December 08, 2023

Royal Sundaram General Insurance Co. Limited: Rating reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Subordinated debt programme	126.00	126.00	[ICRA]AA+ (Stable); reaffirmed
Total	**126.00**	**126.00**	

**Instrument details are provided in Annexure I*

Rationale

The rating factors in Royal Sundaram General Insurance Co. Limited's (Royal Sundaram) strong promoter profile with Sundaram Finance Limited {SFL; rated [ICRA]AAA (Stable)} and Ageas Insurance International N.V. (Ageas) holding equity stakes of 50% and 40%, respectively. SFL's strong parentage support is reflected in its operational, managerial and financial aid to Royal Sundaram. SFL's representation on Royal Sundaram's board of directors and the presence of a shared brand name strengthen ICRA's expectation that the promoters will provide capital support to the company, as and when required. In addition, Ageas contributes to new product development in terms of risk management, reinsurance support and channel development, among others. The rating reaffirmation considers Royal Sundaram's strong solvency profile, which is likely to support the growth in the medium term. Given the moderate internal accruals, the solvency is aided by the moderate growth in the business.

The rating remains constrained by the company's modest scale of operations with a market share of 1.2% in H1 FY2024 (2.1% in FY2020) in terms of total gross direct premium income (GDPI). The modest scale of operations is also due to the absence of the bulk crop, aviation and government health segments in the business mix. Further, the company's concentration in the motor segment remained high at more than 70% of GDPI in the last three fiscal years (73.1% in FY2023). The high share of the long-tail motor-third party (Motor-TP) business exposes Royal Sundaram's future profitability and solvency to reserving risks, though it plans to diversify and increase its presence in the health & personal accident (PA) segment. While Royal Sundaram enjoys higher investment float and income due to the high share of the long-tail business, this is offset by the higher underwriting losses, which result in moderate profitability. Going forward, the company's ability to diversify its product mix, improve its underwriting performance and operating efficiency would be critical for improving its profitability profile.

The Stable outlook reflects ICRA's expectation that Royal Sundaram is likely to receive timely and adequate support from the promoters and maintain its solvency level above the negative rating trigger.

Key rating drivers and their description

Credit strengths

Strong parentage with operational, managerial and financial support from shareholders – Royal Sundaram is owned by SFL (50.00% equity stake as on September 30, 2023) while Ageas (40.00%) is the other key shareholder. SFL is one of the large non-banking financial companies (NBFCs) in the country with assets under management (AUM) of Rs. 40,106 crore as of September 2023. It is the flagship company of the T S Santhanam Group. SFL primarily finances commercial vehicles (CVs) and cars and has invested in various entities to provide a gamut of financial services like housing finance (Sundaram Home Finance Limited), insurance (Royal Sundaram) and mutual funds (Sundaram Asset Management Company Limited). Ageas is one of Europe's largest insurance companies with around 47 million customers in 14 countries across Europe and Asia as of 2022. It offers products and services across the life, health and non-life businesses.

The strong parentage, shared brand name with SFL and the track record of equity infusions strengthen ICRA's expectation that the company will receive timely support if required.

Further, as the CV segment accounted for ~31% of Royal Sundaram's total GDPI in FY2023 and SFL is one of the major financiers in the CV segment, the business sourced from SFL accounted for 16.6% of total GDPI in the CV business in FY2023 (25.6% in FY2022). Royal Sundaram also has adequate board representation from the sponsors with three directors from SFL and two from Ageas.

Strong solvency levels – The company's capitalisation remained strong with a solvency ratio of 2.62 times as on September 30, 2023 (2.09 times as on September 30, 2022), which is significantly above the regulatory requirement of 1.5 times and ICRA's negative trigger of 1.7 times. The improvement in the solvency profile in H1 FY2024 was also supported by the receipt of crop insurance premium of Rs. 212 crore, which was overdues receivable from the Jharkhand Government and was excluded from the available solvency margin (ASM) as on March 31, 2023, as per regulatory directions.

The last capital infusion was Rs. 295 crore in FY2018 to support the company's growth plans. Royal Sundaram has the headroom to raise additional sub-debt of ~Rs. 226 crore, which could boost the solvency to 2.96 times on a proforma basis as on September 30, 2023. ICRA does not expect incremental capital requirement as the solvency ratio is expected to support growth in the medium term while maintaining a solvency ratio above 1.90 times. Further, ICRA draws comfort from the commitment of the shareholders to infuse equity, if required.

