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India Ratings Affirms Star Health and Allied Insurance Company at 'IND AA'/Stable

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India Ratings and Research (Ind-Ra) has affirmed Star Health and Allied Insurance Company Limited's (Star) Long-Term Issuer Rating at 'IND AA'. The Outlook is Stable. The instrument-wise rating action is as follows:

Instrument Type	Date of Issuance	Coupon Rate	Maturity Date	Size of Issue (billion)	Rating/Outlook	Rating Action
Subordinated debt*	-	-	-	INR7.5 (reduced from INR9.5)	IND AA-/Stable	Affirmed

*Details in Annexure

Key Rating Drivers

Sustained Leadership Position in Health Insurance: Star is the largest retail private health insurance provider in India, with a market share of 33% in FY22 (FY20: 31.3%, FY20: 28.6%) and 42% in incremental business in retail health segment. Furhtermore, at FYE22, it had a market share of 5.2% in the overall general insurance space and 14.2% in the overall health insurance & personal accident space. Star had 88.3% of its gross written premium under the retail category in FY22 (FY21: 87.9%). The renewals also remained higher at 94% in FY22 (FY21: 97.9%). The gross written premium increased at a CAGR of 34% to INR114 billion over FY16-FY22, against the industry growth of 20%.

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. Star has a wide distribution network encompassing agents, bancassurance partners and brokers, and alternate channels such as online, direct marketing and tele-calling, which support the growth of the business. The company has tie ups with around 12,820 hospitals, with more than 8548 hospitals on its agreed network, and 807 branches across 26 states and four union territories. It has a large agency channel, with 0.55 million agents, 8,292 in-house sales managers and 1,627 employees in underwriting, including full-time medical professionals, for the company.

Liquidity Indicator- Adequate: Star has 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 asset over liabilities cover of 1.66x in FY22 (FY21:1.44x, FY20: 1.56x). Considering only the high-quality liquid assets (government securities, and cash and bank balance), the above ratio stood at 0.76x in FY22 (FY21: 0.8x, FY20: 0.85x).

Star had adequate capital buffers at 1QFYE23, supported by its sizeable net worth and solvency margins. Its shareholding has been distributed among three large shareholders, who infused INR5 billion in FY20 for growth needs. The company raised INR26.2 billion in FY21 during the pre-initial public offering (IPO) capital raise from existing shareholders as well as new set of large investors during the pandemic. Star also raised additional capital of about INR20 billion through the IPO in FY22, thereby supporting its solvency margins during challenging years of FY21 and FY22, when the company consumed larger capital due to the claim ratio being higher than historical trends.

Moreover, its investment book portfolio quality has been stable, as more than 69.49% of its investments in FY22 (FY21: 75.7%) 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 35.6% in FY22 (FY21: 42.5%). Thus, the liquidity profile of the investment book is stable to cater to the needs of the policyholders, with 19.4% 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. In FY21, Star had reported a one-time loss, largely due to an accounting change, wherein it had given up its reinsurance treaty for FY22 and moved to the 1/365 method (more conservative method) from the unexpired premium reserve method for recognition of premium. As a result of this change, Star had to seek permission from the Insurance Regulatory and Development Authority for debt servicing, which was granted for servicing the subordinated debt in 1QFY22. Since it also recorded a loss in FY22, it had to seek regulatory permission for servicing coupon in 1QFY23.

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 lower than that of its peers at 93% in FY22 (FY21: 90%). This was largely due to underwriting pre-existing diseases and also because the company has been catering to the mass retail segment, which leads to higher rejection of improper claims. Star, henceforth, 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 help Star negotiate better with hospital networks, and the in-house claim processing would lead to further validating of claims raised by hospitals and would help rationalise the ultimate pay-outs.

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. However, post the change in shareholding in FY19, Star had reshuffled roles and brought in professionals from the industry for the roles of the chief financial officer and chief investment officer. Also, the company has appointed a full-time actuary to enable product monitoring and maintain risk measurement while scaling up the business processes. Star has also seen changes at the board level with the entry of new shareholders enhancing the diversity of the board.

Operating and Capital Buffers Turn Volatile due to COVID-19: The reported claim ratio increased to 85.9% of the net earned premium (excluding 1% claim processing cost) in FY22(FY21: 88.4%)due to the impact of the second and third waves of COVID-19. The severity in claims increased in FY22, largely due to COVID-19 claims, which showed higher severity and formed 21.3% of the overall claims, and also owing to the high severity seen in non-COVID claims in 3QFY22, due to posptoned surgical cases being claimed. The company has, over the years, moved away from government business and has been focussing on the retail health segment, which forms 88.3% of the gross written premium and is likely to continue to do so. In lieu of the COVID-19 outbreak impact, Star also incrementally revised the pricing of products, wherein there has been a permanent change in the loss ratio to contain the rise in same. Star historically had better profitability than 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.

