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INDIAN INSURANCE SECTOR

Despite sizeable headroom to raise debt capital, challenges remain in issuing sub-debt

AUGUST 2024

Highlights

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Given the capital intensiveness of the sector, low insurance penetration, expectations of strong business growth and modest accruals, capital requirements will remain high.

Despite relaxation on limits to raise sub-debt, its share in the overall capital deployed remains limited at 5.8% of the total net worth, amid weak investor appetite.

- The insurance sector has seen a strong business growth in both life as well as general insurance spaces. This has resulted in **doubling of the capital deployed to almost Rs. 2.0 trillion** by companies over the last six years. Within the overall capital deployed, the share of **subordinated debt (sub-debt) in the capital structure has remained limited at 5.8% of the net worth.**
- ICRA notes that **investor participation in sub-debt of the insurance sector has remained weak** with almost two-thirds of the outstanding debt being subscribed by the promoter group or peer insurance companies. With the notification of December 6, 2022, insurance companies have incrementally refrained from investments in sub-debt of peers. The other large investor category, i.e., mutual funds, has also refrained from such investments, given the poor liquidity in the secondary markets, thereby limiting the investor base. This remains a **key challenge for capital raise and growth of the sector.**
- Further, **given features of the instrument** whereby coupon payment is subject to meeting the regulatory solvency level, and risk to solvency arising from adverse claim experiences that are difficult to predict, **investors seem to factor in the strong parentage of the issuer**. As a result, part of the sub-debt rated in higher categories were also subscribed by the promoter group.
- Given the capital intensiveness of the sector, low insurance penetration, expectations of strong business growth and modest internal accruals, **capital requirements will remain high**. Though the regulator had increased the limit to raise sub-debt in December 2022, **the weak investor appetite could pose challenges to growth**. Lack of sufficient capital also constraints the ability of the life insurers to underwrite protection and annuity business and the ability of general insurers to retain granular risk.
- Further, with the equity listing for large insurers in the sector, **investor awareness of the business risks have improved.** Nonetheless, only eight of the total 52 insurance companies are equity listed. ICRA expects that **as the companies gain longer track records** and build stronger standalone credit profiles, the investor appetite and **volume of issuances can improve**.

Capital deployed by sector has doubled in last six years; share of sub-debt in overall capital deployed remains limited

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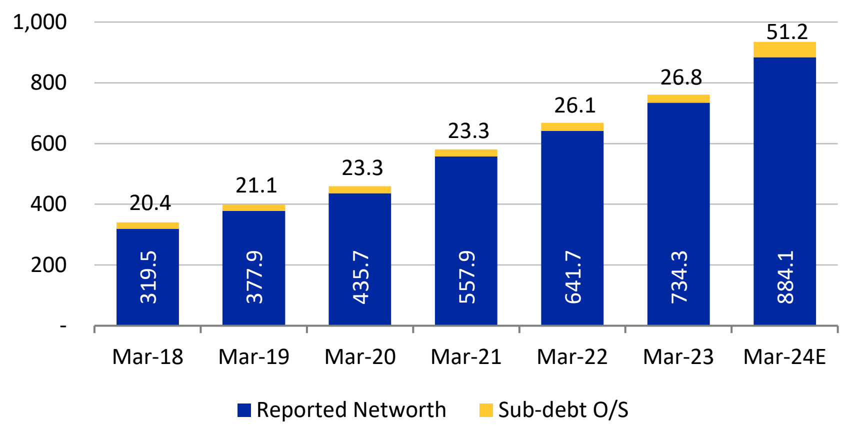
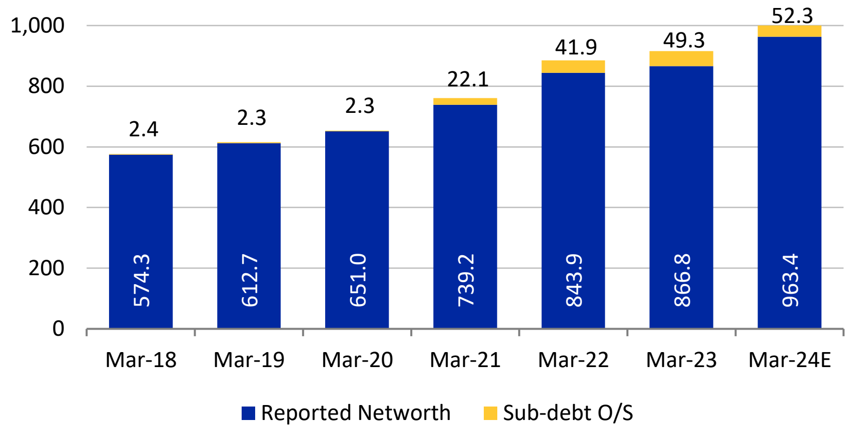
Exhibit 1: Total capital deployed – Private general insurers



