

# Softlogic Life Insurance PLC

## A structural growth story

An underpenetrated segment spearheading ahead  
with COVID-19 driven awareness

### Bloomberg ticker – AAIC.SL

Insurance Sector

Price (LKR) – 30.8

Target Price (LKR) – 44.5

Total Return (%) – 53%

### Share Data

Market Cap (USD mn) 57.0

Market Cap (LKR bn) 11.5

12M H/L (LKR) 36/20

Free Float (%) 10.3%

Analysts

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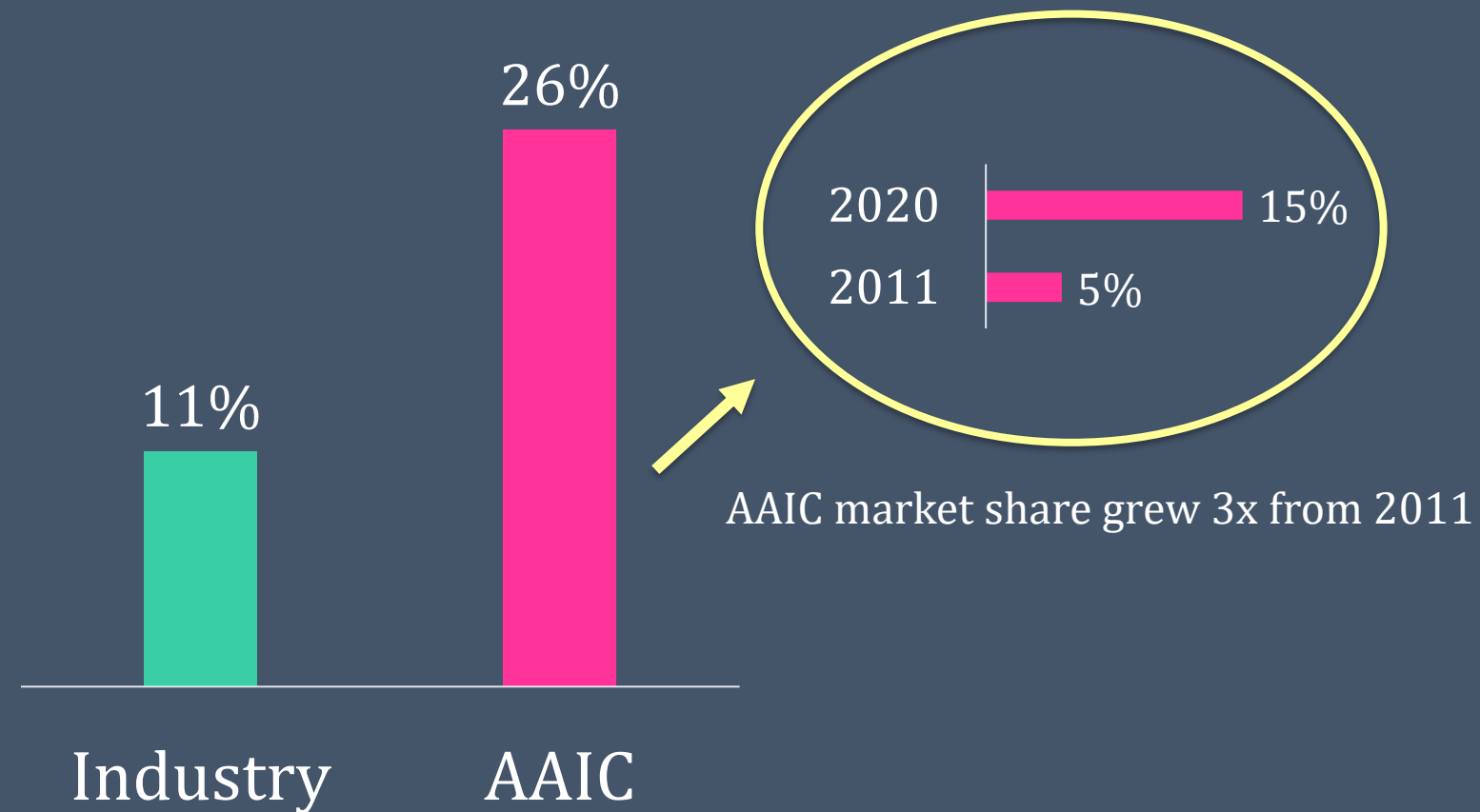
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# Executive Summary: We expect AAIC to provide a total return of 53% (44% share price upside and ~9% forward dividend yield)

## Growing beyond the industry with a GWP CAGR of 26%

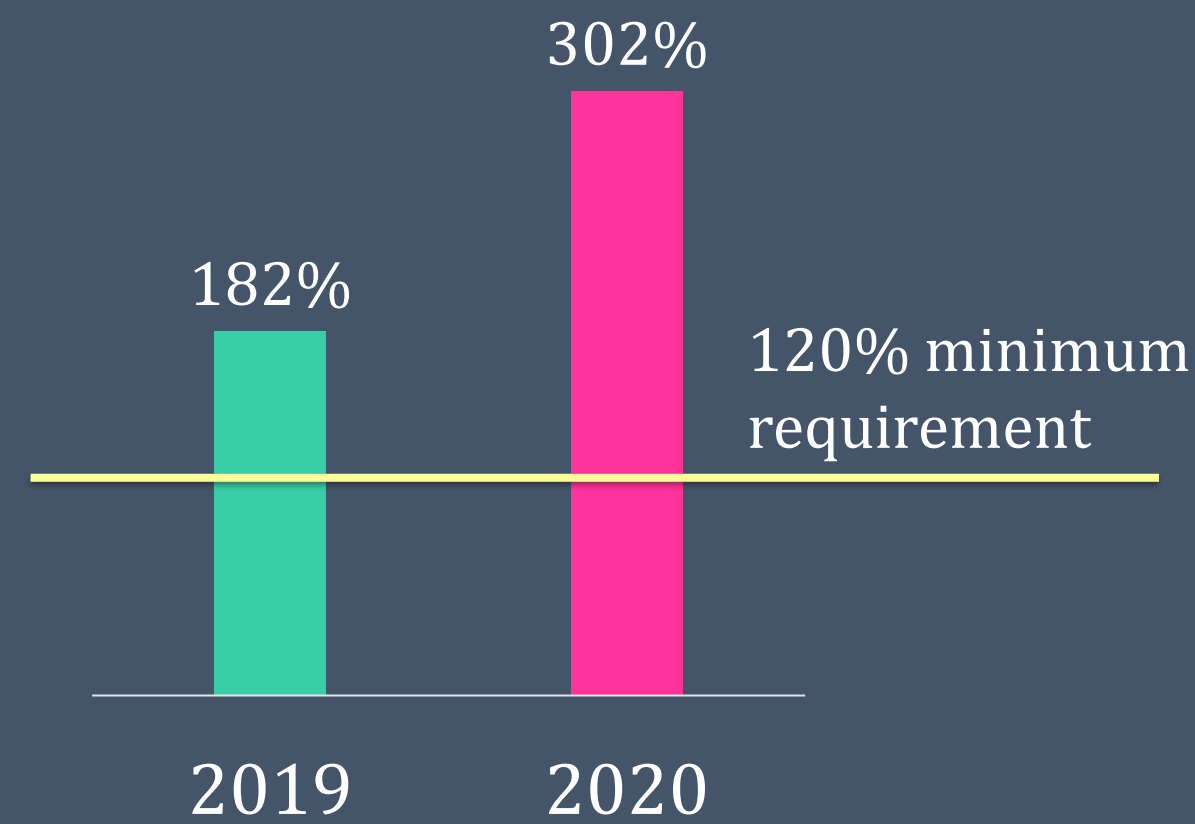
CAGR of GWP from 2011 to 2020



Over the past decade, AAIC has comfortably outgrown the Life Insurance sector. The 10-year compound growth in premiums from 2011 to 2020 was 26% p.a., well above the 11% p.a. industry growth rate. As a result of this superior growth, AAIC's market share has nearly tripled, from 4.5% in 2011, to 15.2% in 2020.

## Strong capital position with a higher ROE of 20%

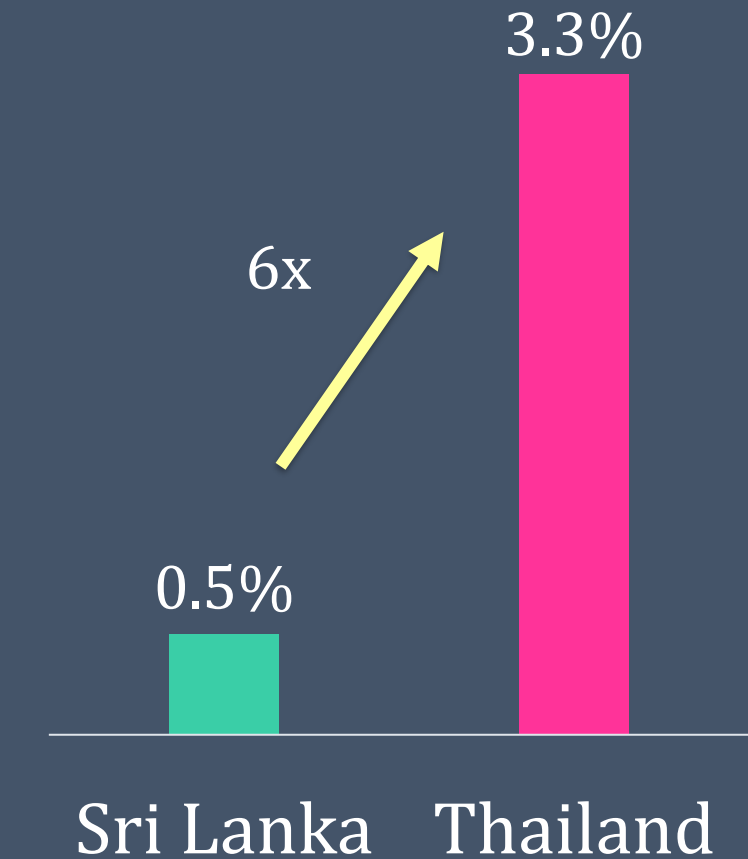
Capital Adequacy Ratio of AAIC



AAIC's capital position continues to be very strong, with capital ratio of 302% in excess capital above the minimum 120% solvency level, up from 182% in 2019. Capital profile was further augmented due to funding of LKR 2.8bn with Munich Re, and Tier II capital infusion of LKR 2.8bn by Finfund and Norfund.

## Long growth runway as penetration remains low

Life Insurance penetration as a % of GDP



Given the lower penetration of Life Insurance sector, we believe COVID-19 driven awareness and country's economic development should enable a longer-term superior growth profile to reach LKR 600bn market size like Thailand from present LKR 103bn.

\*GWP – Gross Written Premium is a term used in the Life insurance sector to describe the total amount that customers are required to pay for insurance coverage policies issued by a company during a specified period.

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AAIC growth profile remains strong due to innovative strategy and lower market penetration

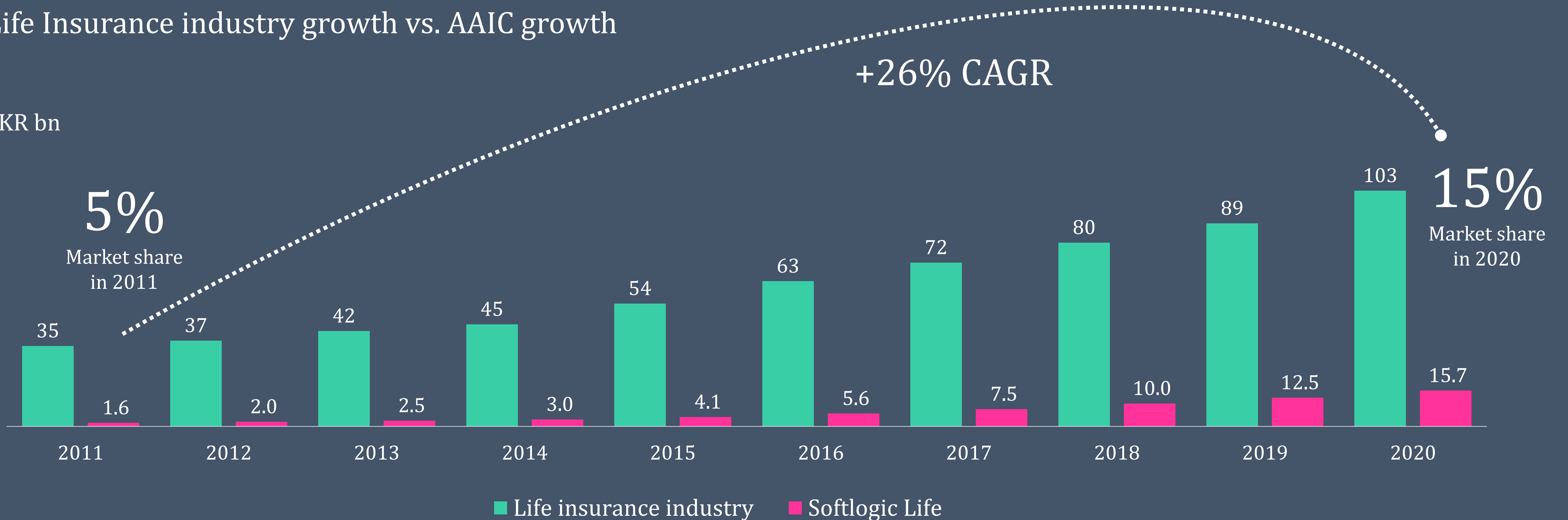
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# Since its acquisition from Asian Alliance in 2011 by Softlogic, AAIC's GWP grew at a CAGR of 26% cf. industry growth of 11%