As the combined ratio stabilises with the end of pandemic, the franchise size and scale would help business drive underwriting profit and build-up of investment float would drive the overall profitability in the medium-to-long term. The expense ratio (including claim processing costs) as a percentage of the net earned premium was 30%-36% in the last four years (FY22: 31.9%, FY21: 31.6%). Star’s combined ratio (adjusted for the claim processing costs) weakened to 117.8% in FY22 (FY21: 120%), as higher covid claims in 1HFY22 and elective and surgical claims in 3QFY22 led to the overall claim ratio being higher than envisaged. 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. The claim ratio on reported basis for 1QFY23 stood at 66.3% with combined ratio of 98.2%, leading to profitability of INR2.1 billion, thereby driving the business’s return to normalcy. If there are no further waves of the pandemic, the managament expects the claim ratio to normalise in FY23.

As per Ind-Ra’s estimates, Star’s solvency margin (FY22: 1.67x, FY21: 2.22x, FY20: 1.88x) utilisation is highly sensitive to the 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 67.5% without witnessing a material impact on its solvency margin, factoring in growth of up to 30% in the gross written premium.

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 pandemic, there could be a heightened volatility in claim ratio if a single segment is impacted compared to diversified general insurers. However, within the 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 flow during periods of stress needs to be monitored.

Rating Sensitivities

Positive: A sizable rise in the overall health insurance market share and further strengthening of franchise could be a positive rating trigger. Furthermore, demonstrated ability to maintain stable combined ratio through the cycles with continued underwriting profitability and stable claim ratio, along with adequate solvency margin buffer over and above the regulatory requirements through internal accruals or equity infusion to navigate volatile times would be positive for the ratings.

Negative: The inability to manage volatility in the claim ratio on a sustained basis, along with weakening of the underwriting performance, thereby affecting the profitability and solvency buffers, would lead to a negative rating action. Delay in infusion of capital to support solvency margin during volatile times, would be key rating monitorable. The claim ratio remaining above 67% or the combined ratio remaining above 100% or the solvency margin falling below 1.65x on a sustained basis could lead to a negative rating action.

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.

Company Profile

Star commenced its operations in 2006. The business interests span health insurance, overseas mediclaim policy and personal accident policy. It has a pan-India presence, with 807 branch offices, a network of 549,501 agents, with cashless and reimbursement facilities, and over 12,820 network hospitals across India. The key promoters are Safecorp Investments India LLP (Westbridge Capital) with 41% stake and Rakesh Jhunjhunwala & family (17.5%), while Madison group (7.4%) remains as the shareholder. Nearly 39% of the company's revenues was derived from south India, 23% from west India, 30% from north India and 8% from east India at FYE22.

FINANCIAL SUMMARY

Particulars	FY22	FY21
Gross written premium (INR million)	114,635	93,885
Total equity (INR million)	45,134	34,843
Net profit (INR million)	-10,407	-10,857
Solvency margin (x)	1.67	2.22
Combined ratio(%)	117.8	120
Return on net worth (%)	-23.1	-31.1
Source: Star		

Solicitation Disclosures

Additional information is available at www.indiaratings.co.in. The ratings above were solicited by, or on behalf of, the issuer, and therefore, India Ratings has been compensated for the provision of the ratings.

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Rating History

Instrument Type	Current Rating/Outlook			Historical Rating/Outlook			
	Rating Type	Rated Limits (billion)	Rating	22 October 2021	20 September 2021	12 November 2020	14 November 2019
Issuer rating	Long-term	-	IND AA/Stable	IND AA/Stable	IND AA/Stable	INDAA-/Stable	IND AA-/Stable
Subordinated debt	Long-term	INR7.5	IND AA-/Stable	IND AA-/Stable	IND AA-/Stable	IND A+/Stable	IND A+/Stable

Annexure

Instrument	ISIN	Date of Issuance	Coupon Rate (%)	Maturity Date	Size of Issue (billion)	Rating/Outlook
Subordinated debt	INE575P08016	6 September 2017	10.25	6 September 2024	INR2	WD (Paid in full)
Subordinated debt	INE575P08024	30 October 2017	10.20	30 October 2024	INR0.5	IND AA-/Stable
Subordinated debt	INE575P08032	29 September2021	8.75	29 September 2028	INR4.0	IND AA-/Stable
Subordinated debt	INE575P08040	28 October 2021	8.75	29 October 2028	INR0.7	IND AA-/Stable
				Total utilised limit	INR5.2	
				Total unutilised limit	INR2.3	IND AA-/Stable

Complexity Level of Instruments

Instrument Type	Complexity Indicator
Subordinated debt	High

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

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