Source: Company disclosures, IRDAI, ICRA Research; Figures in Rs. billion; Incl SAHI

Exhibit 2: Total capital deployed – Private life insurers



Source: Company disclosures, IRDAI, ICRA Research; Figures in Rs. billion

- Total capital deployed in the sector has almost doubled over the last six years to Rs. 1.95 trillion as on March 31, 2024, driven by the strong business growth.
- With average return on equity (ROE) of 10% for the general insurance (GI) and 7% for the life insurance (LI) segments during FY2019-FY2024, future growth will be partially supported by raising of additional capital.
- The **share of sub-debt** for private insurers remains **limited** at Rs. 107.7 billion, or **at 5.83% of the net worth** as on July 31, 2024.

Capital requirements to remain high, given expectations of strong growth

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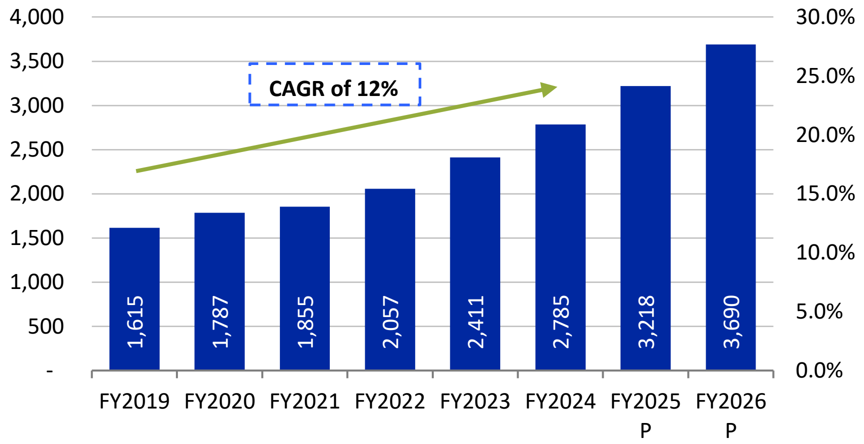
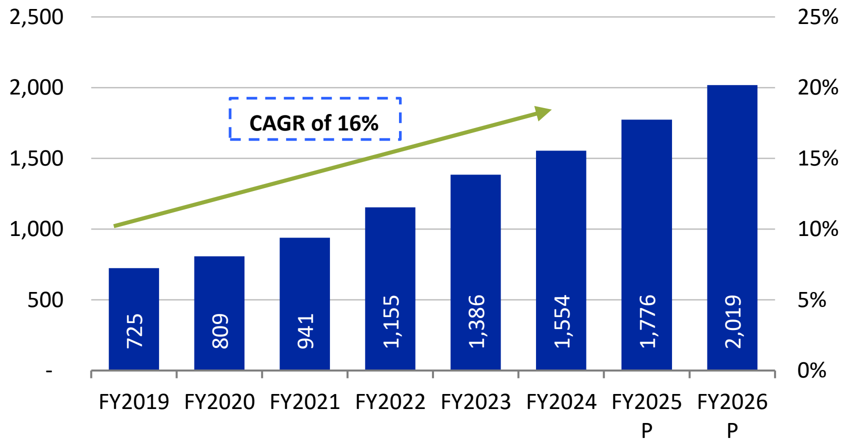
Exhibit 3: General insurance – Gross Direct Premium Income (GDPI)



Source: ICRA Research, GI Council, IRDAI; Industry excluding ECGC and AIC; Figures in Rs. billion