Life Insurance industry growth vs. AAIC growth

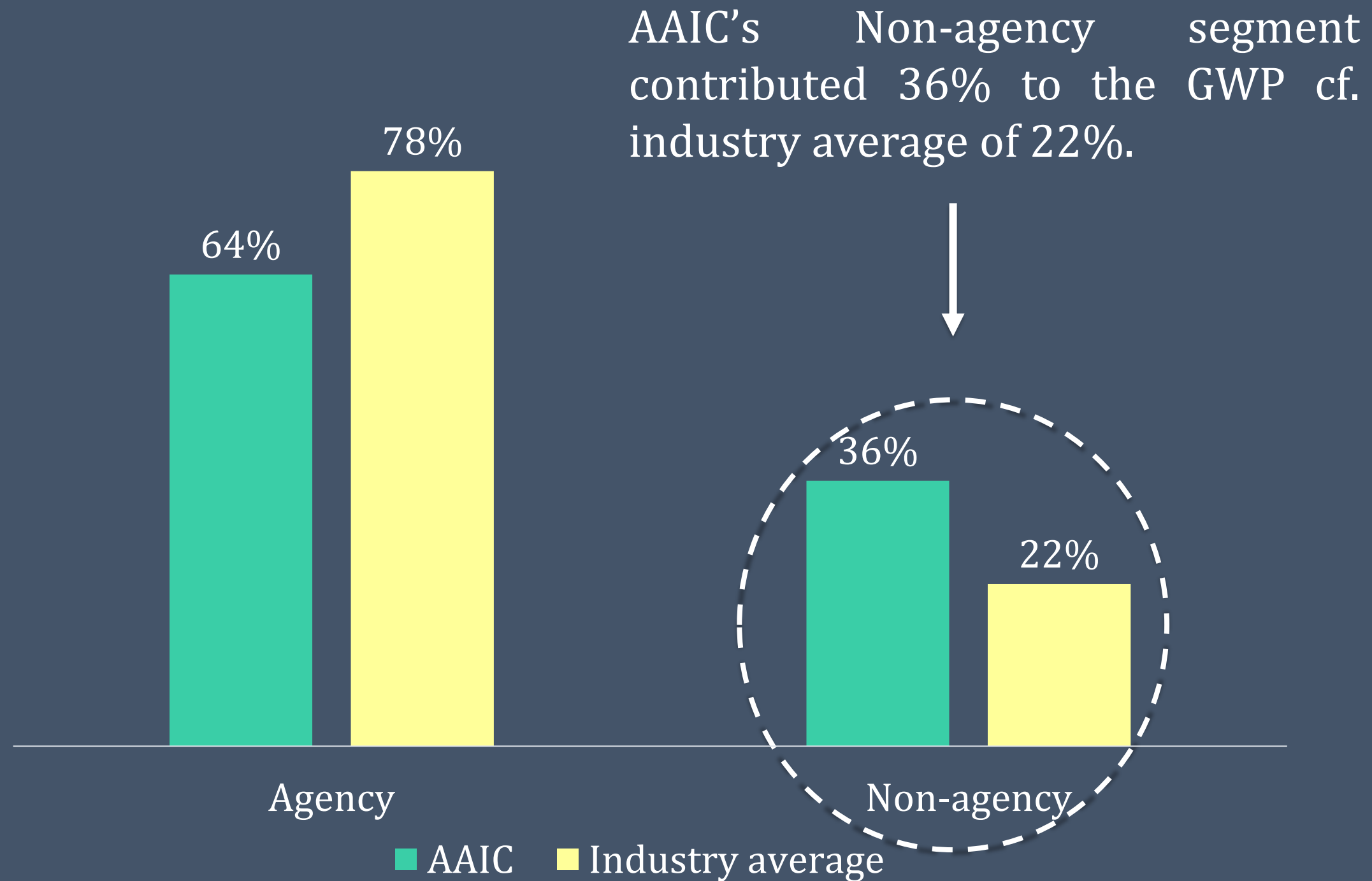
LKR bn



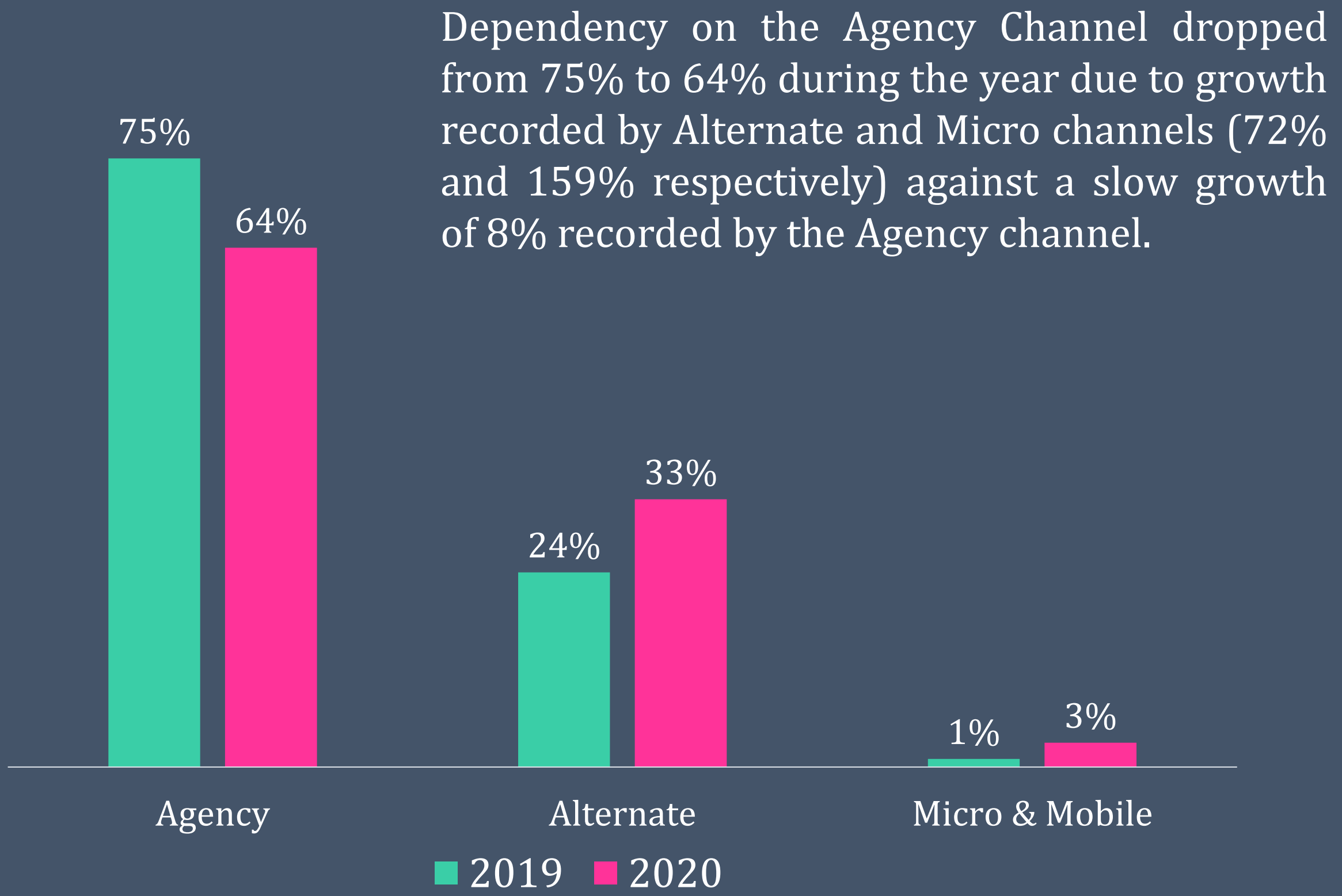
AAIC currently has a market share of 15% out of an LKR 103bn market and is intending to claim market leadership in a couple of years while maintaining an ROE of over 20%. AAIC's growth is expected to be driven by a well-diversified distribution channel, which has a 2x higher focus towards non-agency business models cf. industry average of 22%

# Growth is mainly driven by a **Diversified Distribution Strategy**, having a higher focus on non-agency models than the industry

Comparison of Agency and non-agency business model of AAIC with the sector average as of Dec-20



Channel wise GWP performance of AAIC

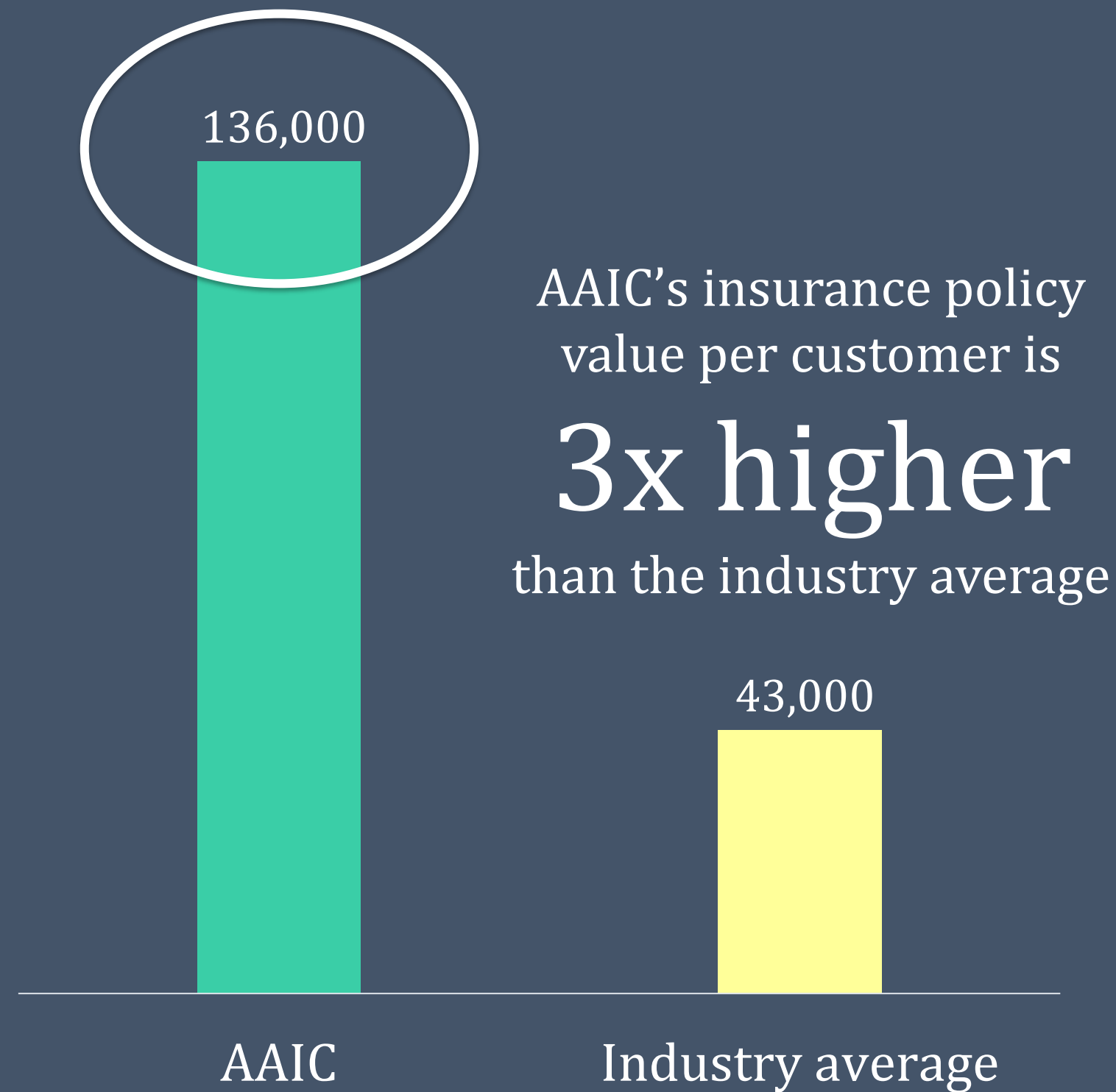


\*Agency – Sells Life insurance to individual customer base

\*Non-agency – Sells Bancassurance/corporate life insurance solutions and Micro and Mobile

