth of 9.5%. Premium base of PRCL amounted to Rs. 12.6b in 9M19; business in the last quarter is likely to be higher as aviation business is largely renewed in the last quarter of the year. Growth in industry premium may augment business volumes for PRCL, if the risk profile of ceded business remains within acceptable limits for the company.

Table 1: Business Mix

In Rs. Millions	2016	2017	2018	9M19
Fire	18.1%	19.4%	15.2%	12.1%
Marine Cargo	0.4%	0.6%	0.5%	0.3%
Marine Hull	1.3%	0.9%	0.9%	3.1%
Accident & Others	1.7%	1.9%	1.8%	1.6%
Aviation	13.2%	15.8%	13.1%	4.4%
Engineering	16.4%	19.5%	27.0%	46.4%
Treaty	49.0%	41.9%	41.6%	32.1%
Total Gross Premium	**8,806.7**	**8,035.6**	**10,734.5**	**12,596.1**

Underwriting operations of the company depicted improvement at the bottom line; claims and expense ratios remained within manageable limits in comparison to previous year's performance

Barring 2017, underwriting results of PRCL have historically depicted positive results at the bottom line. These profitability metrics were largely a function of controlled expenses and maintained loss ratios. The company experienced positive claims experience across all segments, excluding accident & health business; this segment is loss-making for majority of the insurance players and is primarily used as a cross-selling tool. Underwriting profit of the company amounted to Rs. 569.3m in 2018 vis-à-vis a loss of Rs. 741.2m in the previous year. The company's facultative business was profitable across all segments while treaty business continued to remain a loss-making segment for PRCL, during 2018. Underwriting profit improved significantly to Rs. 1.1b in the period ended September 30, 2019. Maintaining these profitability metrics will remain a key rating driver. With an improved claims ratio, combined ratio of the company remained below 100% mark and compares favorably to peers.

Table 2: Underwriting Profit (Loss)

In Rs. Millions	2016	2017	2018	9M19
Fire	401.5	(7.7)	276.0	373.7
Marine Cargo	4.3	3.0	8.8	40.1
Marine Hull	19.3	(28.1)	15.2	67.0
Accident & Others	16.8	81.5	41.3	111.8
Aviation	48.6	(76.6)	92.8	(337.6)
Engineering	236.7	(213.6)	370.6	1,408.2
Treaty	(236.3)	(499.9)	(235.5)	(497.5)
Total Underwriting Profit	**491.0**	**(741.2)**	**569.3**	**1,165.7**

Table 3: Profitability Metrics

	2016	2017	2018	9M19
Gross Claims Ratio (%)	57.8%	62.6%	25.6%	79.5%
Net Claims Ratio (%)	57.5%	74.7%	54.8%	55.0%
Underwriting Expense Ratio (%)	34.0%	40.1%	34.8%	27.2%
Combined Ratio (%)	91.5%	114.8%	89.6%	82.2%

Reinsurance panel of the company depicted significant changes with addition of various international reinsurers; retrocession levels was reported higher in comparison to its historical 5 year average

Given aggressive stance of the management, PRCL further diversified shares in its reinsurance panel with mostly 'A' and above rated companies; Hannover Ruck SE, Germany enjoys the lead share in fire and engineering segments while cover for marine is mainly provided by Korean Reinsurance Company. Treaty capacities have increased in major segments. Maximum retention on net account in relation to equity remained within manageable levels.

Table 4: Cession Ratio

	2016	2017	2018	9M19
Fire	27.8%	26.7%	21.4%	30.9%
Marine Cargo	0.0%	0.0%	0.0%	0.0%
Marine Hull	54.6%	50.5%	50.4%	62.9%
Accident & Others	2.3%	5.4%	2.5%	3.2%
Aviation	86.9%	91.7%	84.0%	72.9%
Engineering	69.5%	72.0%	83.4%	89.1%
Treaty	10.0%	17.6%	16.7%	12.0%
Overall Cession	33.5%	41.7%	44.2%	54.1%

Risk adjusted capitalization levels of the institution are considered sound in view of healthy capital coverage of claims and strong leverage indicators; liquidity indicators remain sufficient to meet underwriting liabilities

Insurance debt as a proportion of gross premiums remains on the higher side at 50.6% (FY17: 53.6%), at end-December 2018, s sizeable proportion of business is underwritten during the last month of the year. However, aging profile of insurance debt is considered satisfactory. Equity base of the company decreased to Rs. 9.9b (2017: Rs. 10.5b) on account of lower surplus on investments, at end-December 2018; the same increased to Rs. 10.2b at end-9M19. Given the size of the equity base, leverage indicators compare favorably to peers.

