RATING REPORT

Reliance Insurance Company Limited (RICL)

REPORT DATE:
January 2nd, 2024

RATING ANALYSTS:
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RATING DETAILS

	Latest Rating	Previous Rating
Rating Category	Long-term	Long-term
IFS	A+	A+
Rating Date	*January 2, '24*	*December 30, '22*
Rating Outlook	Stable	Stable
Rating Action	Reaffirmed	Reaffirmed

COMPANY INFORMATION

Incorporated in 1981	**External auditors:** BDO Ebrahim & Co. Chartered Accountants
Public Limited Company	**Chairman of the Board:** Mr. Irfan Zakaria Bawany
Key Shareholders (with stake 5% or more):	**Chief Executive Officer:** Mr. A. Razak Ahmed
Individuals - 47.9%	
Directors, CEO, & Other Spouses & Minor Children - 24.46%	
Joint Stock Companies - 25.03%	

APPLICABLE METHODOLOGY(IES)

VIS Entity Rating Criteria Methodology – General Insurance, October 2023
https://docs.vis.com.pk/docs/GeneralInsurance-2023.pdf

APPLICABLE RATING SCALE(S)

VIS Issue/Issuer Rating Scale:
https://docs.vis.com.pk/docs/VISRatingScales.pdf

Reliance Insurance Company Limited (RICL)

OVERVIEW OF THE INSTITUTION

RICL was incorporated as a public limited company and commenced operations in 1981. Financial statements for 2022 were audited by BDO Ebrahim & Co. Chartered Accountants. The company is engaged in provision of general insurance business services and takaful services through its Window Takaful Operations.

Profile of the Chairman:

Mr. Irfan Zakaria Bawany has been the Chairman of the Board of Directors of RICL from 28th July, 2020. He has diversified experience in various industries.

Profile of the CEO

Mr. Razak Ahmed is the CEO of RICL since 1995. He has over 45 years of experience in the insurance industry both in public and private sectors.

RATING RATIONALE

Rating assigned to Reliance Insurance Company Limited (RICL) derives strength from the sponsorship backing of two renowned industrial groups of the country, namely, the Al-Noor Group and the Amin Bawany Group, which have business interests in sugar, modaraba, board manufacturing and trading. The assigned rating also takes into account the stability and experience of the management team. On the other hand, the business risk profile of the insurance industry is currently elevated owing to projected slowdown in the domestic economic activity due to high interest rates, rupee devaluation, heightened inflation levels, destruction caused by floods coupled with expected rate hardening by international reinsures. Nevertheless, the topline expanded during the rating review period on account of inflation adjustments to premium prices coupled with the onboarding of a major client in the motor segment. On the flipside, loss ratios were marked by weakening owing to rise in average claim size; nonetheless, net claim performance remained favorable in comparison to industry benchmarks. While rise in the net claim ratio was offset by improvement in the expense ratio due to higher net premium during the ongoing year, the expense ratio remained on the higher side resulting in underwriting losses being registered. On the flip side, the bottom-line was supported by higher investment income on the back of increase in equity dividends coupled with healthy profit from WTO business.

In addition, the rating reflects the overall risk profile being supported by sound reinsurance arrangements with reputed international reinsurers; however, removal of non-proportional surplus treaties in the F&P and engineering segments was noted. The rating remains sensitive to increase in overall risk retention levels coupled with sizable investment in equity portfolio entailing higher price risk. The overall liquidity profile, as exhibited by liquid asset coverage of net technical reserves and insurance debt relative to gross premium, remains sound relative to rating benchmarks. Moreover, while capitalization levels have increased on a timeline as persistent underwriting losses have limited internal capital generation, the same remain on the lower side indicating room for growth. Additionally, the aging of claims is healthy with no claim overdue for more than year at end of the outgoing year. Going forward, the rating will remain sensitive to the Company's ability to boost profitability metrics, particularly through enhanced underwriting performance, amidst the challenging market environment.

