RATING REPORT

Security General Insurance Company Limited (SGICL)

REPORT DATE:
January 06, 2021

RATING ANALYSTS:

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RATING DETAILS		
	Latest Rating	**Previous Rating**
Rating Category	**Long-term**	**Long-term**
IFS	AA	AA
Rating Date	*Dec 31, '20*	*Dec 04,'19*
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 **Chief Executive Officer:** Mr. Farrukh Aleem
Key Shareholder(s):	
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 November 2019 *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 12 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 14 years of experience in the insurance industry and holds a postgraduate degree in Business Administration.

Financial Snapshot

Net Equity: 9M20: Rs. 13.8b; FY19: Rs. 14.9b; FY18: Rs. 13.9b

Net Profit: 9M20: Rs. 641.2m; FY19: Rs. 959.0m; FY18: Rs. 853.8m

RATING RATIONALE

The rating assigned to 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. Growth momentum of the company in terms of gross premiums was impacted by the economic disruption and initiation of industry-wide price war amidst the outbreak of COVID-19; SGICL, however, remained focused on retention of existing business with no active participation in price war. Sound capitalization and leverage indicators exhibiting strong loss absorption capacity remain the key rating factor. Going forward, growth in business may emanate from recovery in motor segment, introduction of new products in healthcare, crop, and engineering segments and rollout of an online insurance platform.

Credit risk emanating from reinsurance panel selection remains sound with all reinsurers, except one, rated in category 'A' or higher. The conservative approach towards underwriting insurance policies, effective pre-screening of market-based clients for their past track record, and adequate reinsurance coverage led to consistently good claim performance. The rating derives strength from sizeable recurring dividend income emanating from investment in blue chip companies, though dividend income decreased during the period under review due to temporary regulatory suspension of dividends from banks. The liquidity profile of the company is considered adequate reflected by sizeable liquid assets maintained in relation to borrowings and technical reserves. However, insurance debt in relation to gross premium needs to remain within the peer group parameters.

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 and miscellaneous segments. Gross written premium increased marginally to Rs. 2.9b (FY19: Rs. 3.1b; FY18: Rs. 2.5b) during 9MFY20 vis-à-vis last corresponding period as the company focused on client retention and tried to avoid price war in view of economic disruption caused by the outbreak of COVID-19. Going forward, growth in gross written premium is expected to emanate from recovery in motor segment, introduction of new products in healthcare, crop, and engineering segments and rollout of an online insurance platform by end-June 2021. However, there is no plan to open new branch during the next year.

Overall cession was recorded at 75.3% (FY19: 73.9%; FY18: 75.2%) during 9MFY20; however the same did not impact the net premium revenue which increased to Rs. 613m (FY19: Rs. 696m; FY18: Rs. 600m) mainly due to increase in gross earned premium. The increase in premium written mainly emanated from the related parties which accounted for 41.7% (FY19: 37.2%; FY18: 38.2%) of gross premium during 9MFY20. The snapshot of business mix is presented in the table below:

	FY17	FY18	FY19	9MFY20
Fire	72.1%	72.5%	71.4%	77.4%
Marine	3.9%	4.0%	4.0%	2.7%
Motor	13.4%	13.7%	13.7%	11.3%
Miscellaneous	10.6%	9.8%	10.9%	8.7%
Gross Premium (Rs. m)	2,000.3	2,495.9	3,121.7	2,945.7

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 FY20, Antares Underwriting and General Insurance Corp, India were removed from the existing panel of SGICL owing to rating downgrade and their share was distributed amongst other reinsurers; no new reinsurer was added during the period.

Barring an addition of third layer XOL in motor segment due to increase in prices of vehicles, the treaty capacity and retention limits remained unchanged during the period under review. In order to maintain its business risk profile, SGICL ceded three-fourth 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-'.

Claims Experiences

The conservative approach of the company towards underwriting insurance policies, effective pre-screening of market-based clients for their past track record, and adequate reinsurance coverage lead to consistently good claim performance. During 9MFY20, overall net claim ratio improved driven largely by improvement in net claims ratio of miscellaneous segment, followed by motor segment and fire segment. The loss retention on company's books was recorded the lowest in fire segment. The segment-wise net claims ratios are presented in the table below:

	FY17	FY18	FY19	9MFY20
Net Claims Ratio	**18.8%**	**13.9%**	**15.9%**	**13.7%**
Fire	9.9%	2.6%	2.9%	1.9%
Marine	23.7%	-1.4%	-12.0%	39.5%
Motor	35.2%	37.3%	39.7%	37.4%
Miscellaneous	40.9%	31.8%	45.5%	14.6%

Underwriting Performance

During 9MFY20, underwriting results of the company were under pressure on account of challenged business environment amidst the outbreak of COVID-19 despite marginal improvement in overall scale of operations. Underwriting profit was reported at Rs. 281.7m (FY19: Rs. 289.9m; FY18: Rs. 282.4m) as the impact of growth in fire segment was more than offset by decline in profitability of motor and marine segments coupled with higher underwriting loss in miscellaneous segment.

