RATING REPORT

Security General Insurance Company Limited (SGICL)

REPORT DATE:

December 29, 2022

RATING ANALYSTS:

Tayyaba Ijaz, CFA
tayyaba.ijaz@vis.com.pk

RATING DETAILS		
	Latest Rating	Previous Rating
Rating Category	Long-term	Long-term
IFS	AA+	AA+
Rating Date	*Dec 29, '22*	*Mar 31, '22*
Rating Outlook	Reaffirmed	Harmonized

COMPANY INFORMATION	
Incorporated in 1996	**External Auditors:** Riaz Ahmad & Company, 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) (above 5%):	
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%	
Roomi Holdings (Pvt.) Limited -9.66%	
Roomi Enterprises (Pvt.) Limited- 8.57%	
Mrs. Naz Mansha – 7.50%	

APPLICABLE METHODOLOGY(IES)

Applicable Rating Criteria: General Insurance (March 2022)
https://docs.vis.com.pk/docs/VIS%20General%20Insurance%20-%2020220331%20-%20FinalFinal.pdf

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 13 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 16 years of experience in the insurance industry and holds a postgraduate degree in Business Administration.

Financial Snapshot

Net Equity: 9MCY22: Rs. 14.8b; CY21: Rs. 16.8b; CY20: Rs. 14.4b

Net Profit: 9MCY22: Rs. 702.2m; CY21: Rs. 1.5b; CY20: Rs. 707.1m

RATING RATIONALE

The rating assigned to Security General Insurance Company Limited (SGICL) takes into account its association with a large diversified conglomerate "Nishat Group" having business interests in banking, textile, cement, power generation, real estate, hospitality, automobile, dairy and paper products. The company posted a steady growth in gross premium revenue on YoY basis. Financial and operating leverage have remained low on a timeline basis and reflects strong loss absorption capacity. The liquidity position is considered adequate in terms of sizeable liquid assets in relation to technical reserves and borrowings. However, insurance debt in relation to gross premium needs to remain within the peer group parameters.

The assigned rating is also supported by a sound reinsurance panel; all reinsurers, except one, are rated in category 'A' or higher. During 9MCY22, claims performance remained under pressure due to higher incidence of claims pertaining to flood related damages during third quarter of the ongoing year. SGI has very limited exposure in Agri and Livestock, which majorly pertained to insurances by microfinance banks while major losses emanated from destruction of motor vehicles from floods. Overall 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 also derives strength from recurring investment income from blue chip companies.

Insurance Sector Update: Insurance penetration in Pakistan has remained below that of neighboring counterparts, given non-life insurance penetration of ~0.355% vis-à-vis India at 4.2% and Sri-Lanka 1.39%. During CY21, the gross premiums/ takaful contributions underwritten by the industry grew by 11%, picking up from 8% in 2020. In 1HCY22, given the increase in inflation, we have noted a change in trend wherein industry underwriting posted a growth of 26% vis-s-vis SPLY.

The industry's combined ratio posted a dip in CY21, which was driven by a drop in both net claims and expense ratios. Overall, the impact of investment returns on industry profitability remained similar, investment returns stood at 17% of the net premium. Even though operating leverage of Pakistan's insurance industry remains adequately high, which is partly explained by lagged growth, in June'22, we have noted a trend of an uptick in operating leverage to 67.3% (annualized). Apart from the overall growth in underwriting, this is also partly attributable to dividend payouts in Q1 and mark to market losses on fixed income portfolios in Q2.

(Rs. in Billions)	CY20	CY21	1H'CY22
Insurance Premium (Gross)	89.6	97.4	55.8
Takaful Contributions (Gross)	12.6	16.2	10.4
Industry Total (Gross)	102.3	113.6	66.2
Combined Ratio	95.3%	84.4%	89.8%
- Net Claims Ratio	54.8%	49.4%	53.2%
- Underwriting Expense Ratio	40.5%	35.0%	36.7%
Net Operating Ratio	78.6%	67.5%	74.6%
RoAA	4.4%	5.4%	3.8%*
RoAE	10.1%	12.8%	9.6%*
Operating Leverage	52.5%	58.3%	67.3%*

**Annualized*

Investment returns in 1HCY22, have not depicted much deviation, unlike the one noted in life insurance portfolios. This is partly attributable to a different asset management strategy, albeit also implies that the industry was well placed in terms of portfolio duration leading up to 400 bpts steep drop in benchmark rates noted in Q2'2022. Given higher benchmark rates, investment yield is expected to improve in 2023.