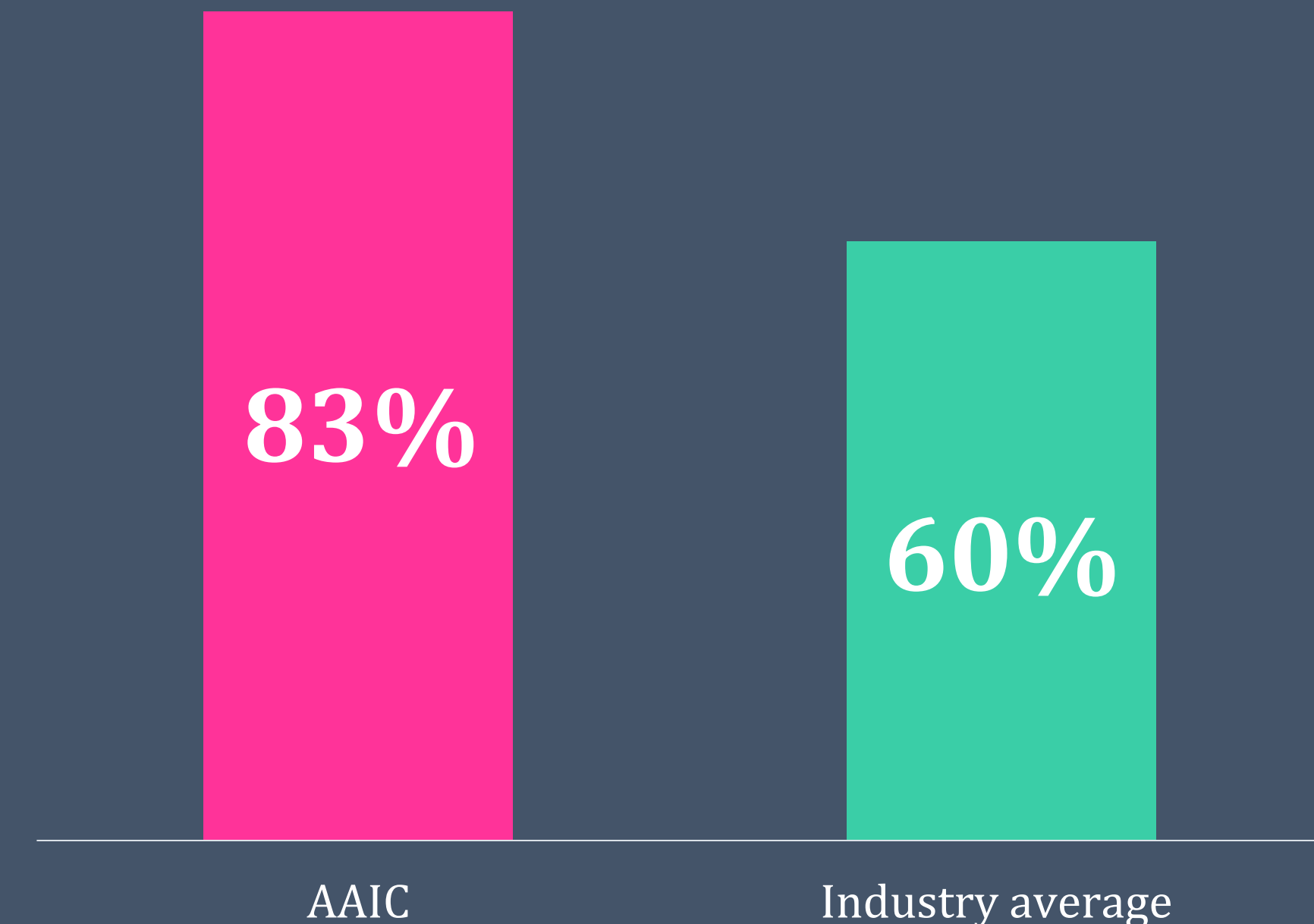
# Innovative product offering results in 1mn+ customer base for AAIC, with higher policy value and superior policy retention rate

Policy value per customer in LKR



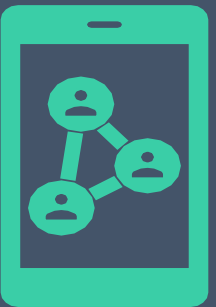
Higher focus of healthcare enabled AAIC to maintain an LKR 136,000 per policy rate cf. industry average of LKR 43,000.

AAIC's 1<sup>st</sup> year customer retention ratio of 83% remains much higher cf. industry average of 60%



Above industry customer retention was mainly driven by increased customer satisfaction due to the settlement of 86% claims within a day and user-friendly digital drive.

# Higher customer retention is due to a user-friendly digital drive, one-day settlements and new initiatives which revolutionized the industry



## 100% digitalized sales platform,

*100% digitalized selling process to improve the speed of processing by eliminating all the delays.*



## Automated claims assessment,

*Machine learning mechanism to automatically verify customer claims enabled AAIC to process claims with high level of accuracy.*



## Cashless claims settlement,

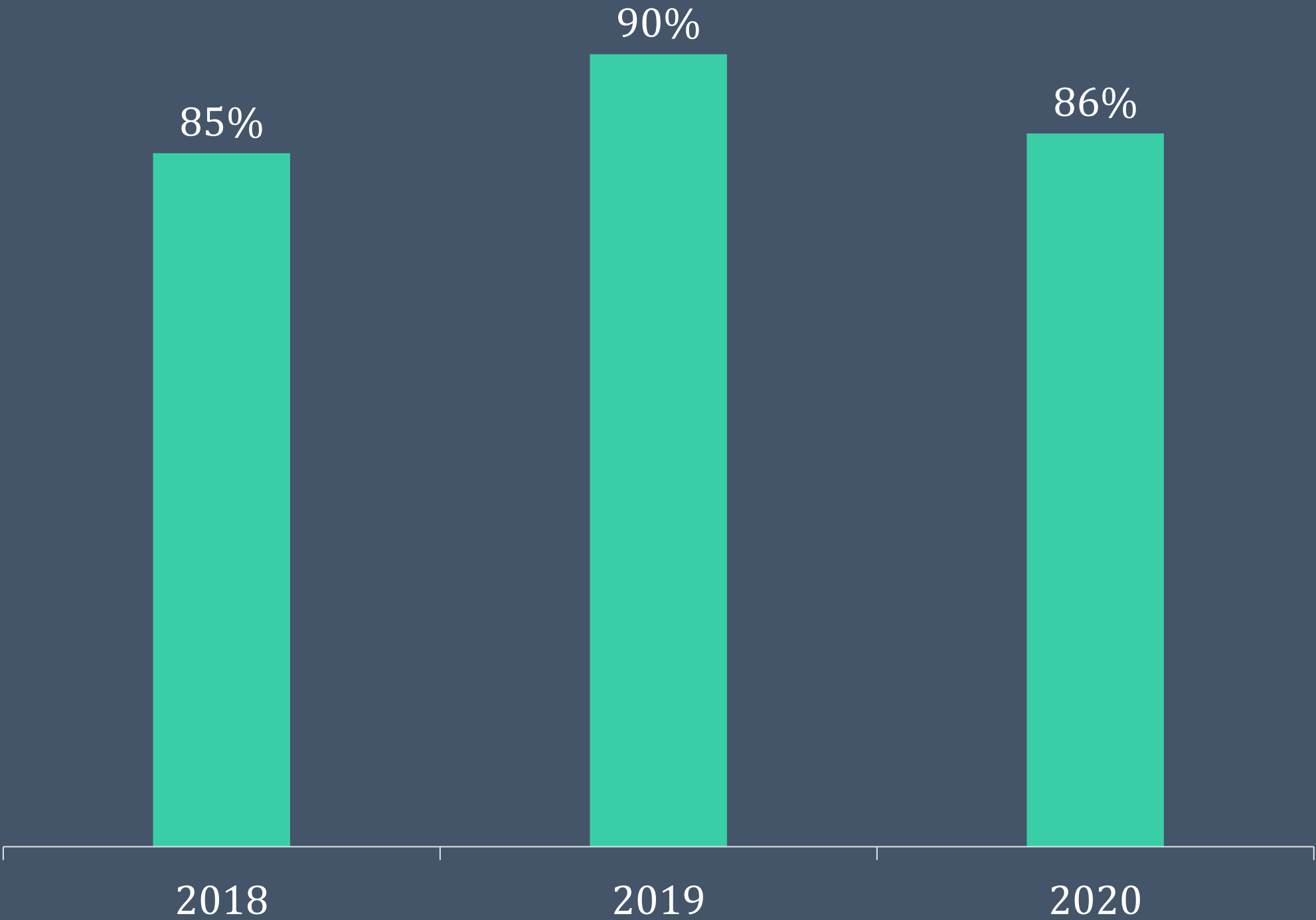
*Pioneered this initiative with ASIRI hospitals, now this process is expanded to 60+ hospitals where AAIC settles the claim directly to the hospital on behalf of customers.*



## Speedy customer discharge,

*A dedicated unit working closely with hospitals to speed up the customer discharge process resulting in higher customer satisfaction level.*

One day claim settle ratio stood above 80% for the last three years for AAIC...

