RATING REPORT

Security General Insurance Company Limited (SGICL)

REPORT DATE:
December 09, 2019

RATING ANALYSTS:

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RATING DETAILS

	Latest Rating	Previous Rating
Rating Category	**Long-term**	**Long-term**
IFS	AA	AA
Rating Date	*Dec 04,'18*	*Dec 28,'18*
Rating Outlook	Stable	Stable

COMPANY INFORMATION

Incorporated in 1996	**External Auditors:** A.F. Ferguson & Co, Chartered Accountants
Unquoted Public Limited Company	**Internal Auditors:** Ahsan & Ahsan Chartered Accountants
	Chairman: Mian Hassan Mansha
Key Shareholder(s):	**Chief Executive Officer:** Mr. Farrukh Aleem
Allied Bank Limited -18.22%	
Nishat Mills Limited - 15.02%	
Adamjee Insurance Co. Ltd – 14.22%	
Mian Hassan Mansha – 13.30%	
Mian Umer Mansha – 13.30%	
Mian Raza Mansha – 11.95%	
Mrs. Naz Mansha – 7.50%	

APPLICABLE METHODOLOGY(IES)

VIS Entity Rating Criteria: General Insurance March 2017:
https://www.vis.com.pk/kc-meth.aspx

Security General Insurance Company Limited (SGICL)

OVERVIEW OF THE INSTITUTION

SGICL was incorporated as an unquoted public limited company in May 1996. Headquartered in Lahore, the company operates with a network of 8 branches providing insurance coverage against risks related to fire, marine, motor and other categories.

Profile of Chairman

Mian Hassan Mansha continues to Chair the Board. Mr. Hassan carries over 11 years of professional experience and is on the Board of various Nishat group companies.

Profile of CEO

Mr. Farrukh Aleem serves as Chief Executive Officer (CEO) of the company. Mr. Aleem carries 13 years of experience in the insurance industry and also holds a postgraduate degree in Business Administration.

Financial Snapshot

Net Equity: 9M19:Rs. 12.7b; FY18: Rs. 13.9b; FY17: Rs. 15.4b

Net Profit: 9M19: Rs. 696.3m; FY18: Rs. 853.8m; FY17: Rs. 824.7m

RATING RATIONALE

Ratings assigned to Security General Insurance Company Limited (SGICL) take into account its association with a large diversified conglomerate "Nishat Group" having business interests in banking, textile, cement, power generation, real estate and paper products. Ratings draw strength from growth in business volumes, improved underwriting results and conservative risk appetite leading to cautious business selection. The sound capitalization and leverage indicators exhibiting strong loss absorption capacity remain the key rating driver. Credit risk emanating from reinsurance panel selection remains sound with all reinsurers, except one, rated in category 'A' or higher. The ratings derive strength from sizeable recurring dividend income emanating from investment in blue chip companies.

Business Strategy

The company primarily offers insurance cover for fire and property damage, marine and transport, motor, crop and miscellaneous risks including burglary, loss of cash in safe and cash in transit, engineering losses, business interruption losses, accident and natural calamities. The business mix of the company is dominated by fire segment followed by motor; meanwhile exposure in marine segments remains limited owing to risk averse approach adopted by the management on account of incidence of higher quantum claims in respect to premium earned. During the period under review, business volumes of the company increased to Rs. 2.9b (FY18: Rs. 2.5b; FY17: 2.0b) during 9M19 primarily on the back of new power projects underwritten in the fire segment. The company has surpassed the target of Rs. 2.8b for FY19 during 9M19. The management expects to close the current year at Rs. 3.2b. To increase its market penetration the company opened a new branch in Lahore primarily to focus on the business of car leasing. Although there has been a sharp increase in retail prices of cars, the management plans to focus on this segment since a fewer number of clients tapped will result an equivalent gross premium. Moreover, there has been an overall decline in motor theft thereby increasing the cushion of loss absorption.

Overall cession improved during 9M18; however the same did not have an impact on net premium revenue as a result of increase in gross written premium. Further, around two-fifths of premium growth emanated from related parties, constituting 40.4% (FY18: 38.2%; FY17: 41.3%) of gross premium. The snapshot of business mix is presented in the table below:

	FY16	FY17	FY18	9M19
Fire	79.8%	72.1%	72.5%	74.7%
Marine	3.6%	3.9%	4.0%	3.2%
Motor	10.6%	13.4%	13.7%	12.0%
Miscellaneous	6.1%	10.6%	9.8%	10.2%
Gross Premium (m)	2,087.1	2,000.3	2,495.9	2,849.6

The takaful operations were initiated during FY18 after the company received license from the regulator. Although the growth in takaful business has been sluggish on account of limited capacity in the market, the company was able to materialize the projection of breaking even during the ongoing year. Owing to the current economic dynamics, the company plans to focus on group related business since that caters to limited risk appetite of the company. As per the management, currently writing secure market based business is relatively difficult therefore the company has opted for consolidation strategy during the rating horizon.

