RATING REPORT

Alpha Insurance Company Limited

REPORT DATE:
September 29, 2021

RATING ANALYSTS:
Asfia Aziz
asfia.aziz@vis.com.pk

Sundus Qureshi
sundus.qureshi@vis.com.pk

RATING DETAILS		
	Latest Rating	**Previous Rating**
Rating Category	**Long-term**	**Long-term**
IFS	A	A
Rating Outlook	Stable	Negative
Rating Date	*September 29, 2021*	*October 20, 2020*

COMPANY INFORMATION	
Incorporated in 1951	**External auditors:** **2021 -** Grant Thornton Anjum Rahman Chartered Accountants
Public Limited Company	**Chairman of the Board:** Mr. Muhammad Izqar Khan
Key Shareholders (with stake 5% or more):	**Chief Executive Officer:** Mr. Nadeem Bessey
State Life Insurance Corporation– 95%	
Individuals - 5%	

APPLICABLE METHODOLOGY(IES)
VIS Entity Rating Criteria: General Insurance (November 2019)
https://docs.vis.com.pk/docs/Meth-GenInsurance201911.pdf

Alpha Insurance Company Limited

OVERVIEW OF THE INSTITUTION

Alpha Insurance Company Limited was incorporated in 1951. State Life Insurance Corporation is the parent company of the organization, possessing 95% stake in the company. Registered office of the company is located in Karachi. AICL has branch net work in all the major cities of Pakistan including Lahore, Multan, Faisalabad, Peshawar, Islamabad, Rawalpindi, and Karachi.

RATING RATIONALE

Assigned rating of Alpha Insurance Company Limited (AICL) is underpinned by financial and sponsor profile of its primary shareholder, State Life Insurance Corporation of Pakistan (SLIC). SLIC is the largest life insurance company in the country and is owned by the Government of Pakistan. Nonetheless, the rating is constrained on account of persistent trend in underwriting losses, low business volumes and quality of insurance debt in comparison to peers. Going forward, materialization of projected business growth as a result of rehabilitation program is considered important.

Key Rating Drivers

Despite challenging macroeconomic environment amidst COVID-19, insurance industry grew by ~9% (in terms of gross premium underwritten) in 2020. Overall industry depicts significant room for growth, given a very low non-life insurance penetration to GDP.

Financial Indicators- Insurance Industry		
(Rs. in Billions)	2019	2020
Insurance Premium (Gross)	83.7	89.6
Takaful Contributions (Gross)	11	12.6
Industry Total (Gross)	94.6	102.3
Combined Ratio	89.10%	95.30%
- Net Claims Ratio	51.70%	54.80%
- Underwriting Expense Ratio	37.40%	40.50%
Net Operating Ratio	72.50%	78.60%
RoAA	4.70%	4.40%
RoAE	10.50%	10.10%
Operating Leverage	49.60%	52.50%

- The gross premiums/ takaful contributions underwritten by the industry grew by 8% in 2020, as data published by Insurance Association of Pakistan. The growth mainly emanated from additional marine segment underwriting from a single company (Security General Insurance Company Limited), while the remaining industry participants – apart from a few small-sized insurers – posted meagre growth, thus trailing the prevailing inflation during the period.
- As a result, non-life insurance penetration, estimated at ~0.2%, has receded further. Overall non-life insurance penetration in Pakistan lags regional peers.
- Given the meagre growth in premiums, the industry's combined ratio posted an uptick, which was driven by an uptick in both net claims and expense ratios.
- The investment performance remained strong during the period, with overall investment income posting an uptick of 13%.
- The sector's operating leverage remains at around 50%, which is considered to be on the lower side and there is certainly room for additional insurance penetration in the domestic market. With the Government entering its final 2 years, GDP growth is projected to pick pace, which is expected to lift insurance industry growth over the medium term horizon.
- Overall capitalization & liquidity buffers in place are considered to be adequate.

- Going forward, plans of implementation of IFRS 17 across the industry is expected to require additional provisioning. However, the industry's IFRS 17 implementation is scheduled for January 1' 2022 and so far we have not received an estimation of the related provisioning charge.

Measured impact of Covid-19 outbreak on insurance industry

The outbreak had an impact on a wide variety of sectors which variably weighs down on the insurance industry. However, with insurance penetration to GDP already being too low and bulk of the policies representing repeat policy issuances, impact on Property and Miscellaneous Business was limited but the Marine (due to reduced international trade) and Motor Business (lower auto sales) depicted an overall downward trend.

Rehabilitation Program

To revive the company and make it financially sustainable, the management has formulated a rehabilitation plan; key focus points of the same being the following:

- Identifying new un-tapped market segments;
- Re-enlistment and enhancement of limits with banks;
- Improving efficiency through cost management;
- Consolidation through closure of un-productive branches, and opening new branches over the medium term

New business generation has been a challenge in the outgoing year given the slowdown in economic activity due to COVID-19 outbreak. However, GPW witnessed growth and stood at a higher level in HY21 as compared to the preceding year.