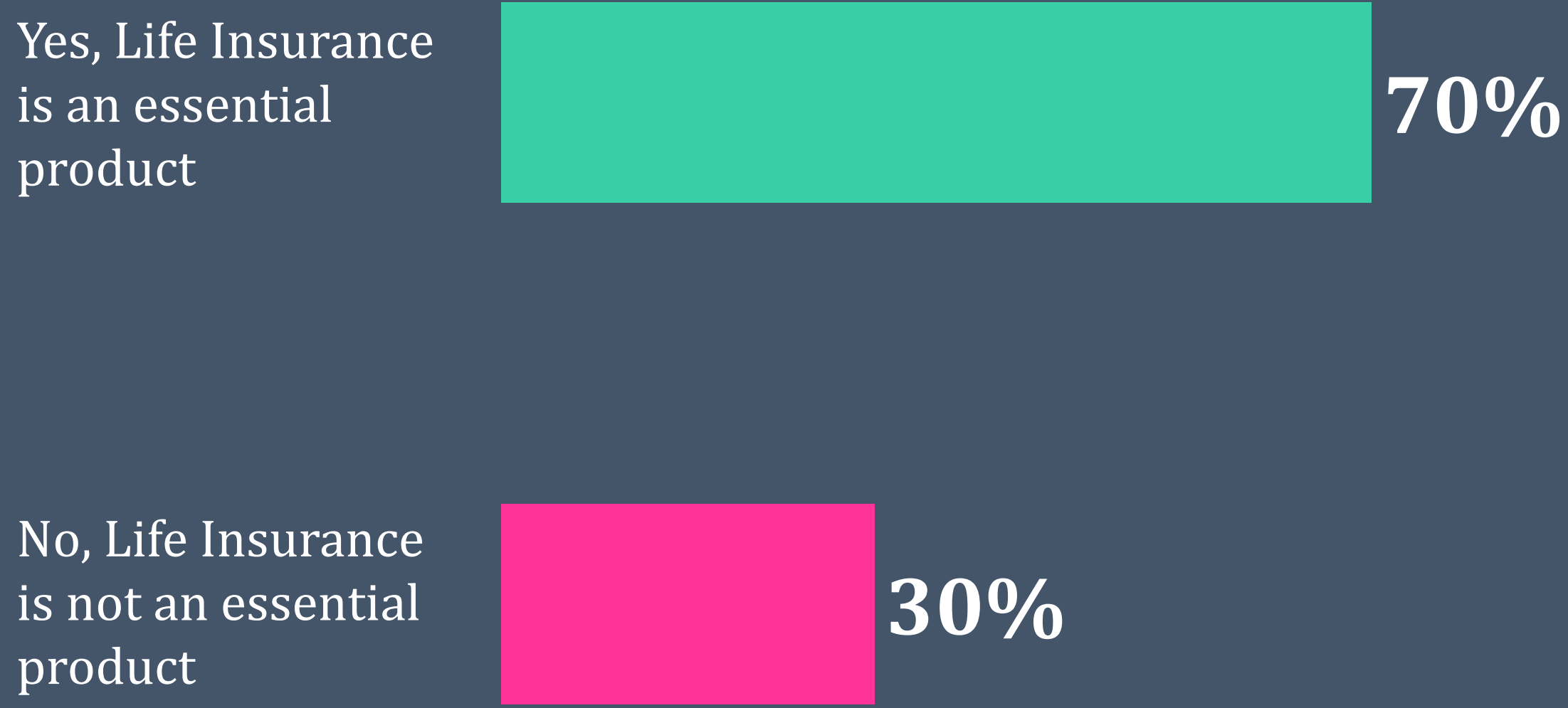


Source: Company data, SSB Research

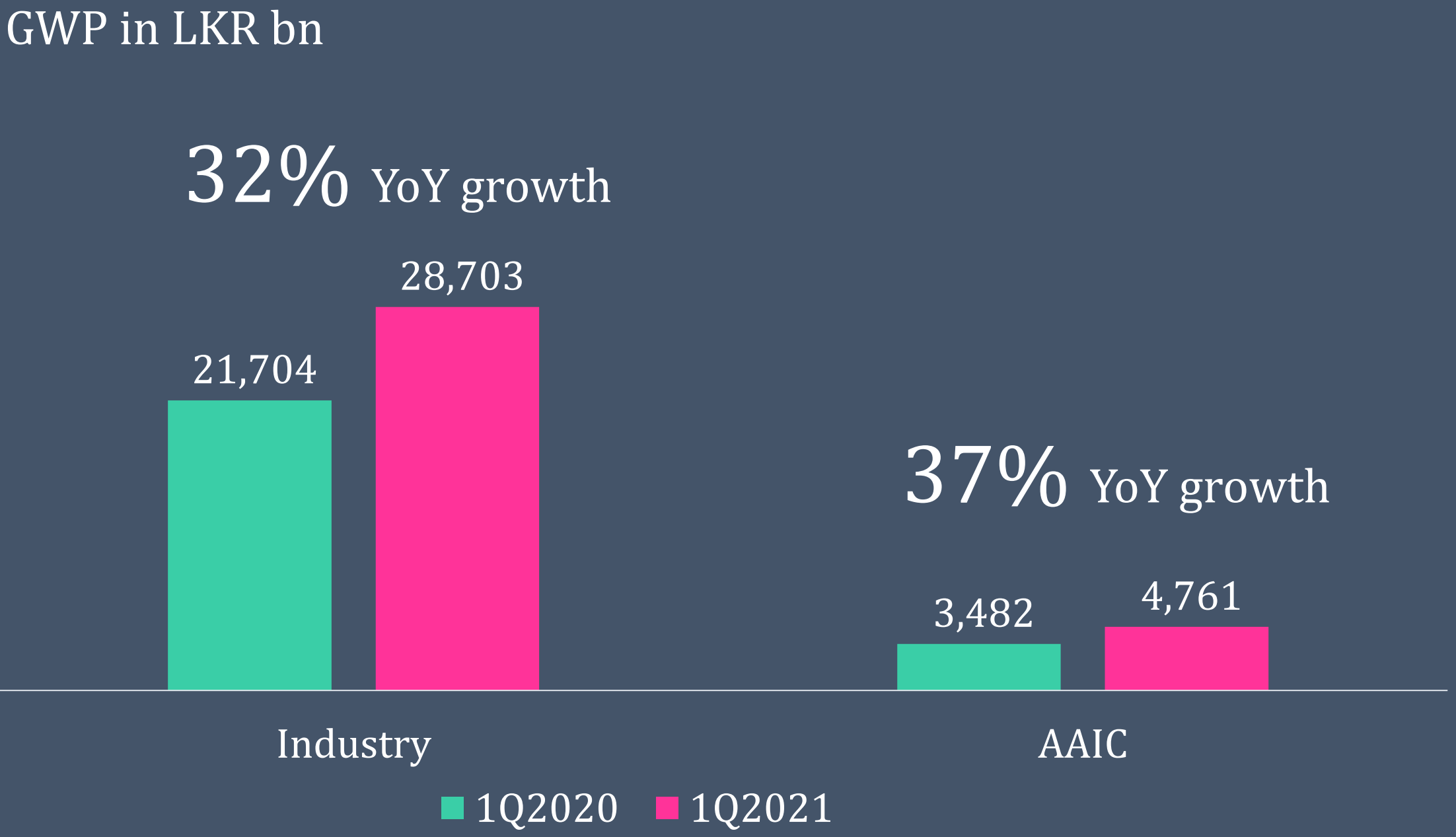


# New premiums observed a sharp uptick as perception about Life Insurance products saw a structural change due to COVID-19

According to a survey conducted by Benori knowledge India, 70% of uninsured respondents feel the need to purchase life insurance products after COVID-19



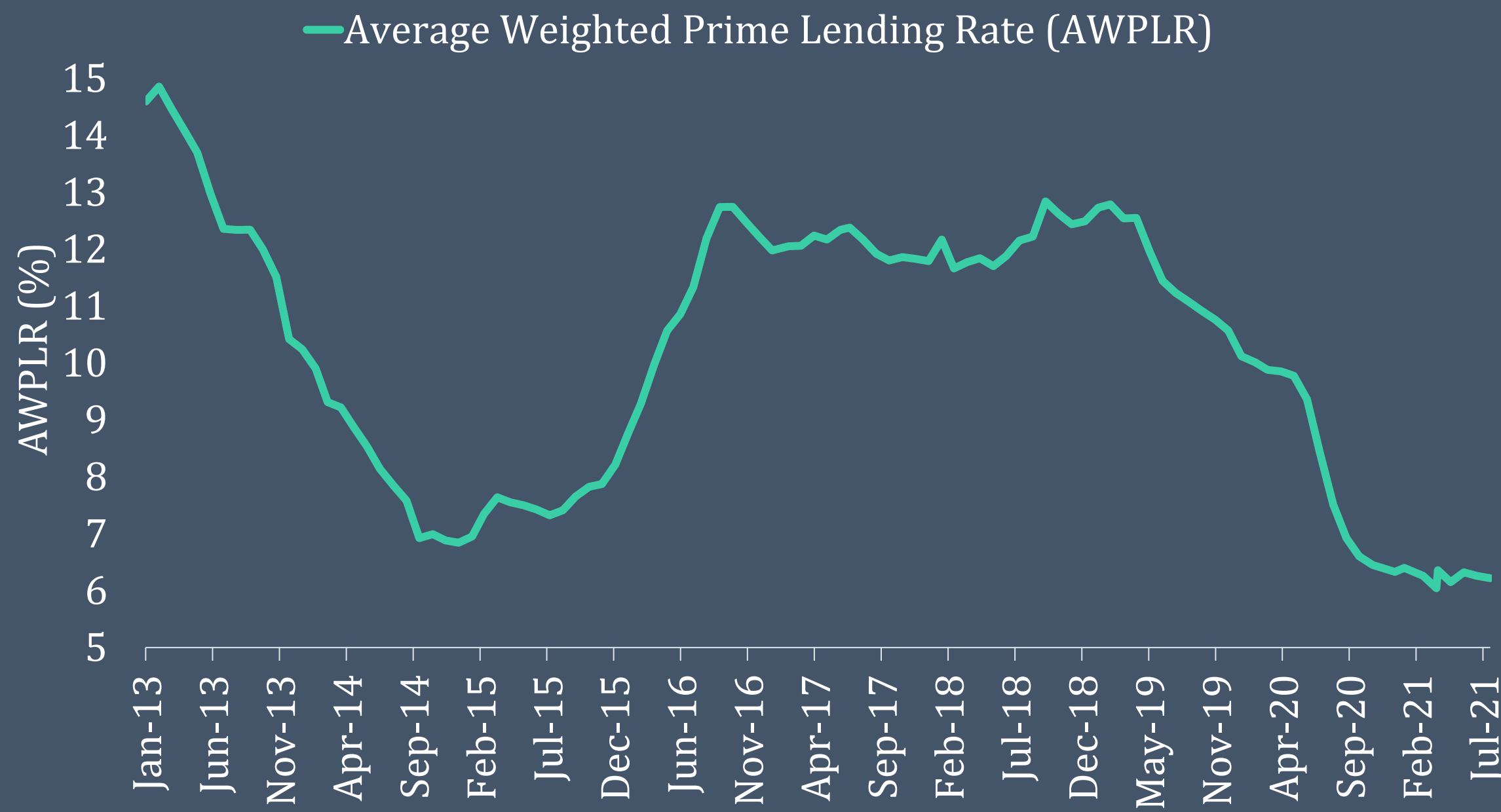
Gross written premium recorded an exponential growth in 1Q2021, Industry and AAIC recorded 32% and 37% YoY growth in GWP respectively



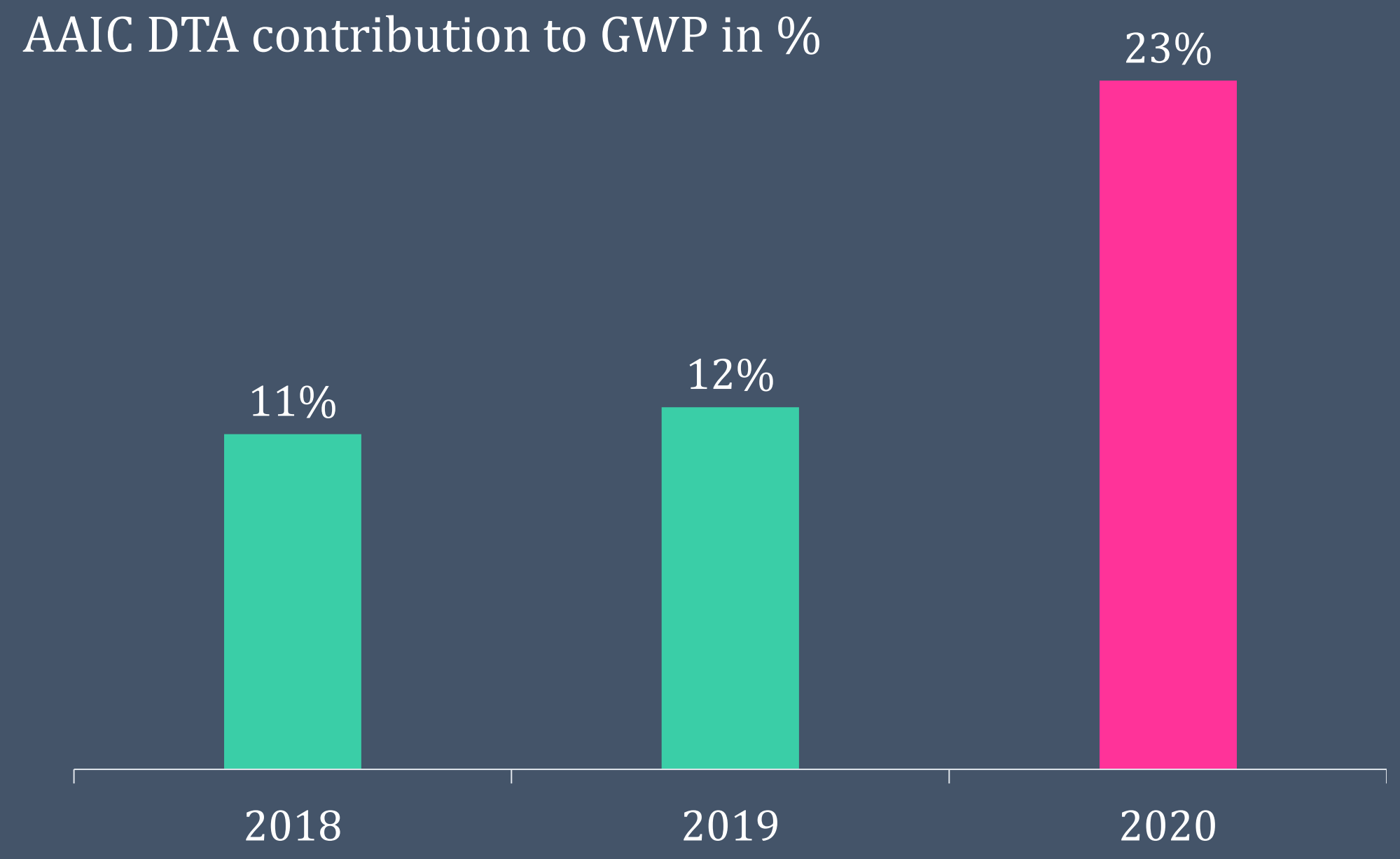
The demand for term plans has gone up in the last few months due to the ongoing pandemic, as people have now become aware of the need to have term insurance. The life insurance industry is witnessing a sharp uptake in single premium policies, as industry GWP expanded to LKR 28.7bn in 1Q2021 cf. LKR 21.7bn in 1Q2020.