Reinsurance Arrangement

SGICL's risk profile is supported by strong capitalization indicators and adequate reinsurance coverage provided by diversified panel of reinsures. Risk profile of the reinsurance panel is considered sound as majority of the reinsurers are rated 'A-' or higher. For FY19, Labuan Reinsurance (L) Limited, Malaysia and Peak Reinsurance, Hong Kong were added to the existing reinsurer panel of SGICL while Trust Reinsurance was removed from the panel owing to the rating downgrade during FY18. The table below depicts the rating profile of reinsurers along with their respective share:

Reinsurer	2018	2019	Ratings
Fire, Engineering, Misc Accident & Bond			
Quota share & Surplus-Treaty			
PRCL	35%	35%	AA+ (VIS)
Hannover Re	25%	25%	AA-; A+(S&P; A.M. Best)
Malaysian Re	8%	8%	A- (A.M. Best)
Korean Re	6%	7%	A (S&P; A.M. Best)
Saudi Re	6%	7%	BBB+(S&P)
Sava Re	5%	6%	A (S&P; A.M. Best)
Labaun Re	-	5%	A- (S&P)
General Insurance Corp, India	3%	3%	A- (S&P)
Peak Re, Hong Kong	-	2%	A- (A.M. Best)
Qatar Re	-	2%	A- (A.M. Best)
Trust Re	12%	-	
Fire, Engineering & CAT			
XOL-Treaty			
Hannover Re	75%	65%	AA-; A+ (S&P; A.M. Best)
PRCL	25%	35%	AA+ (VIS)
Marine Cargo			
Surplus-Treaty			
PRCL	30%	35%	AA+(VIS)
Antares	24%	33.3%	A+; A (S&P; A.M. Best)
Korean Re	4%	14.7%	A (S&P; A.M. Best)
Saudi Re	5%	6%	BBB+(S&P)
Malaysian Re	5%	5%	A- (A.M. Best)
Qatar Re	-	4%	A- (A.M. Best)
Peak Re, Hong Kong	-	2%	A- (A.M. Best)
Trust Re	30%	-	A- (S&P; A.M. Best)
Oman Re	2%	-	B+ (A.M. Best)
XOL- Treaty			
PRCL	20%	35%	AA+(VIS)
Antares	10%	30%	A+; A (S&P; A.M. Best)
Korean Re	-	25%	A (S&P; A.M. Best)
Saudi Re	7.5%	10%	BBB+(S&P)
Trust Re	62.5%	-	A- (S&P; A.M. Best)

Motor and W.C.			
XOL- Treaty			
Hannover Re	65%	65%	AA-; A+ (S&P; A.M. Best)
PRCL	35%	35%	AA+(VIS)
Crops			
XOL-Treaty			
Hannover Re	65%	65%	AA-; A+ (S&P; A.M. Best)
PRCL	35%	35%	AA+ (VIS)

Given the anticipated increase of business in fire segment, the company increased company's retention and total treaty liability under the aforementioned segment for FY19. Moreover, the company also has a special fire treaty with total treaty capacity of Rs. 750m. Other than the aforementioned change, the treaty capacities and retention limits remained unchanged. In order to maintain its business risk profile, SGICL ceded two-thirds of its business to reinsurers. As per SGICL's internal policy, the company cannot cede more than 30% of the premium written to a reinsurance company with a rating below 'A-'. Treaty capacities are tabulated in the table below:

In Rs. Million	2018			2019		
Treaties	**SGI's Max. Retention**	**No. of Lines**	**Max. Liability Under Total Treaty**	**SGI's Max. Retention**	**No. of Lines**	**Max. Liability Under Total Treaty**
Fire & Eng.						
Surplus – Fire (market business)	15m	30	450m	20m	26	520m
Surplus – Fire (group business)	25m	30	750m	35m	26	910m
Fire – Special Business	20m	37.5	750m	20m	37.5	750m
Surplus – Eng.	15m	20	300m	15m	20	300m
Catastrophe- Fire & Eng						
XoL						
1st Layer	50m in excess of 25m			50m in excess of 25m		
2nd Layer	100m in excess of 75m			100m in excess of 75m		
3rd Layer	325m in excess of 175m			325m in excess of 175m		
General Accident						
Quota Share	3.6m	-	8.4m	3.6m	-	8.4m
Marine Cargo						
Surplus (market business)	5m	20	100m	5m	20	100m
Surplus ((event limit)	5m	60	300m	5m	60	300m
Marine Cargo						

