HDFC ERGO General Insurance Company Limited

Instrument	Amount in INR Crores	Rating Action (February 2015)
Claims Paying Ability	-	iAAA Reaffirmed

ICRA has reaffirmed iAAA (pronounced as I triple A) rating, indicating the highest claims paying ability of HDFC ERGO General Insurance Company Limited (HDFC ERGO). The rating takes into account the strong parentage of HDFC ERGO, with HDFC (rated [ICRA]AAA with stable outlook and [ICRA]A1+) and ERGO (primary insurance entity of Munich RE – rated Aa3 by Moody's Investors Service) as the key shareholders. HDFC ERGO has a strong management team led by experienced professionals, with focus on systems and processes in critical areas of underwriting, reinsurance and claims management. This, coupled with ERGO's international experience as a multi-liner with strong skills in all relevant insurance lines and segments of insurance business, lends strong foundation for HDFC ERGO's business success. HDFC and its other group companies provide cross-selling opportunities for HDFC ERGO. Despite the favourable long-term growth prospects on the back of current low penetration levels, the slowdown in the economy leading to moderation in growth rates coupled with regulatory changes impacting the business and financial profile of the underlying entities continue to pose challenges to the sector. Going forward, achieving scale and size while managing costs, building quality portfolio with acceptable levels of risk and focus on customer service and claims settlement will be critical in maintaining the rating profile of the Company.

HDFC ERGO continues to maintain its strong position in the country's general insurance segment with a market share of about 4% in FY2014 (4% in FY2013). The Motor (34%[*] for 9MFY2015), Health (18%[*] for 9MFY2015) and weather insurance (7%[*] for 9MFY2015) segments remain the key business drivers for the Company. During FY2014, HDFC ERGO reported a 19% YoY growth in GDP (Gross Direct Premium) to Rs. 2,907 Crores lead by growth in the motor (25% YoY growth) and weather insurance (20% YoY growth) segments. HDFC ERGO's net retention ratio has remained stable at around 60-61% in the last few years with the lower retention ratios in the motor segment being partly cushioned by rising retention ratios in the retail health insurance segments. Consequently, Net Premium Earned (NPE) grew by 28% YoY to Rs. 1,585 Crores in FY2014 from Rs 1,243 Crores in FY2013.

The gross claims paid for the Company rose by 59% YoY to Rs. 1,416 Crores in FY2014 due to higher claims on the GMC (Group Medical Coverage) schemes. In order to bring down claims paid, the management intends to shift focus towards retail health schemes (due to the non-bulky nature of claims). During 9MFY2015, as per the management, its adequate catastrophe loss coverage aided in limiting the claims from J&K floods and the Hudhud cyclone to about Rs. 25 Crores even as, at a gross level, the impact stood at Rs. 170-180 Crores.

HDFC ERGO partially cushioned the impact of sharp rise in claims by efficiently utilizing existing capacity leading to a moderate shrinkage in Operating Expenses/NPE to 28% in FY2014 from 30% in FY2013. However, the underwriting losses increased to Rs. 39.3 Crores in FY2014 from Rs. 16.5 Crores in FY2013. Underwriting losses were adequately cushioned by a sizeable investment income of Rs. 265.9 Crores (Rs 199.9 Crores in FY2013) to enable the Company to end FY2014 with a PAT of Rs. 195.4 Crores (PAT of Rs. 154.5 Crores in FY2013) and a RoE of 22.1%[2] (RoE of 21.5%[2] in FY2013. Given the Company's notable branch expansion undertaken in Q4FY2014 and Catastrophic losses, ICRA expects profitability during FY2015 to be under pressure.

[*] As a proportion of total GDP written during the period
[2] RoE has been calculated on closing Net worth

During the initial phase of the JV, HDFC ERGO's business growth was driven largely by corporate agents as it increased its market share at a faster clip. However, over the last few years, the share of the Company's corporate channel has gradually been declining and stood at 33% in FY2014 vis-à-vis 40% in FY2013. Proportion of business from Direct and individual agent channels has been on an uptrend for the past couple of years. The growth in direct business has been aided primarily by the Weather Insurance segment – which is primarily Direct Business. In addition to HDFC Bank, the Company has now entered into a partnership with Deutsche Bank to strengthen its bancassurance channel.

The spread of investments across the credit curve has undergone marginal changes with the proportion of AAA-rated debt papers shrinking from 59% in FY2013 to 56% in FY2014 while the proportion of AA-rated papers rising from 8% to 11% during this period. The proportion of the book with more than 7 years residual tenor has inched up from 27% in FY2013 to 34% in FY2014 and further to 42% by Dec-2014 as the Company increased investments in long tenure instruments including tax-free bonds of various public sector entities. While the Company has increased its equity portfolio in the current fiscal, it remains low at around 1% of total investments. The decline in yields and the uptick in equity markets provide HDFC ERGO with strong unrealised gains as on date.

The Company's liquidity profile remains comfortable with 19% of the debt investments maturing within a year as on December 31,2014 and majority of the debt investments in highly liquid G-Secs and top rated corporate entities. Other than a sizeable proportion of the book in short-term instruments, ICRA derives comfort from the Company's solvency ratio (which stands at 1.60 as on December 2014) and adequate networth of about Rs. 1,003 Crores as on December 31, 2014. In December 2014, the Company received an equity infusion of Rs. 60 Crores from both the JV partners.

Company Profile
HDFC ERGO General Insurance Company Limited is a joint venture between HDFC Limited, India's premier housing finance institution (rated [ICRA]AAA with stable outlook - holding 73.63% stake as on Dec-14) and ERGO International AG, the primary insurance entity of Munich Re Group (holding 25.84% as on Dec-14 with balance being held by employees of HDFC ERGO). The Company offers complete range of general insurance products ranging from Motor, Health, Travel, Home and Personal Accident in the retail space and customized products like Property, Marine and Liability Insurance in the corporate space. HDFC ERGO has been expanding its presence across the country and with 107 branch offices as on Dec-14. In existence for over 35 years and with a presence in banking, insurance and asset management, the HDFC group is an important part of the Indian financial services sector. ERGO is represented in more than 30 countries and concentrates on Europe and Asia. In Europe, ERGO is no. 1 in the health and legal expenses insurance segments, and in its home market of Germany it is among the market leaders.

Recent Results
During 9MFY2015, HDFC ERGO reported a Gross Direct Premium (GDP) of Rs. 2,329 Crores and a PAT of Rs. 59 Crores as compared with a GDP of Rs. 2,079 Crores and a PAT of Rs. 146 Crores in 9MFY2014. As on December 31, 2014, the Company's networth stood at Rs. 1,003 Crores and with a regulatory solvency ratio of 1.6 times.

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