# The growth was further fueled by lower interest environment which resulted in exponential growth of DTA products

AWPLR reached a historical low due to CBSL maintaining accommodative monetary policy



Bancassurance of AAIC observed a significant growth in 2020 due to prevailing lower interest environment and COVID-19 uncertainties



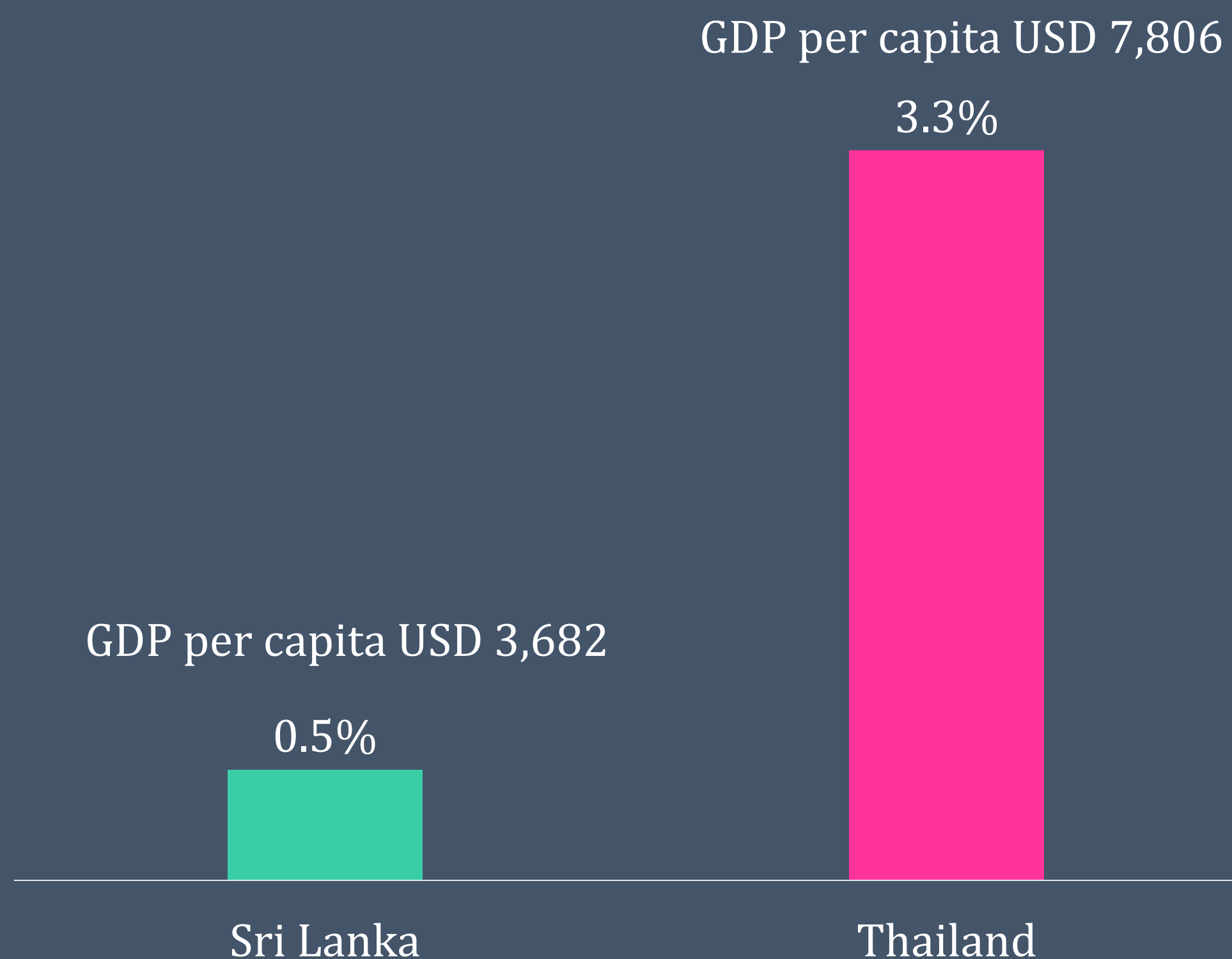
\*DTA – Decreasing Term Assurance is renewable term life insurance with coverage decreasing over the life of the policy at a predetermined rate.

\*Bancassurance - Bancassurance is an arrangement between a bank and an insurance company allowing the insurance company to sell its products to the bank's client base.

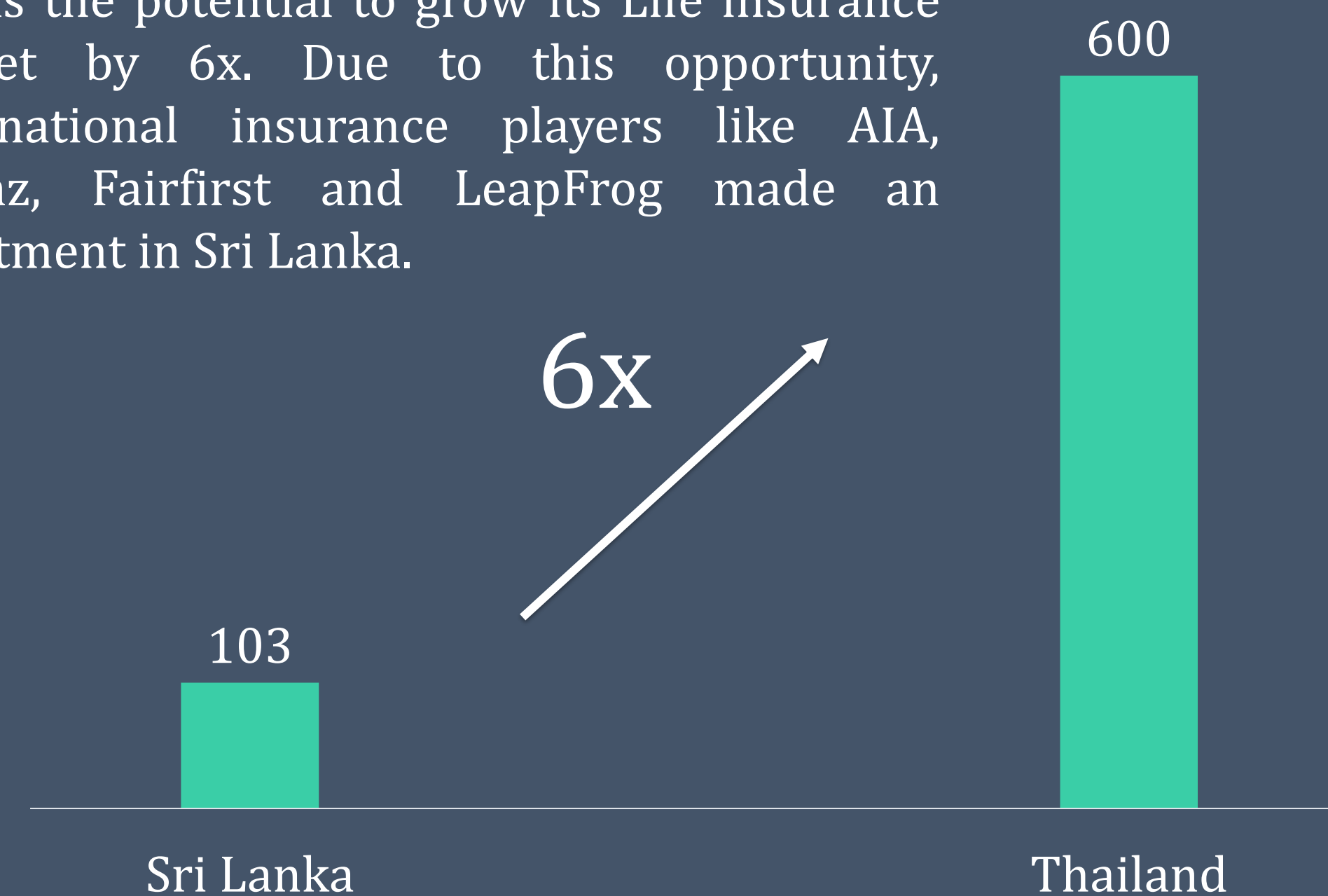
# AAIC's long term growth prospects remain strong amidst SL's lower Life Insurance penetration (0.5% of GDP cf. 3.3% of Thailand)

Life Insurance penetration as a % of GDP

Life Insurance market size in LKR bn



SL has the potential to grow its Life insurance market by 6x. Due to this opportunity, multinational insurance players like AIA, Allianz, Fairfirst and LeapFrog made an investment in Sri Lanka.



Given the lower penetration of Life Insurance sector, we believe country's economic development will give rise to improved household income and wealth levels, enabling a longer-term superior growth profile to reach LKR 600bn market size like Thailand from LKR 103bn.

# Operating under one of Sri Lanka's most diversified business conglomerates: "Softlogic Holdings", provides AAIC an excellent opportunity to build brand awareness amongst group customers



## Healthcare

The leader is Sri Lanka's private healthcare industry, operating over 800 beds in 7 hospitals through the Asiri Health brand.



## Retail

With over +120 international fashion brands the sector further operates many restaurants through a franchisee model whilst also functions the GLOMARK supermarket chain.



## Financial Service

Apart from AAIC, the group holds Softlogic Finance PLC – a licensed finance company and Softlogic Stockbrokers one of the leading stockbroking firms in the country.



## Leisure

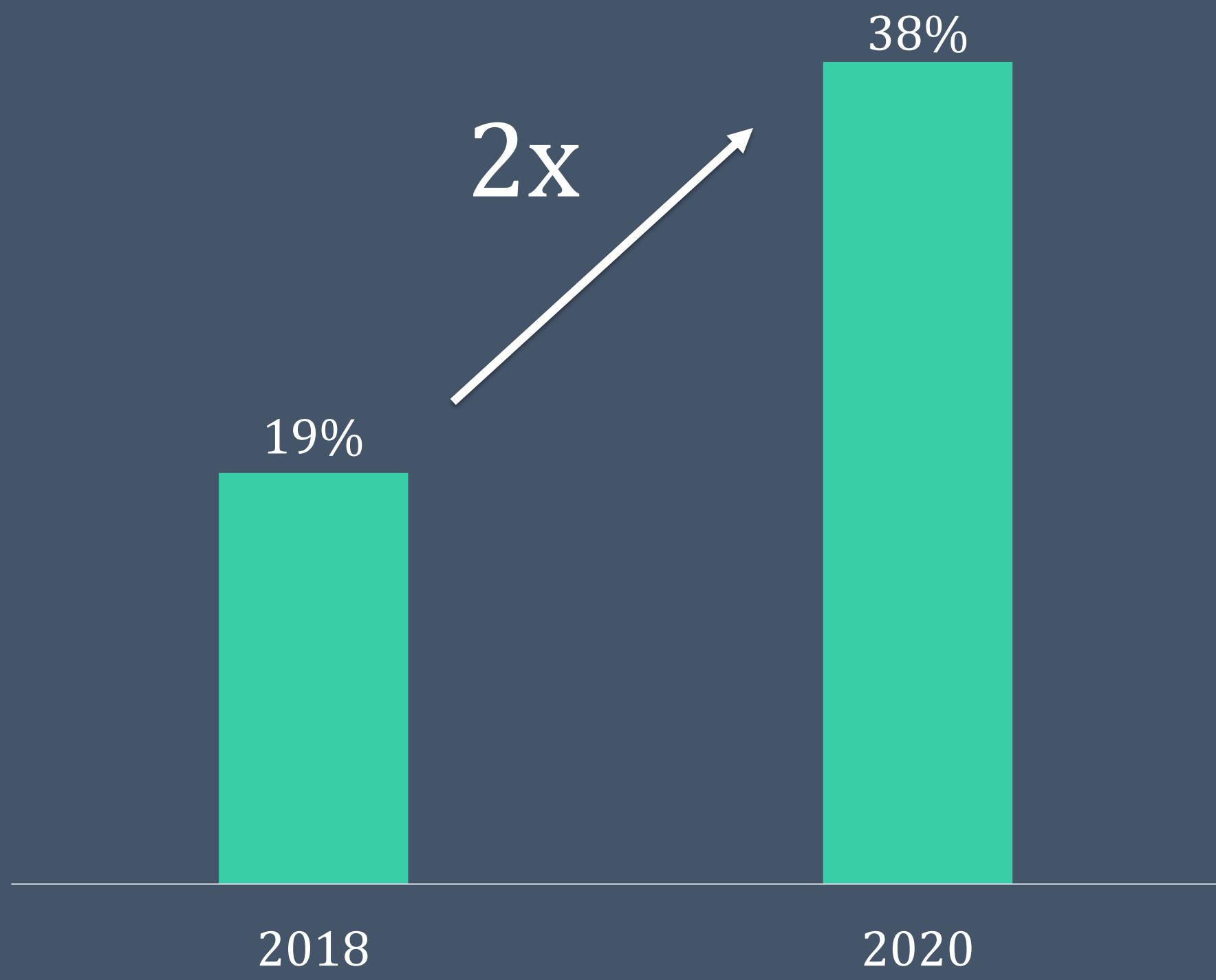
The segment includes 2 hotel properties, Centara Ceysands Resort in Bentota the 5-star city hotel Movenpick, as well as an online ticketing platform and Softlogic Destination Management.

Hence, given the group synergies, it could provide AAIC a chance to build its brand awareness amongst the Softlogic Holdings entire customer base of ~2-2.5 mn.