In 2020, gross premiums written (GPW) amounted to Rs. 97.04m (2019: Rs. 114.9m), registering a decline of ~16% vis-à-vis ~9% industry growth. Fire & property, motor and marine segment have continue to contribute more than three-fourth of topline and are projected to remain the key growth drivers, going forward. Generation of new business as a result of the pandemic was a challenge in 2020; however, GPW witnessed growth and stood at a higher level in HY21 as compared to the preceding year. Business mix is projected to remain the same going forward with sizeable concentration in fire, marine and motor segments. As a part of management's strategy exposure in health insurance will continue to be limited, going forward. AICL is also in the process of establishing Window Takaful Operations which will further enhance the business base of the company.

Business Mix	CY18	CY19	CY20	HY21
Fire and property damage	33%	29%	30%	34%
Marine, aviation and transport	14%	20%	23%	22%
Motor	24%	27%	25%	32%
Accident and health	11%	9%	13%	0%
Bond	4%	0%	2%	0%
Miscellaneous	15%	15%	7%	12%
GPW- Gross Premium Written	**83.47**	**114.85**	**97.04**	**51.51**

Reinsurance limits enhanced in 2020 to Rs. 500m (2019: Rs. 300m) with projected enhancement in the same to Rs. 750m with similar retention levels. Reinsurance treaties consist of a diversified panel of local and international reinsurers.

Reinsurance treaties of the company depicted some changes during the period under review. With a new business plan in place, reinsurance treaties for the year 2020 were revised with higher capacities. Ocean International Reinsurance Company Limited (A-) has replaced Best Meridian International Insurance Company (A-) during 2021. As per the treaty arrangements, all segments are covered by XoL treaties, barring terrorism which has a quota share treaty in place. Going forward, as per the rehabilitation program of the company, the management plans to increase reinsurance capacity to Rs. 750m with similar retention levels. Ratings draw comfort from a diversified panel of local and international reinsurers. Retention ratio of the company has remained stable over the past two years at 65%. Management expects retention levels to remain unchanged, going forward.

Loss ratios deteriorated in CY20 on account of higher amount of carried forward claims expensed as compared to the preceding year. However, claims ratio on gross and net basis depicted improvement during 1H2021.

Loss ratios deteriorated in CY20 on account of higher amount of carried forward claims expensed as compared to the preceding year. The weakening in CY20 was primarily due to high claims across all operating segments. However, Gross claims ratio and Net claims ratio of the company, both improved and were reported lower during 1H2021. As the business volumes grow, loss ratios will need to be monitored closely given that it will continue to be a function of the quality of underwriting undertaken by management.

Net Claims Ratio	CY18	CY19	CY20	HY21
Fire and property damage	277%	-258%	80%	-133%
Marine, aviation and transport	433%	-41%	56%	0%
Motor	0%	39%	40%	39%
Accident and health	102%	88%	98%	66%
Bond	101%	0%	0%	0%
Miscellaneous	-98%	14%	82%	73%
Total Net Claims Ratio	**97%**	**4%**	**63%**	**-4%**

Return from investments continues to support the underwriting operations of the company. As per management, the trend is expected to persist till a breakeven level of premium is achieved by AICL.

The company has maintained a balanced investment portfolio with around one-half of the total asset base parked in fixed income instruments followed by exposure in equities contributing around 20% of the asset base at end-June'21.

At end-December 2020, investment mix of the company largely comprised of long-term government securities. With declining interest rates in the market, investment returns from government securities increased from Rs. 48.1m in 2019 to Rs. 51.5m in 2020. Despite support from investments, underwriting loss in the outgoing year has remained significant on account of low business volumes. Given the higher level of business volumes in first half of 2021, and projected improvement in the same, management envisages to report higher profit after tax in the ongoing year largely supported by higher investment income.

The combined ratio improved to 188% in 2020 as compared to 199% in the preceding year attributable to higher premium net of insurance premium. Given higher investment income, the company reported a positive bottom line during 2020 with net operating ratio being reported at 102% (2019: 127%) during 2020. Net Operating Ratio significantly improved to 26% in 1H2021 led by higher business volumes and lower claims expense. Going forward, maintaining these profitability metrics in view of the prevalent competition faced by the industry players is considered important. Given no expected reduction in interest rates, the investment income of the company is expected to remain subdued due to absence of capital gains. While reduced economic activity is likely to have a positive impact on claims ratio, expenses are likely to remain sticky, which should resultantly increase underwriting expense ratio. Subsequently, the combined ratio is likely to remain range bound. Moreover, projected increment in overall business volumes and net profitability is contingent on successful implementation of the rehabilitation program.

Capitalization levels continue to remain sound to support future growth plans. Leverage indicators have depicted improvement.