Credit challenges

Moderate profitability – Royal Sundaram's profitability remained moderate with a return on equity (RoE) of 7.7% in FY2023 (8.3% in FY2022). While the company has been reporting underwriting losses, the net profitability is supported by investment income. The overall net loss ratio improved to 77.0% in FY2023 (84.2% in FY2022 and 80.4% in FY2021). This was mainly driven by the improvement in the net loss ratio of the Motor-TP segment due to the significant release of provisions in this segment in FY2022 and FY2023 (Rs. 152 crore and Rs. 142 crore, respectively). Given the high share of the long-tail Motor-TP business, Royal Sundaram enjoys higher investment leverage[1] (4.8 times as on March 31, 2023) and investment income. Thus, despite the high combined ratio of 111.4% in FY2023 (116.7% in FY2022), the company is able to generate profits, though the profitability is moderate. Royal Sundaram reported a net profit of Rs. 116.3 crore in H1 FY2024 compared to Rs. 47.3 crore in H1 FY2023 with the improvement in the net claims ratio. However, the sustainability of the same remains to be seen.

Royal Sundaram reported expense of management to gross premium written of 31.7% in FY2023 (29.1% in FY2022), which was above the Insurance Regulatory and Development Authority of India's (IRDAI) regulatory limit of 30%. The company is looking to reduce the same below the regulatory limit in the next couple of years by underwriting group health and private car businesses, which have a relatively lower operating cost.

Royal Sundaram reported an income tax demand of Rs. 446 crore, which has not been considered as a contingent liability on the basis of internal assessments supported by expert legal advice. This is related to the disallowance of the payments made to the motor dealers based on the order passed by Customs Excise and Service Tax Appellate Tribunal (CESTAT) reversing the input credit availed on these payments. The matter is currently pending before the tax authorities. ICRA takes cognizance of the relatively high level of this demand (26.4% of net worth as of September 2023), which if crystallised would further constrain the profitability and solvency and would be a key rating monitorable.

Rising share of long-tail business exposes the company to reserving risks – Royal Sundaram's market share remains modest at 1.2% in terms of GDPI in H1 FY2024 (2.1% in FY2020), largely contributed by the Motor-TP segment. The company witnessed a consistent rise in the share of its Motor-TP segment to 50.9% of the total GDPI in FY2023 from 36.8% in FY2020. The long-tail nature of the Motor-TP segment, given the legal process involved for claims settlement, could result in uncertainty regarding the level of future claims in relation to the reserves made for this segment. Royal Sundaram's loss-reserving triangle, which involves actuarial estimates, indicates that there have been additional provisioning requirements in the past, though there has been a release of provisions in the last two years. The eventual outcome for the risk-in-force may be known with

[1] *Investment leverage = {(Total investment – sub-debt)/Net worth}*

considerable lag, which could impact the company's future profitability and solvency. Further, as the pricing of Motor-TP rates is regulated, this could impact the overall GDPI growth and profitability.

Liquidity position: Strong

The company's net premium was Rs. 2,702 crore in FY2023 in relation to the maximum net claims paid of Rs. 1,625 crore in the last few years. For H1 FY2024, the net premium stood at Rs. 1,336 crore against net claims paid of Rs. 746 crore. The company's operating cash flows were positive in FY2023, reflecting its ability to meet the expense and claims payments through premium inflows. Additionally, Royal Sundaram had investments in Central/state government securities of Rs. 3,281 crore, accounting for 41% of the total investments as on September 30, 2023, further supporting the liquidity to meet the claims of policyholders in the event of a rise in policyholders' claims. The company's shareholders' investment of Rs. 1,353 crore also remains strong in relation to the Rs. 126-crore sub-debt outstanding as on September 30, 2023.

Rating sensitivities

Positive factors – The rating could be revised or outlook changed to positive if there is a sustained improvement in the company's profitability along with an improvement in its market share.

