IIFL Securities

Banking on life, protecting future

IIFL Securities

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Dynamics of Indian life insurance

ICICI Prudential Life – BUY		
CMP	Target	Upside
316	395	25%

SBI Life Insurance – BUY		
CMP	Target	Upside
599	712	19%

HDFC Standard Life – BUY		
CMP	Target	Upside
391	458	17%

Prices as on 03/01/2019

Financials (₹cr)

ICICI Prudential	FY19E	FY20E
Total Premium	31,580	36,847
VNB Margin (%)	17.9	19.0
Op. RoEV (%)	18.3	18.9
P/EV (x)	2.1	1.8

SBI Life	FY19E	FY20E
Total Premium	32,509	40,282
VNB Margin (%)	18.8	19.7
Op. RoEV (%)	17.5	18.1
P/EV (x)	2.6	2.2

HDFC Life	FY19E	FY20E
Total Premium	28,831	34,678
VNB Margin (%)	23.9	24.7
Op. RoEV (%)	20.2	21.2
P/EV (x)	4.4	3.7

Source: IIFL Research

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The Indian life insurance industry has progressed rapidly by capturing significant opportunities arising from favorable demographic profile. Increased workforce participation (~40% - 2011 census) coupled with higher financial savings is leading to the surge in demand for insurance products. Private life insurers are witnessing improvement in persistency since FY15 with focus towards protection products (more structural) vs. traditional saving / investment offerings (cyclical). We expect banking-led insurance players to gain market share over the medium term considering stable regulatory regime and strong distribution framework.

Protection coverage backed by favorable demographics

Inadequacy of pure protection coverage in India (~$8,560bn protection gap in 2015), as compared to other emerging and developed markets, provides an excellent opportunity to capture new business under this segment. Thus, the next leg of growth is explicitly big for protection products with private players focusing on these owing to their high margin nature.

Banca channel, digital foray to expand market share

Bancassurance dominates the channel mix for the top three private sector insurers (cumulative market share increased from 43.6% in FY14 to 53% in FY18) by virtue of having a strong bank as their distribution partner. Additionally, insurance companies tend to benefit as banca provides cost advantage vis-à-vis other channels. Further, we see higher traction for banca players under digital platform for sourcing new business owing to the brand recognition of their respective banks.

Outlook & valuation

Banking-led insurance players, in our view, have a substantial medium to long-term outlook and are trading at attractive valuations, which offers a favorable entry point for investors. We recommend (1) **ICICI Prudential Life Insurance (IPru Life; FY20E P/EV target multiple of 2.3x)** owing to improvement in product mix; persistency to drive VNB margin coupled with robust digital platform; (2) **SBI Life Insurance (SBI Life; 2.6x)** due to operating cost leadership in the industry; and (3) **HDFC Standard Life Insurance (HDFC Life; 4.3x)**, owing to best-in-class VNB margin.

Scenario of life insurance in India

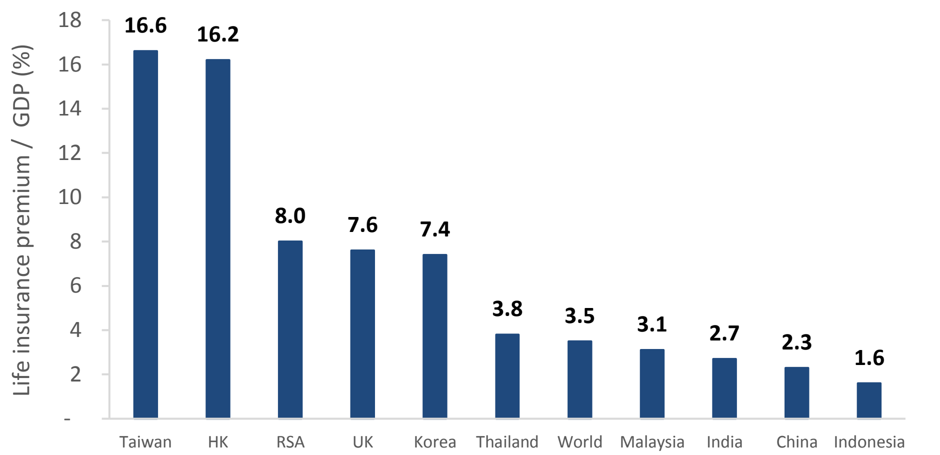
India is 10th largest life insurance market worldwide

The life insurance density has increased from ₹2,476 in FY14 to ₹3,112 in FY17

Life insurance penetration lower than global average

India is 10th largest life insurance market worldwide and 5th largest in Asia with total premium business of Rs4.6 lakh crore (FY18). The global average life insurance penetration was 3.5% in 2017 as compared to average of 2.7% in India. This indicates the untapped potential of the Indian life insurance market.

Exhibit 1: Penetration of life insurance in India vs. globally

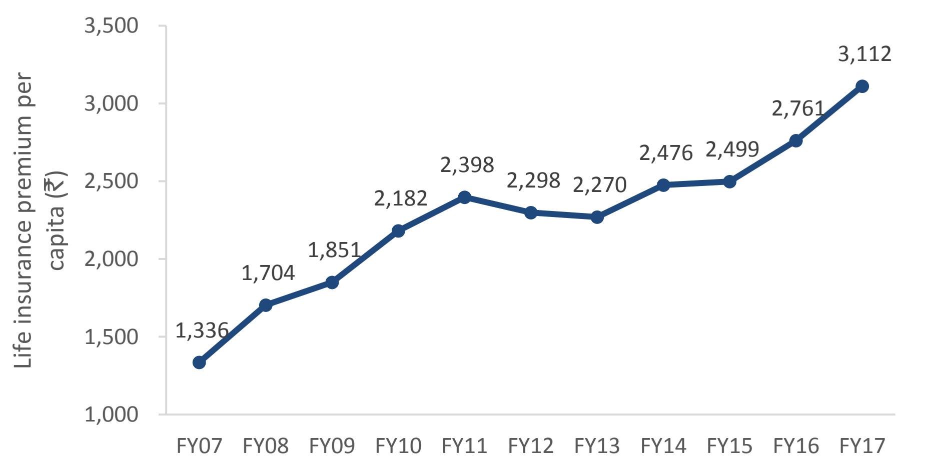


Source: Swiss Re Sigma, IRDAI, IIFL Research

Life insurance density in India witnessing an upward trend

The life insurance density (insurance premium per capita) has gone up from ₹1,336 in FY07 to ₹2,182 in FY10. However, it exhibited a declining trend over FY10-14 on account of regulatory clampdowns through stringent guidelines under the ULIP segment. Post regulatory curbs, the density has increased from ₹2,476 in FY14 to ₹3,112 in FY17.