Insurance Sector Update

Global Perspective

Despite building macroeconomic challenges, the insurance industry continued to grow in FY22, both globally and in Pakistan. Global insurance industry faced repricing of risks due to macroeconomic stresses and natural catastrophes with economic losses from natural disasters recorded higher in FY22; however insured losses covered 45% of these damages amounting to USD 125 billion. In addition, claims increased as high inflation increased the cost of repairing buildings, motor vehicles and other fixed assets that are usually covered by insurance. This led to continued rise in premium rates to cover the expenses. However, elevated interest rates augmented the investment income for insurers across the globe.

Local Perspective

Pakistan's insurance industry posted growth despite weak macroeconomic situation in CY22 with continued dominance of Life Insurance & Family Takaful segments in terms of assets and gross premiums. Gross premiums increased from Rs. 417.2 billion in CY21 to Rs. 531.7 billion in CY22 with Life & Family Takaful segment, and Non-Life & General Takaful segments posting increases of Rs. 81.9 billion and Rs. 29.4 billion respectively. Moreover, the industry's asset base grew by 14.8% in CY22 to Rs. 2,459.9 billion particularly on the back of significant growth in the Life Insurance segment. In addition, despite building macroeconomic pressures characterized by dwindling foreign reserves, stabilization measures, slowdown in economic activity, etc. along with

catastrophic floods affecting one-third of the country during the year under review, all segments of the industry continued to expand. This was the result of a combination of general factors affecting the whole insurance industry such as inflation leading to a rise in premium rates and idiosyncratic factors pertaining to all segments. The growth in Life Insurance segment was an outcome of the implementation of the government's health insurance programs carried out by State Life; the same increased health coverage to the low and middle-income strata of society. However, the claims ratio for the sector witnessed an increase due to a rise in group claims and higher surrender claims by individuals. Nevertheless, since life insurers maintain most of their investments in government securities due to lackluster performance of capital market, the resulting higher investment income boosted their profitability due to hike in interest rates. In non-life insurance sector, motor premiums drove the growth in net premiums as the cost of motor vehicles increased drastically during the outgoing year. However, torrential rains and flooding, some major fire incidents, and higher cost of repairing fixed assets contributed to the increase in claims. Accordingly, financial performance indicators for the non-life sector slightly weakened on a timeline. Further, the industry's combined ratio increased in CY22, which was driven by a spike in both net claims and expense ratios. With the increase in combined ratio, insurers are expected to reprice their products in the ongoing year. Going forward, due to the prevailing slowdown in economic activity and stressed macro financial conditions, the growth trajectory in non-life premiums is expected to be uncertain while the growth in the life sector will continue to largely depend on traction in the health insurance programs. Moreover, the SECP has issued instructions of phase wise implementation of IFRS 17. The implementation is expected to translate in sizable provisioning burden for the industry; however, the actual impact of the same on industry capitalization is yet to be ascertained. The SECP has issued the deadline of 1st January, 2026 to complete the implementation of IFRS 17.

Future Outlook

Globally, it is expected that there will be premium rate hardening in CY23 in response to the high inflation, geopolitical tensions, natural catastrophes and financial market losses of CY22. These global insurance developments will lead to increases in reinsurance rates offered by international re/insurers which coupled with the exchange rate depreciation, may lead to increase in reinsurance expense for insurers in EMDEs, particularly non-life insurers that have extensive reinsurance arrangements with international reinsurers. The rate hardening along with the elevated policy rate is expected to influence insurers' financial performance in the near term. Global premiums are expected to grow at 2.1% in real terms on average in 2023. Given that non-life insurance is correlated with economic growth and the latest data indicates that Pakistan's economy will significantly slowdown in 2023, accordingly the growth trajectory of non-life premiums in Pakistan could also face pressures. Moreover, if inflation remains elevated, then there could be further rate hardening leading to an uncertain growth trajectory for non-life premiums. Furthermore, in the backdrop of high interest rates, non-life insurers may also consider recalibrating their investment portfolios in order to pad the bottom-line. Life insurance business, with a longer time horizon, is expected to remain relatively immune to the prevailing macroeconomic pressures. The growth in this sector is now partially dependent on the continuity of the government's health insurance programs.