Meanwhile, in the aftermaths of recent floods, many insurance industry players have posted underwriting losses during Q3'22 on account of augmentation in claims. The growth outlook for insurance industry also seems somewhat vague due to prevailing uncertainty in economic and political environment.

The implementation of IFRS 17 will commence from January 1' 2025. The SECP has issued instructions of phase-wise implementation of IFRS 17. The deadline to complete phase-II is end-Dec'22. 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.

Business Strategy: The company primarily offers general insurance for fire and property damage, marine, aviation and transport, motor, and miscellaneous risks including crop, livestock, burglary, loss of cash in safe and cash in transit, engineering losses, business interruption losses, accident, and natural calamities. The company operates via eight branches spread across Pakistan while the management does not intend to expand its branch network in the medium term. The business mix remained largely dominated by Fire segment, followed by Motor, Marine and Miscellaneous during 9MFY22. The contribution of Marine segment declined in the ongoing year due to elimination of a major policy, i.e., PIA, covered by the company. The PIA business was obtained by the end-Dec'20 while the company was not able to retain the client owing to highly competitive public sector insurance industry dynamics. Despite that, during 9MCY22, gross business written by the company posted a growth of ~14% YoY, amounting to Rs. 4.1b (9MCY21: Rs. 3.6b; CY21: Rs. 3.9b; CY20: Rs. 8.8b) majorly on account of growth in Fire segment; gross written premium (GWP) in Fire increased to Rs. 3.2b (9MCY21: Rs. 2.4b). Motor business also showed some YoY growth to Rs. 456.4m (9MCY21: Rs. 387.4; CY21: Rs. 538.9m; FY20: Rs. 435.0m). Marine and Miscellaneous segments remained relatively subdued during the ongoing year. The company did not accept facultative business during the ongoing year due to higher risk involved (9MCY21: Rs. 855.3m; CY21: Rs. 855.6m; CY20: 861.5m).

Underwriting business from group companies has provided notable support to the portfolio on a timeline basis, with a contribution of around 34% (FY21: 14%; FY20: 37%) to the GWP. During 9MCY22, underwriting business from related parties increased to Rs. 1.77b, which, as a percentage of gross premium also increased to Rs. 43.7%. Business from takaful operations increased to Rs. 208.5m (CY21: Rs. 105.8m; CY20: Rs. 67.9m) in 9MCY22. The management foresees steady growth in takaful operations, going forward. The management expects to close CY22 at around Rs. 6b in GWP. The business mix of SGI is presented below:

Business Mix	**CY20**	**CY21**	***9MCY21***	**9MCY22**
Fire	27.3%	64.6%	*66.3%*	78.1%
Marine	64.1%	15.0%	*15.0%*	6.1%
Motor	4.9%	13.7%	*10.7%*	11.2%
Miscellaneous	3.6%	6.7%	*8.0%*	4.6%
Gross Premium (Rs. m)	**8,799.0**	**3,923.9**	***3,623.6***	**4,069.6**

Reinsurance Arrangement: During CY21 and CY20, the overall cession ratio seemed somewhat distorted due to one-time business ceded under marine segment. Meanwhile, in 9MCY22, overall, cession ratio was reported substantially lower at 53.7% (9MCY21: 172.9%). Therefore, despite lower premium earned in CPLY, the company was able to report higher net insurance premium of Rs. 730.4m (9MCY21: Rs. 691.7m) in 9MCY22. The cession was lower in all operating segments was reported lower vis-à-vis preceding period.