Exhibit 2: Life insurance density in India



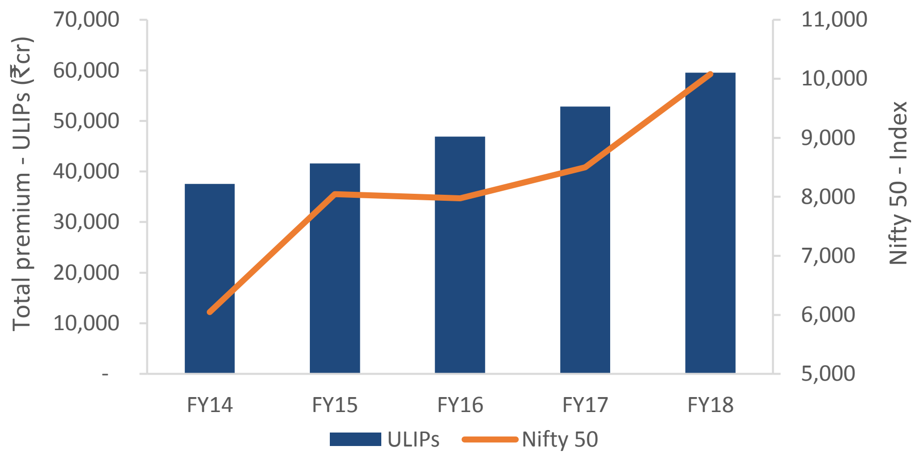
Source: IRDAI, IIFL Research

ULIP premium has witnessed ~12% CAGR over FY14-18

Cyclicality aspect on offering saving products

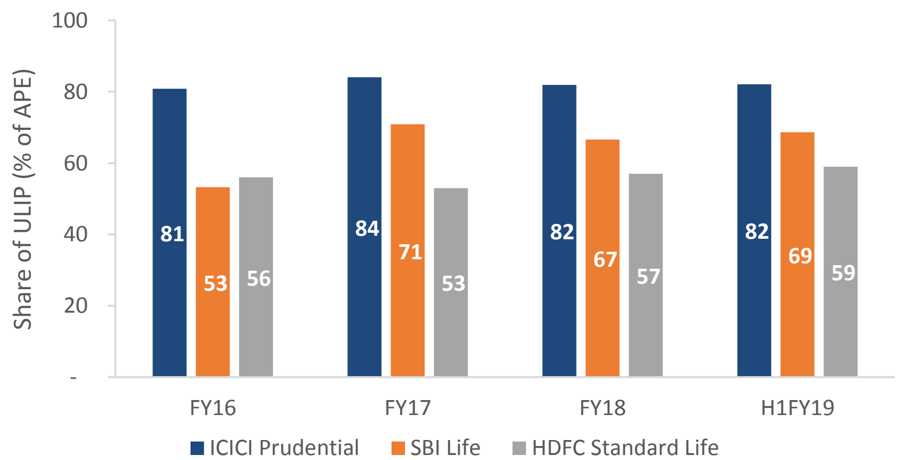
Insurance companies in developing markets like India focus on protection and linked products, while developed markets like US focus on products like retirement savings. The focus on linked products leads to greater cyclicality in new business volume due to its sensitivity to capital markets performance. The total industry ULIP premium has witnessed ~12% CAGR over FY14-18 backed by positive return delivered by Indian equities (~14% CAGR in Nifty 50 over FY14-18).

Exhibit 3: Total industry premium under ULIPs



Source: IRDAI, IIFL Research

Exhibit 4: Share of ULIPs, in terms of APE



Source: IRDAI, IIFL Research

The cyclicality associated with savings product (especially linked) implies that performance of insurance players with higher business mix under linked business is subject to the returns and stability of the Indian equity and debt markets.

Insurance products forming part of savings function

In terms of financing and insurance, the most important source of funds is the gross national disposable income (GNDI). The share of gross financial saving (GFS) out of GNDI has increased from 10.5% in FY13 to 11.1% (estimated) in FY18 in India. We expect life insurance business to remain a key proxy play in the midst of rising GFS.

The share of gross financial saving has increased from 10.5% in FY13 to 11.1% (estimated) in FY18

Exhibit 5: Gross financial savings to propel insurance demand

Particulars (%)	FY13	FY14	FY15	FY16	FY17	FY18E
Currency & Deposits	7.1	6.7	5.8	6.0	4.3	5.7
Shares and debentures	0.2	0.2	0.2	0.3	0.2	0.9
Claims on government	(0.1)	0.2	-	0.5	0.4	-
Insurance funds	1.8	1.8	2.4	1.9	2.3	1.9
Provident & pension funds	1.5	1.5	1.5	2.1	2.0	2.1
Others	-	-	-	-	-	0.5
Gross financial saving	**10.5**	**10.4**	**9.9**	**10.8**	**9.2**	**11.1**

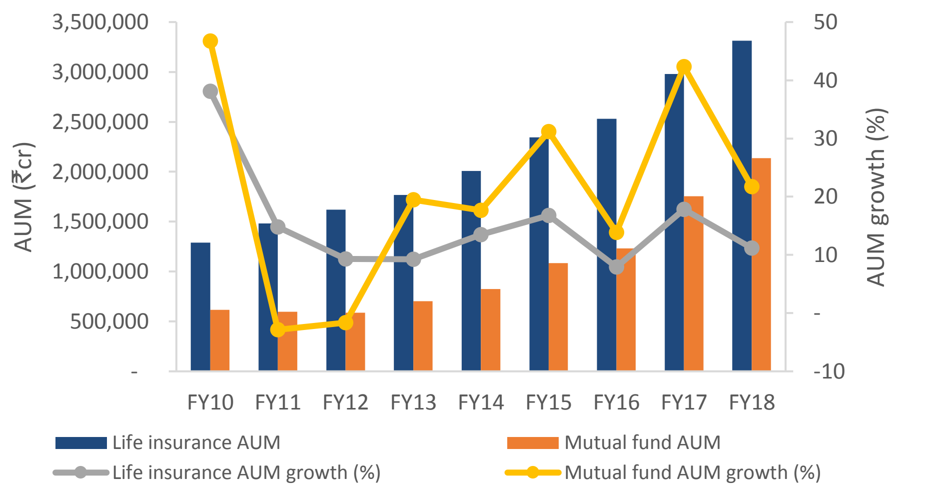
Source: RBI Annual Report 2018, IIFL Research

Financial savings has propelled AUM

The life insurance AUM has witnessed a CAGR of ~13% over FY10-18

Indian investors have been predominantly investing in traditional asset classes like real estate and gold, however, growing financial awareness has led to a rise in financial savings over last decade. This has led to traction in the mutual fund and life insurance assets under management (AUM). The life insurance AUM has witnessed a CAGR of ~13% over FY10-18, whereas the mutual fund AUM registered ~17% CAGR over the same period.