Table 5: Capitalization and Liquidity Indicators

In Rs. Millions	**2016**	**2017**	**2018**	**9M19**
Net Worth	12,316.2	10,506.0	9,871.5	10,179.0
Operating Leverage (%)	42.1%	41.7%	49.7%	77.5%
Financial Leverage (%)	48.9%	58.2%	61.6%	87.5%

The company maintains a healthy investment portfolio; support for underwriting operations from investments remains strong

Investment portfolio has grown over the years, translating into healthy investment income for the company. However, investment portfolio of the company was revised in the back drop of interest rate scenario and downward trajectory in the stock market. Given the downtick in the equities market, the company revised its exposure in listed equities by reducing its proportion from 66.0% at end-2016 to 48.2% at end-2018 in the overall portfolio. Remaining exposure is mostly deployed in government paper. Both credit and market risk arising from the portfolio is considered manageable.

Table 6: Investment Portfolio

In Rs. Millions	**2016**	**2017**	**2018**	**9M19**
Listed Equities	8,829.52	5,006.81	4,163.30	3,188.15
Government Securities	4,106.04	4,185.86	4,470.40	4,457.01
Term Deposit Receipts	440.00	30.00	-	-
Total	**13,375.56**	**9,222.67**	**8,633.70**	**7,645.16**

The company also owns a building property which is valued at Rs. 1.1b at end-September 2019. Rental income earned amounted to Rs. 62.3m (FY17: Rs. 56.3m) in FY18. As a result of significant support from investments, net operating ratio of the company improved from 97.0% in 2017 to 78.7% in 2018.

Senior management remained stable while there was a change at the helm of the organization

During the years, management addressed significant gaps in the senior management cadres, which is considered important from a rating perspective. However, there was a change in the senior management team with resignation of CEO. An acting CEO, Mr. Mushtaq Ahmed Mahar was deputed by the government till a permanent resource is hired. Timely appointment of key executives is considered essential from a governance perspective as also the future business strategy.

Pakistan Reinsurance Company Limited — Appendix I

FINANCIAL SUMMARY				*(amounts in PKR millions)*
BALANCE SHEET	**DEC 31, 2016**	**DEC 31, 2017**	**DEC 31, 2018**	**SEP 30, 2019**
Cash and Bank Deposits	2,240.0	2,517.1	2,602.5	2,770.2
Investments	13,375.6	9,222.7	8,633.7	7,538.2
Investment Properties	31.4	29.8	28.3	27.2
Insurance Debt	4,545.1	4,304.8	5,435.8	9,050.2
Total Assets	25,983.6	24,341.6	24,830.9	32,408.5
Paid Up Capital	3,000.0	3,000.0	3,000.0	3,000.0
Net Worth	12,316.2	10,506.0	9,871.5	10,179.0
Underwriting Liabilities	8,489.7	8,855.0	9,236.0	14,890.3
INCOME STATEMENT				
Net Premium Revenue	5,801.8	5,006.4	5,463.6	6,562.0
Net Claims	3,335.6	3,740.0	2,991.8	3,609.5
Expenses	1,921.6	1,943.3	1,891.2	1,779.9
General & Administrative Expenses	53.7	64.3	11.4	6.9
Underwriting Profit/(Loss)	491.0	(741.2)	569.3	1,165.7
Investment Income	961.2	3,325.9	691.0	391.1
Recurring Investment Income	923.0	890.6	592.5	378.3
Rental Income	55.8	56.3	62.3	52.4
Exchange Gain	(0.7)	102.9	415.1	
Profit Before Tax	1,426.9	2,875.8	1,739.9	2,252.8
Profit After Tax	974.3	2,226.3	1,235.3	1,549.5
RATIO ANALYSIS				
Retrocession Ratio	33.5%	41.7%	44.2%	54.1%
Gross Claims Ratio	57.8%	62.6%	25.6%	79.5%
Net Claims Ratio	57.5%	74.7%	54.8%	55.0%
Underwriting Expense Ratio	34.0%	40.1%	34.8%	27.2%
Combined Ratio	91.5%	114.8%	89.6%	82.2%
Net Operating Ratio	75.6%	97.0%	78.7%	76.5%
Insurance Debt to Gross Premium	51.6%	53.6%	50.6%	53.9%
Operating Leverage	42.1%	41.7%	49.7%	77.5%
Financial Leverage	48.9%	58.2%	61.6%	87.5%
Adjusted Liquid Assets to Technical Reserves	3.40x	1.97x	1.73x	1.73x

