RATING REPORT

Pak-Qatar Family Takaful Limited

REPORT DATE:
December 07, 2023

RATING ANALYSTS:
Maham Qasim
maham.qasim@vis.com.pk

Basel Ali Assad
basel.ali@vis.com.pk

RATING DETAILS		
	Latest Rating	**Previous Rating**
Rating Category	**Long-term**	**Long-term**
Entity	A++ (IFS)	A++ (IFS)
Rating Outlook	Stable	Stable
Rating Date	*December 07, '23*	*June 29, '22*
Rating Action	*Reaffirmed*	*Reaffirmed*

COMPANY INFORMATION	
Incorporated in 2006	**External auditors:** M/s. Yousuf Adil Chartered Accountants
Public Unlisted Company	**Chairman of the Board:** H.E. Sheikh Ali Bin Abdullah Al Thani
Key Shareholders (with stake 5% or more):	**Chief Executive Officer:** Mr. Azeem Iqbal Pirani
Pak-Qatar Investment (Pvt.) Limited – 34.58%	
FWU Global Takaful Solutions – 15.20%	
Qatar Islamic Insurance Company – 10.97%	
Sheikh Ali Bin Abdullah Al Thani – 10.18%	
Qatar International Islamic Bank – 9.95%	

APPLICABLE METHODOLOGY(IES)

VIS Entity Rating Criteria: Life Insurance Family Takaful (October, 2023)
https://docs.vis.com.pk/docs/LifeTakaful-Oct-2023.pdf

APPLICABLE RATING SCALE(S)

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

Pak-Qatar Family Takaful Limited

OVERVIEW OF THE INSTITUTION

Established in 2006 as an unlisted public limited company, Pak Qatar Family Takaful Limited (PQFTL) was the first family takaful operator in Pakistan. The company offers individual and group life covers, with individual policies being the company's major business line in terms of premium income.

Profile of Chairman

A member of the Royal Family, Sheikh Ali is a prominent businessman in Qatar. By qualification, he is Bachelor of Science in Political Science from Portland State University, USA. Currently, he is the Chairman of Umm-Haish International, and Al-Jazeera Trading & Contracting. Earlier, he was the Chairman of Qatar International Islamic Bank.

Profile of CEO

Mr. Azeem Pirani brings along over 18 years of vast experience of Banking & Islamic Finance industry. He holds a Postgraduate Diploma in Islamic Banking and Finance from the Center of Islamic Economics in Pakistan, an MBA in International Business from the University of New Brunswick in Canada, and a BBA in Finance from the University of Houston in the United States.

Before joining Pak-Qatar Takaful, he was

RATING RATIONALE

The IFS rating assigned to Pak Qatar Family Takaful Limited ('PQFTL; or 'the Company') draws comfort from its strong sponsorship profile comprising of prominent Qatar-based financial institutions including Qatar International Islamic Bank and Qatar Islamic Insurance Company along with the joint-venture company, Pak-Qatar Investments (Pvt.) Limited (PQIL). The challenging macroeconomic environment during the rating review period truncated business activity, reflected particularly in the decline of individual first-year and renewal contributions, as inflationary pressure diminished disposable incomes. However, the Company aimed at arresting policy withdrawals by introducing a new non-conventional insurance product offering competitive savings returns in line with the high interest rate environment. Premium rate hardening coupled with cyclical uptick in group renewal contributions during 4QCY23 are expected to uplift the topline going forward; materialization of targets will be an important factor from a rating's perspective. Overall underwriting performance depicted a downturn owing largely to sizeable increase in claims from the Group Health segment and policy withdrawals despite improvement in operational efficiencies. However, growth in investment income, emanating largely from debt-securities, helped boost the bottom-line. Underwriting activity is supported by retakaful treaties with renowned international reinsurers, however, majority of underwriting risk is incurred by the Company owing to low cessation on a timeline basis. Furthermore, the Company's investment strategy witnessed a shift towards a more conservative approach in conjunction with the adverse stock market performance with the overall investment portfolio tilting towards government securities. Moreover, with sufficient available liquid assets as well as adequate capital coverage of claims, liquidity and capitalization levels remained satisfactory.