Exhibit 6: Mutual fund and life insurance AUM trend



Source: Life Insurance Council, AMFI, IIFL Research

Life insurance products become attractive for distributors

Life insurance products have become remunerative for financial product distributors

Financial product distributors have emerged as the key beneficiaries with the growth across financial asset classes, including insurance premium and mutual fund. Distribution network is crucial for life insurance as well as mutual funds, to source new business.

The insurance as well as mutual fund regulator viz. IRDAI and AMFI have capped the commission rates (TER – Total Expense Ratio for mutual funds) in the past. With applicability of new TER caps for mutual funds from April 01, 2019, we expect life insurance products to become more remunerative for distribution agents.

Exhibit 7: Commission structure for life insurance products

Premium paying terms (number of years)	Maximum *commission as a % of premium	
	1st year	Renewal Premium
5	15	7.5
6	18	7.5
7	21	7.5
8	24	7.5
9	27	7.5
10	30	7.5
11	33	7.5
12 years or more	35	7.5

*Source: IRDAI, IIFL Research; *structure for regular premium based insurance products*

Exhibit 8: Revised TER for mutual funds w.e.f. April 01, 2019

Cumulative Fund Size (₹ cr)	Effective TER for Equity Oriented Schemes (%)
500	2.25
750	2.17
2,000	1.91
5,000	1.72
10,000	1.61
15,000	1.56
20,000	1.52
25,000	1.48
30,000	1.45
35,000	1.42
40,000	1.40
45,000	1.37
50,000	1.34

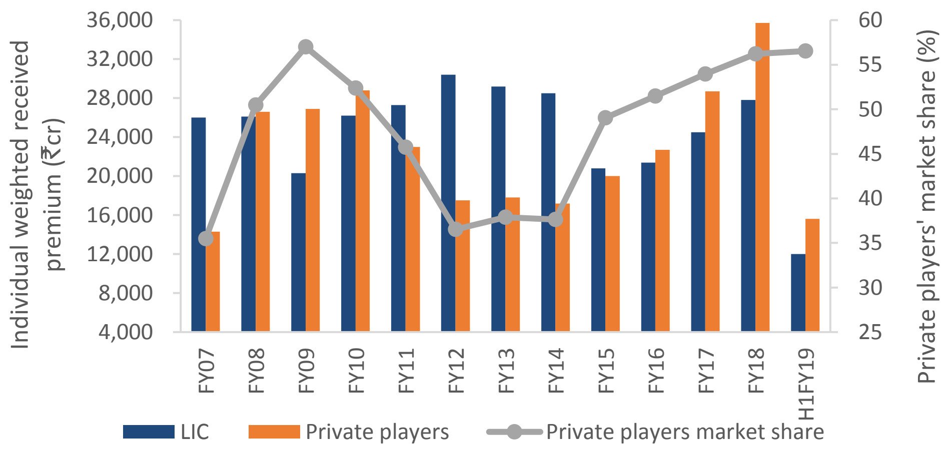
Source: SEBI, AMFI, IIFL Research

Private life insurer's individual business market share has increased from 38% in FY14 to 56% in FY18

Decline in LIC's share of individual business

The market share of private life insurance companies under individual business has increased significantly from 38% in FY14 to 56% in FY18. Private sector companies have gained significant market share post regulatory changes pursued by IRDAI in FY11. The major reasons for drop in LIC's market share are overdependence on long time established policies and replacement of its best-selling traditional policies after new regulations. LIC's investment in state-owned enterprises has remained a matter of concern for the policyholders, which has resulted into a shift towards private life insurers.

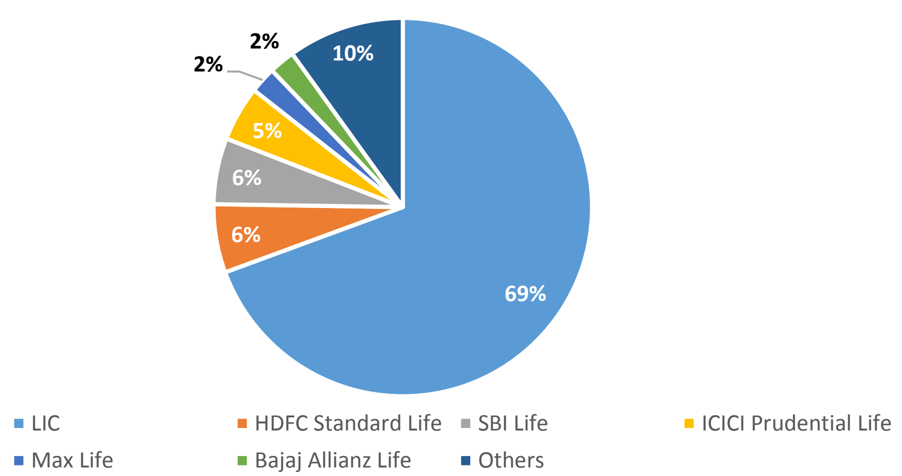
Exhibit 9: Private players gaining market share since FY14



Source: HDFC Standard Life, IRDAI, Life Insurance Council, IIFL Research

LIC's market share (in terms of total new business) has decreased to 69% in FY18 from 71% in FY17

Exhibit 10: Share of insurance players in total new business (FY18)