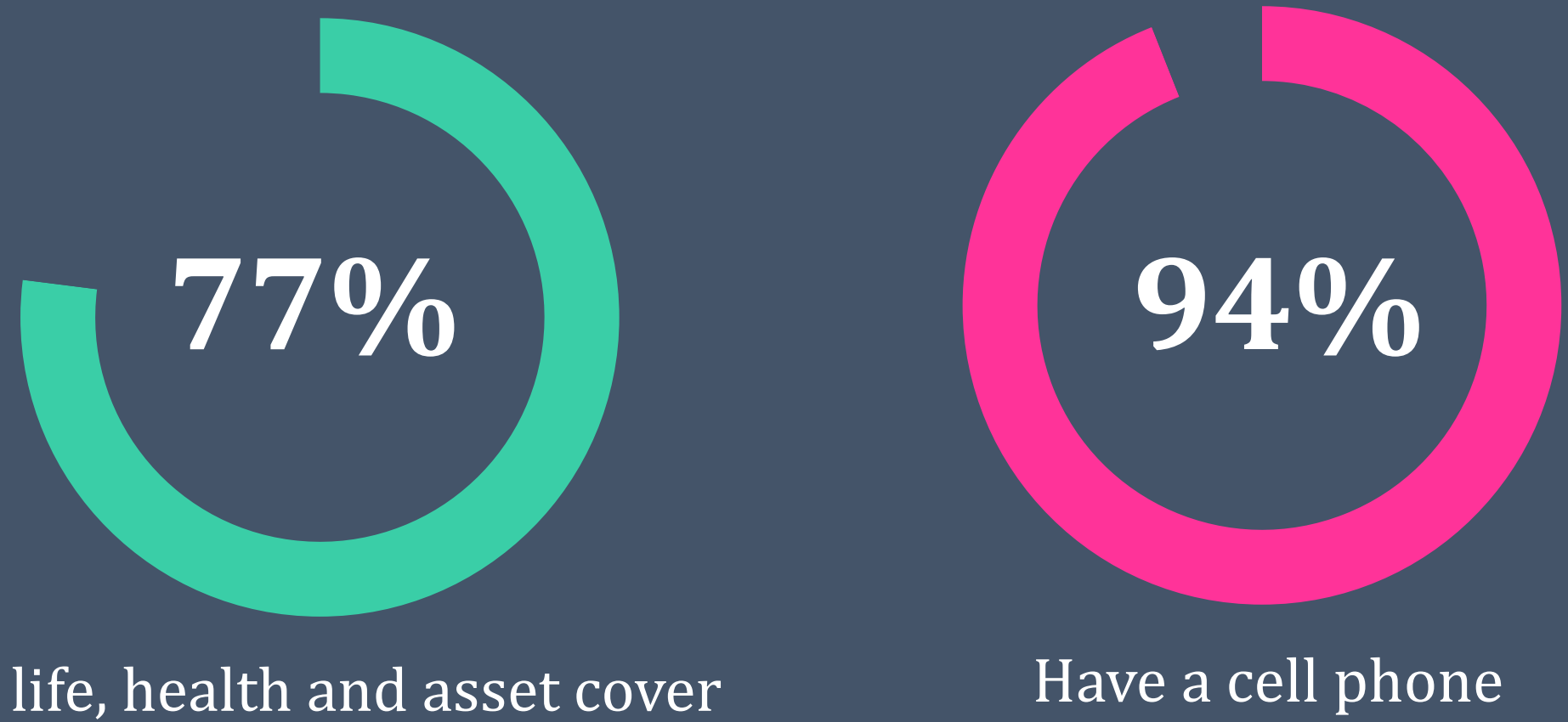


# AAIC being backed by LeapFrog with investments in healthcare and financial services to add micro and insurance exposures

Leapfrog doubled its stake to 38% from 19% in 2018



Northern Arc which secured debt funding from Leapfrog is going after a USD 120mn life insurance market targeting low-income earners



AAIC micro segment which target low-income earners grew from 1% to 3% GWP in 2020. As of 2020 AAIC served 346,000 micro insurance customers.



LeapFrog invests in emerging markets in Asia and Africa, along with the capital injection LeapFrog deploy its group knowledge and experience

Source: Company data, SSB Research

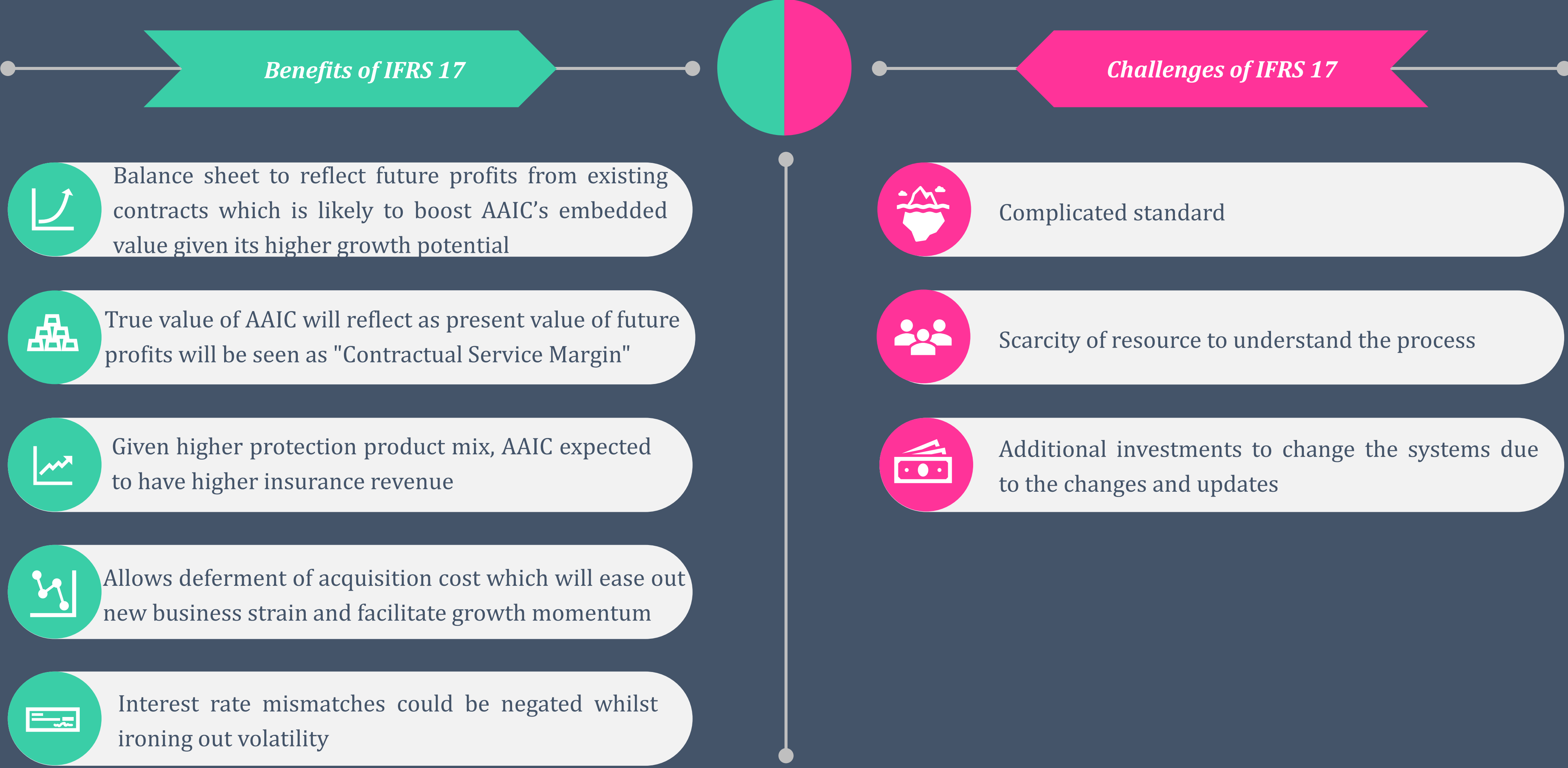


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IFRS 17 to elevate AAIC's value proposition given  
its rapid GWP growth

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# AAIC to retain its competitive edge in GWP growth, backed by IFRS 17 from Jan'23 onwards



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# Valuation

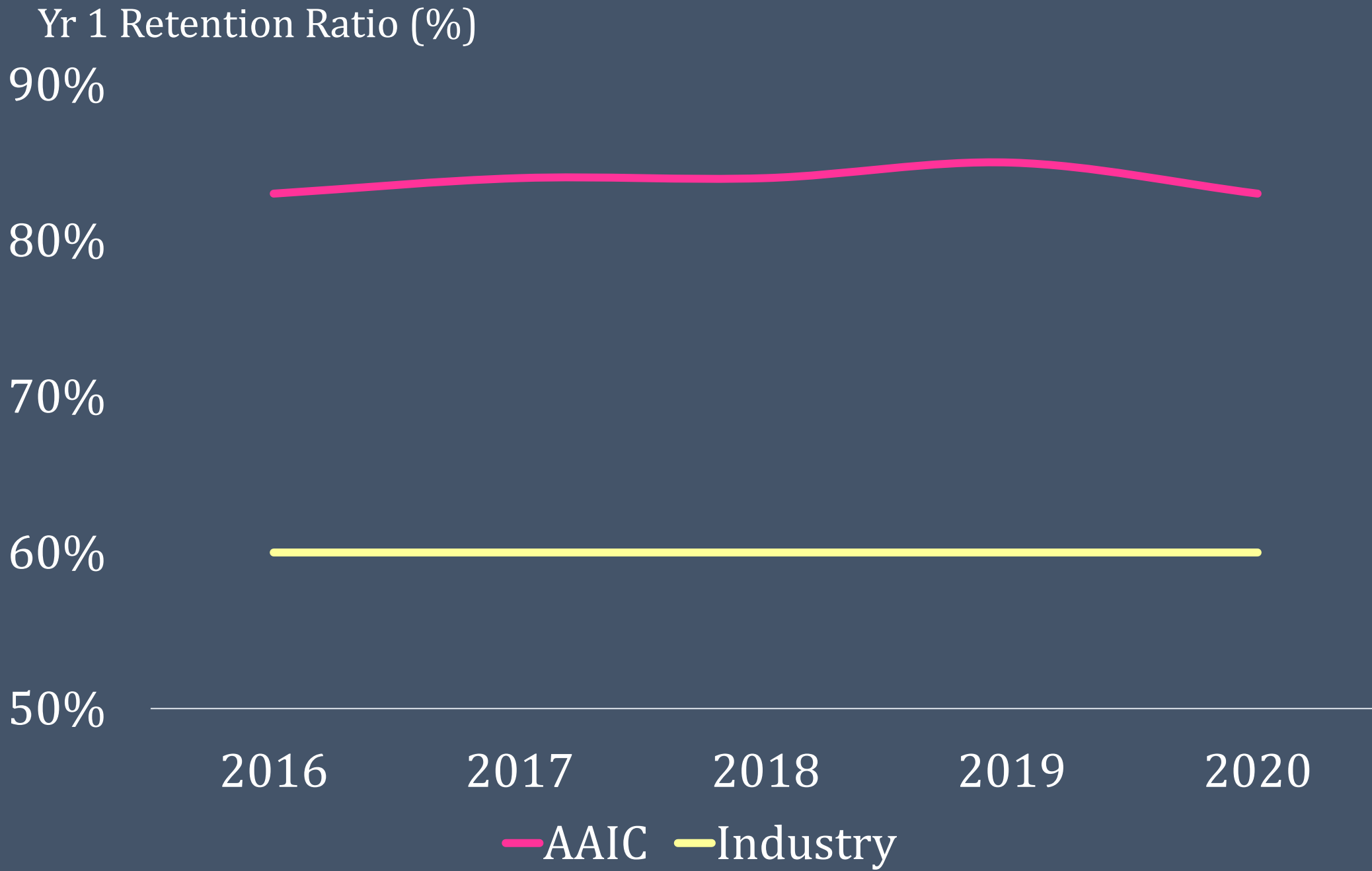
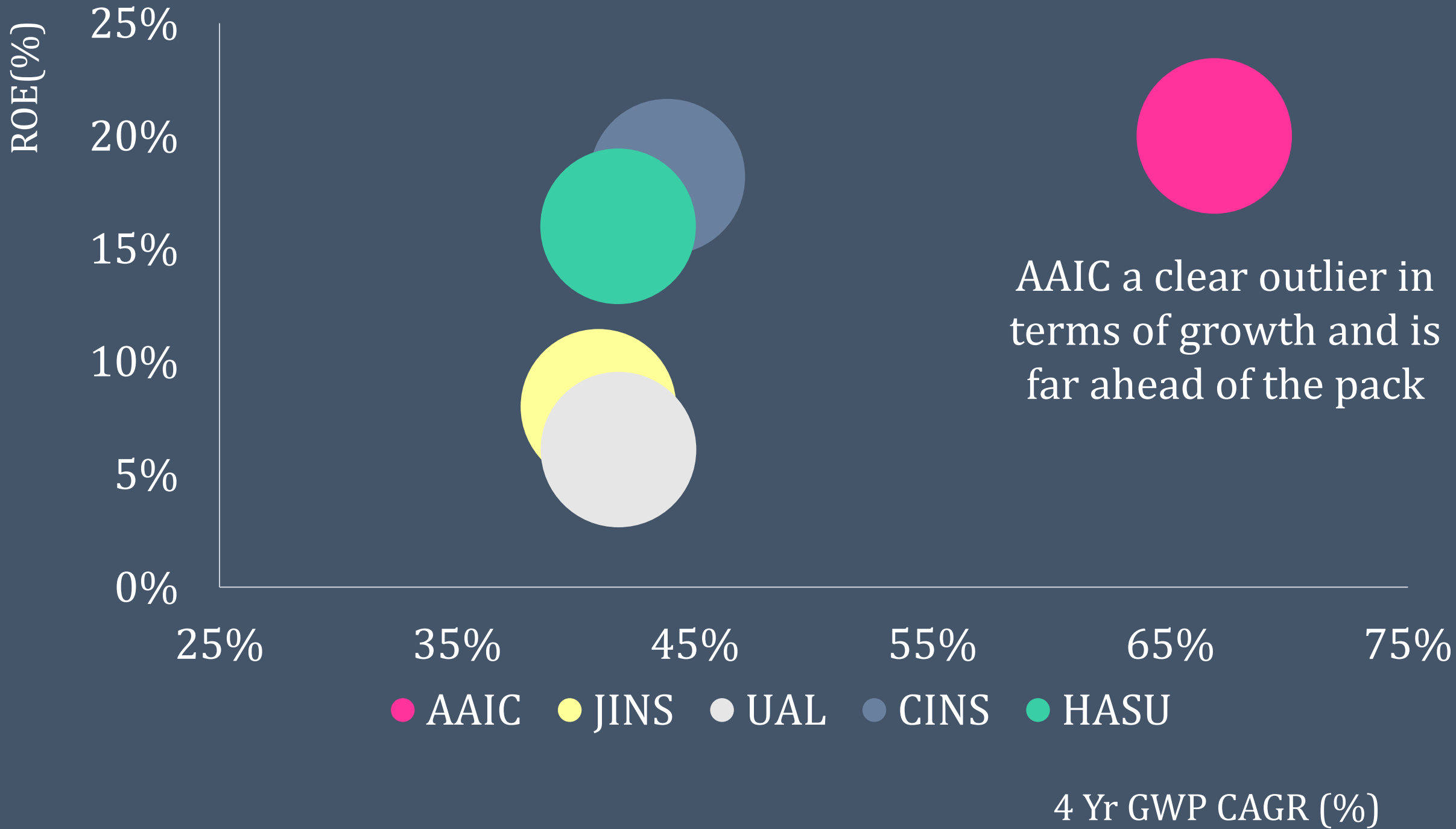
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# Robust Embedded Value growth to warrant a much higher Appraisal Value: The strong +65% GWP growth CAGR of AAIC amidst a stable retention assures a much higher Appraisal value

Above industry GWP growth and ROE indicates higher embedded value for AAIC...