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. Moreover, 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 larger increase in claims. Accordingly, financial performance indicators for the

the Regional Head for Pakistan at FWU AG. As the main representative for the Munich headquartered company in Pakistan, he was responsible for setting up the branch as well as putting in place the required agreements to enable it to carry out its business of facilitating BancaTakaful.

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. No final timeline for the same is announced yet.

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 nonlife 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 elevated 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

Key Rating Drivers

Business Strategy

The Company's topline remained relatively stable, registering an annualized growth of 4.5% to Rs. 5.3b during 1HCY23 (CY22: Rs. 10.2b, CY21: Rs. 10.0b), largely due to reduction in individual contributions related to first-year policies. The same was an outcome of erosion of disposable income in line with steep inflation coupled with the already nominal local insurance penetration discouraging onboarding of new policyholders. Additionally, the challenging macroeconomic environment resulted in decline in renewal contributions which in turn impacted overall persistency levels; the same decline to 65.4% (CY22: 69.9%, CY21: 80%) during the ongoing year. Specifically, second-year persistency levels dropped notably to 48.9% (CY22: 52.2%, CY21: 63%) as the quantum of policy surrenders/withdrawals increased, which could impact topline growth going forward. In order to address the decline in gross contributions from the individual first-year and renewal segments, a new non-conventional unit-linked insurance product, Mahana Bachat Scheme (MBS), was introduced during the rating review period. This product offers policyholders competitive returns and shorter payback periods in the backdrop of the current high policy rate environment, akin to other savings products available in the market. Through this, the management aims to incentivize policyholders seeking to fully or partially surrender their current policies to remain vested in the Company. Consequently, the business mix shifted appreciably towards the top-up and single premium segment. Additionally, composition of the group segment grew as well given that the large-sized corporate entities were better positioned to absorb the inflation-adjusted revisions in policy prices. Moreover, while the Company's growth was hampered during the rating review period, it was able to navigate the difficult market circumstances comparatively better than peers with PQFTL's market share growing to 8.8% (CY22: 8.1%, CY21: 7.9%). Breakdown of business mix can be seen below:

	2020	2021	2022	1HCY23
First Year Contribution	20.9%	20.6%	14.4%	5.6%
Renewal Contribution	54.5%	48.1%	46.8%	38.3%
Top-up & Single Premium	4.3%	9.6%	12.3%	29.3%

Group Contribution	20.3%	21.8%	26.5%	26.7%
Total	**100.0%**	**100.0%**	**100.0%**	**100.0%**

In terms of sales channels, the Company continued its long-term strategy of focusing on expanding the topline through its direct sales force owing to greater cost efficiency. Therefore, the direct sales force contribution to total individual contributions increased on a timeline to 76% (CY22: 64.1%, CY21: 62.4%) during 1HCY23. According to management, the aforementioned strategy was reinforced on account of the recent implementation of SECP regulations on the bancassurance segment. Additionally, the Company added 3 new locations to its branch network during the rating review period, expanding the total network to 113 branches.

Going forward, the management projects total gross contributions to reach Rs. 14.5b by end-CY23 driven by higher expected demand for the new unconventional insurance product, inflation-adjusted premium pricing and uptick in renewal contributions from the group segment during 4QCY23 in line with cyclical trends. While the materialization of targets may prove to be challenging, gross contributions are, nonetheless, on track to exceed CY22 levels.