Capitalization levels of the company are considered adequate as evident from low leverage indicators in line with lower underwriting levels. Capitalization levels are sufficient to cater to the short to medium term growth plans of the company. Equity level stands higher at Rs. 716m at end-June 2021. At half year-end 2021, financial leverage (adjusted for reinsurance recoveries against outstanding claims) exhibited considerable improvement and was reported at 22% (2020: 37%; 2019: 39%) while operating leverage has slightly increased on a timeline basis given the growth in business base (HY21: 11.0%; 2020: 10.0%; 2019: 9.0%). Nevertheless, both leverage indicators are aligned with peer median. Going forward, mandatory implementation of IFRS 17 (as planned to be implemented by Jan'22) would impact the overall capitalization metrics, the magnitude of which is unknown.

Liquidity profile has shown significant improvement on account of lower underwriting liabilities and adequate exposure in liquid assets. Net insurance debt (after accounting or impairment provisions) as a proportion of gross premium continues to remain within manageable limits.

Given lower economic activity in 2020, cash outflow decreased primarily on account of lower quantum of claims paid, and lower reinsurance premiums paid. Liquidity profile has shown significant improvement on account of lower underwriting liabilities and adequate exposure in liquid assets.

Net insurance debt (after accounting or impairment provisions) as a proportion of gross premium continues to remain within manageable limits. (HY21: 50%; 2020: 27%; 2019: 54%). However, it is pertinent to mention that on an average, the company has recorded provisions for impairment on around 72% of the total gross insurance debt portfolio. Moreover, AICL has maintained an adequate buffer of solvency margin (2020: Rs. 654.2; Rs. 2018: Rs. 615.8m).

FINANCIAL SUMMARY				*(amounts in PKR millions)*
BALANCE SHEET	**31-Dec-18**	**31-Dec-19**	**31-Dec-20**	**30-Jun-21**
Cash and Bank Deposits	31.4	142.0	46.4	56.0
Investments	808.0	654.2	754.6	681.2
Insurance Debt	183.6	179.2	152.2	176.0
Total Assets	1,216.1	1,112.0	1,082.9	997.1
Paid-up Capital	500.0	500.0	500.0	500.0
Net Worth	705.6	705.5	700.1	716.0
Total Liabilities	510.5	406.4	382.8	281.1
INCOME STATEMENT				
Net Insurance Premium	47.4	60.2	70.3	40.0
Net Claims	(46.0)	(2.7)	(44.6)	1.7
Underwriting Profit/(Loss)	(97.5)	(56.0)	(57.9)	(3.7)
Other Income	4.4	24.8	6.8	2.9
Profit Before Tax	(53.5)	5.7	3.0	31.5
Profit After Tax	(49.6)	3.6	1.8	22.9
RATIO ANALYSIS				
Cession Ratio (%)	55%	35%	35%	35%
Retention Ratio (%)	45%	65%	65%	65%
Gross Claims Ratio (%)	55%	-14%	53%	-31%
Net Claims Ratio (%)	97%	4%	63%	-4%
Underwriting Expense Ratio (%)	217%	195%	124%	117%
Combined Ratio (%)	314%	199%	188%	113%
Net Operating Ratio (%)	222%	127%	102%	26%
Gross Insurance Debt to Gross Premium (%)	220%	156%	157%	171%
Net Insurance Debt to Net Premium (%)	115%	104%	37%	64%
Net Insurance Debt to Gross Premium (%)	65%	54%	27%	50%
Operating Leverage (%)	7%	9%	10%	11%
Financial Leverage (%)	20%	20%	17%	9%
Adjusted Liquid Assets to Technical Reserves (%)	225%	288%	310%	459%

INSURER FINANCIAL STRENGTH RATING SCALE & DEFINITIONS Appendix II

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: 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	Alpha Insurance Company Limited
Sector	Insurance
Type of Relationship	Solicited
Purpose of Rating	IFS Rating
Rating History	
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.
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.
Disclaimer	Information herein was obtained from sources believed to be accurate and reliable; however, VIS does not guarantee the accuracy, adequacy or completeness of any information and is not responsible for any errors or omissions or for the results obtained from the use of such information. VIS is not an NRSRO and its ratings are not NRSRO credit ratings. Copyright 2021 VIS Credit Rating Company Limited. All rights reserved. Contents may be used by news media with credit to VIS.
Due Diligence Meetings Conducted	

Rating History

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: IFS				
9/29/2021	A	-	Stable	Maintained
10/20/2020	A	-	Negative	Reaffirmed
6/28/2019	A	-	Negative	Maintained
1/31/2018	A	-	Stable	Reaffirmed
12/07/2016	A	-	Stable	Reaffirmed
12/15/2015	A	-	Stable	Reaffirmed
12/10/2014	A	-	Stable	Reaffirmed
9/30/2013	A	-	Stable	Maintained

Due Diligence Meetings Conducted

	Name	Designation	Meeting Date
1	Mr. Nadeem Bessey	Chief Executive Officer	August 25, 2021
2	Mr. Khawaja Balighuddin	Head of Underwriting & Re-insurance	August 25, 2021
3	Mr. Sabir Ali	Head of Claims	August 25, 2021
4	Mr. Faraz Ahmed	Chief Financial Officer	August 25, 2021