...Whilst higher retention ratio cf. industry average warrants future growth potential of AAIC

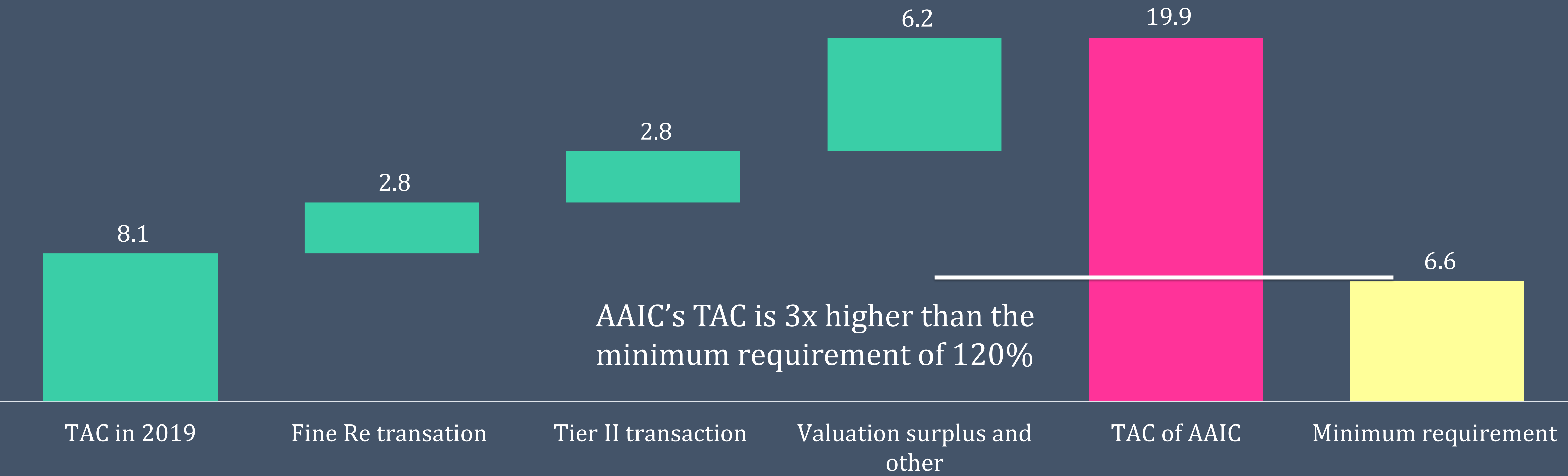


\*Note – Assuming the product mix remains unchanged  
 \*ROE is as of year end 2020  
 \*GWP CAGR is calculated from 2017 to 2020

Source: Company data, SSB Research

# Strong capital position: AAIC's capital adequacy continued its strong stance, with >LKR 13.3bn in excess capital above the minimum 120% solvency level

Total Available Capital (TAC) growth from 2019 to 2020 in LKR bn

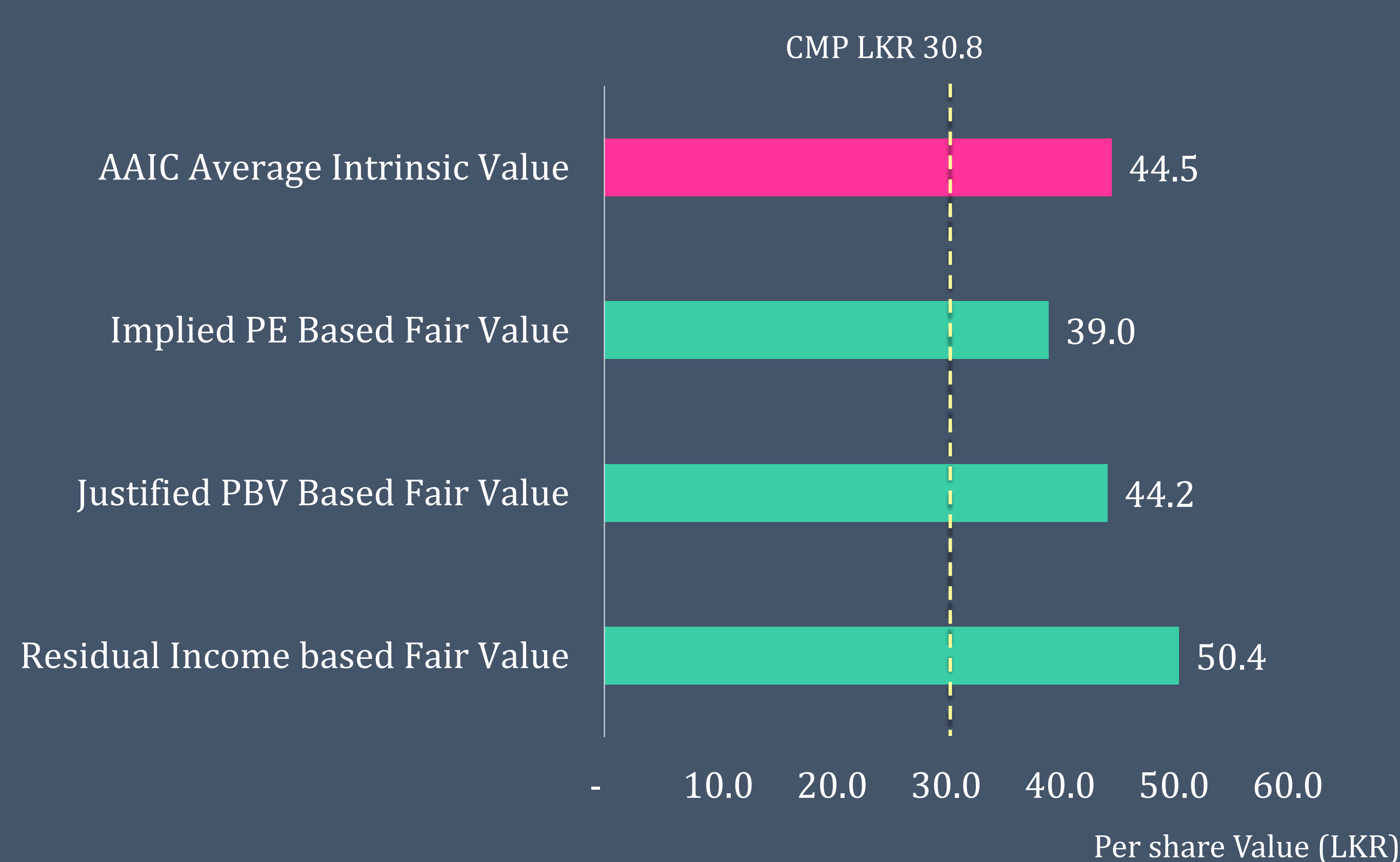


AAIC's final dividend represents a dividend payout ratio of around 60% for the full year. AAIC stated that its aim was to pay sustainable and progressive dividends. With its very strong excess capital position LKR 13.3bn above minimum requirement, AAIC is in a strong position to undertake capital management and maintain a dividend payout ratio of 50 %.

Source: Company data, SSB Research

AAIC derives a total return of ~53% to its intrinsic value which clearly defines the growth potential along with the expected uptick in industry penetration

### Fair Value based on different valuation techniques



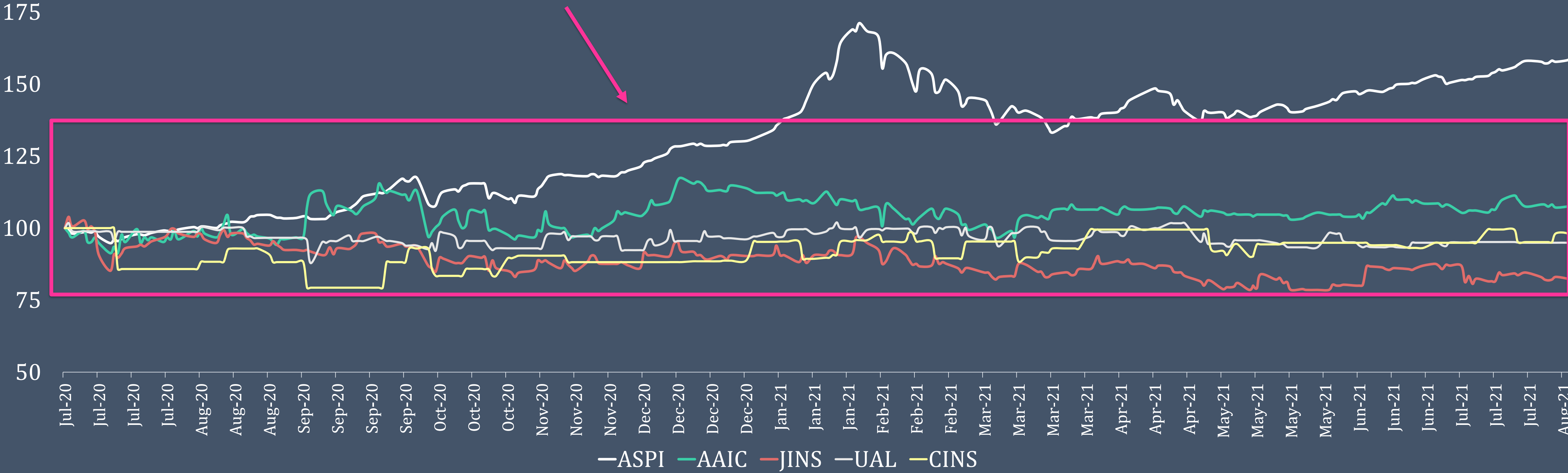
|                                      |               |
|--------------------------------------|---------------|
| Terminal ROE                         | 22.0%         |
| Terminal growth                      | 2.0%          |
| Cost of equity                       | 14.0%         |
| Risk free rate                       | 7.5%          |
| Market return                        | 5.0%          |
| Beta                                 | 1.30          |
| Implied PER                          | 8.5x          |
| Justified PBV                        | 1.67x         |
| <b>Average Intrinsic Value (LKR)</b> | <b>44.5</b>   |
| Capital Appreciation                 | +44.4%        |
| Forward Dividend Yield               | 9.0%          |
| <b>Total return</b>                  | <b>+53.4%</b> |

# The life sector appears to have decoupled from the broader equity market in 2021, despite a 32% YoY growth in 1Q GWP

ASPI price movement vs. Life Insurance individual share price movement

Index movement

Insurance sector share prices remained relatively flat in 2021 compared to ASPI movement