Profitability Performance

The Company's overall underwriting profit contracted to Rs. 544.5m (CY21: Rs. 1.1b) during CY22 largely on the back of higher net claims expense amounting to Rs. 6.6b (CY21: Rs. 5.8b). The weakening in the claims' ratio is an outcome of Group Health segment incurring net losses to the tune of Rs. 1.7b (CY21: Rs. 1.2b); the same was a function of inflationary pressure which notably augmented payout expenses. Additionally, the growth in surrenders/withdrawals of individual policies contributed to overall claim costs as policyholders sought to liquidate their holdings in order to meet immediate financial needs amidst the adverse macroeconomic environment. However, as per management, the majority of the surrendered policies were reinvested into the Company's new unconventional insurance product, MBS. The expense ratio, on the other hand, depicted improvement to 26.7% (CY21: 28.3%) due to reduction in commission expenses to Rs. 847.9m (CY21: Rs. 1.1b). This is in tandem with the lower commission rates extended to sales agents for onboarding existing clients onto the new insurance product. Additionally, the Company's digitalization efforts during the rating review period, which include the development of an online hospital billing platform, helped keep operational expenses in check. Although the impact of higher net claims was partially offset as a result, the combined ratio, nonetheless, increased to 94.4% (CY21: 89.0%). Moreover, surplus from the Participant's Takaful Fund (PTF) also witnessed improvement across all segments, increasing to Rs. 220.9m (CY21: Rs. 33m) largely on account of decrease in related technical reserves. Furthermore, aging of claims is considered adequate as 75.5% of claims were outstanding up to one year at end-Dec'22. (CY21: 79.5%)

During 1HCY23, PQFTL's underwriting performance further weakened, registering a loss of Rs. 212.4m, owing to sizeable increase in net claims ratio to 81.3% (CY22: 67.7%, CY21: 60.7%) with the continued uptick in Group Health claims and surrenders/withdrawals. However, reduction in underwriting expense ratio to 22.8% in line with lower acquisition and commission charges partially allayed the stress on the combined ratio, which grew to 104.2%. PTF deficit of Rs. 158.3m was also booked owing mainly to adverse claims experience within the individual and Group Health segments.

	2021	2022	1HCY23
Net Contribution	9,555.0	9,771.7	5,091.4
Net Takaful Benefits	(5,794.9)	(6,618.3)	(4,141.4)
Net Claims Ratio	*60.6%*	*67.7%*	*81.3%*
Acquisition Expenses	(945.4)	(1,016.6)	(450.3)
Commission Expenses	(1,071.5)	(847.9)	(304.4)
Other Expenses (total)	(103.7)	(89.7)	-
Marketing and admin	(559.8)	(673.0)	(395.1)
Surplus Income	45.6	91.0	-
Surplus Distribution	(70.9)	(73.3)	(13.6)
Expense Ratio	*28.3%*	*26.7%*	*22.8%*

Combined Ratio	*89.0%*	*94.4%*	*104.2%*

Reinsurance Treaties

The Company has maintained its retakaful arrangements with reputable reinsurers constituting of Munich Re, Hannover Re and Hannover ReTakaful, all of which have been assigned a rating of A+ or above as per Standard and Poor's (S&P). No change in the treaty panel or terms was witnessed over the rating review period. While the strong reputation of the retakaful partners provides support to operational activities, the minimal cessation ratio of 4.5% (CY21: 4.3%) results in the Company undertaking the majority of underwriting risk.

