

Title

India Ratings Upgrades Star Health and Allied Insurance Company to 'IND AA+/Stable' and its Sub-debt to 'IND AA+/Stable'

Brief

Ind-Ra-Mumbai-xx July 2024: India Ratings and Research (Ind-Ra) has upgraded Star Health and Allied Insurance Company Limited's (Star) Long-Term Issuer Rating to 'IND AA+' from 'IND AA'. The Outlook is Stable. The detailed rating actions are as follows:

Details of Instruments

Instrument Type	Date of Issuance	Coupon Rate	Maturity Date	Size of Issue (billion)	Rating Assigned along with Outlook/Watch	Rating Action
Issuer rating	-	-	-	-	IND AA+/Stable	Upgraded
Subordinated debt*	-	-	-	INR7	IND AA/Stable	Upgraded

*Details in Annexure

Analytical Approach

Ind-Ra continues to take a standalone view of Star to arrive at the ratings. The notching difference between issuer rating and subordinated debt factors characteristic of the instrument along with diversified shareholding structure.

Detailed Rationale of the Rating Action

The upgrade reflects Star's consistency in underwriting profits, maintenance of market share and leadership position within the industry, its large distribution network of agents, adequate solvency margin buffer supported by internal accruals, wider product basket under the health segment, multiple avenues to aid capital support for growth and during stress times, and stable profitability. The ratings also factor in a stable investment book and defined underwriting practises. The ratings remain constrained by Star's single line of business and regulatory changes that might lead to increased competition from established players with similar distribution franchise.

List of Key Rating Drivers

Strengths

- Sustained leadership position in health insurance and reasonable market share in general insurance (GI) space
- Wider distribution franchise through agent network
- Experienced management
- Investment book remains stable
- Established claim processing and underwriting practices
- Profitability buffers stable
- Capital remains adequate, with internal accruals building up

Weaknesses

- Single line of business could lead to volatile claims; diversified shareholding structure
- Regulatory changes, and performance of entity in maintaining leadership remains monitorable

Detailed Description of Key Rating Drivers

Sustained Leadership Position in Health Insurance and Reasonable Market Share in GI Space: Star is a leading retail private health insurance provider in India, with an overall retail health segment market share of 33% in FY24 (FY23: 34%) and 30% (39%) in incremental business in the segment. Furthermore, at FYE24, Star had a market share of 5.3% (FYE23: 5.0%) in the overall general insurance space and 14% (13.3%) in the overall health insurance & personal accident space. Star had 92.7% of its gross written premium under the retail category in FY24 (FY23: 93.5%). The renewals also remained high at 95.1% in FY24 (FY23: 94%). The gross written premium grew at a CAGR of 23.1% over FY19-FY24 to INR152.5 billion, against the industry growth of 18.1%.

The company has a long and established track record in health insurance, a reasonable in-house claim processing efficiency, and a large team of doctors and empanelled hospitals. Incrementally, the company plans to scale up its group business as well, increasing its share to 20% from 8% over medium term.

Wider Distribution Franchise through Agent Network: Star has a wide distribution network encompassing agents, bancassurance partners and brokers, and alternate channels such as online, direct marketing and tele-calling. The company has tie ups with around 14,295 hospitals, with more than 10,750 hospitals on its agreed network, and 881 branches across 26 states and seven union territories. It has one of largest agency channel, with 0.70 million agents, 7,883 in-house sales managers and 1,627 employees in underwriting, including full-time medical professionals, for the company. The agency channel contributes to 81.8% of the total gross written premium (GWP) in FY24. The banca partnership, which is on the rising trend, stood at 4.8%, direct business at 8.4% and brokers at 4.7% in FY24. Star has built 58 bancassurance and non-banking finance company tieups for distribution expansion, thereby diversifying from the current concentration in the agency channel.