Increase in management expenses was a result of continued distribution of bonus amongst the employees, inflationary adjustment in salaries, and hiring of some resources related to sales while the industry players reduced the workforce to cut costs in view of COVID-19. Net commission expense was recoded at Rs. 14.8m (FY19: Rs. 12.9m; FY18: Rs. 7.5m) during 9MFY20. As per management, the commission rates received from the re-insurers and commission rates paid to dealers remained largely unchanged during the period. Despite that, expense ratio improved slightly to 40.3% (FY19: 42.5%; FY18: 39.0%) owing to relatively higher increase in net premium revenue, which coupled with improved net claims ratio led to slightly lower combined ratio of 54.0% (FY19: 58.3%; FY18: 52.9%). 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 FY19 and 9MFY20. Going forward, ability of the company to maintain these performance metrics will remain a key rating factor. The snapshot of underwriting results is tabulated below:

Rs. in millions	FY17	FY18	FY19	9MFY20
Underwriting Profit	**186.1**	**282.4**	**289.9**	**281.7**
Fire	134.0	185.1	177.4	179.6
Marine	9.3	17.6	29.6	6.4
Motor	37.8	69.1	85.2	78.0
Miscellaneous	5.0	10.5	-2.3	17.7

Investment income, around 96% of which pertained to dividend income, remained sizable and continued to support the bottom line of the company. The investment income has declined mainly due to suspension of bank dividends as directed by the State Bank of Pakistan for two quarters ending March 31, 2020 and June 30, 2020. Meanwhile, other income which mainly pertained to return on bank balances also decreased as the impact of higher cash & bank balances was more than offset by lower interest rates. During 9MFY20, contribution from takaful operations remained minimal as net profit generated by takaful business amounted to Rs. 8.3m (FY19: Rs. 3.2m). Resultantly, the company earned a lower net profit of Rs. 641.2m (FY19: Rs. 959m; FY18: Rs. 853.8m) during 9MFY20.

Investments

Investment portfolio of the company mainly comprises 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, Nishat Hotels and Properties Limited (NHPL), and Hyundai Nishat Motors (Private) Limited (HNML). During the period under review, the company mobilized long-term borrowings of Rs. 1.8b to purchase additional shares of NHPL.

The company continues to maintain a long-term investment horizon for equities; the management is not actively involved in trading. However, owing to the asset composition, investment portfolio is subject to considerable market risk. Moreover, due to lackluster performance of capital market, market value of its investment portfolio decreased to Rs. 15.3b (FY19: Rs. 16.2b; FY18: Rs. 13.9b) by end-9MFY20. On the other hand, in line with investment in high-yield dividend stocks, investment portfolio translates into healthy dividend income which supports core operations of the company.

Cash flows and Liquidity Profile

Liquidity of the company is considered strong as reflected in sizeable liquid assets (including strategic listed investments) maintained in relation to borrowings and technical reserves. However, adjusted liquid assets in relation to adjusted technical reserves and borrowings are low and are on a declining trend on a timeline basis. Insurance debt in relation to gross premium has increased on a timeline basis to 87.8% (FY19: 73.3%; FY18: 87.2%) and is significantly higher than the rating benchmark and peer companies.

During 9MFY20, the company generated lower cash flows from operations amounting to Rs. 247m (FY19: Rs. 1.8b; FY18: Rs. 365m) mainly due to higher reinsurance premiums paid and some reduction in dividend income. Paid up capital of the company remained at Rs. 680.6m at end-9MFY20 that is higher than the regulatory requirement of Rs. 500m. Despite healthy net profit of Rs. 641.2m, equity base of the company declind to Rs. 13.8b (FY19: Rs. 14.9b; FY18: Rs. 13.9b) due to decrease in unrelized fair value gain on available-for-sale portfolio of investments and dividend payment.