Investments

Investment income grew over the rating review period, standing at Rs. 362.6m at end-June'23 (CY22: Rs. 565.8m, CY21: Rs. 210.5m) on the back of greater returns generated from debt-securities. This is in line with policy rate hikes and the Company's shift towards a more cautious investment approach. The total investment portfolio booked on the Balance Sheet increased to Rs. 26.8b (CY21: Rs. 25.7b), inclusive of investment property of Rs. 983.4m (CY21: Rs. 600m). The majority of the portfolio was vested in asset allocation mutual funds amounting to Rs. 14.9b (CY21: Rs. 15.9b), ensuring sufficient liquidity against unexpected claims expense. Out of this amount, the Company recalibrated Rs. 4.2b towards its associated company, Pak-Qatar Asset Management Company (PQAMC), which recently obtained its license in Dec'21. Given adverse stock market performance due to macroeconomic deterioration, the equity portfolio truncated to Rs. 6.2b (CY21: Rs. 7.7b) at end-CY22 on account of dip in prices as volume of shares remained largely intact. Major exposure of listed equities included oil and gas companies at 45.8% (CY21: 40.8%), cable and electrical goods at 13% (CY21: 10.3%), cement at 11.4% (CY21: 11.8%) and engineering at 11% (CY21: 13.4%). Given almost one-third of the total investment mix constitutes stock market exposure coupled with one-quarter of it vested in engineering and electrical goods sectors, the credit and price risk are currently elevated. Net investment in unlisted shares was minimal at Rs. 21m (CY21: Rs. 21m), pertaining to PQAMC exclusively. Moreover, in order to mitigate the risk exposure emanating from equity investments, the Company enhanced its holdings in government securities to Rs. 4.4b (CY21: Rs. 1.2b), primarily consisting of GoP Ijarah Sukuks with returns between 7.53-8.37%. Additionally, a nominal sum of Rs. 189.3m was registered in Neelum-Jhelum Sukuks (CY21: Rs. 289.7m) with profit rate of 6M KIBOR plus 1.13%. Investments in corporate sukuks also rose to Rs. 228.4m (CY21: Rs. 33.4m). The remainder was parked in fixed term-deposits with commercial Islamic Banks, amounting to Rs. 100m (CY21: Rs. 290m). Going forward, the management projects continuation of its conservative investment strategy during the medium-term in light of the country's depressed macroeconomic outlook.

The Company manages a total of seven unit-linked funds which vary according to risk exposure and investment avenues, two of which pertain to policies generated from banca channels. Total Assets Under Management (AUM) increased on a timeline basis to Rs. 30.3b (CY22: Rs. 27.5b, CY21: Rs. 26.2b) at end-Aug'23. In conjunction with the challenging market conditions and lower risk appetite of policyholders, the fund mix depicted shift towards fixed income funds. Additionally, two new funds, namely the Pure Savings and Mustekham Munafa funds, were introduced during the rating review period which, according to management, are primarily geared towards offering competitive returns for policy holders who have invested in the non-conventional insurance product. These funds are primarily vested in mutual funds/sukuks and bank placements, respectively. In terms of returns, fixed income funds depicted superior performance relative to assigned benchmarks while both equity and balanced funds produced comparatively subpar returns. Breakdown of fund mix and returns can be seen below:

AUMs	**Dec-19**	**Dec-20**	**Dec-21**	**Dec-22**	**Aug-23**
Aggressive	21.5%	10.2%	9.9%	7.7%	5.6%
Balanced	56.9%	26.9%	25.3%	20.4%	14.9%
Conservative	20.7%	13.4%	19.5%	26.9%	24.7%
Secure Wealth	0.9%	0.3%	0.3%	1.3%	0.1%
Pure Savings	0.0%	0.0%	0.0%	3.3%	13.7%
Mustekham Munafa	0.0%	0.0%	0.0%	0.0%	3.8%
Banca - Growth	0.0%	25.8%	21.7%	23.3%	15.1%

Banca - Conservative	0.0%	23.5%	23.4%	17.1%	22.0%
Total	**100.0%**	**100.0%**	**100.0%**	**100.0%**	**100.0%**

Returns of Funds	Dec-19	Dec-20	Dec-21	Dec-22	Aug-23
Aggressive	12.50%	13.50%	-11.20%	-17.30%	2.80%
Balanced	9.50%	12.10%	-1.00%	-5.91%	3.47%
Conservative	11.30%	9.00%	6.20%	10.64%	15.59%
Secure Wealth	11.00%	8.10%	4.80%	9.56%	13.26%
Pure Savings	-	-	-	13.91%	18.66%
Mustekham Munafa	-	-	-	-	15.28%
Banca - Growth	-	14.53%	-11.30%	-17.51%	7.25%
Banca - Conservative	-	8.85%	5.99%	10.27%	17.12%