Experienced Management: Star has an experienced and professional management team, and underwriting and claim-processing business heads, who have been with the company for a long period, with minimal attrition at the senior level. The shareholding resides with Safecrop Investments India LLP and Jhunjhunwala family at 40.39% and 17.21%, respectively, at end-June 2024. Its shareholding had been distributed among three large shareholders, which infused INR5 billion in FY20 for growth needs. The company raised INR26.2 billion in FY21 during the pre-initial public offering (IPO) from the existing shareholders as well as a new set of large investors during the pandemic. Star had also raised capital of about INR20 billion through an initial public offering in FY22, which supported its solvency margins, as the company had consumed larger capital due to its claim ratio being higher than historical trends. Incrementally, Star has adequate room to raise subordinated debt as well as raise equity capital as and when required, according to Ind-Ra.

Investment Book remains Stable: Star's investment book portfolio quality has been stable, as more than 67.52% of its investments in FY24 (FY23: 67.4%) consisted of debt securities either rated 'AAA' and under government-backed securities. Also, the share of debt investments (based on book value) in government securities stood at 31.8% in FY24 (FY23: 33.65%). Star has also been increasing its holding across the AA+ and below categories to around 25.19% in FY24 (FY23: 25.4%, FY22: 23.11%). Thus, the liquidity profile of the investment book is stable to cater to the needs of the policyholders, with 18.06% of the book having a maturity profile of up to one year. The extent of surplus in solvency is critical in determining the insurer's ability to service the subordinated debt. The investment book stood at INR158 billion at end-1QFY25 (FY24: INR155 billion) and yield on investments stood at 7.5% (7.7%). The management plans to maintain an optimum balance between regulatory requirements and optimise yield through new products such as real estate investment trust and infrastructure Investment trust, along with an increasing equity share in the overall AUM, however keeping it within the prescribed limit.

Established Claim Processing and Underwriting Practices: Star has a well-established risk management framework to identify, assess, and monitor risks across the health segment, with a strong focus on retail health policyholders. The company has a specialised underwriting team, comprising segment experts, which enables quick and efficient assessment and management of business-specific risks. However, Star's settlement ratio was higher than that of its peers at 98.4% in FY24 (FY23: 88.4%). The star settlement through cashless mode moved up to 87.4% in FY24 (FY23: 80.4%). Henceforth, Star plans to retain a large portion of its business, with reinsurance being limited to minimal mandatory requirements, and incremental reinsurance being more risk-based than a capital saving tool. The increased size and scale will boost Star's negotiating power with hospital networks, and the in-house claim processing further validates the claims raised by hospitals and helps Star rationalise the ultimate pay-outs.

Profitability Buffers Remain Stable: The reported claim ratio increased to 66.5% of the net earned premium (excluding 1% claim processing cost (CPC)) in FY24 (FY23: 63.9%); however, this has been trend across industry due to rise in incident rates

and increased portability across players. The claim ratio (including 1% CPC cost) for 1QFY25 increased to 67.6% compared to 65.4% in 1QFY24 due to the increased portability in the industry, along with certain preponement of seasonal diseases claims. The high incident rates in claims along with an increase in the overall severity compared to that in FY20, largely due to medical inflation and a rise in the awareness across policyholders. Star has implemented price hikes for its flagship products and will be implementing hikes for other products too in FY25, thereby mitigating medical inflation and the rising incident rate risk on claim ratio. It also plans to implement price hikes in few older products depending upon its claim ratio, evolving regulation on customer benefits and the overall profile of customers. The company has, over the years, moved away from government business and has been focussing on the retail health segment, which forms 91.5% of the gross written premium and is likely to continue to do so. Historically, Star had better profitability than its peers', with its combined ratios remaining below 100% during FY16-FY20. In FY21, due to accounting and reinsurance treaty changes, the combined ratio had exceeded 100%; however, after factoring in the previous unexpired premium reserve method, re-adding the reinsurance treaty provision and excluding one-off items, Star's combined ratio would have been around 98.4% in FY21 whereas FY22 saw Covid impact, leading to a combined ratio of 117.9%.

