

RATING REPORT

Allianz EFU Health Insurance Limited

REPORT DATE:

April 20, 2022

RATING ANALYSTS:

Arsal Ayub, CFA

arsal.ayub@vis.com.pk

Musaddeq Ahmed Khan

musaddeq@vis.com.pk

RATING DETAILS

Rating Category	Latest Rating	Previous Rating
Insurer Financial Strength	A+(IFS)	A+(IFS)
Rating Date	April 20, 2022	March 31, 2022
Rating Outlook	Stable	Stable
Outlook Date	April 20, 2022	March 31, 2022

COMPANY INFORMATION

Incorporated in 2000	External auditors: M/s EY Ford Rhodes, Chartered Accountants
Public unlisted Company	Chairman of the Board: Mr. Saifuddin N. Zoomkawala
Key Shareholders (with stake 5% or more):	Chief Executive Officer: Mr. Akhtar Kurban Alavi
Allianz SE – 49.00%	
EFU Services (Pvt.) Limited – 24.00%	
Aitkenstuart Pakistan (Private) Limited – 9.94%	
Mr. Saifuddin N Zoomkawala – 8.00%	
Mr. Jahangir Siddique – 7.28%	

APPLICABLE METHODOLOGY(IES)

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

Allianz EFU Health Insurance Limited

**OVERVIEW
OF THE
INSTITUTION**

Incorporated in 2000, Allianz EFU Health Insurance Limited (Allianz EFU) is a joint venture of Allianz SE and EFU Services (Private) Limited. Allianz EFU is a pioneer and one of the largest health insurers in Pakistan

RATING RATIONALE

Allianz EFU Health Insurance Limited (‘AEFU’ or ‘the Company’) provides health insurance products catering to both individual and corporate customers. The Company underwrites business under three broad categories namely; group business, individual business-bancassurance and individual business-consumer sales. AEFU commenced Window Takaful Operation in April 2017. The Company belongs to a prominent business conglomerate, EFU Group, which operates in both life and non-life insurance segments. Prominent shareholders of Allianz EFU include EFU Services (Pvt.) Limited.

Insurance Sector Update

- Growth in insurance industry premiums stood lower at 8% in 2020 as per data published by Insurance Association of Pakistan (IAP) vis-à-vis 10% in the preceding year. Historically, growth in the insurance premiums has been reported at more than 2x of the GDP growth. However, in last 5 year period, this has dropped. Industry experts remain conservative in their projections, maintaining the same within the single digit domain and close to the GDP growth projection of ~5%.
- Gross underwriting depicted growth of 19% in 9M’2021 vis-à-vis SPLY, which is mainly attributable to a low base effect, caused by the pandemic-induced slowdown in 9M’2020.
- Non-life insurance penetration, estimated at ~0.2%, remains notably lower than 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 around ~50%, which is considered to be on the lower side and there is certainly room for additional insurance penetration in the domestic market.
- Overall capitalization & liquidity buffers in place are considered to be adequate. Industry capitalization & liquidity are expected to persist.
- The implementation of IFRS 17 has been postponed. The SECP has issued instructions of phase-wise implementation of IFRS 17, as per which the insurance companies submitted a gap analysis with SECP in September’2021.
- Phase 2 of IFRS-17, which pertain to financial impact assessment has to be submitted with SECP by or before December 31, 2022.

Table 1: Insurance Industry Financial Indicators (Source: IAP)

(Rs. in Billions)	2019	2020	9M’2021
Insurance Premium (Gross)	83.7	89.6	76.8
Takaful Contributions (Gross)	11.0	12.6	12.0
Industry Total (Gross)	94.7	102.2	88.8
Combined Ratio	89.1%	95.3%	90.8%
- Net Claims Ratio	51.7%	54.8%	52.6%
- Underwriting Expense Ratio	37.4%	40.5%	38.2%
Net Operating Ratio	72.5%	78.6%	69.2%
RoAA	4.7%	4.4%	5.3%*
RoAE	10.5%	10.1%	13.1%*
Operating Leverage	49.6%	52.5%	55.6%*

* Annualized

Business Review: AEFU
Business Mix

- AEFU's gross underwriting depicted contraction of 1% in 2020, as a result of which the Company experienced some attrition in market share. The trend of market share attrition was aligned with most industry participants, as growth entirely emanated from a single private sector player that underwrote a public sector exposure; given flat performance across the board, most industry participants posted attrition in market share.
- During 2021, the Company's business volumes grew at 9.2% (2021: Rs. 2.58b; 2020: Rs. 2.36b; 2019: Rs. 2.38b). It is likely that the Company maintained its market share in 2021, albeit given IAP is yet to publish industry figures, market share for 2021 can't be ascertained as of report date. As per the management, growth target is planned at 12% for 2022.
- AEFU's business is largely composed of underwriting for large corporates, which constitutes 98% of the overall underwriting. The remaining comprises individual health underwriting, major part of which constitutes bancassurance policies.