Exhibit 4: Life insurance – Private New Business Premium (NBP)

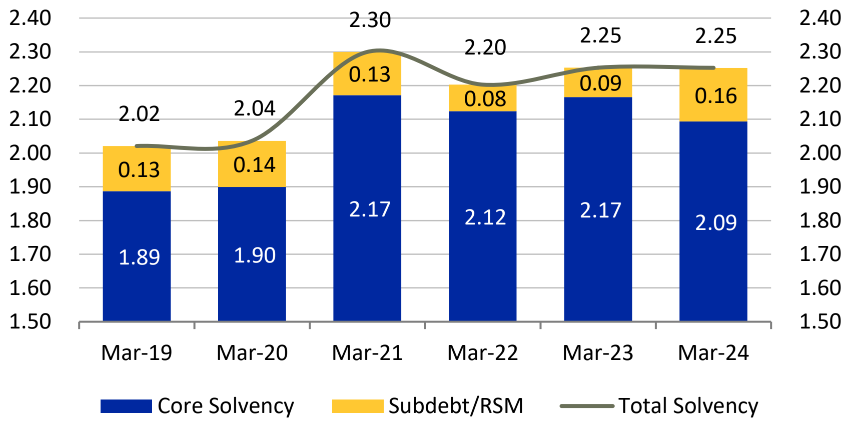


Source: ICRA Research, IRDAI; Figures in Rs. billion; Private life insurers excluding LIC

- The low penetration for both health and life insurance and improved awareness after the pandemic are expected to drive strong growth in the demand for risk coverage for both LI as well as GI sectors. In addition, strong growth in vehicle sales and retail credit have also been other drivers of growth.
- The growth outlook with modest internal accruals is likely to drive high capital requirements and in such a scenario, a vibrant sub-debt market could partially help to meet the same.
- Impact of the risk-based solvency on the capital requirements for the sector also remains to be seen.

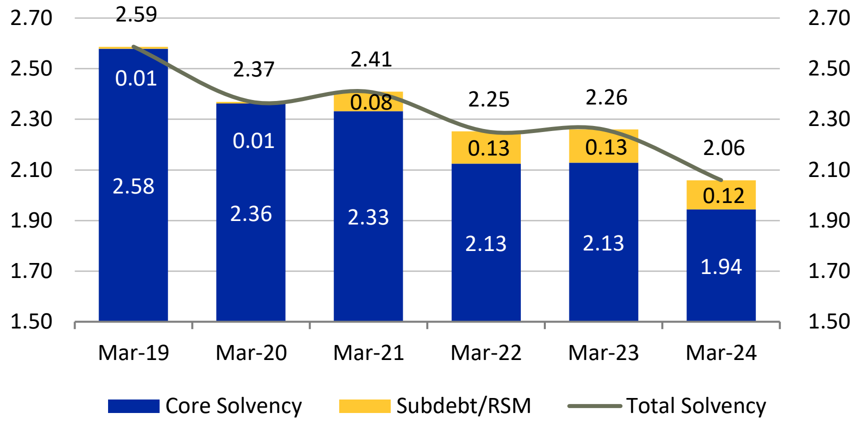
Capital intensity higher for life insurance sector

Exhibit 5: Solvency – Select^ private general insurers



Source: Company disclosures, ICRA Research; ^13 private general insurers (excl. SAHI); Aggregate solvency