Source: IRDAI, Life Insurance Council, IIFL Research

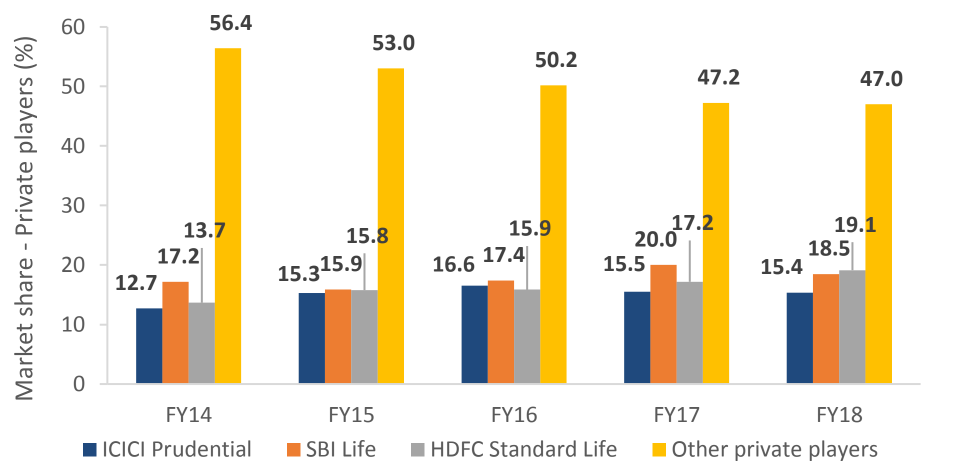
Bank-led insurance players well positioned under private space

Insurance companies having strong bancassurance channel are expected to continue their dominance in capturing the share through market penetration and acquiring LIC's business (refer exhibit 13). Further, banking-based players are poised to benefit from leveraging the brand recognition of their banking partners towards online / direct business. As a result, cumulative market share (in terms of total new business) for IPru Life, SBI Life and HDFC Life under private space has increased from 43.6% in FY14 to 53% in FY18.

Thus, bank-led insurance players are expected to register higher growth than the industry with further market share gains on consolidation under the private space.

Cumulative market share for top three private players has increased from 43.6% in FY14 to 53% in FY18

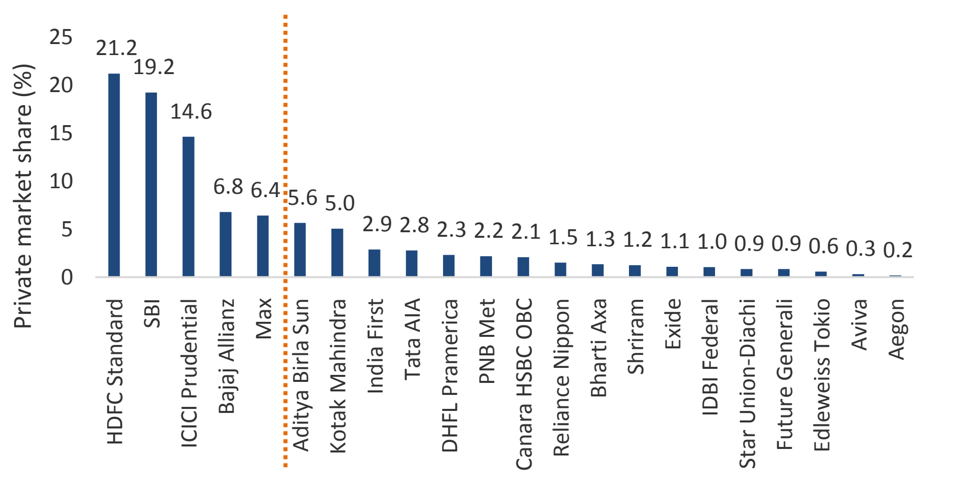
Exhibit 11: Consolidation in private market aiding banca players



Source: IRDAI, IIFL Research

Top five private life insurers account for 68.2% of the total private life insurance market

Exhibit 12: Life insurers - Private market share

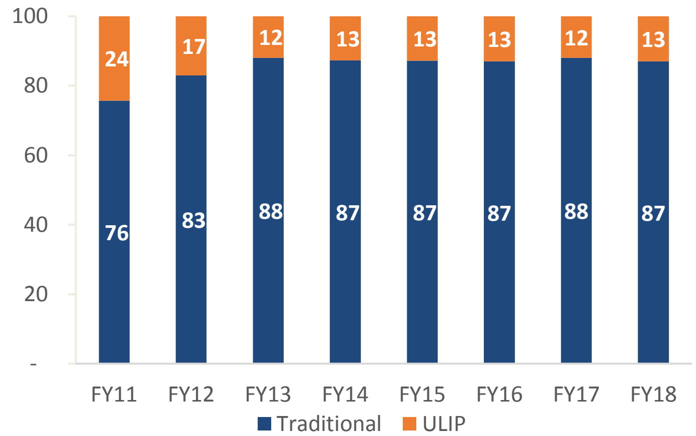


*Source: IRDAI, IIFL Research; *based on total new business premium over April-November 18*

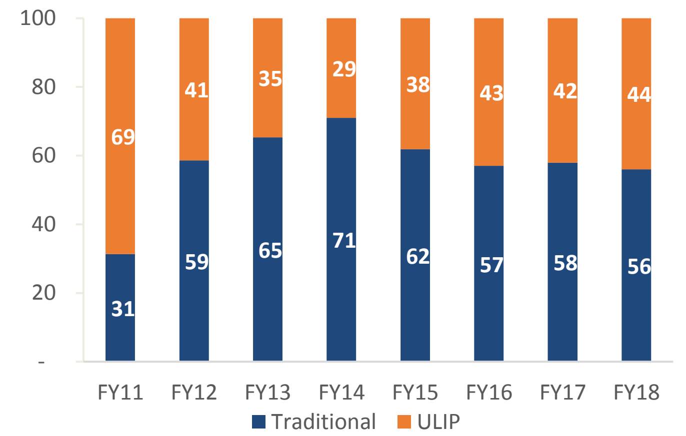
Exhibit 13: Product portfolio and Channel Mix