Cession	**CY20**	**CY21**	***9MCY21***	**9MCY22**
Fire	74.9%	76.2%	*59.4%*	53.0%
Marine	5.6%	981.2%	*822.3%*	89.1%
Motor	50.3%	44.4%	*46.6%*	40.6%
Miscellaneous	76.6%	94.0%	*64.9%*	51.2%

Overall Cession Ratio	**29.3%**	**208.4%**	***172.9%***	**53.7%**

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. There were no major changes in reinsurance treaties in CY22. For FY23, the management is striving to retain previous year's terms with the reinsurers.

Claims Experiences: During 9MCY22, claims performance remained under pressure due to higher incidence of claims pertaining to flood related damages during third quarter of the ongoing year. SGI has very limited exposure in agri and livestock, which majorly comprised insurances by microfinance banks while major losses emanated from destruction of motor vehicles from floods. Net claim ratio of Fire segment increased mainly due to the fire incident at Bulleh Shah Packaging (Pvt.) Ltd. in Feb'22, which has been so far the biggest loss in the insurance industry; SGI had net exposure of 7.5% in the same which was largely placed in facultative insurance. Overall 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 led to good claim performance over the years. The segment-wise net claims ratios are presented in the table below:

Net Claim Ratio	**CY20**	**CY21**	***9MCY21***	**9MCY22**
Fire	3.3%	-0.7%	*2.6%*	4.5%
Marine	19.7%	6.6%	*8.5%*	10.3%
Motor	36.9%	44.2%	*40.2%*	48.0%
Miscellaneous	14.7%	17.6%	*20.7%*	25.4%
Overall Net Claim Ratio	**13.7%**	**13.0%**	***13.8%***	**21.0%**

Underwriting Performance: The underwriting performance of the company remained subdued during 9MCY22 as compared to CPLY owing to the impact of higher net claim ratio. Whereas underwriting expense ratio remained largely stable due to increase in scale of operations despite inflationary impact on operating expenses and higher commission expenses. Combined ratio was reported higher at 65.7% (9MCY21: 58.1%; CY21: 59.6%; CY20: 59.6%). However, the combined ratio of the company continues to remains one of the lowest amongst the peer insurance companies. All segments reported profits during 9MCY22 and CY21 while profitability of the Fire segment was reported notably lower YoY owing to higher allocation of expenses in line with its proportion in business mix. The snapshot of underwriting results is tabulated below:

Underwriting Profit	**CY20**	**CY21**	***9MCY21***	**9MCY22**
Fire	370	290	*203*	109
Marine	(178)	35	*42*	47
Motor	120	25	*29*	72
Miscellaneous	43	24	*16*	23
Total	**354**	**374**	***290***	**250**

During 9MCY22, the company generated a healthy investment income amounting Rs. 978.3m (9MCY21: Rs. 1.6b; CY21: Rs. 1.8b; CY20: Rs. 724.5m). Investment income appeared inflated in the preceding year as the company received additional dividend income from a bank during that period which was put on hold for the last two quarters of FY20 on directives of the regulator amidst covid. Around 98% of investment income constituted dividend income which has provided considerable support to the core operations on a timeline basis. Other income, majorly comprising return on bank balances was reported higher at Rs. 65.3m (9MCY21: Rs. 27.1m; CY21: Rs. 41.9m; CY20: Rs. 42.4m) mainly due to higher average markup rates during 9MCY22. Contribution from takaful operations amounted to Rs. 20.0m (9MCY21: Rs. 15.2m; CY21: Rs. 20.4m; CY20: Rs. 11.2m). Accounting for taxation, net profit was recorded at Rs. 702.2m (9MCY21: Rs. 1.3b;

CY21: Rs. 1.5b; CY20: Rs. 707.1m) during 9MCY22.

As per management, underwriting performance in the last quarter of ongoing year has so far been relatively better than CPLY. Moreover, with no other major claims expected and support from investment income, the management projects healthy bottomline in full year as well.