Exhibit 6: Solvency – Private life insurers

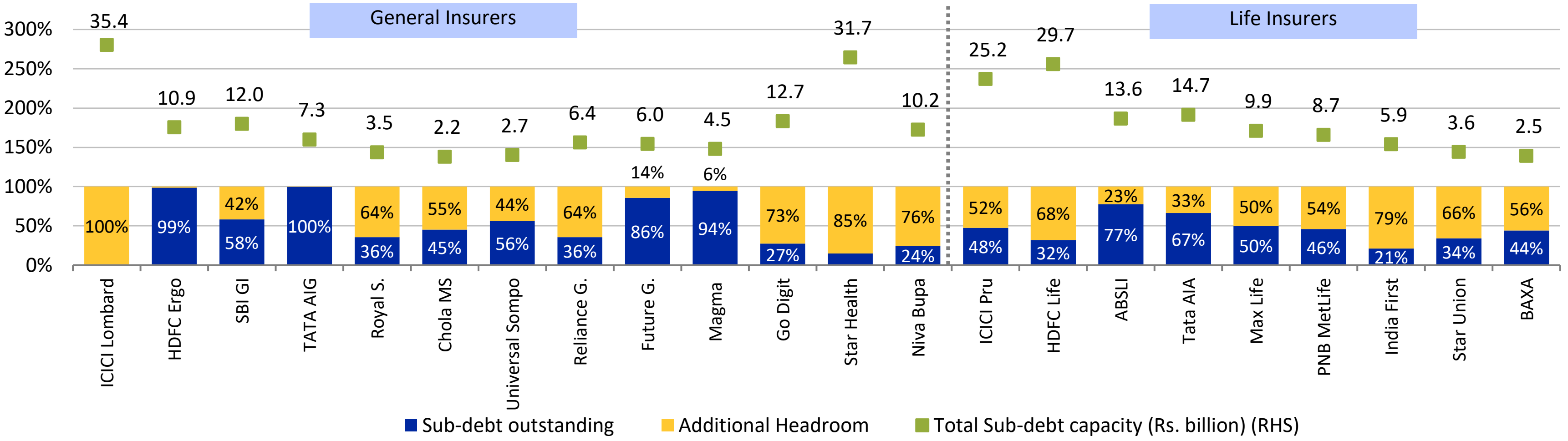


Source: Company disclosures, ICRA Research; Aggregate solvency

- High initial reserving for new business drives subdued accounting profitability and, hence, a higher capital consumption for the LI sector.
- Further, within the product mix of LI companies, the share of protection business is currently low; and to increase this share, the capital requirements for the sector will be significantly higher.
- Given that profitability is better for the GI sector, it can support the business growth. However, the sector remains exposed to increasing instances of natural catastrophes and depends heavily on reinsurance. A higher capital could improve its risk retention capacity and resilience to such events.

Insurance companies have significant headroom to raise sub-debt

Exhibit 7: Overall sub-debt raising capacity and outstanding position



Source: Company disclosures, ICRA Research

- Insurance companies can raise sub-debt equivalent to 50% of their net worth^ as per regulatory norms, which offers sizeable market opportunity, given the net worth of the companies in the sector.
- While all the issuers may not have a strong financial position to raise sub-debt but based on the above insurers, who have issued sub-debt in the past, the companies can additionally raise ~Rs. 154 billion, which will be over and above the Rs. 108-billion outstanding as on July 31, 2024. However, some of them enjoy a strong solvency position and may not require sub-debt.
- Investor appetite would be key to the increase in sub-debt in the overall capital profile of insurers.

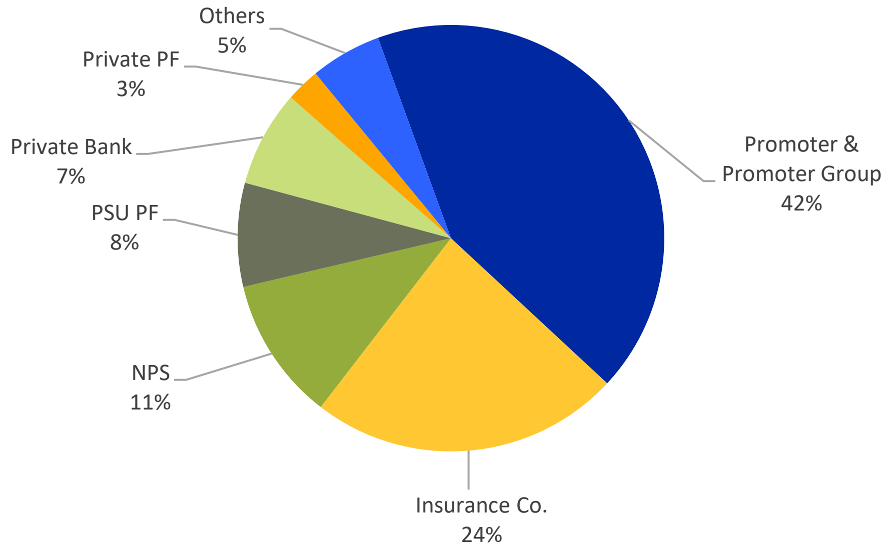
^ minimum of 50% of adjusted NW (excl Fair Value Change Account) or 50% of paid-up capital + share premium