Product portfolio

Overall Industry

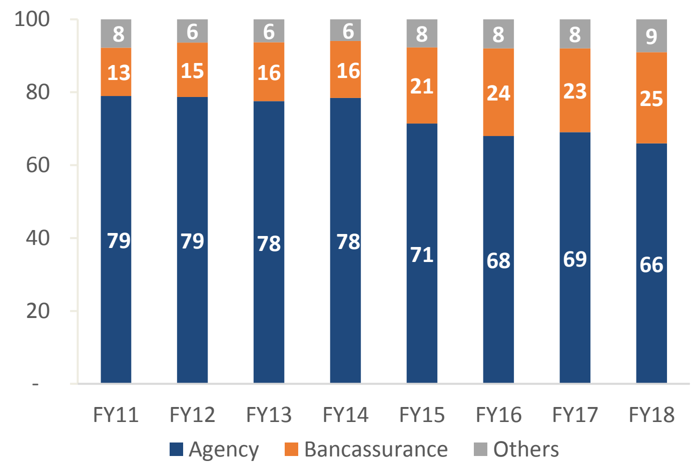


Private Players

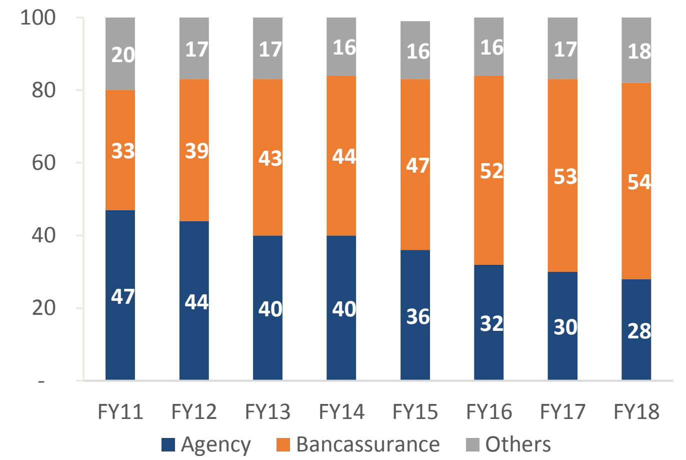


Channel Mix

Overall Industry



Private Players



Source: IRDAI, Life Insurance Council, IIFL Research; based on new business premium

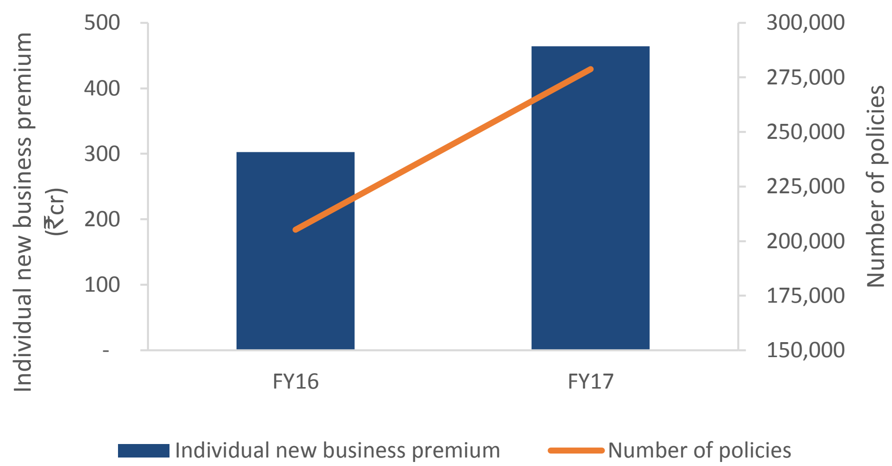
Digitization in life insurance

Digitization is an important aspect which has enhanced and enabled scalability across the BFSI sector. Life insurance, being a push service, is gaining traction through digital technology and artificial intelligence.

There has been a drastic increase in the new business premiums collected through web aggregators and online channels. For FY16, the total amount of premium collected was ₹303cr. However, by end-FY17, total premium collected through digital rose to ₹464cr with increase in number of policies sold by ~36% yoy.

Number of policies underwritten through digital channel has increased by ~36% yoy (FY17)

Exhibit 14: Web aggregators and online business statistics



Source: IRDAI, IIFL Research

Digital insurance - The way forward

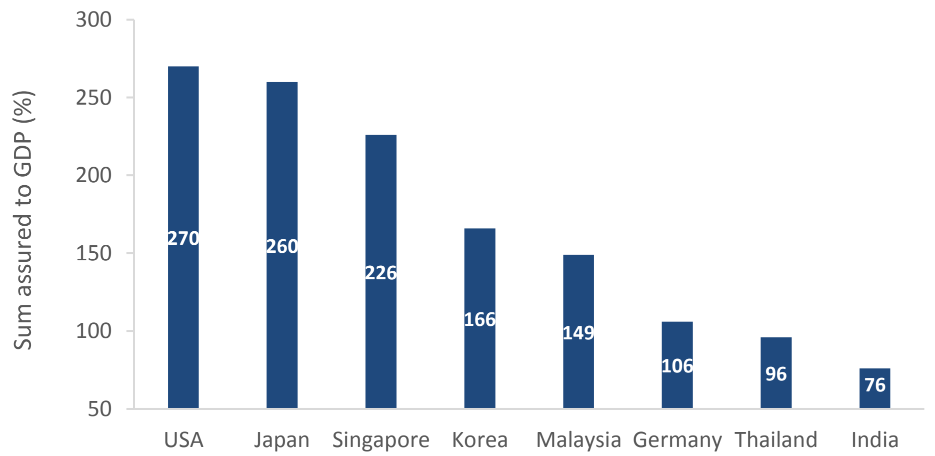
The advent of technology has already led to the digitalization of insurance companies. However, this will require further investments in digital technology by the companies to sustain their market share going ahead. There lies a huge opportunity for sourcing policies online (current contribution is less than ~2% of the total new business) with greater internet penetration and a shift towards digital services.

Potential to capture protection opportunity in Indian markets

India has lower ratio of total sum assured to GDP of 76% vs. other emerging (Malaysia - 149%) and developed markets (USA - 270%). This provides an opportunity to the Indian life insurance companies to offer protection products to the population. Further, urbanization, increase in GDP per capita, etc. are the major triggers for capturing this opportunity.

India's total sum assured to GDP ratio stands at 76%

Exhibit 15: India vs. world scenario - Sum assured to GDP

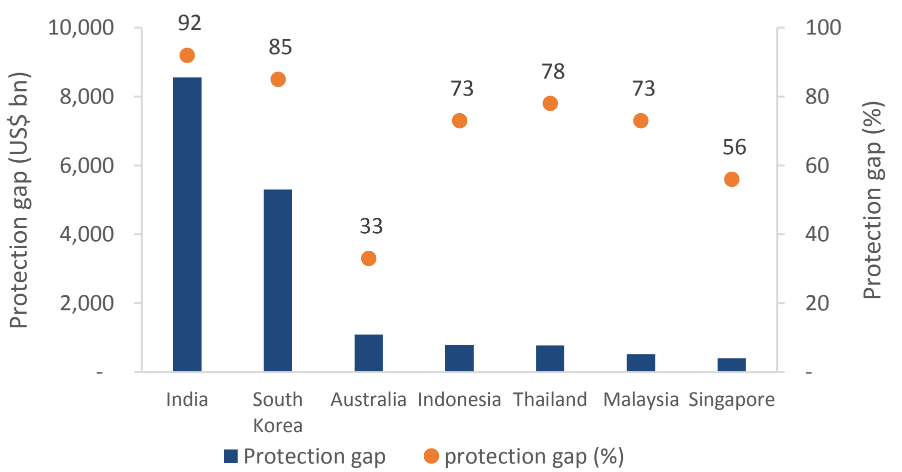


Source: ICICI Prudential Life Insurance, McKinsey, Life Insurance Council, IIFL Research

India has a protection gap of 92% (ratio of protection deficit to protection requirement), which is significantly wider than other emerging economies and developed countries. Protection gap for India in absolute terms stands at US$8,560bn (2015).