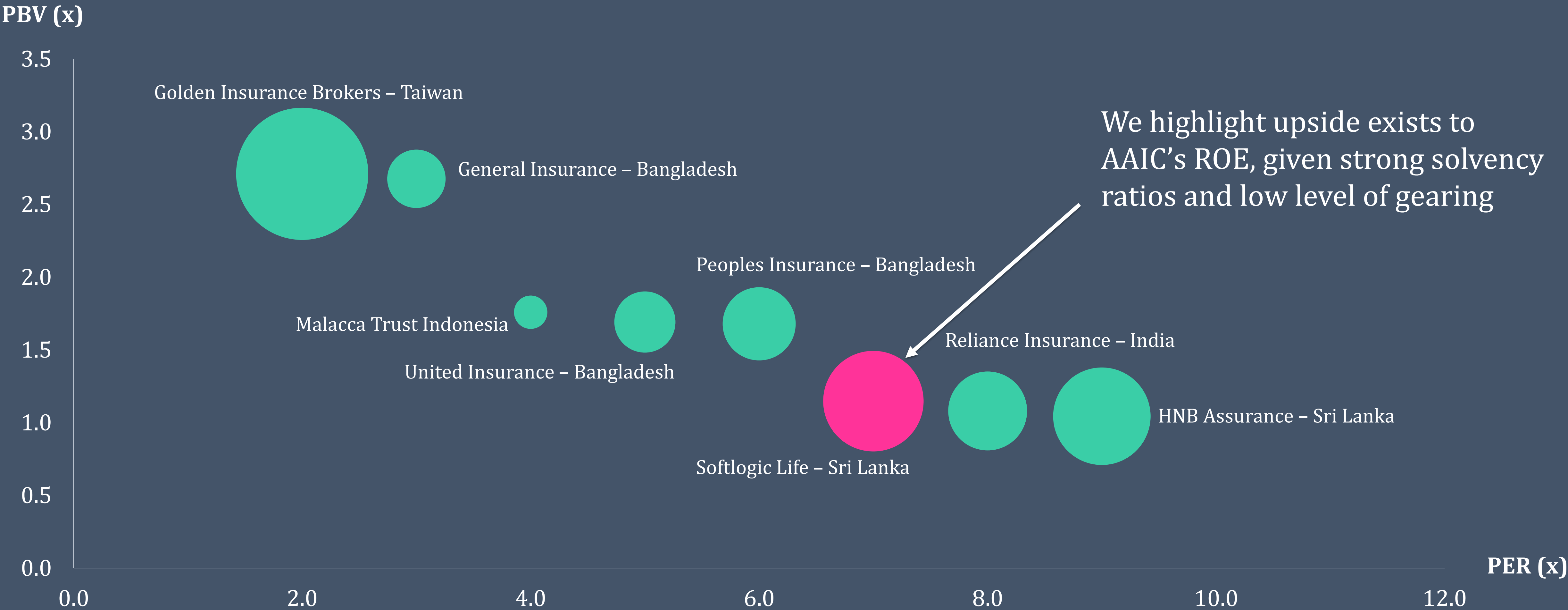




# However, we note that AAIC is trading at lower-end of historic ranges cf. global players, which warrants an upside

PBV vs. ROE industry

\*Bubble size represents ROE



Source: Company data, Bloomberg, SSB Research

# Sensitivity analysis carried out on AAIC's fair values using different valuation techniques further justifies the capital appreciation

Justified PBV based Fair Value gives a capital appreciation of +43%

|                   |       | ROE   |       |       |       |       |
|-------------------|-------|-------|-------|-------|-------|-------|
|                   |       | 20.0% | 21.0% | 22.0% | 23.0% | 24.0% |
| Terminal Growth % | 44.16 |       |       |       |       |       |
|                   | 1.0%  | 38.73 | 40.76 | 42.80 | 44.84 | 46.88 |
|                   | 1.5%  | 39.22 | 41.33 | 43.45 | 45.57 | 47.69 |
|                   | 2.0%  | 39.74 | 41.95 | 44.16 | 46.37 | 48.58 |
|                   | 2.5%  | 40.32 | 42.63 | 44.93 | 47.23 | 49.54 |
|                   | 3.0%  | 40.95 | 43.36 | 45.77 | 48.18 | 50.58 |

Based on a justified PBV multiple of 1.7x using an average ROE of 22% and a terminal growth of 2%, AAIC generates a fair value of LKR 44.2

Residual Income based Fair Value depicts a price upside of +63%

|                   |       | Cost of Equity |       |       |       |       |
|-------------------|-------|----------------|-------|-------|-------|-------|
|                   |       | 12.0%          | 13.0% | 14.0% | 15.0% | 16.0% |
| Terminal Growth % | 50.43 |                |       |       |       |       |
|                   | 1.0%  | 61.84          | 54.92 | 49.13 | 44.22 | 40.01 |
|                   | 1.5%  | 63.04          | 55.79 | 49.76 | 44.67 | 40.33 |
|                   | 2.0%  | 64.36          | 56.74 | 50.43 | 45.15 | 40.67 |
|                   | 2.5%  | 65.83          | 57.77 | 51.17 | 45.68 | 41.04 |
|                   | 3.0%  | 67.45          | 58.91 | 51.98 | 46.25 | 41.44 |

AAIC further derives a fair value of LKR 50.4 using the Residual income whilst using a terminal growth of ~2% along with a cost of equity of 14%

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# Annexures

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# Mini Model

| YE Dec/(LKR Mn)                   | 2015         | 2016         | 2017         | 2018          | 2019          | 2020          | 2021E         | 2022E         |
|-----------------------------------|--------------|--------------|--------------|---------------|---------------|---------------|---------------|---------------|
| <b>Net Profit</b>                 | <b>924</b>   | <b>967</b>   | <b>2,325</b> | <b>3,336</b>  | <b>2,173</b>  | <b>1,521</b>  | <b>1,720</b>  | <b>2,069</b>  |
| <i>YoY Growth (%)</i>             | 22.4%        | 4.6%         | 140.4%       | 43.5%         | -34.9%        | -30.0%        | 13.1%         | 20.3%         |
| <b>GWP</b>                        | <b>4,091</b> | <b>5,636</b> | <b>7,531</b> | <b>10,006</b> | <b>12,531</b> | <b>15,660</b> | <b>18,009</b> | <b>21,611</b> |
| <i>YoY Growth (%)</i>             | -14.3%       | 37.8%        | 33.6%        | 32.9%         | 25.2%         | 25.0%         | 15.0%         | 20.0%         |
| <b>Profit before tax</b>          | <b>993</b>   | <b>877</b>   | <b>1,905</b> | <b>1,095</b>  | <b>2,604</b>  | <b>2,130</b>  | <b>2,409</b>  | <b>2,897</b>  |
| <i>YoY Growth (%)</i>             | 29.2%        | -11.6%       | 117.1%       | -42.5%        | 137.8%        | -18.2%        | 13.1%         | 20.3%         |
| EPS (LKR)                         | 2.5          | 2.6          | 6.2          | 8.9           | 5.8           | 4.1           | 4.6           | 5.5           |
| DPS (LKR)                         | -            | 2.7          | -            | 1.5           | -             | 2.5           | 2.3           | 2.8           |
| BVPS (LKR)                        | 4.9          | 5.2          | 10.4         | 17.8          | 21.9          | 26.5          | 29.4          | 33.0          |
| <b><u>Ratios (%)</u></b>          |              |              |              |               |               |               |               |               |
| Claims Ratio                      | 11%          | 21%          | 19%          | 25%           | 25%           | 26%           | 26%           | 26%           |
| Expense Ratio                     | 58%          | 69%          | 62%          | 57%           | 55%           | 49%           | 58%           | 58%           |
| Dividend Payout                   | 0%           | 104%         | 0%           | 16%           | 0%            | 62%           | 50%           | 50%           |
| ROE (%) ( adjusted)               | 47%          | 46%          | 48%          | 31%           | 34%           | 20%           | 20%           | 20%           |
| <b><u>Investor Ratios (%)</u></b> |              |              |              |               |               |               |               |               |
| PE (x)                            | 12.5         | 11.9         | 5.0          | 3.5           | 5.3           | 7.6           | 6.7           | 5.6           |
| PBV (x)                           | 6.3          | 5.9          | 3.0          | 1.7           | 1.4           | 1.2           | 1.0           | 0.9           |
| Div Yield (%)                     | 0.0%         | 8.7%         | 0.0%         | 4.7%          | 0.0%          | 8.1%          | 7.4%          | 9.0%          |



# Income Statement

| FY Dec/ LKR Mn   | 2015           | 2016           | 2017           | 2018           | 2019            | 2020            | 2021E           | 2022E           |
|--|----------------|----------------|----------------|----------------|-----------------|-----------------|-----------------|-----------------|
| <b>Income Statement (LKR Mn)</b>                         |                |                |                |                |                 |                 |                 |                 |
| <b>Gross Written Premium</b>                             | <b>4,091</b>   | <b>5,636</b>   | <b>7,531</b>   | <b>10,006</b>  | <b>12,531</b>   | <b>15,660</b>   | <b>18,009</b>   | <b>21,611</b>   |
| Net Earned Premium                                       | 3,590          | 5,003          | 6,728          | 9,279          | 11,540          | 13,788          | 15,856          | 19,027          |
| Other Revenue  | 621            | 700            | 875            | 954            | 1,219           | 1,634           | 2,107           | 2,732           |
| <b>Total Net Income</b>                                  | <b>4,457</b>   | <b>5,666</b>   | <b>7,798</b>   | <b>10,233</b>  | <b>13,124</b>   | <b>16,064</b>   | <b>18,605</b>   | <b>22,400</b>   |
| Insurance Claims and Benefits                            | (411)          | (1,073)        | (1,245)        | (2,299)        | (2,886)         | (3,546)         | (4,078)         | (4,893)         |
| Change in contract liabilities life fund                 | (966)          | (288)          | (1,315)        | (1,501)        | (1,170)         | (3,600)         | (2,881)         | (3,458)         |
| Underwriting & Net Acquisition Costs                     | (993)          | (1,580)        | (1,831)        | (2,044)        | (2,969)         | (3,269)         | (3,760)         | (4,512)         |
| Other Operating and Administrative Expenses              | (1,047)        | (1,781)        | (2,299)        | (3,187)        | (3,268)         | (3,325)         | (5,295)         | (6,483)         |
| <b>Total Benefits, Claims &amp; Net Acquisition Cost</b> | <b>(3,465)</b> | <b>(4,789)</b> | <b>(5,893)</b> | <b>(9,138)</b> | <b>(10,520)</b> | <b>(13,933)</b> | <b>(16,196)</b> | <b>(19,504)</b> |
| Profit Before Taxation                                   | 993            | 877            | 1,905          | 1,095          | 2,604           | 2,130           | 2,409           | 2,897           |
| <b>Profit After Taxation</b>                             | <b>924</b>     | <b>967</b>     | <b>2,325</b>   | <b>3,336</b>   | <b>2,173</b>    | <b>1,521</b>    | <b>1,720</b>    | <b>2,069</b>    |

# Balance Sheet

| Balance Sheet (LKR Mn)                            | 2015          | 2016         | 2017          | 2018          | 2019          | 2020          | 2021E         | 2022E         |
|---|---------------|--------------|---------------|---------------|---------------|---------------|---------------|---------------|
| <b>Assets</b>                                     |               |              |               |               |               |               |               |               |
| Financial Assets                                  | 9,265         | 8,218        | 9,994         | 12,065        | 14,911        | 27,368        | 30,105        | 36,125        |
| Property, Plant and Equipment                     | 519           | 485          | 578           | 619           | 675           | 661           | 823           | 755           |
| Reinsurance Receivables                           | 122           | 86           | 150           | 155           | 188           | 323           | 372           | 446           |
| Premium Receivable                                | 551           | 92           | 291           | 507           | 744           | 856           | 985           | 1,182         |
| Other Assets                                      | 434           | 632          | 579           | 691           | 924           | 834           | 960           | 1,151         |
| Deferred Tax Assets                               | 62            | 0            | 420           | 2,751         | 2,231         | 1,622         | 1,622         | 811           |
| Cash in Hand and Balance at Bank                  | 224           | 233          | 319           | 381           | 377           | 554           | 573           | 292           |
| <b>Total Assets</b>                               | <b>11,472</b> | <b>9,918</b> | <b>12,478</b> | <b>17,333</b> | <b>20,683</b> | <b>33,206</b> | <b>36,289</b> | <b>41,377</b> |
| <b>Shareholders' Equity</b>                       |               |              |               |               |               |               |               |               |
| Stated Capital                                    | 1,063         | 1,063        | 1,063         | 1,063         | 1,063         | 1,063         | 1,063         | 1,063         |
| Available for sale reserve                        | (640)         | (1,349)      | (965)         | (1,513)       | -             | -             | -             | -             |
| Retained reserves                                 | 1,400         | 2,223        | 2,942         | 6,275         | 7,764         | 9,290         | 10,150        | 11,185        |
| <b>Total Shareholders' Equity</b>                 | <b>1,847</b>  | <b>1,962</b> | <b>3,886</b>  | <b>6,671</b>  | <b>8,219</b>  | <b>9,936</b>  | <b>11,039</b> | <b>12,365</b> |
| <b>Liabilities</b>                                |               |              |               |               |               |               |               |               |
| Insurance Provision - Life                        | 6,569         | 6,935        | 7,439         | 9,022         | 10,377        | 17,484        | 18,984        | 21,984        |
| Interest Bearing Borrowings                       | 1,003         | 131          | 77            | 370           | -             | 2,852         | 2,567         | 2,156         |
| Reinsurance creditors                             | 140           | 139          | 236           | 321           | 429           | 636           | 890           | 1,247         |
| Other liabilities                                 | 497           | 649          | 749           | 838           | 1,331         | 1,890         | 2,363         | 2,953         |
| <b>Total Liabilities</b>                          | <b>9,625</b>  | <b>7,955</b> | <b>8,592</b>  | <b>10,662</b> | <b>12,464</b> | <b>23,270</b> | <b>25,250</b> | <b>29,012</b> |
| <b>Total Liabilities and Shareholders' Equity</b> | <b>11,472</b> | <b>9,918</b> | <b>12,478</b> | <b>17,333</b> | <b>20,683</b> | <b>33,206</b> | <b>36,289</b> | <b>41,377</b> |

Source: Company data, SSB Research

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