Source: Financial Stability Review – 2022 | State Bank of Pakistan

Business Update

RICL is engaged in providing general insurance and window takaful operations to four primary segments, namely, fire & property damage, marine, motor and miscellaneous. The Company has a branch network of 24 locations across the country; no new branches were introduced over the rating review period. The business mix continued to remain dominated by the fire & property segment, constituting over half of the topline followed by the marine segment; however, downtrend in both was witnessed over the rating review period owing to the Company's cautious underwriting approach. Decline in proportion of the marine segment was further contributed by the stiff competition in the segment due to dominance of larger players. On the flipside, the motor segment expanded notably during the rating review period despite overall dip in demand for motor vehicles due to unprecedented price inflation mainly on account of onboarding of a major client in the

banking industry for its corporate fleet management. Overall, GWP augmented by 13.1% on an annualized basis to Rs. 646.1m during 9MCY23 (CY22: Rs. 761.9m, CY21: Rs. 651.2m); the same wan mainly a function of upward revision of premium prices owing to impact of dollar appreciation combined with inflationary pressure on sum insured valuation. Going forward, the management aims to continue its careful underwriting strategy and projects GWP emanating from the conventional business to reach Rs. 1.15b at end-CY23. Given that Rs. 861m has already been booked by end-Nov'23, the aforementioned target is considered achievable, particularly factoring in the inherent cyclicality of policy renewals. Breakdown of business mix can be seen below:

Gross Premium Mix	2020	2021	2022	3QCY23
Fire	53.3%	54.3%	58.4%	52.6%
Marine	24.4%	25.5%	20.4%	21.3%
Motor	18.2%	15.2%	15.4%	20.1%
Misc	4.0%	5.0%	5.8%	6.0%
Total	**100.0%**	**100.0%**	**100.0%**	**100.0%**

The overall cession ratio depicted a slight decline to 49.4% during 9MCY23 (CY22: 50.6%, CY21: 50.6%) as retention levels in the marine cargo surplus treaty increased to boost net premium. However, cession in the miscellaneous exhibited a marked increase over the rating review period on account of lower net retention under quota share cum surplus arrangements in the bond segment due to increase in average sum insured; nonetheless, minimal proportion of the segment in the business mix resulted in limited impact on overall of cession ratio.

On the WTO front, the Company registered gross and net contributions amounting to Rs. 92.1m and Rs. 12.6m, respectively (CY22: Rs. 96.0m, Rs. 5.0m; CY21: Rs. 75.2m, Rs. 4.0m). The business mix was dominated by the F&P segment which contributes more than half of the takaful topline followed by the motor segment. The Participant's Takaful Fund (PTF) also reported a surplus of Rs. 5.3m (CY22: Rs. 5.2m, CY21: Rs. 6.2m) on the back of higher dividend income from equity investments. Going forward, the Company is on track to meet its topline target of Rs. 150m for CY23 with Rs. 109m already booked by end-Nov'23. However, expansion of the WTO business is expected to be restricted owing to the limited availability of reinsurance coverages and competitive shariah compliant investment avenues.

Claims experience

The Company reported an increase in gross claims to Rs. 271.8m during the outgoing year (CY21: Rs. 260.0m). The same was manifested largely in the F&P segment, particularly due to a sizable claim of Rs. 60m pertaining to Pioneer Cables Ltd. Notable reduction in gross claims related to the marine segment was also witnessed given no major losses were booked in line with the Company's conservative underwriting approach. However, net claims increased to Rs. 93.6m (CY21: Rs. 64.2m) owing to increase in average claim cost, particularly in the motor segment as vehicle prices reached unprecedented levels over the rating review period.