India has a protection gap of 92% ($8,560bn in absolute terms)

Exhibit 16: Protection gap in India vs. world



Source: ICICI Prudential Life Insurance, Swiss Re, IIFL Research

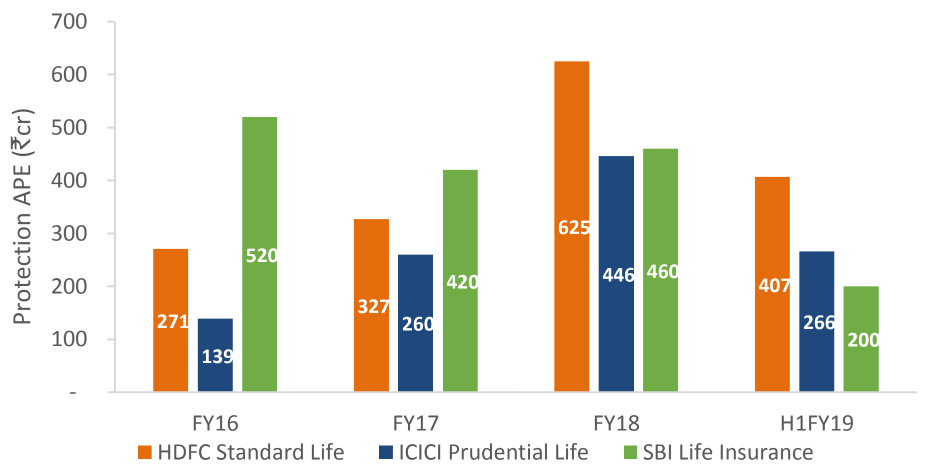
HDFC Life has highest protection biz amongst the listed peers

HDFC Standard Life, has gained traction across the individual and group protection business as compared to its listed peers. It has been able to maintain the balance between risk and new business margin on underwriting of protection policies. The proportion of protection to total business in terms of APE has increased from ~7% in FY16 to 16% in H1FY19 with an increase in VNB margin by ~331bps over FY16-18.

Considering the shift towards protection segment, we expect IPru Life and SBI Life (lower protection business mix) to witness significant VNB margin expansion going ahead. For FY18, IPru Life and SBI Life's VNB margin stood at 16.5% and 18.4% respectively.

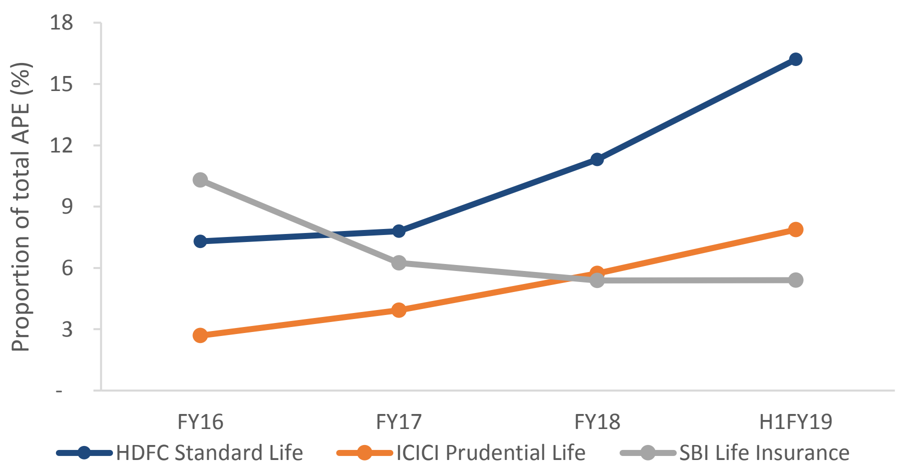
HDFC Life has higher proportion of protection business as against its listed peers

Exhibit 17: Protection business across listed peers



Source: Company data, IIFL Research

Exhibit 18: Contribution of protection towards total APE



Source: Company data, IIFL Research

ALM is crucial for managing investment and liquidity risk

Life insurance companies face investment risk arising out of variations in the level or volatility of market prices of financial instruments. However, they witness limited liquidity risk as the liabilities are backed by adequate quantum of assets held in form of investments. The liabilities for the life insurance companies is in the form of in-force policies (that become due on maturity), policy withdrawal and early redemption of ULIPs.

In terms of the total investment mix of life insurance companies, significant portion (>85% of the total investment) is invested into equities, government and other approved securities, and debentures / bonds (refer exhibit 19). The insurance companies have an asset liability management (ALM) committee which formulates and implements strategies, both at the product and enterprise level.

Valuation of investment in debt instruments

Debt instruments under non-linked / shareholder's investments are categorized as 'HTM'

The debt instruments under non-linked and shareholder's investment are categorized as 'held to maturity' (HTM), and thereby are measured at historical cost with amortization of discount or premium over the maturity. Thus, the impact of change in yields for debt securities under these segments are not restated in the financial statements of the insurance companies.

Investment in debt instruments under linked business are measured at 'fair value', the change in value of the instrument is linked to the units held by the policy holder.

Life insurance players have limited sensitivity to yield

Life insurance companies have limited exposure towards money market instruments

Life insurance companies have limited sensitivity towards change in interest yield on account of:

- Significant portion of investment in government and other approved securities thereby maintaining credit risk
- Limited liquidity risk for investment in money market instruments as it is usually less than 10% of the total investments of the company

Potential downsides to embedded value

- Expense under recovery due to high underwriting cost, variance in actual expenses vs. assumptions and lower volume of premium could lead to deceleration in EV growth
- Negative impact arising from economic & investment variance (non-operational) due to subdued performance of equity markets and rising bond yield could hamper EV.