Investments: Investment portfolio mainly comprises blue-chip companies, 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). Carrying value of the investment portfolio decreased to Rs. 15.9b (CY21: Rs. 19.4b; CY20: Rs. 16.6b) primarily due to fair value net losses amounting Rs. 3.1b (CY21: Gain of Rs. 1.6b; CY20: gain of Rs. 65.1m) on NHPL and HNML. There were net redemptions in available for sale equity securities amounting Rs. 505.7m which largely entailed mutual fund investments. Investment of Rs. 30m was made in HNML during 9MCY22. Net addition of Rs. 36m was made in term deposits. Investment in debt securities stood higher at Rs. 151.8m (CY21: Rs. 109.7m; CY20: Rs. 67.7m) which comprised Pakistan Investment Bonds (PIBs) amounting Rs. 73.8m (CY21: Rs. 75.7m; CY20: Rs. 67.7m) while the rest pertained to short-term deposits. The PIBs are placed as statutory deposit with the State Bank of Pakistan (SBP) in accordance with the requirement Insurance Ordinance, 2000 (Section 29(2)(a)).

The company intends to invest an additional amount to the tune of Rs. 1.1b in right shares of HNML to support its working capital requirements. The investment would be partly financed with long-term bank borrowings upto Rs. 600m and the rest would be funded through own sources. The management expects to receive dividend income from NHPL and HNML in FY23.

Liquidity and capitalization: Overall liquidity of the company is considered strong as reflected by sizeable liquid assets (including strategic listed investments) maintained in relation to borrowings and technical reserves. Adjusting liquid assets for strategic investments, the proportion in relation to adjusted technical reserves and borrowings stood at 33.5% (CY21: 36.4%; CY20: 31.6%). Insurance debt in relation to gross premium remained sizeable on a timeline basis, relative to the rating benchmarks and peer companies. This has primarily been due to major policies relating to power projects being underwritten in July and September every year. Operating cash flows were reported negative during 9MCY22 mainly owing to higher net cash outflows in underwriting activities as compared to return and dividend received from its cash and bank balances and investment portfolio.

	CY20	**CY21**	**9MCY22**
Total liquid assets	17,288	20,071	16,635
Total liquid assets/ net technical reserves + borrowings	659.5%	862.7%	627.3%
Liquid assets (ex-strategic)	828	846	887
Liquid assets (ex-strategic)/ net tech reserves + borrowings	31.6%	36.4%	33.5%
Insurance debt to gross premium	100.3%	76.2%	87.8%*
Operating cash flows to net premium	87.7%	286.8%	n.m.

**Annualized*

Paid up capital of the company remained at Rs. 680.6m, higher than the regulatory requirement of Rs. 500m. Equity base augmented to Rs. 16.8b (CY21: Rs. 14.4b) on account of internal capital generation and unrealized gain on AFS investment. Meanwhile, during 9MCY22, equity base decreased to Rs. 14.8b as a result of unrealized fair vlaue loss. The company paid dividend of Rs. 136.2m (CY21 & CY20: Rs. 340.3m) during 9MCY22.

The company has arranged short-term running finance facilities from various banks to ensure sufficient availability of funds. Short-term running finances available from commercial banks under markup arrangements amounted to Rs. 1.05b (CY21: Rs. 1.15b; CY20: Rs. 1.4b), out of which the company availed Rs. 636.3m (CY21: Rs. 246.6m; CY20: Rs. 309.3m) as of September 30, 2022. Long-term financing amounting Rs. 1.2b (CY21: Rs. 1.4b; CY20: Rs. 1.6b) has been obtained at three months KIBOR plus fixed spread of 0.5% per annum, payable quarterly on the balance outstanding. The long-term facilities have largely been obtained by the company to finance its strategic investments. Net technical reserves increased to Rs. 1.0b (CY21: Rs. 683.4; CY20: Rs. 684.9m) by end-9MCY22. Operating and financial leverage remained low at 6.5% (CY21: 4.1% CY20: 5.7%) and 6.8% (CY21: 4.1%; CY20: 4.8%), respectively. 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