Limited investor appetite, however, remains a key challenge

- Prior to December 2022, insurance companies were allowed to hold sub-debt of other insurance companies without taking a knock on their solvency position. Almost one-fourth of the outstanding sub-debt were placed with other insurance companies. However, these were largely done prior to amendments. Incrementally **no such investments are made by insurance companies**. Insurance companies being large investors in corporate bonds are absent as an investor from this segment.
- **Participation by mutual funds has also remained limited** as the investors focus on liquidity risks of the instruments in addition to credit risk. A lower ticket size per issuer (than other large issuers) and lack of secondary market liquidity raise liquidity risk premium sought by the investors.
- Investor awareness is gradually improving with increase in number of listed companies in the sector. However, entities who are equity listed remain limited at just eight (out of 57).
- **As a result, the promoters and legacy investments of other insurance companies make up 66%** of the total outstanding sub-debt.
- National Pension Schemes (NPS) and provident funds have emerged as large investors in issuances during the last two years.

Exhibit 8: Investor profile for sub-debt – General insurance and life insurance

Total Sample Size = Rs. 75 billion

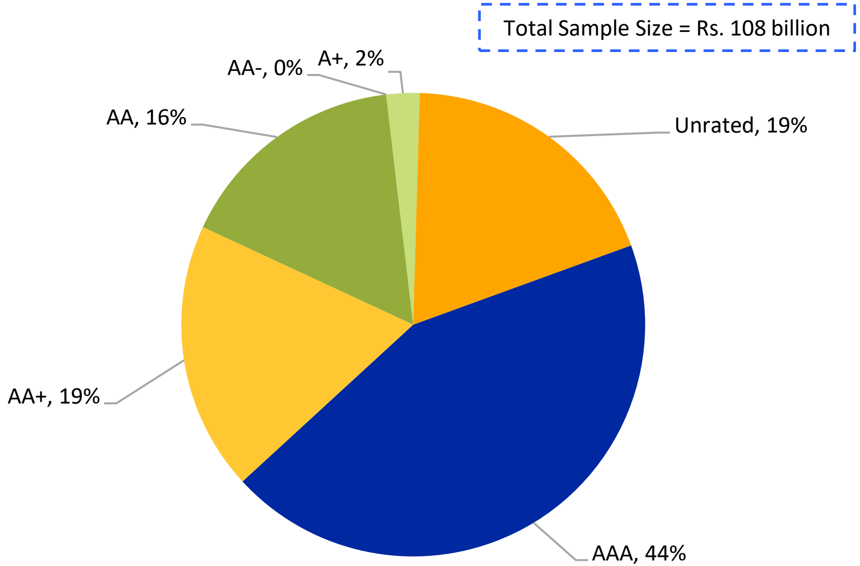


Source: Company disclosures, ICRA Research

Strong parentage and strong standalone credit profile drive investor interest

- Given the inherent risks of the sub-debt instrument, wherein servicing of interest is contingent upon the company maintaining a solvency ratio above the levels stipulated by the regulator; the investors seem to factor in the parentage of the issuer, apart from its standalone credit profile.
- ICRA also notes that the reserving for risk in force can see significant quarterly/yearly variations depending on the claims experience across various business segments, which may emerge over a longer time-frame. This also casts uncertainty on the future profitability and solvency of issuers.
- Also, the initial years of business are likely to result in losses for an insurer because of which the dependence on equity capital raise is high. This is likely to constrain the credit profile of an issuer and appetite of a debt investor. As a result, of the 52 overall private insurance companies, **only 25 have issued sub-debt**.
- **However, companies with a better standalone credit profile**, where the capital requirement is largely for growth, do attract investor appetite, especially if they are owned by strong promoter groups (including banks).
- While a large portion of unrated debt is held by the promoter group, even the debt rated in the AA category was placed with the promoter group.