In terms of impact of change in yield rate over the embedded value (refer exhibit 20), HDFC Standard Life has lowest sensitivity (FY18) followed by ICICI Prudential Life. SBI Life comparatively has higher sensitivity towards yield as compared to its peers.

Exhibit 19: Investment mix across asset categories (FY18)

Investment - Asset mix (%)	ICICI Prudential				SBI Life				HDFC Standard Life			
	Linked funds	Non-Linked funds	Share holders' funds	Total	Linked funds	Non-Linked funds	Share holders' funds	Total	Linked funds	Non -Linked funds	Share holders' funds	Total
Equity shares	59.4	16.5	20.4	46.7	30.4	8.5	20.7	19.4	52.2	11.6	11.1	33.3
Government and other approved securities	12.4	58.5	34.5	25.0	48.5	70.7	54.5	59.5	25.5	68.2	71.6	45.4
Debentures and bonds	16.4	15.4	28.5	16.8	7.6	10.6	12.3	9.3	10.0	11.9	5.4	10.6
Money market instruments	8.4	1.8	3.2	6.5	1.4	2.5	2.0	2.0	4.8	4.0	2.4	4.4
Fixed deposits	0.1	0.9	3.1	0.5	4.1	2.9	0.5	3.4	-	0.5	2.7	0.3
Mutual funds	2.3	4.2	3.4	2.8	-	2.6	2.0	1.3	-	1.6	5.0	0.9
Investment property	-	0.2	4.9	0.3	-	-	-	-	-	-	-	-
Loan against policies	-	0.4	-	0.1	-	-	-	-	-	-	-	-
Net current assets and other investments	1.0	2.1	2.0	1.3	7.9	2.1	8.0	5.1	7.5	2.3	1.8	5.1

Source: Company, IIFL Research

Exhibit 20: Interest rate sensitivity on VNB margin and Embedded Value

Interest rate sensitivity	Change in EV (%)		Change in VNB (%)	
	+100bps	-100bps	+100bps	-100bps
ICICI Prudential Life (FY18)	(2.1)	2.2	(4.9)	5.2
SBI Life (H1FY19)	(5.0)	7.0	3.0	(3.0)
HDFC Standard Life (H1FY19)	(2.0)	2.1	0.9	(2.3)

Source: Company, IIFL Research

IIFL Securities

ICICI Prudential Life Insurance

CMP: ₹316; 1-year target: ₹395

Sector	Life Insurance
Recommendation	BUY
Upside	25%

Stock Data

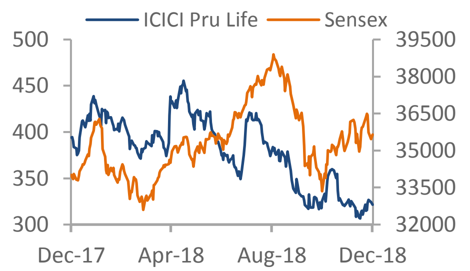
Sensex	35,514
52 Week h/l (₹)	462/302
Market cap (₹ Cr)	45,362
BSE Code	540133
NSE Code	ICICIPRULI
FV (₹)	10
Div yield (%)	2.06

Shareholding Pattern (%)

	Mar-18	Jun-18	Sept-18
Promoters	80.7	78.7	78.7
DII+FII	10.2	12.9	13.2
Individuals	9.1	8.4	8.1

Source: ACE Equity, IIFL Research

Share Price Trend



Prices as on 03/01/2019

ICICI Prudential Life Insurance (IPru Life), a leading private life insurance player, enjoys strong retail presence with 11.4% (H1FY19) market share within total industry. IPru Life is poised to gain traction under new business backed by healthy bancassurance channel. We expect new business premium (APE) CAGR of ~9% over FY18-21E with shift in mix towards protection. We project VNB margin to expand by ~319bps over FY18-21E to 19.7% in FY21E owing to favorable mix and cost optimization. We recommend BUY on the stock.

Strong distribution channel with robust digital platform: IPru Life's strong bancassurance channel through its banking partner is expected to continue sourcing concentrated portion of the new business premium. Robust digital platform will further drive direct channel APE by more than 25% over FY18-21E (~37% CAGR over FY15-18).

Product mix and persistency to drive VNB margin: We expect margin improvement on the back of (1) new product launches under protection segment; (2) sustainability of existing persistency; (3) maintenance of operating costs. We estimate VNB margin to expand by ~319bps over FY18-21E and thereby shrinking the gap vs. peers.

Outlook & Valuation: IPru Life is currently trading at attractive valuations (~33% discount to one-year forward P/EV) given its strong brand recognition and scope of VNB margin improvement. We value the stock using embedded valuation with a target multiple of ~2.3x FY20E P/EV.

Financial Summary

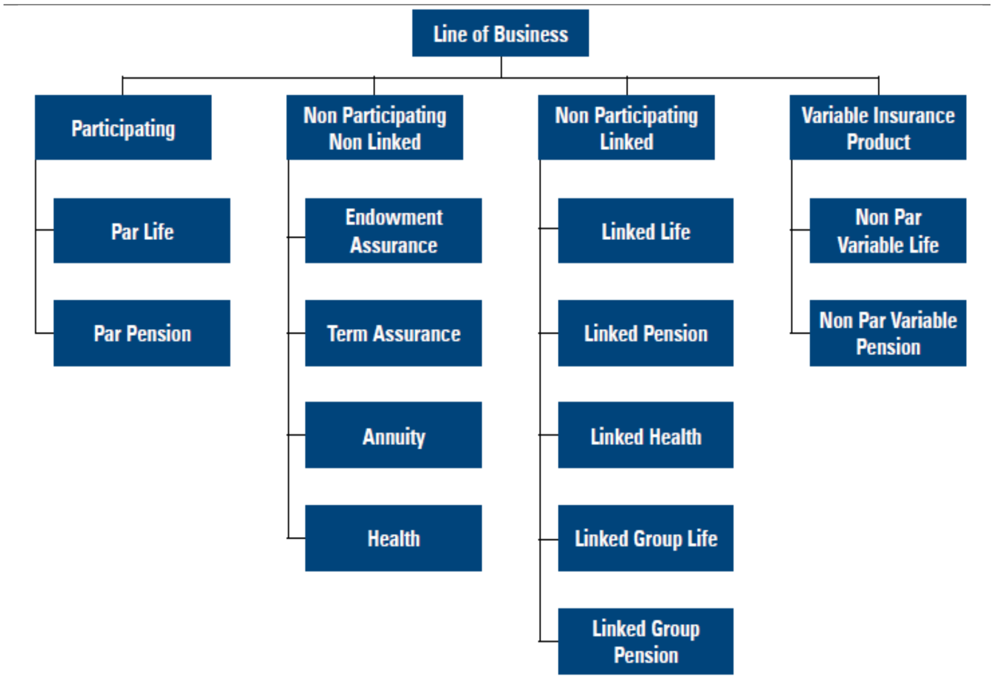
Particulars ₹Cr	FY17	FY18	FY19E	FY20E	FY21E
Total Premium Income	22,354	27,069	31,580	36,847	42,051
APE	6,625	7,792	8,233	9,605	10,192
VNB	666	1,286	1,472	1,826	2,007
VNB margin* (%)	10.1	16.5	17.9	19.0	19.7
PAT	1,683	1,620	1,541	1,853	2,000
PAT growth (%)	2.1	(3.8)	(4.9)	20.3	7.9
Operating RoEV (%)	16.5	22.7	18.3	18.9	17.6
Price/Embedded Value	2.8	2.4	2.1	1.8	1.6