XoL						
1st Layer	3m in excess of 2m			3m in excess of 2m		
2nd Layer	45m in excess of 5m			45m in excess of 5m		
3rd Layer	50m in excess of 50m			50m in excess of 50m		
Bond						
Quota Share (per bond)	8m	-	32m	8m	-	32m
Quota Share (per contractor)	16m	-	64m	16m	-	64m
Motor						
XoL						
1st Layer	1m in excess of 0.6m			1m in excess of 0.6m		
2nd Layer	3.4m in excess of 1.6m			3.4m in excess of 1.6m		
Crops						
XoL						
1st Layer	20.4m in excess of 10.4m			20.4m in excess of 10.4m		
Workers Compensation						
XoL						
1st Layer	0.4m in excess of 0.3m			0.4m in excess of 0.3m		

Claims Experiences

The conservative approach of the company towards underwriting insurance policies, effective pre-screening of market-based clients for their past track record coupled with higher proportion of group related business resulted in improved claims performance of the company during FY18. However during 9M19, claims performance slightly deteriorated with the highest net claims ratio emanating from the miscellaneous segment on account of higher retention on net account in line with incidence of lower quantum claims under quota-share arrangement. The loss retention on company's books was recorded the lowest in fire segment followed by marine. The segment-wise net claims ratios are presented in the table below:

	FY16	FY17	FY18	9M19
Net Claims Ratio	**16.8%**	**18.8%**	**13.9%**	**17.7%**
Fire	2.7%	9.9%	2.6%	1.2%
Marine	14.2%	23.7%	-1.4%	20.6%
Motor	39.0%	35.2%	37.3%	41.6%
Miscellaneous	72.3%	40.9%	31.8%	56.1%

Underwriting Performance:

The underwriting results of the company have improved on a timeline basis primarily as a function of increase in overall scale of operations. However, management expenses increased during the ongoing year owing to additional bonus distributed amongst employees as a retention technique coupled with inflationary pressure on salaries. Further, the net commission expense was also recoded lower at Rs. 8.4m (FY18: Rs. 7.5m; FY17: Rs. 18.7m) during 9M19 as a result of higher quantum of business ceded to the re-insurers. As per the management, the commission rates received from the re-insurers and commission rates paid to dealers remained unchanged during the review period. Subsequently, expense ratio increased slightly during 9M19 leading to higher combined ratio. The combined ratio of the company continues to remains one of the lowest amongst the peer insurance companies. Other than miscellaneous, all segments reported profits during FY18 and 9M19; ability to maintain these performance metrics will remain a key rating factor: The snapshot of underwriting results is tabulated below:

Rs. in millions	FY16	FY17	FY18	9M19
Underwriting Profit	**150.5**	**186.1**	**282.4**	**206.5**
Fire	120.8	134.0	185.1	128.9
Marine	8.2	9.3	17.6	16.8
Motor	25.3	37.8	69.1	63.3
Miscellaneous	(3.8)	5.0	10.5	(2.4)

Investment income, around 99% of which pertained to dividend income, remained sizable and continued to support the bottom line of the company. Despite increase in investment in equities, the investment income has declined on a timeline basis on account of overall lackluster performance of the stock market. The company reported a minimal profit of Rs. 0.3m on takaful operations during 9M19. On the other hand, in line with higher scale of operations, the company earned a higher net profit during the ongoing year.

Investments

Investments are largely manifested in blue chip equities with strategic investment in group companies, namely MCB Bank Limited (MCB), Adamjee Insurance Company Limited (AIGL), DG Khan Cement Company Limited, Pakgen Power Limited, Lalpir Power Limited and Nishat Hotels and Properties Limited (HNPL). During FY18, the company acquired a 10% equity stake Hyundai Nishat Motors (Private) Limited (HNML) coupled with slight increase in shareholding of MCB, AIGL and Pakistan Petroleum Limited. On the other hand, SGICL fully divested its investment MCB- Arif Habib saving and Investment and MCB Pakistan Sovereign Fund during FY18. Further investment of Rs. 300m and Rs. 198m was made HNPL and MCB respectively during the ongoing year. Going forward, the management plans to make an additional investment of Rs. 150m in HNML during the last quarter of FY19. The operations of aforementioned company have initiated with pickup production. Moreover, expansion of one of NHPL's project is underway given the occupancy of the existing hotel is almost around 100%. The company continues to maintain a long-term investment horizon for equities; therefore it is not actively involved in trading. However, owing to the asset composition, investment portfolio is subject to considerable market risk. Moreover, in the backdrop of lackluster capital market performance, market value of investment portfolio witnessed a decline by end-9MFY19.The market value of the existing portfolio declined by Rs. 1.9b during 9M19. On the other hand, in line with higher scale of operations, in line with investment in high dividend yielding stocks, investment portfolio translated into healthy dividend income thereby supporting core operations of the company.