Operating and financial leverage remained low at 4.5% (FY19: 6.2%; FY18: 4.3%) and 13.2% (FY19: 11.2%; FY18: 9.6%) respectively during 9MFY20. 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 — Annexure I

Financial Summary (*amounts in PKR millions*)			
BALANCE SHEET	**DEC 31, 2018**	**DEC 31, 2019**	**SEP 30, 2020**
Cash and Bank Accounts	233.1	268.6	761.3
Deposits Maturing Within 12 Months	-	-	-
Investments	14,015.0	16,254	15,330
Insurance Debt	2,176.6	2,289.5	3,447.6
Total Assets	18,996.7	21,820.3	23,057.2
Paid Up Capital	680.6	680.6	680.6
Net Worth	13,870.4	14,917.6	13,768.0
Borrowings	194.9	193.2	1,952.7
Total Liabilities	5,125.4	6,902.7	9,289.1
INCOME STATEMENT	**DEC 31, 2018**	**DEC 31, 2020**	**SEP 30, 2020**
Net Premium Revenue	599.6	696.0	612.7
Net Claims	83.2	110.5	83.9
Underwriting Profit/(Loss)	282.4	289.9	281.7
Investment Income	995.1	1,037.2	673.6
Other Income	27.6	48.4	22.5
Profit Before Tax	1,291.8	1,375.5	903.1
Profit After Tax	853.8	959.4	641.2
RATIO ANALYSIS	**DEC 31, 2018**	**DEC 31, 2020**	**SEP 30, 2020**
Cession Ratio (%)	75.2	73.9	75.3
Gross Claims Ratio (%)	13.0	20.8	13.3
Net Claims Ratio (%)	13.9	15.9	13.7
Underwriting Expense Ratio (%)	39.0	42.5	40.3
Combined Ratio (%)	52.9	58.3	54.0
Insurance Debt to Gross Premium (%)	87.2%	73.3%	87.8*
Operating Leverage (%)	4.3	4.7	4.5*
Financial Leverage (%)	9.6	11.2	13.2
Adjusted Liquid Assets to Technical Reserves & Borrowing (%)	27.3	24.1	16.2

**Annualized*

ISSUE/ISSUER RATING SCALE & DEFINITIONS — Annexure II

VIS Credit Rating Company Limited

RATING SCALE & DEFINITIONS: ISSUES / ISSUERS

Medium to Long-Term

AAA
Highest credit quality; the risk factors are negligible, being only slightly more than for risk-free Government of Pakistan's debt.

AA+, AA, AA-
High credit quality; Protection factors are strong. Risk is modest but may vary slightly from time to time because of economic conditions.

A+, A, A-
Good credit quality; Protection factors are adequate. Risk factors may vary with possible changes in the economy.

BBB+, BBB, BBB-
Adequate credit quality; Protection factors are reasonable and sufficient. Risk factors are considered variable if changes occur in the economy.

BB+, BB, BB-
Obligations deemed likely to be met. Protection factors are capable of weakening if changes occur in the economy. Overall quality may move up or down frequently within this category.

B+, B, B-
Obligations deemed less likely to be met. Protection factors are capable of fluctuating widely if changes occur in the economy. Overall quality may move up or down frequently within this category or into higher or lower rating grade.

CCC
Considerable uncertainty exists towards meeting the obligations. Protection factors are scarce and risk may be substantial.

CC
A high default risk

C
A very high default risk

D
Defaulted obligations

Short-Term

A-1+
Highest certainty of timely payment; Short-term liquidity, including internal operating factors and /or access to alternative sources of funds, is outstanding and safety is just below risk free Government of Pakistan's short-term obligations.

A-1
High certainty of timely payment; Liquidity factors are excellent and supported by good fundamental protection factors. Risk factors are minor.

A-2
Good certainty of timely payment. Liquidity factors and company fundamentals are sound. Access to capital markets is good. Risk factors are small.

A-3
Satisfactory liquidity and other protection factors qualify entities / issues as to investment grade. Risk factors are larger and subject to more variation. Nevertheless, timely payment is expected.

B
Speculative investment characteristics; Liquidity may not be sufficient to ensure timely payment of obligations.

C
Capacity for timely payment of obligations is doubtful.

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

(SO) Rating: A suffix (SO) is added to the ratings of 'structured' securities where the servicing of debt and related obligations is backed by some sort of financial assets and/or credit support from a third party to the transaction. The suffix (SO), abbreviated for 'structured obligation', denotes that the rating has been achieved on grounds of the structure backing the transaction that enhanced the credit quality of the securities and not on the basis of the credit quality of the issuing entity alone.

(blr) Rating: A suffix (blr) is added to the ratings of a particular banking facility obtained by the borrower from a financial institution. The suffix (blr), abbreviated for 'bank loan rating' denotes that the rating is based on the credit quality of the entity and security structure of the facility.

'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

'SD' Rating: An 'SD' rating is assigned when VIS believes that the ratee has selectively defaulted on a specific issue or obligation but it will continue to meet its payment obligations on other issues or obligations in a timely manner.

REGULATORY DISCLOSURES				Annexure 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			
	31/12/2020	AA	Stable	Reaffirmed
	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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Due Diligence Meetings Conducted	**Name**	**Designation**	**Date**	
	Mr. Farrukh Aleem	CEO	December 21, 2020	
	Mr. Khuram Shahzad	CFO	December 21, 2020	