The expense ratio (including claim processing costs) as a percentage of the net earned premium was 30%-36% over FY20-FY24 (FY24: 31.3%, FY23: 31.4%). Star's combined ratio (adjusted for the claim processing costs) remained stable at 96.6% in FY24 (FY23: 95.3%), as claims had normalised when compared to the pandemic period, along with the product premium hikes implemented in FY23 and FY24. The combined ratio in 1QFY25 stood at 99.2%, due to higher claim ratios. Historically, the cases related to Covid contributed 21.3% to the total claims in FY22 (FY21: 33.1%); however, the share of non-Covid claims remained high and rose to 65.8% in FY22 (FY21: 61.3%), impacting the profitability for both years.

Capital Remains Adequate, with Internal accruals Building Up: As per Ind-Ra's estimates, Star's solvency margin (1QFY25: 2.29x, FY24: 2.21x, FY23: 2.14x, FY22: 1.67x) utilisation is highly sensitive to growth in the gross written premium as well as the net claim ratio. In FY22, the solvency margin was supported by the infusion of primary capital of INR20 billion raised through the IPO and the issuance of subordinated debt of about INR4.7 billion. As per Ind-Ra's stress test, Star can sustain a claim ratio below 74.5% with its solvency margin remaining above the regulatory minimum, factoring in growth of up to 30% in the gross written premium in FY25. The internal accruals are also on an improving trend Star posing an underwriting profit. This, along with investment book support, led to the return on equity improving to 14.4% in FY24 (FY23: 12.4%). Based on the management's expectation of the claim ratio moderating and the combined ratio improving, there will be an improvement in the underwriting profit in the medium term. Also, Star GWP growth is likely to range between 18% to 20% in FY25 and the incremental capital requirement is likely to moderate with internal accruals building up, thereby improving and maintaining the overall solvency ratio. Also, with IFRS implementation, there could be a further improvement in internal accruals by 300-350bp, as per management.

Single Line of Business Could lead to Volatile Claims; Diversified Shareholding Structure: The ratings are constrained by Star's single product line of business compared with other general insurance companies. During events such as the recent pandemic, there could be a heightened volatility in claim ratio if a single segment is impacted compared to diversified general insurers. Also, with the reduced share of overall reinsurance, Star remains exposed to event risks impacting individuals to a large extent across geographies. However, within a single product line, Star has diversified its offerings, with the granular retail health segment accounting for a larger share of the gross written premium, thereby mitigating this risk to a certain extent. Also, the diversified nature of shareholders could support the entity during growth times. However, the flow of capital during periods of stress needs to be monitored.

Regulatory Changes and Performance of Entity in Maintaining Leadership Remains Monitorable: With regulatory discussion on composite licence, along with any large life entity with a wide agent network looking to expand in the health insurance space, could increase competition within the retail health space, thereby impacting Star's dominance. Any impact on Star's market share and growth due to increased competition will remain a key monitorable.

Liquidity

Adequate: Star has an adequate cover for policyholders' liabilities (unexpired risk reserve plus claims outstanding plus dues to other insurance companies) through assets (investment book plus cash and bank balance), with an asset over liabilities cover of 1.77x in 1QFY25 (FY24: 1.71x, FY23: 1.68x). Considering only the high-quality liquid assets (government securities, and cash and bank balance), the above ratio stood at 0.75x in 1QFY25 (FY24: 0.68x, FY23: 0.72x). Also, the investment book has a large share of investment (68%) to debt securities either rated 'AAA' and in government-backed securities which could be liquidated at ease when necessitated. Also, as a policy, it maintains liquid investments to cover immediate net 30 days outflow and adds a risk margin over it to maintain 5.5%-7% of investment book in liquid instruments.