Cash flows and Liquidity Profile

Liquidity profile is considered adequate reflected by sizeable liquid assets maintained in relation to borrowings and technical reserves. However, insurance debt in relation to gross premium has increased on a timeline basis and is significantly higher than the rating benchmark and peer companies. Premium due but unpaid from related parties represented 82.4% (FY18: 78.7%; FY17: 75.1%) of total premium due but unpaid from clients at end-9M19. According to the management, the increase was a function of higher new insurance policies with related companies during Aug-Sep'19. Further, overdue amounts from reinsurers also exhibited an upward trend mainly as a result of delay in payables from the local reinsurance company; the trend is inherent in the national insurance sector. Moreover, adjusting for reinsurance payables, insurance debt in terms of gross written premium also decreased on timeline basis to 37.2% (FY18: 49.5%; FY17: 27.2%) at end-9M19.

The cash flow from operations exhibited postive impetus on a timeline basisas a result of higher scale of operations and was recorded high at Rs. 1.2b (FY18: Rs. 365.5m; FY17: Rs. 977.9m) during 9M19. In line with regulatory requirement, SGICL has a paid up capital above Rs. 500m, at end-9M19. Despite reaping a healthy after tax profit of Rs. 696.3m during 9M19, the equity base of the company declind to Rs. 12.7b (FY18: Rs. 13.9b; FY17: Rs. 15.4b) on account of re-measurement of fair value reserve for available for sale investments. Given enhancement in overall business volumes, operating leverage of the company improved on a timeline basis. Moreover, financial leverage also exhibited an increasing trend during the period under review owing to increase unearned premium reserves as a result of increase in overall scale of operations coupled with decline in equity base. Both operating and financial leverage remain the lowest amongst the peer insurance companies and well below the rating benchmarks for the assigned rating. The company has enough room to optimize its leverage indicators by expanding its business further.

Security General Insurance Company Limited (Rs. in millions)			Appendix I	
BALANCE SHEET	**DEC 31, 2016**	**DEC 31, 2017**	**DEC 31, 2018**	**SEP 30, 2019**
Cash and Bank Accounts	386.2	644.2	233.1	423.3
Deposits Maturing Within 12 Months	50.4	50.4	-	-
Investments	9,126.9	17,043.5	14,015.0	12,726.1
Insurance Debt	1,332.2	1,546.0	2,176.6	2,991.5
Total Assets	12,588.1	21,241.8	18,996.7	19,518.9
Paid Up Capital	681	681	681	681
Net Worth	9,563.2	15,394.3	13,870.4	12,692.1
Borrowings	100.0	-	194.9	-
Total Liabilities	3,024.9	5,847.5	5,117.4	6,796.9
INCOME STATEMENT	**DEC 31, 2016**	**DEC 31, 2017**	**DEC 31, 2018**	**SEP 30, 2019**
Net Premium Revenue	445.7	502.5	599.6	505.8
Net Claims	74.7	94.4	83.2	89.3
Underwriting Profit/(Loss)	150.3	186.1	282.4	206.5
Investment Income	1,016.5	1,082.6	995.1	764.5
Other Income	4.2	0.3	7.3	0.1
Profit Before Tax	1,186.3	1,278.1	1,291.8	982.0
Profit After Tax	799.6	824.7	853.8	696.3
RATIO ANALYSIS	**DEC 31, 2016**	**DEC 31, 2017**	**DEC 31, 2018**	**SEP 30, 2019**
Cession Ratio (%)	76.0	74.0	65.8	76.4
Gross Claims Ratio (%)	112.3	32.8	14.5	26.2
Net Claims Ratio (%)	16.8	18.8	13.9	17.7
Underwriting Expense Ratio (%)	49.5	44.2	39.0	41.5
Combined Ratio (%)	66.3	63.0	52.9	59.2
Insurance Debt to Gross Premium (%)	66.6	80.6	97.1	107.9
Operating Leverage (%)	2.6	3.3	4.3	5.3
Financial Leverage (%)	6.8	9.4	9.6	13.4
Adjusted Liquid Assets to Technical Reserves & Borrowing (%)	46.6	60.6	29.8	29.3

ISSUE/ISSUER RATING SCALE & DEFINITIONS Appendix II

JCR-VIS Credit Rating Company Limited

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: JCR-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.jcrvis.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.jcrvis.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.jcrvis.com.pk/images/policy_ratings.pdf

REGULATORY DISCLOSURES	Appendix III			
Name of Rated Entity	Security General Insurance Company Limited (SGICL)			
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			
	04/12/2019	AA	Stable	Reaffirmed
	09/14/2017	AA	Stable	Upgrade
	06/16/2016	AA-	Stable	Reaffirmed
	09/23/2015	AA-	Stable	Reaffirmed
	04/22/2015	AA-	Stable	Reaffirmed
	02/04/2014	AA-	Stable	Upgrade
	12/26/2012	A+	Stable	Reaffirmed
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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