Negative factors – The rating or outlook could be revised if there is a downward revision in SFL's rating or a decline in the strategic importance of Royal Sundaram to SFL or decline in the expectation of support from SFL. In addition, a decline in the company's solvency ratio below 1.70 times on a sustained basis could lead to a rating downgrade.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Rating Methodology – General Insurance Impact of Parent or Group Support on an Issuer's Credit Rating
Parent/Group support	Parent/Investor: Sundaram Finance Limited (SFL) The rating factors in the high likelihood of support from SFL, given the shared brand name and the representation on the board.
Consolidation/Standalone	Standalone

About the company

Royal Sundaram General Insurance Co. Limited (Royal Sundaram), incorporated on August 22, 2000, is a privately-owned general insurance company offering general insurance services across a variety of segments. With its head office in Chennai (Tamil Nadu), Royal Sundaram has 161 branches across India with an employee base of 2,924 as on September 30, 2023. The company recorded gross direct premium of Rs. 1,686 crore, an underwriting loss of Rs. 151 crore and a net profit of Rs. 116 crore in H1 FY2024.

Key financial indicators (audited)

Royal Sundaram General Insurance Co. Limited	FY2022	FY2023	H1 FY2023#	H1 FY2024#
Gross direct premium	2,867	3,380	1,550	1,686
Total underwriting surplus/(shortfall)	(370)	(368)	(213)	(151)
Total investment + Trading income	546	553	288	317
PAT	131	121	47	116
Total net worth	1,579	1,568	1,537	1,690
Total technical reserves	5,693	6,209	5,982	6,499
Total investments	7,105	7,649	7,445	8,082
Total assets	8,165	8,774	8,512	9,005
Return on equity^	8.3%	7.7%	6.1%	13.8%
Combined ratio*	116.7%	111.4%	117.1%	112.1%
Regulatory solvency ratio (times)	2.10	2.27	2.09	2.62

Source: Royal Sundaram, ICRA Research; Amount in Rs. crore
 # H1 FY2023 and H1 FY2024 figures are unaudited
^ Return on equity is annualised for H1 FY2023 and H1 FY2024
** Combined ratio – (net claims incurred/net premium earned) + (management expenses + net commission expenses)/net premium written*

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2024)				Chronology of Rating History for the Past 3 Years			
		Type	Amount Rated (Rs. crore)	Amount Outstanding as of Nov 30, 2023 (Rs. crore)	Date & Rating in FY2024	Date & Rating in FY2023	Date & Rating in FY2022		Date & Rating in FY2021
					Dec 08, 2023	Dec 13, 2022	Dec 17, 2021	Nov 18, 2021	Nov 20, 2020
1	Subordinated debt programme	Long term	76.0	76.0	[ICRA]AA+ (Stable)	[ICRA]AA+ (Stable)	[ICRA]AA+ (Stable)	[ICRA]AA+ (Stable)	[ICRA]AA+ (Stable)
2	Subordinated debt programme	Long term	50.0	50.0	[ICRA]AA+ (Stable)	[ICRA]AA+ (Stable)	[ICRA]AA+ (Stable)	-	-
3	Subordinated debt programme	Long term	-	-	-	[ICRA]AA+ (Stable); reaffirmed and withdrawn	[ICRA]AA+ (Stable)	[ICRA]AA+ (Stable)	[ICRA]AA+ (Stable)
4	Subordinated debt programme	Long term	-	-	-	-	-	[ICRA]AA+ (Stable); reaffirmed and withdrawn	[ICRA]AA+ (Stable)

Complexity level of the rated instruments

Instrument	Complexity Indicator
Subordinated debt programme	Moderately Complex

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analysing an entity's financial, business, industry risks or complexity related to the structural, transactional or legal aspects. Details on the complexity levels of the instruments are available on ICRA's website: Click Here

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
INE499S08039	**Subordinated debt**	Sep-27-2021	7.85%	Sep-27-2031#	76.00	[ICRA]AA+ (Stable)
INE499S08047	**Subordinated debt**	Mar-15-2022	8.05%	Mar-15-2032*	50.00	[ICRA]AA+ (Stable)

 # Call option on September 25, 2026

**Call option on March 15, 2027; if not exercised, call options subsequently every year on March 15 till maturity*

Key features of rated debt instrument

The rating also factors in the key features of the instrument, in line with the applicable guidelines for subordinated debt:

» Servicing of interest is contingent on the company maintaining a solvency ratio above the levels stipulated by the regulator[2]

» If the interest payouts lead to a net loss or an increase in the net loss, prior approval of the regulator would be required to service the debt

Annexure II: List of entities considered for consolidated analysis – Not applicable

[2] *As per IRDAI regulations, insurers are required to maintain a minimum solvency ratio of 150%*

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About ICRA Limited:

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