However, gross and net claims expense increased to Rs. 387.9m and Rs. 93.8m respectively during 9MCY23 on account of several sizable claims incurred in the F&P segment, including a Rs. 40m payout pertaining to Time Ceramics (Pvt.) Ltd., coupled with further rise in average claim cost due to inflationary pressure and dollar appreciation. Despite deterioration in loss ratios during the ongoing year, the Company's net claims ratio performance compares favorably to the overall industry's which stood at 60.7% at end-June'23. Breakdown of net claims ratio by segment can be seen below:

	2020	2021	2022	3QCY23
Fire	13.3%	8.9%	11.9%	24.3%
Marine	28.5%	21.5%	33.6%	25.2%

Motor	35.5%	41.1%	51.3%	41.1%
Misc.	8.1%	5.1%	5.4%	1.4%
Total	**23.9%**	**21.2%**	**26.0%**	**29.1%**

Underwriting performance

RICL continued to post underwriting losses on a timeline basis, however, improvement was witnessed over the rating review period to Rs. (1.2m) by end-Sept'23 (CY22: Rs. (15.9m), CY21: Rs. (18.2m)) despite deterioration in net claim performance. This is attributable to decline in the underwriting expense ratio to 71.3% (CY22: 79.5%, CY21: 84.8%) owing to higher net premium booked; the same is largely an outcome of expansion of revenue generated from the motor segment which inherently has minimal cession levels due to Excess of Loss (XOL) treaties. Consequently, the overall combined ratio decreased to 100.4% (CY22: 105.5%, CY21: 106.0%). Moreover, increase in recurring investment income to Rs. 99.7m during 9MCY23 (CY22: Rs. 101.5m, CY21: Rs. 71.5m) on the back of higher dividend income emanating from equity investments resulted in the net operating ratio improving to 69.4% (CY22: 77.3%, CY21: 82.4%). Moreover, uptick in profit generated from WTO business to Rs. 20.7m (CY22: Rs. 19.3m, CY21: Rs. 10.7m) further boosted the bottom-line, with profit after tax amounting to Rs. 90.3m during 9MCY23 (CY22: Rs. 44.1m, CY21: Rs. 53.0m).

Reinsurance arrangements

The Company's risk profile is supported by sound reinsurance arrangements with a diversified panel of international and local reinsurers. However, the overall risk profile of the reinsurance panel witnessed a downward movement following the exit of Saudi Re (rated 'A-' by S&P) and Qianhi Re (rated 'A-' by A.M. Best) which were replaced by MISR Re (rated 'B++' by A.M. Best). Nonetheless, Swiss Re (rated 'AA-' by S&P) remains the lead reinsurer across all segments followed by Pakistan Reinsurance Company Ltd. (PRCL) (except for F&P, engineering and bond segments) owing to specific quota extended to the local reinsurer.

In the F&P and engineering segments, shift in treaty terms was observed for CY23 with removal of non-proportional treaties which reinforced quota share arrangements owing to increase in loss ratios in the preceding year. On the other hand, non-proportional treaties are still in place for the marine cargo segment; however, the number of lines for the same were reduced to 12 from 15, slightly increasing net retention in order to boost profitability. However, retention levels and treaty capacities across the F&P, engineering and bond segments were reduced to bring risk exposure in sync with risk appetite level of the Company. Therefore, the size of maximum risk per claim is considered manageable relative to equity base. Moreover, terrorism cover treaties were removed in the ongoing year on account of non-renewal by the reinsurer; however, as per management, the associated policies are booked on a case-to-case basis in facultative arrangements, hence, reducing impact of claim payouts on the Company's net account. Going forward, no major changes are expected in the reinsurance panel, treaty terms and commission rate for CY24.