Table 2: AEFU Market Share in Non-Life Insurance (Source: IAP)

	2018	2019	2020
Market Share (Private Sector)	2.4%	2.7%	2.4%

Profitability
Table 3: Income Statement

In PKR' Millions	2019	2020	2021
Net Premium	1,615.7	1,464.6	1,739.5
Net Claims	1,493.6	1,097.4	1,504.6
<i>Net Claims Ratio</i>	92.4%	74.9%	86.5%
Net Commission Income / (Expense)	36.1	6.1	11.5
<i>Acquisition Income / (Cost)</i>	2.2%	0.4%	0.7%
Underwriting Expense	263.6	300.9	328.6
<i>Underwriting Expense Ratio</i>	16.3%	20.5%	18.9%
Underwriting Profit/ (Loss)	(141.6)	66.3	(93.8)
<i>Combined Ratio</i>	108.8%	95.5%	105.4%
Recurring Investment Income	86.9	112.2	103.5
<i>Net Operating Ratio</i>	103.4%	87.8%	99.4%
Finance Cost	6.7	4.7	3.3
Other Income	6.8	5.7	0.8
Profit/ (Loss) Before Tax	(54.5)	179.4	7.2
Profit/ (Loss) After Tax	(80.0)	148.1	3.9

- Subsequent to posting a 9.4% contraction in underwriting in 2020 AEFU's net underwriting posted growth of 18.8% in 2021. Nevertheless, despite the strong growth, the Company's profitability came under pressure as combined ratio jumped to 105.4% in 2021 vis-à-vis 95.5% in 2020.
- As illustrated in the table above, combined ratio was negatively affected by a higher claims ratio in 2021. As per management, the higher claims ratio in 2021 was mainly a product of pent up demand, as scheduled medical procedures planned for 2020 were delayed into 2021 on account of pandemic related operational issues faced by the health sector in 2020.
- Investment income was lower by 8% in 2021, mainly on account of the lower benchmark rates prevailing during the period. Accordingly, the differential between combined ratio and net operating ratio, which was 7.7% for 2020, reduced to 5.9% in 2021.

- AEFU's investment portfolio remains concentrated in sovereign securities, which comprised 96% of the portfolio as of Dec'21. The duration of PIBs was stands at 3 years, while credit risk of the portfolio is very low, given that it mainly represents sovereign exposure.

Table 4: Investment Portfolio

In PKR' Millions	Dec'19	Dec'20	Dec'21
Government Securities	592.1	809.0	730.2
Equity Securities	2.0	5.8	30.1
	594.1	814.8	760.3

Liquidity & Capitalization

- AEFU's liquidity profile remains adequate, given full coverage of net technical reserves.
- Insurance debt in relation to gross premium decreased during 2021. The aging profile of insurance debt is considered satisfactory, as less than 2.5% was overdue for more than one year as of Dec'2021.
- AEFU's capitalization profile is underpinned by limited equity in relating to underwriting. This is mainly because of limited internal capital generation capacity and sizable dividend payout of 2020, as a result of which capital bases has remained stagnant YoY. Given steady growth in business volumes over the years, operating leverage once again spiked to 326.7%, subsequent to posting a drop in 2020. Furthermore, the financial leverage also stood on the higher side. Given business growth envisaged by the management, leveraging is likely increase going forward.

In PKR' Millions, unless stated otherwise

	Dec'19	Dec'20	Dec'21
Liquid Assets	624.6	902.9	822.8
Liquid Assets to Net Technical Reserves	0.71x	1.01x	0.96x
OCF to Gross Premium	(0.09)	0.11	(0.01)
Insurance Debt to Gross Premium	21.2%	15.2%	13.4%
Equity	446.6	590.9	532.4
Operating Leverage	361.7%	247.9%	326.7%
Financial Leverage	196.0%	152.0%	161.4%
Dividend Payout	-	33.8%	-

Key Rating Drivers:

Assigned rating derives strength from Sponsor Profile

The assigned rating derives strength from the sponsor profile of Allianz SE, a Germany-based financial services provider and holding company of the Allianz Group (Allianz SE rated AA by Standard & Poor's and A+ by A.M.Best). Allianz Group is present in more than 70 countries with major operations in Europe.