Rating Sensitivities

Positive: A sizable rise in the overall general & health insurance market share, diversification of the distribution network and a further strengthening of the franchise through segmental diversification to reduce monoline concentration risk could be a positive rating trigger.

Negative: The inability to manage volatility in the claim ratio on a sustained basis, along with a weakening of the underwriting performance, thereby affecting the profitability and solvency buffers, will lead to a negative rating action. A delay in the infusion of capital to support the solvency margin during volatile times, will be key rating monitorable. The claim ratio remaining above 67% or the combined ratio remaining above 100% or the solvency margin falling below 1.7x on a sustained basis could lead to a negative rating action.

Disclosures for CE Rating

Disclosures for Provisional Rating

ESG Issues

ESG Factors Minimally Relevant to Rating: Unless otherwise disclosed in this section, the ESG issues are credit neutral or have only a minimal credit impact on Star, either due to their nature or the way in which they are being managed by the entity. For more information on Ind-Ra's ESG Relevance Disclosures, please click [here](#). For answers to frequently asked questions regarding ESG Relevance Disclosures and their impact on ratings, please click [here](#).

Any Other Information

No

About the Company

COMPANY PROFILE

Star commenced operations in 2006. The business interests span health insurance, overseas mediclaim policy and personal accident policy. It has a pan-India presence, with 887 branch offices, a network of 0.718 million agents, with cashless and reimbursement facilities, and over 15,133 network hospitals across India at end-June 2024. The key promoters are Safecrop Investments India LLP (Westbridge Capital) with 40.4% stake and Rakesh Jhunjunwala & family (17.3%). Nearly 39% of the company's revenues was derived from south India, 22% from west India, 30% from north India and 8% from east India at FYE24.

Key Financial Indicators

Particulars	FY24	FY23
Gross written premium (INR million)	152,545	129,525
Total equity (INR million)	63,416	54,301
Net profit (INR million)	8,448	6,186
Solvency margin (x)	2.21	2.14
Combined ratio(%)	96.6	95.3
Return on net worth (%)	14.4	12.4
Source: Star; Ind-Ra		

Applicable Criteria

- Insurance Rating Criteria
- Evaluating Corporate Governance
- Financial Institutions Rating Criteria
- The Rating Process

Status of Non-Cooperation with Previous Rating Agency

Not applicable

Rating History

Instrument Type	Rating Type	Rated Limits (billion)	Current Ratings	Historical Rating/Outlook		
				10 October 2022	22 October 2021	20 September 2021
Issuer rating	Long-term	-	IND AA+/Stable	IND AA/Stable	IND AA/Stable	IND AA/Stable
Subordinated debt	Long-term	INR7	IND AA/Stable	IND AA-/Stable	IND AA-/Stable	IND AA-/Stable

Complexity Level of the Instruments

Instrument Type	Complexity Indicator
Subordinated debt*	High

* As instrument is part of regulatory capital, where the solvency margin should remain above the regulatory minimum for coupon payment or impact of such payment results in loss or increase in net loss, prior regulatory approval is required for payment.

For details on the complexity level of the instruments, please visit <https://www.indiaratings.co.in/complexity-indicators>.

Annexure

Instrument	ISIN	Date of Issuance	Coupon Rate (%)	Maturity Date	Size of Issue (billion)	Rating/Outlook
Subordinated debt	INE575P08032	30 September 2021	8.75	29 September 2028	INR4.0	IND AA/Stable
Subordinated debt	INE575P08040	29 October 2021	8.75	27 October 2028	INR0.7	IND AA/Stable
Total utilised limit					INR4.7	
Total unutilised limit					INR2.3	IND AA/Stable
Source: NSDL						

COMPLEXITY LEVEL OF THE INSTRUMENTS

Instrument Type	Complexity Indicator
Subordinated debt*	High

* As instrument is part of regulatory capital, where the solvency margin should remain above the regulatory minimum for coupon payment or impact of such payment results in loss or increase in net loss, prior regulatory approval is required for payment.

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