Investments

The overall investment portfolio reduced on a timeline basis to Rs. 832.6m by end-Sept'23 (CY22: Rs. 794.0m, CY21: Rs. 837.9m) as adverse stock market performance amidst macroeconomic deterioration resulted in downward movement in share prices. Despite the current high interest rate environment and volatile stock market, the investment mix continues to be dominated by equities owing to the Company's commitment toward investing solely in Shariah-compliant avenues. Consequently, the overall risk profile of the investment portfolio is assessed to be elevated. However, the associated market and price risk is partially moderated by an increasing tilt of the equity mix toward money market mutual funds which constitute about 35.3% of the overall portfolio at end-Sept'23 (CY22: 30.1%, CY21: 25.9%). The remainder of the equity portfolio constitutes largely of blue-chip scrips across a diversified range of sectors, concentrated particularly in the fertilizer, chemical, oil & gas and commercial banking industries. Debt securities contribute only a minimal proportion to the investment mix amounting to Rs. 70.1m at end-9MCY23 (CY22: Rs. 70.1m, CY21: Rs. 70.1m); the same comprise solely of Pakistan Energy Sukuks which will mature in May'30 and carry a profit rate of 6M KIBOR – 0.1%. The remaining portion of the investment portfolio

constitutes of term deposits receipts, amounting to Rs. 44.3m (CY22: Rs. 42.6m, CY21: Rs. 38.6m). Going forward, given that macroeconomic conditions and stock market performance are projected to be volatile in the medium-term, diversification of the investment portfolio to mitigate overall risk profile and boost investment income will be viewed positively from a rating's perspective.

	2021	%	2022	%	3QCY23	%
Equities	729.3	87.0%	681.3	85.8%	718.2	86.3%
Debt Securities	70.1	8.4%	70.1	8.8%	70.1	8.4%
Term Deposit Receipts	38.6	4.6%	42.6	5.4%	44.3	5.3%
Total	**837.9**	**100.0%**	**794.0**	**100.0%**	**832.6**	**100.0%**

Liquidity

RICL's liquidity position remained strong as represented by liquid assets to net technical reserves recorded at 327.6% (CY22: 350.4%, CY21: 445.5%) at end-Sept'23. The decline in the aforementioned coverage was a function of reduction in the overall investment portfolio size coupled with cyclical increase in unearned premium reserves. Nevertheless, the same is expected to depict improvement once unearned premium reserves are gradually realized by end-CY23. On the flipside, insurance debt to gross premium improved marginally on a timeline to 45.5% during 9MCY23 (CY22: 50.8%, CY21: 46.7%) owing to swifter payments received from policyholders in line with change in accounting policy pertaining to recording of receivables.

Capitalization

The Company's equity base witnessed slight increase over the rating review period, amounting to Rs. 1.1b at end-Sept'23 (CY22: Rs. 1.1b, CY21: Rs. 1.0b), despite consistent underwriting losses and dividend payout of Rs. 31.7m (CY22: Rs. 30.2m, CY21: nil) on account of profit retention from emanating from investment income. However, growth in business activity outstripped expansion of equity levels, resulting in the operating leverage rising to 38.5% at end-9MCY23 (CY22: 34.0%, CY21: 28.9%). Nonetheless, RICL is considered sound from a solvency risk perspective as the Company has adequate cushion in terms of total admissible assets over liabilities. Additionally, financial leverage also scaled upwards to 25.5% (CY22: 23.9%, CY21: 19.9%) in sync with increase in net technical reserves; the same was manifested largely in higher outstanding claims as well as unearned premium reserve. However, as unearned premium reserves are gradually realized over the ongoing year, financial leverage is expected to rationalize by end-Dec'23. In addition, the leverage indicators are commensurate with the assigned rating. Aging of claims payables is also considered sound with no claims outstanding for more than a year at end-CY22. Going forward, the ratings will factor in improvement in underwriting performance to ensure leverage indicators remain rangebound.