Rating incorporates market positioning, business mix & profitability metrics of AEFU

The assigned rating incorporates the market positioning of AEFU, in non-life insurance market, as a small-medium sized insurer, holding a market share of 2.4% as of 2020. AEFU is primarily engaged in underwriting health business, which generally features higher loss ratios than other business lines. Resultantly, the Company's combined ratio exceeds peers and the overall industry in general.

Rating is constrained by financial risk profile of the Company

AEFU's financial risk profile is underpinned by adequate liquidity, given close to full coverage of net technical reserves. However, leveraging levels of the Company are elevated, subsequent to posting slight contraction in 2020. Given limited internal capital generation capacity, growth in business will require external equity infusion going forward.

Allianz EFU Health Insurance Limited
Appendix I

FINANCIAL SUMMARY				
<i>(amounts in PKR millions)</i>				
<u>BALANCE SHEET</u>	31-Dec-18	31-Dec-19	31-Dec-20	31-Dec-21
Cash and Bank Deposits	122.9	30.4	88.1	62.5
Investments	696.0	594.2	814.8	760.3
Total Assets	1,814.9	1,741.2	1,918.6	1,865.3
Paid-up Capital	500.0	500.0	500.0	500.0
Net Worth	561.4	446.6	590.9	532.4
Total Liabilities	1,253.4	1,294.6	1,327.8	1,333.0
<u>INCOME STATEMENT</u>				
	2018	2019	2020	2021
Net Premium Revenue	1,335.4	1,615.7	1,464.6	1,739.5
Net Claims	1,069.4	1,493.6	1,097.4	1,504.6
Underwriting Profit	34.3	(141.6)	66.3	(93.8)
Net Investment Income	40.1	86.9	112.2	103.5
Profit Before Tax	76.9	(54.5)	179.4	7.2
Profit After Tax	57.0	(80.0)	148.1	3.9
<u>RATIO ANALYSIS</u>				
	31-Dec-18	31-Dec-19	31-Dec-20	31-Dec-21
Market Share (Non-Life Insurance Private Sector)	2.4%	2.7%	2.4%	NA
Cession Ratio	34.5%	33.7%	34.1%	34.3%
Gross Claims Ratio	80.8%	93.9%	76.1%	87.2%
Net Claims Ratio	80.1%	92.4%	74.9%	86.5%
Underwriting Expense Ratio	17.3%	16.3%	20.5%	18.9%
Combined Ratio	97.4%	108.8%	95.5%	105.4%
Net Operating Ratio	94.4%	103.4%	87.8%	99.4%
Insurance Debt to Gross Premium	21.5%	21.2%	15.2%	13.4%
Operating Leverage	237.9%	361.7%	247.9%	326.7%
Financial Leverage	141.5%	196.0%	152.0%	161.4%
Adjusted Liquid Assets to Technical Reserves	103.1%	71.3%	100.5%	95.8%

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	Allianz EFU Health Insurance Limited				
Sector	Insurance				
Type of Relationship	Solicited				
Purpose of Rating	Insurer Financial Strength Rating				
Rating History	Rating Date	Medium to Long Term	Outlook	Short Term	Rating Action
	RATING TYPE: IFS				
	04/20/2022	A+(IFS)	Stable		Reaffirmed
	03/31/2022	A+(IFS)	Stable		Harmonised
	05/31/2021	A	Stable		Reaffirmed
	06/12/2020	A	Stable		Reaffirmed
	07/03/2019	A	Stable		Downgrade
	04/26/2018	A+	Stable		Reaffirmed
	03/20/2017	A+	Stable		Initial
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. Copyright 2022 VIS Credit Rating Company Limited. All rights reserved. Contents may be used by news media with credit to VIS.				
Due Diligence Meetings Conducted	Name		Designation	Meeting Date	
	1	Mr. Nooruddin Jaffer Ali	Chief Financial Officer	March 18, 2022	
	2	Mr. Kamran Ansari	Operational Head		