Liquidity and Capitalization

The equity base contracted to Rs. 2.2b at end-June'23 (CY22: Rs. 2.5b, CY21: Rs. 2.3b) on the back of underwriting losses reported during the ongoing year. No movement was witnessed in the Qard-e-Hasna which remained unchanged at Rs. 175m. Overall risk absorption capacity of the Company is considered sound, in view of healthy solvency margin levels. Moreover, as more liquid resources were utilized in meeting financial obligations in line with uptick in claims, liquid assets relative to total liabilities declined slightly on a timeline to 93.4% (CY22: 95.4%, CY21: 96.4%); however, the same remained comfortable and in sync with the assigned rating.

Pak-Qatar Family Takaful Limited **Appendix I**

FINANCIAL SUMMARY *(amounts in PKR millions)*					
BALANCE SHEET	**31-Dec-19**	**31-Dec-20**	**31-Dec-21**	**31-Dec-22**	**30-Jun-23**
Cash and Bank Deposits	4,085.6	2,936.5	3,427.3	3,293.2	2,147.8
Investments	18,894.9	24,286.9	25,103.4	25,856.6	27,738.5
Total Assets	25,840.7	30,129.8	31,841.4	33,008.5	34,117.0
Net Equity (incl. Qard-e-Hasna)	2,067.1	2,243.5	2,256.6	2,516.8	2,173.4
Total Liabilities	23,773.6	27,886.3	29,584.8	30,491.8	31,943.6
INCOME STATEMENT	**31-Dec-19**	**31-Dec-20**	**31-Dec-21**	**31-Dec-22**	**30-Jun-23**
Gross Contributions	8,287.1	7,961.5	9,986.4	10,235.6	5,345.8
Net Contributions – PTF	7,861.4	7,557.8	9,555.2	9,771.7	5,091.4
Surplus (before distribution) – Overall	31.5	86.6	33.0	220.9	(158.3)
- Individual	130.0	95.9	99.0	153.5	(58.0)
- Group Family	14.9	(27.6)	14.3	25.2	4.5
- Group Health	(113.3)	18.3	(80.3)	42.2	(104.7)
Profit Before Tax	84.1	208.1	224.7	184.6	(99.4)
Profit After Tax	55.2	163.6	175.3	149.1	(110.4)
RATIO ANALYSIS	**31-Dec-19**	**31-Dec-20**	**31-Dec-21**	**31-Dec-22**	**30-Jun-23**
Market Share (Gross Premium-Private)	7.6%	7.1%	7.9%	8.1%	8.8%
Liquid Assets to Total Liabilities	96.7%	97.6%	96.4%	95.4%	93.4%
Cession Ratio	5.1%	5.1%	4.3%	4.5%	4.8%
Persistency*	78.4%	74.7%	80.0%	69.9%	65.4%

**Annualized*

REGULATORY DISCLOSURES — Appendix II

Name of Rated Entity	Pak-Qatar Family Takaful 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 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.
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. Copyright 2023 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				
12/07/2023	A++(IFS)		Stable	Reaffirmed
6/29/2022	A++(IFS)		Stable	Reaffirmed
3/31/2022	A++(IFS)		Stable	Harmonized
4/16/2021	A+		Stable	Reaffirmed
10/15/2019	A+		Stable	Reaffirmed
7/18/2018	A+		Stable	Upgrade
6/23/2017	A		Positive	Maintained
12/4/2015	A		Stable	Maintained
5/13/2014	A		Positive	Maintained

Due Diligence Meetings Conducted

Name	Designation	Date
Mr. Muhammad Ahsan Qureshi	CFO	5-Oct-23