BALANCE SHEET	Dec 31, 2019	Dec 31, 2020	Dec 31, 2021	Sep 30, 2022
Investments	16,253.8	16,589.9	19,429.7	15,900.7
Insurance Debt	2,289.5	8,825.5	2,988.3	4,754.3
Cash and Bank Deposits	268.6	697.9	641.6	734.7
Total Assets	21,820.3	34,532.2	26,352.6	26,126.5
Paid Up Capital	680.6	680.6	680.6	680.6
Net Worth	14,917.6	14,410.6	16,766.2	14,844.2
Total Liabilities	6,902.6	20,121.6	9,586.4	11,282.3
INCOME STATEMENT	**Dec 31, 2019**	**Dec 31, 2020**	**Dec 31, 2021**	**Sep 30, 2022**
Gross Premium Revenue	3,122	8,799	3,924	4,070
Net Premium Revenue	696.0	815.9	924.4	730.4
Net Claims	110.5	111.5	119.9	153.2
Underwriting Profit	289.9	354.4	373.5	250.4
Net Investment Income	1,037.2	724.5	1,831.3	978.3
Profit Before Tax	1,354.0	1,008.0	2,104.4	1,172.0
Profit After Tax	959.4	707.1	1,499.6	702.2
RATIO ANALYSIS	**Dec 31, 2019**	**Dec 31, 2020**	**Dec 31, 2021**	**Sep 30, 2022**
Cession Ratio (%)	69.3	29.3	208.4	53.7
Gross Claims Ratio (%)	22.7	15.6	6.7	44.9
Net Claims Ratio (%)	15.9	13.7	13.0	21.0
Underwriting Expense Ratio (%)	42.5	43.0	46.6	44.7
Combined Ratio (%)	58.3	56.7	59.6	65.7
Insurance Debt to Gross Premium (%)	73.3	100.3	76.2	87.8
Operating Leverage (%)	4.7	5.7	4.1	6.5
Financial Leverage (%)	4.5	4.8	4.1	6.8
Liquid Assets to Net Technical Reserves (%)	1916.6	659.5	862.7	627.3
Adjusted Liquid Assets to Net Technical Reserves plus borrowings (%) **	49.6	31.6	36.4	33.5

**Annualized*

***Liquid assets adjusted for strategic investments*

ISSUE/ISSUER RATING SCALE & DEFINITIONS Annexure II

RATING SCALE & DEFINITIONS: INSURER FINANCIAL STRENGTH

AAA(IFS)
Exceptionally Strong. Exceptionally strong capacity to meet policy holders and contract obligations. Risk factors are minimal, and the impact of any adverse business and economic factors is expected to be extremely small.

AA++(IFS), AA+(IFS), AA(IFS)
Very Strong. Very strong capacity to meet policy holders and contract obligations. Risk factors are very low, and the impact of any adverse business and economic factors is expected to be very small.

A++(IFS), A+(IFS), A(IFS)
Strong. Strong capacity to meet policy holders and contract obligations. Risk factors are low, and the impact of any adverse business and economic factors is expected to be small.

BBB++(IFS), BBB+(IFS), BBB(IFS)
Good. Good capacity to meet policyholder and contract obligations. Risk factors are moderate, and the impact of any adverse business and economic factors is expected to be manageable.

BB++(IFS), BB+(IFS), BB(IFS)
Marginal. Marginal capacity to meet policyholders and contract obligations. Though positive factors are present, risk factors are relatively high, and the impact of any adverse business and economic factors is expected to be significant.

B++(IFS), B+(IFS), B(IFS)
Weak. Weak capacity to meet policyholder and contract obligations. Risk factors are high, and the impact of any adverse business and economic factors is expected to be very significant.

CCC(IFS) , CC(IFS), C(IFS)
Very Weak. Very weak capacity to meet policyholder and contract obligations. Risk factors are very high, and the impact of any adverse business and economic factors may lead to insolvency or liquidity impairment.

D(IFS)
Distressed. Extremely weak capacity with limited liquid assets to meet policyholders and contractual obligations, or subjected to some form of regulatory intervention or declared insolvent by the regulator.

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. https://docs.vis.com.pk/docs/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. https://docs.vis.com.pk/docs/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. https://docs.vis.com.pk/docs/private_ratings.pdf

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			
29/12/2022	AA+	Stable	Reaffirmed
31/03/2022	AA+	Stable	Harmonized
31/01/2022	AA	Stable	Reaffirmed
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.
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Due Diligence Meetings Conducted

Name	Designation	Date
Mr. Khuram Shahzad	CFO	November 29, 2022