Reliance Insurance Company Limited — Appendix I

FINANCIAL SUMMARY *(amounts in PKR millions)*

BALANCE SHEET	31-Dec-20	31-Dec-21	31-Dec-22	30-Sep-23
Cash and Bank Deposits	111.3	93.7	101.8	108.2
Investments	813.5	837.9	794.0	832.6
Liquid Assets	919.2	926.9	888.7	932.1
Insurance Debt	231.8	304.3	386.7	392.0
Prepaid Reinsurance Ceded	137.1	163.4	153.3	156.6
Total Assets	1,714.0	1,847.7	1,888.9	2,134.1
Paid Up Capital	561.4	603.5	633.7	665.4
Net Worth	997.6	1,048.1	1,060.3	1,116.5
Technical Reserves	523.7	550.1	559.4	742.5
Total Liabilities	716.3	799.6	828.6	1,017.7
INCOME STATEMENT	**2020**	**2021**	**2022**	**9M'23**
Net Premium Revenue	319.5	303.1	360.5	322.5
Net Claims	76.4	64.2	93.6	93.8
Underwriting Expenses	261.8	257.1	286.5	229.9
Underwriting Profit/(Loss)	-18.7	-18.2	-15.9	-1.2
Investment Income	83.5	74.7	67.4	119.3
Profit Before Tax	83.6	70.5	67.6	142.9
Profit After Tax	68.5	53.0	44.1	90.3
RATIO ANALYSIS	**2020**	**2021**	**2022**	**9M'23**
Cession Ratio (%)	46.0%	50.6%	50.6%	49.4%
Gross Claims Ratio (%)	44.7%	42.3%	37.3%	60.9%
Net Claims Ratio (%)	23.9%	21.2%	26.0%	29.1%
Underwriting Expense Ratio (%)	81.9%	84.8%	79.5%	71.3%
Combined Ratio (%)	105.9%	106.0%	105.5%	100.4%
Net Operating Ratio (%)	87.0%	82.4%	77.3%	69.4%
Insurance Debt to Gross Premium (%)*	40.7%	46.7%	50.8%	45.5%
Operating Leverage (%)*	32.0%	28.9%	34.0%	38.5%
Financial Leverage (%)	20.6%	19.9%	23.9%	25.5%
Adjusted Liquid Assets to Net Technical Reserves (%)	448.2%	445.5%	350.4%	327.6%

**Annualized*

REGULATORY DISCLOSURES — Appendix II

Name of Rated Entity	Reliance Insurance Company Limited
Sector	Insurance
Type of Relationship	Solicited
Purpose of Rating	Insurer Financial Strength (IFS) Rating

Rating History

Rating Date	Medium to Long Term	Rating Outlook	Rating Action
	Rating Type: IFS		
02/01/2024	**A+(IFS)**	**Stable**	**Reaffirmed**
30/12/2022	A+(IFS)	Stable	Reaffirmed
31/03/2022	A+(IFS)	Stable	Harmonized
31/12/2021	A	Stable	Maintained
31/12/2020	A	Positive	Reaffirmed
31/12/2019	A	Positive	Reaffirmed
31/12/2018	A	Positive	Reaffirmed
27/11/2017	A	Positive	Reaffirmed
29/12/2016	A	Positive	Reaffirmed
30/12/2015	A	Positive	Maintained

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 credit quality only and is not a recommendation to buy or sell any securities.
Probability of Default	VIS' ratings opinions express ordinal ranking of risk, from strongest to weakest, within a universe of credit risk. Ratings are not intended as guarantees of credit quality or as exact measures of the probability that a particular issuer or particular debt issue will default.
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Due Diligence Meetings Conducted

Name	Designation	Date
Mr. A. Razak Ahmed	Managing Director & CEO	16th Dec 2023
Mr. Ghulam Haider	Chief Financial Officer	
Mr. Faraz Abdul Razzak	Company Secretary & Compliance Officer	
Mr. Ghulam Mujaddid	AVP Accounts	
Mr. Najmullah Khan	Head of Takaful & Underwriting	
Mr. Saleem Memon	Head of Investments	
Mr. A. Rahim Patni	Head of Reinsurance	