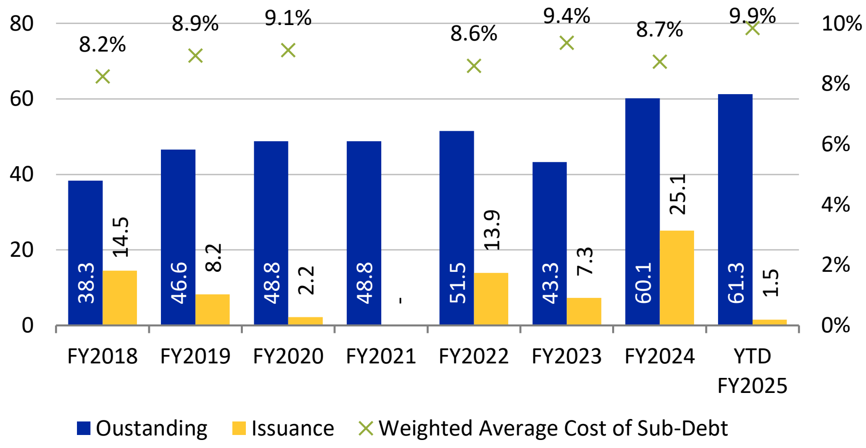
Exhibit 9: Credit rating-wise issuer profile for sub-debt – Private general and life insurance



Source: Company disclosures, ICRA Research; Data as on July 31, 2024

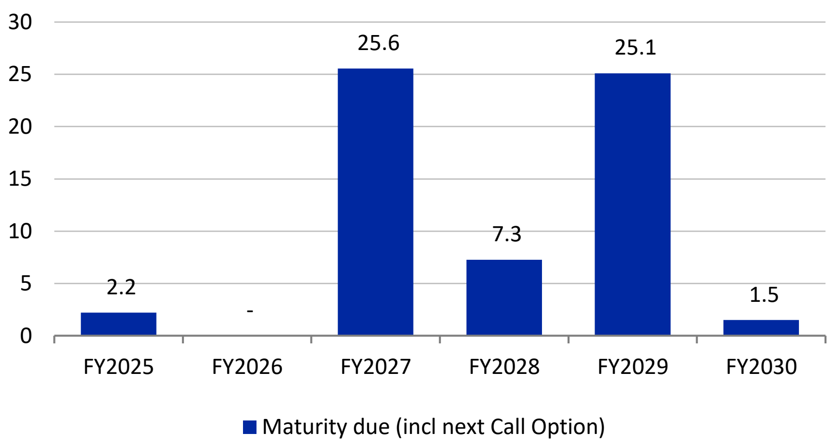
High business growth drives issuances for general insurers in recent years

Exhibit 10: General insurers – Sub-debt issuances and outstanding



Source: Company disclosures, ICRA Research; Figures in Rs. billion

Exhibit 11: Maturity due (incl. first call option) for issued sub-debt

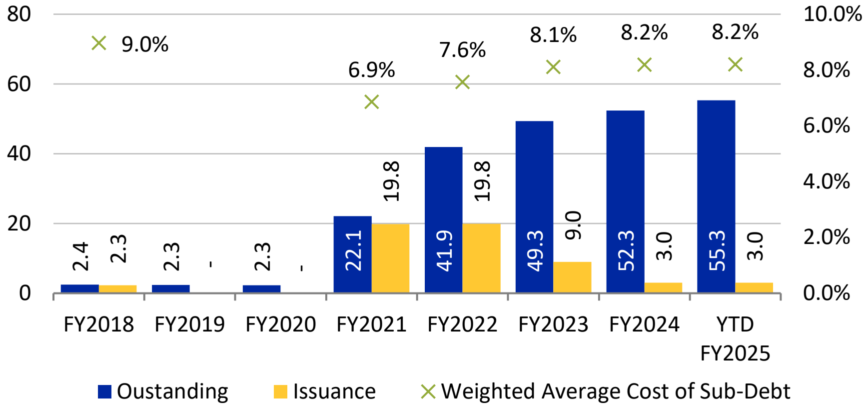


Source: Company disclosures, ICRA Research; Figures in Rs. billion

- Given the high business growth (CAGR of 15% in FY2022-FY2024) and consequent issuances, a large part of the sub-debt outstanding have call options due in FY2027-FY2029.
- While call options remain limited in FY2025-FY2026, companies could raise fresh debt to support growth.
- Of the total sub-debt outstanding of Rs. 61.3 billion, Rs. 8.95 billion is issued by one of the public sector (PSU) insurers (see Exhibit 14). While most of the PSUs in the GI sector have weak credit profiles, they have the regulatory forbearance to service the sub-debt even if the solvency ratio falls below the regulatory requirement.

