# RATING REPORT

# EFU Life Assurance Limited

**REPORT DATE:**
April 16, 2019

**RATING ANALYSTS:**
Talha Iqbal
talha.iqbal@jcrvis.com.pk

Muhammad Ibad Desmukh
ibad.deshmukh@jcrvis.com.pk

## RATING DETAILS

| | Latest Rating | Previous Rating |
|---|---|---|
| **Rating Category** | **Long-term** | **Long-term** |
| **IFS** | AA+ | AA+ |
| ***Rating Date*** | *Mar 15, '19* | *Nov 30, '17* |
| **Rating Outlook** | Stable | Stable |
| ***Outlook Date*** | *Mar 15, '19* | *Nov 30, '17* |

## COMPANY INFORMATION

| | |
|---|---|
| **Incorporated in 1992** | **External auditors:** M/s KPMG Taseer Hadi & Co. – Chartered Accountants |
| **Public Limited Company** | **Chairman of the Board:** Mr. Rafique R. Bhimjee |
| **Key Shareholders:** | **Chief Executive Officer:** Mr. Taher G. Sachak |
| EFU General – 43.1% | |
| Jehangir Siddiqui & Co. Limited – 20.1% | |

## APPLICABLE METHODOLOGY(IES)

**VIS Entity Rating Criteria Methodology – Life Insurance & Family Takaful Rating Methodology (October 2017)**
*http://vis.com.pk/docs/LifeTakaful%20201710.pdf*

# EFU Life Assurance Limited

## OVERVIEW OF THE INSTITUTION

EFU Life Assurance Limited (EFUL) commenced operations in November 1992. The company offers individual and group life covers, with individual policies being the company's major business line in terms of premium income. The shares of EFUL are held by EFU General Insurance Ltd. (EFUG) to the extent of 43%.

Financial statements for the year ending December 2017 were audited by KPMG Taseer Hadi & Company Chartered Accountants. Mr. Omer Morshed is the appointed actuary. The company is listed on Pakistan Stock Exchange.

## RATING RATIONALE

EFU Life Assurance Limited (EFUL) commenced operations in November 1992. The company offers individual and group life covers, with individual policies being the company's major business line in terms of premium income.

EFUL maintains a fairly diversified business mix. Within individual category, regular renewal premiums continue to contribute largest share of business. The company generates ~90% of its premiums through issuance of unit linked insurance products while remaining business is generated through group life policies.

**Key Rating Drivers**

**Strong business profile as reflected by prominent brand and reasonable market share, with favorable long-term growth prospects.**
The private sector life insurance industry has posted compound annual growth rate (CAGR) of ~37% over the last 5 years (2014-18). Business profile derives strength from favorable persistency levels and healthy growth in business volumes where significant room for future growth remains as evident from low life insurance penetration. While some recovery has been noted in market share on a timeline basis, EFUL's market share is still lower vis-à-vis 2015 levels (9M18: 16.5%; 2017: 15.8%; 2016: 14.4%; 2015: 20.1%) in 9M18. This is attributed to increasing competition in the market. Nevertheless, management expects to regain market position on account of faster growth in bancassurrance and direct sales force (DSF) premium vis-à-vis peers. Going forward, industry premium growth is expected to be supported by a). Higher policies underwritten through bancassurance where significant room for growth remains as per industry players b). National Financial Inclusion Strategy's emphasis on increasing insurance penetration which will increase policies sold over the medium to long-term period and c). conducive regulatory environment.

**Diversified business mix.**
In 9M18, gross premium amounted to Rs. 21.0b (9M17: Rs. 22.6b), depicting decline of 7.1% vis-à-vis same period last year. Excluding single premiums, overall business depicted 21% increase during the period. During the period under review, DSF and bancassurance have played a vital role in business and brand enhancement of the company and have contributed 41.8% and 47% respectively of business volumes. Individual life polices constitute around 90% and continue to remain the primary source of revenues. New individual life regular premium amounted to Rs. 4.4b (9M17: Rs. 3.2b), of this, bancassurance represented around 61% of total first year gross premiums. Renewal individual life regular policies increased by 16.0%; bancassurance contributed 45.7% to gross premiums. Single premium policies feature a single premium payment at initiation which is invested in the selected fund; this segment has seen a cyclical shift over the years and declined by 69.6% in 9M18, however, this shift was compensated by increase in regular premium policies. Sale of regular premium policies remains the primary focus of the management given higher volatility and surrenders associated with single premium policies. In contrast, group life business increased by 13.19% during same period.