ISSUE/ISSUER RATING SCALE & DEFINITIONS Appendix II

RATING SCALE & DEFINITIONS: INSURER FINANCIAL STRENGTH

AAA
Highest capacity to meet policyholder and contract obligations; Risk factors are negligible.

AA+, AA, AA-
Very high capacity to meet policyholder and contract obligations; However, risk is modest, but may vary slightly over time due to business/economic conditions.

A+, A, A-
High capacity to meet policyholder and contract obligations; Risk factors may vary over time due to business/economic conditions.

BBB+, BBB, BBB-
Adequate capacity to meet policyholder and contract obligations; Risk factors are considered variable over time due to business/economic conditions.

BB+, BB, BB-
Marginal capacity to meet policyholder and contract obligations; Risk factors may vary widely with changes in business/economic conditions.

B+, B, B-
Low capacity to meet policyholder and contract obligations; Risk factors are capable of fluctuating widely with changes in business/economic conditions.

CCC
Very low capacity to meet policyholder and contract obligations; Risk may be substantial.

CC
Weak capacity to meet policyholder and contract obligations; Risk may be high.

C
Very weak capacity to meet policyholder and contract obligations; Risk may be very high

D
Extremely weak capacity to meet policyholder and contract obligations; Risk is extremely high.

Rating Watch: VIS places entities and issues on 'Rating Watch' when it deems that there are conditions present that necessitate re-evaluation of the assigned rating(s). Refer to our 'Criteria for Rating Watch' for details. www.vis.com.pk/images/criteria_watch.pdf

Rating Outlooks: The three outlooks 'Positive', 'Stable' and 'Negative' qualify the potential direction of the assigned rating(s). An outlook is not necessarily a precursor of a rating change. Refer to our 'Criteria for Rating Outlook' for details. www.vis.com.pk/images/criteria_outlook.pdf

'p' Rating: A 'p' rating is assigned to entities, where the management has not requested a rating, however, agrees to provide informational support. A 'p' rating is shown with a 'p' subscript and is publicly disclosed. It is not modified by a plus (+) or a minus (-) sign which indicates relative standing within a rating category. Outlook is not assigned to these ratings. Refer to our 'Policy for Private Ratings' for details. www.vis.com.pk/images/policy_ratings.pdf

REGULATORY DISCLOSURES — Appendix III

Name of Rated Entity	Pakistan Reinsurance Company Limited (PRCL)
Sector	Insurance
Type of Relationship	Solicited
Purpose of Rating	Insurer Financial Strength (IFS) Rating
Rating History	see table below
Instrument Structure	N/A
Statement by the Rating Team	VIS, the analysts involved in the rating process and members of its rating committee do not have any conflict of interest relating to the credit rating(s) mentioned herein. This rating is an opinion on insurer financial strength only and is not a recommendation to buy or sell any securities.
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Rating History:

Rating Date	Medium to Long Term	Rating Outlook	Rating Action
RATING TYPE: IFS			
12/19/2019	AA	Stable	Reaffirmed
10/12/2018	AA	Stable	Initial