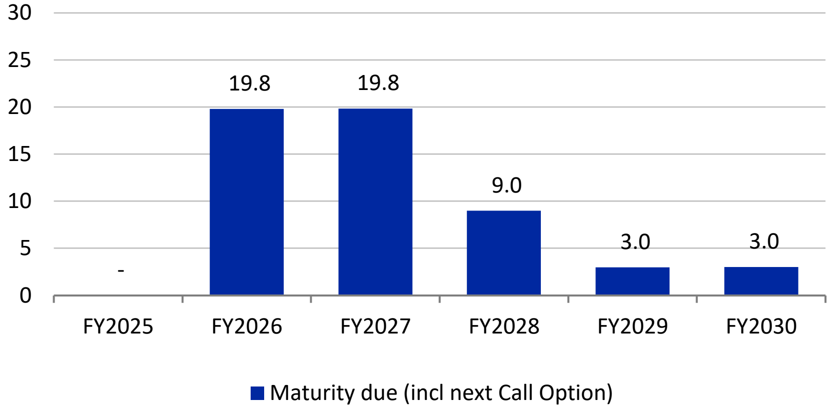
High quantum of call options due in next two years to drive issuances by life insurance companies

Exhibit 12: Life insurers – Sub-debt issuances and outstanding



Source: Company disclosures, ICRA Research; Figures in Rs. billion

Exhibit 13: Maturity due (incl. first call option) for issued sub-debt



Source: Company disclosures, ICRA Research; Figures in Rs. billion

- LI companies saw high capital consumption during and after the pandemic (see Exhibit 6). Apart from profitability impact due to high mortality claims, the high capital consumptions were also driven by increased share of non-par guaranteed business, credit life as well as protection business.
- The business growth for LI companies is expected to remain strong given the high protection gap in terms of sum assured.
- However, unlike most of the business segments in the GI sector, LI is a very long-tail business and the claim experience and, hence, the reserves for risk underwritten, could substantially change the profitability and solvency of an LI company. Further, the falling interest rates also expose the profitability of the companies to remuneratively deploy the future premiums at originally assumed interest rates while underwriting the policies.

Annexure 1: General insurance companies - Sub-debt issuances

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Exhibit 14: Issuer-wise issuance break-up: FY2018 – YTD FY2025

General Insurance Companies	FY2018	FY2019	FY2020	FY2021	FY2022	FY2023	FY2024	YTDFY2025	O/S as on July 31, 2024
Sub-Total - Private	**3.00**	**0.74**	**2.20**	**-**	**6.01**	**7.26**	**25.11**	**1.50**	**44.03**
HDFC Ergo General Insurance - HDFC Ergo Health	0.80	0.74	-	-	3.75	3.80	3.20	-	10.75
TATA AIG General Insurance	-	-	1.85	-	-	-	5.45	-	7.30
SBI General Insurance	-	-	-	-	-	-	7.00	-	7.00
Future Generali India Insurance	-	-	-	-	-	2.46	2.71	-	5.17
Magma HDI General Insurance	-	-	-	-	1.00	-	3.25	-	4.25
Go Digit General Insurance	-	-	-	-	-	-	3.50	-	3.50
Reliance General Insurance	-	-	-	-	-	-	-	-	2.30
Universal Sompo General Insurance	-	-	-	-	-	-	-	1.50	1.50
Royal Sundaram General Insurance	-	-	-	-	1.26	-	-	-	1.26
Cholamandalam MS General Insurance	-	-	-	-	-	1.00	-	-	1.00
ICICI Lombard General Insurance - BAXA	2.20	-	0.35	-	-	-	-	-	-
Sub-Total - Standalone Health Insurers	**2.50**	**-**	**-**	**-**	**7.88**	**-**	**-**	**-**	**8.31**
Star Health and Allied Insurance	2.50	-	-	-	4.70	-	-	-	4.70
Niva Bupa Health Insurance	-	-	-	-	2.50	-	-	-	2.50
Manipal Cigna Health Insurance	-	-	-	-	0.68	-	-	-	1.11
Sub-Total -PSU Insurers	**9.00**	**7.50**	**-**	**-**	**-**	**-**	**-**	**-**	**8.95**
United India Insurance	9.00	-	-	-	-	-	-	-	-
National Insurance	-	-	-	-	-	-	-	-	8.95^
The Oriental Insurance	-	7.50	-	-	-	-	-	-	-
Overall Total	**14.50**	**8.24**	**2.20**	**-**	**13.89**	**7.26**	**25.11**	**1.50**	**61.29**