Launched in 2015, Window Takaful Operations reported total family takaful contribution of Rs. 2.1b (9M17: 1.6b) in 9M18. Out of this, Rs. 1.9b (9M17: Rs. 1.5b) was from individual family takaful business while Rs. 154.7m (9M17: Rs. 124.2m) was from group family takaful. Management expects growth trajectory to continue in this segment given the higher pace of increase in deposits in the Islamic banking industry vis-à-vis conventional banks.

**Management focused on further expanding and strengthening agency force; bancassurance continues to be major driver of premium growth.**
EFUL has an individual life branch network of ~250 locations across the country with sales force of 6,302 (2017: 5,865) agents. Productivity per agent has improved on a timeline basis. New business and

renewals generated through DSF increased by 17.6% and 15.6% respectively in 9M18. For bancassurance, EFUL has a partnership with 14 banks. New business and renewals generated through bancassurance increased by 57.2% and 16.4% respectively in 9M18. Over the years, cyclical shift in single premium business generated through bancassurance has been observed. Management is focused on strengthening its sales force, improving quality of service and reducing turnaround time, while a dedicated department for improving persistency has also been formed; these measures have resulted in higher persistency levels and higher regular business volumes.

**Well defined underwriting guidelines. In line with industry trends, non-medical underwriting limits have witnessed significant increase over the last few years.**
Life insurance underwriting is based on sum assured applied for and age of the client according to which medical requirements (based on medical underwriting tables) are generated automatically. Medical underwriting is undertaken on a case by case basis; this represents ~10-15% of policies underwritten. Given competition in market and in line with trend adopted by peer companies, underwriting limits have been relaxed over the last few years.

**Strong reinsurance coverage.**
Since last review, reinsurance arrangements for individual life and group business remain unchanged. Reinsurance treaties have been arranged from Munich Re (rated 'AA-' by S&P and 'AA' by Fitch). In accordance with EFUL's improved risk absorption capacity, beginning 2017, the company increased maximum retention amount under surplus treaty to Rs. 2m from Rs. 1.2m. Impact on claims performance of the same will continue to be monitored over time. Crude death rate declined in 9M18 and it continues to remain manageable.

**Investments & returns on funds under management.**
With growth in policies underwritten, investment portfolio under statutory funds has increased and amounted to 103.8b (2017: Rs. 96.3b; 2016: Rs. 95.4b) at end-9M18 despite negative returns of largest funds under management in 2017 and 9M18. Investments are managed by a 4-member team; the department utilizes a combination of in-house and third party research for due diligence purposes. Given the growth in size of assets under management, there is room for enhancing the scope of risk and research related activities. Accordingly, management plans to enhance research function and hire two-three resources for the same. Overall investment strategy entailed reduction in equity exposure and increased fixed income allocation. Accordingly, the company has significantly reduced its listed equity holdings and increased investment in term deposit receipts and treasury bills. For the largest fund under management, equity exposure was reported at 31.5%, government debt was 50.9% and cash & deposits amounted to 3.3%.

With bulk of the business generated by unit linked policies, the asset risk stands transferred to the policyholders particularly for policies with cash values exceeding the sum assured. As EFUL is a growing company, there are also a large number of individual life policies with cash values less than the sum assured. Risk is however considered manageable keeping in view the low crude death rate experienced in the past and reinsurance coverage.

Performance of the largest fund under management was competitive in relation to peers. Management has adopted an active management strategy with respect to equity portfolio. In the backdrop of higher policy rates, EFUL plans to continue undertaking investments in instruments with short term maturities. Given the nature of the company's business, generating consistent investment results and ability to cater to varying investor risk appetites may be key differentiating factors over the long term.

**Healthy liquidity profile along with strong statutory and risk-adjusted capitalization.**
Liquidity profile of the institution is considered sound in view of sizeable liquid assets carried on balance sheet with liquid assets % total policy holder liabilities equaling 84.1% (2016: 89.9%) at end-2017. Reported shareholder's equity was Rs. 5.6b (9M17: Rs. 3.8b; 2016: Rs. 4.2b) at end-9M18. As at end-September 2018, cushion over required solvency margin amounted to Rs. 2.2b, indicating healthy buffer. (Adj Capital - Group Allocated Capital) / (Country crude death rate x Net Sum Assured of Individual Life) was reported at 467.1% (2016: 489.5%) at end-2017 indicating solid risk-adjusted capitalization levels.