Source: Company disclosures; Amount in Rs. billion; Sorted on the basis of the outstanding as on July 31, 2024; ^Issued in FY2017

Annexure 2: Life insurance companies - Sub-debt issuances

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Exhibit 15: Issuer-wise issuance break-up: FY2018 – YTD FY2025

Life Insurance Companies	FY2018	FY2019	FY2020	FY2021	FY2022	FY2023	FY2024	YTDFY2025	O/S as on July 31, 2024
ICICI Prudential Life Insurance	-	-	-	12.00	-	-	-	-	12.00
Aditya Birla Sun Life Insurance	-	-	-	1.50	3.50	-	2.50	3.00	10.50
TATA AIA Life Insurance	-	-	-	-	4.88	4.88	-	-	9.76
HDFC Standard Life Insurance	-	-	-	6.00	-	3.50	-	-	9.50
Max Life Insurance	-	-	-	-	4.96	-	-	-	4.96
PNB Metlife India Insurance	-	-	-	-	4.00	-	-	-	4.00
Star Union Dai-ichi Life Insurance	-	-	-	-	1.25			-	1.25
IndiaFirst Life Insurance	1.00	-	-	-	1.25	-	-	-	1.25
Bharti AXA Life Insurance	0.60	-	-	-	-	0.60	0.50	-	1.10
Bandhan Life Insurance	0.70	-	-	-	-	-	-	-	0.70
Future Generali Life Insurance	-	-	-	0.30	-	-	-	-	0.30
Total	**2.30**	**-**	**-**	**19.80**	**19.84**	**8.98**	**3.00**	**3.00**	**55.32**

Source: Company disclosures; Amount in Rs. billion; Sorted on the basis of the outstanding as on July 31, 2024

Annexure 3: ICRA's rated universe – Insurance sector

General Insurance	Issuer Rating	Subordinated Debt Rating
ICICI Lombard General Insurance Company Limited	[ICRA]AAA (Stable)	
Bajaj Allianz General Insurance Company Limited	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)
HDFC ERGO General Insurance Company Limited	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)
Tata AIG General Insurance Company Limited	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)
SBI General Insurance Company Limited		[ICRA]AAA (Stable)
Royal Sundaram General Insurance Company Limited		[ICRA]AA+ (Stable)
Universal Sompo General Insurance Company Limited	[ICRA]AA+ (Stable)	[ICRA]AA (Stable)
Cholamandalam MS General Insurance Company Limited		[ICRA]AA (Stable)
The Oriental Insurance Company Limited	[ICRA]AA- (Negative)	
National Insurance Company Limited		[ICRA]A+ (Stable)
Life Insurance	**Issuer Rating**	**Subordinated Debt Rating**
HDFC Life Insurance Company Limited	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)
ICICI Prudential Life Insurance Company Limited		[ICRA]AAA (Stable)
Aditya Birla Sun Life Insurance Company Limited		[ICRA]AA+ (Stable)
Max Life Insurance Company Limited		[ICRA]AA+ (Stable)
PNB Metlife India Insurance Company Limited		[ICRA]AA+ (Stable)
IndiaFirst Life Insurance Company Limited		[ICRA]AA (Stable)
Star Union Dai-ichi Life Insurance Company Limited		[ICRA]AA (Stable)

Source: ICRA Research; As on July 31, 2024

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