**In the backdrop of investment losses, revenue base was supported by lower claims incidence and premium growth.**

Despite growth in net premium revenue, investment loss contributed to a decline in overall revenue base to Rs. 27.1b (2016: Rs. 39.5b); revenue base amounted to Rs. 20.8b during 9M18. Attrition in investment returns is largely attributed to loss on listed equity portfolio resulting from downward trajectory in stock market. Overall claims experience of EFUL in individual business improved in 2018 with net claims ratio being lower at 14% (2017: 22%). Going forward, quantum of investment income is expected to be a function of equity market performance while enhanced return on fixed income portfolio (given increase in benchmark rates) are expected to support overall returns.

**Stable and experienced senior management team. Dedicated and independent enterprise risk management function is in place.**

The rating takes into account the quality and stability of the company's senior management as well as the team comprising of experienced and qualified professionals which includes actuaries, accountants and underwriters. The company's strength also emanates from the strong franchise of its sponsors and re-insurers that have been associated with the company for a long period of time.

EFUL has set up a dedicated and independent enterprise risk management (ERM) function. Risk management committee (RMC) meetings are held on quarterly basis and all groups are responsible for risk recognition, assessment and development of controls in their respective areas of operation while risk management function (RMF), with adequate support from such groups, is responsible for collating the results of such exercises and presenting to relevant authorities from time to time.

## EFU Life Assurance Limited Appendix I

| FINANCIAL SUMMARY *(amounts in PKR millions)* | | | |
|---|---|---|---|
| **BALANCE SHEET** | **30-Sep-18** | **31-Dec-17** | **31-Dec-16** |
| **Cash and Bank Deposits** | 3,701.5 | 6,057.9 | 3,037.5 |
| **Investments** | 106,208.4 | 97,959.1 | 98,189.3 |
| **Total Assets** | 114,766.3 | 109,545.2 | 106,301.5 |
| **Net Worth** | 5,595.6 | 5,962.7 | 4,193.4 |
| **Liabilities of Statutory Fund** | 109,170.7 | 100,860.39 | 97,782.1 |
| | | | |
| **INCOME STATEMENT** | **30-Sep-18** | **31-Dec-17** | **31-Dec-16** |
| **Gross Premium Written** | 20,834.2 | 31,499.5 | 24,676.5 |
| **Net Premium Revenue** | 20,293.3 | 30,759.7 | 23,861.9 |
| **Net Claims** | 9,974.2 | 14,195.6 | 17,764.4 |
| **Net Investment Income** | 1,882.2 | (3,605.5) | 15,654.0 |
| **Surplus Transferred from Shareholder's Fund** | 1,069.2 | 2,543.9 | 2,326.1 |
| **Profit Before Tax** | 1,279.8 | 2,680.8 | 2,798.1 |
| **Profit After Tax** | 996.2 | 1,812.4 | 1,872.9 |
| | | | |
| **RATIO ANALYSIS** | **30-Sep-18** | **31-Dec-17** | **31-Dec-16** |
| **Overall Cession Ratio (%)** | 2.6 | 2.3 | 3.3 |
| **Cession in Group Life (%)** | 15.4 | 15.9 | 21.8 |
| **Cession in Individual Regular Premium (%)** | 1.3 | 1.4 | 1.5 |
| **Persistency (%)** | 85.9 | 85.7 | 86.6 |
| **Expense Ratio (%)** | 28.2 | 23.0 | 23.2 |

## ISSUE/ISSUER RATING SCALE & DEFINITIONS Appendix II

### 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:** JCR-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.jcrvis.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.jcrvis.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.jcrvis.com.pk/images/policy_ratings.pdf

## REGULATORY DISCLOSURES — Appendix III

| | |
|---|---|
| **Name of Rated Entity** | EFU Life Assurance Limited |
| **Sector** | Insurance |
| **Type of Relationship** | Solicited |
| **Purpose of Rating** | Insurer Financial Strength |
| **Rating History** | (see table below) |

| Rating Date | Medium to Long Term | Short Term | Rating Outlook | Rating Action |
|---|---|---|---|---|
| RATING TYPE: INSURER FINANCIAL STRENGTH | | | | |
| 3/5/2019 | AA+ | | Stable | Reaffirmed |
| 11/30/2017 | AA+ | | Stable | Reaffirmed |
| 5/24/2016 | AA+ | | Stable | Upgrade |
| 3/10/2015 | AA | | Stable | Reaffirmed |
| 3/26/2014 | AA | | Stable | Reaffirmed |
| 3/27/2013 | AA | | 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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