Source: Company, IIFL Research

Company Overview

IPru Life is promoted by ICICI Bank (52.88% shareholding as on September 30, 2018) and Prudential Corporation Holdings Limited (25.83%). It has consistently remained the top private sector life insurance company since commencement of operations in 2001 on a retail weighted premium (RWRP) basis. It has products across savings (~94% FY18 Total APE) and protection segments (~6%).

Exhibit 1: IPru Life's line of business



Source: Company, IIFL Research

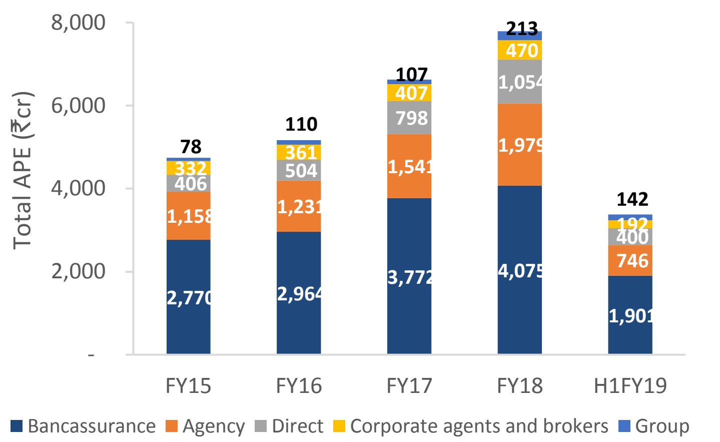
Direct channel gains traction, banca sources maximum business

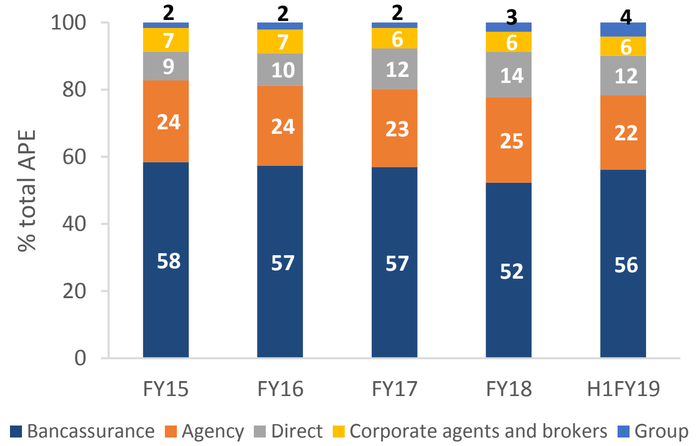
Banca channel contributes ~56% (H1FY19 APE) of the total business

IPru Life has a diversified distribution network with bancassurance channel sourcing the maximum quantum of new business (~56% H1FY19 APE). Direct channel has gained traction with a CAGR of ~37% over FY15-18 (~12% H1FY19 APE). We expect IPru Life's direct channel to continue to gain further traction under this segment for new business premium.

The APE under banca segment has witnessed a CAGR of 13.7% over FY15-18. The company has business arrangement with ICICI Bank and others like Standard Chartered Bank and Capital Small Finance Bank.

Exhibit 2: Blended distribution channel network





Source: Company, IIFL Research

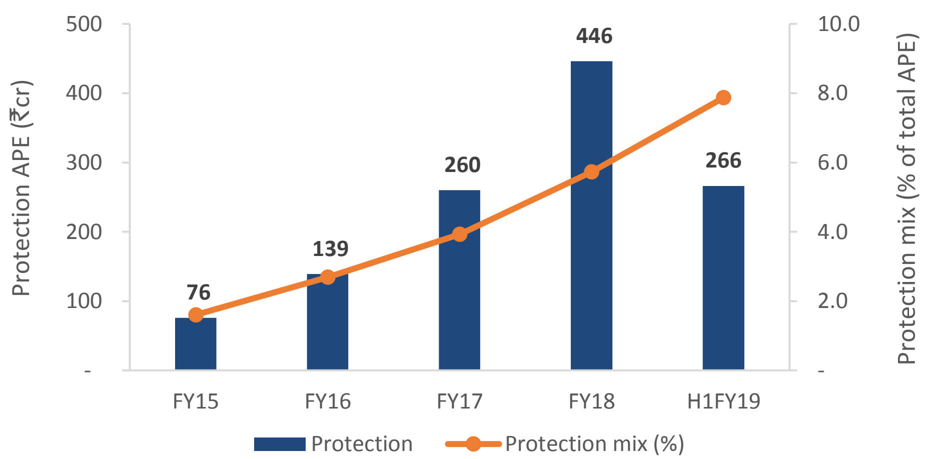
Focus on protection business and improvement in persistency would expand VNB margin

VNB margin improvement on the cards

IPru Life's higher exposure to ULIPs (low margin vs. protection) has kept the VNB margin lower vs. listed peers over FY15-18. However, the VNB margin has improved from 5.7% in FY15 to 16.5% in FY18 on account of traction in protection (APE increased ~6 times over FY15-18). Protection business remains a key focus point due to volatility in ULIPs (higher surrenders). Moreover, the persistency has also improved across all the periods. We estimate VNB margin to expand by ~319bps over FY18-21E. Key factors for VNB margin expansion are:

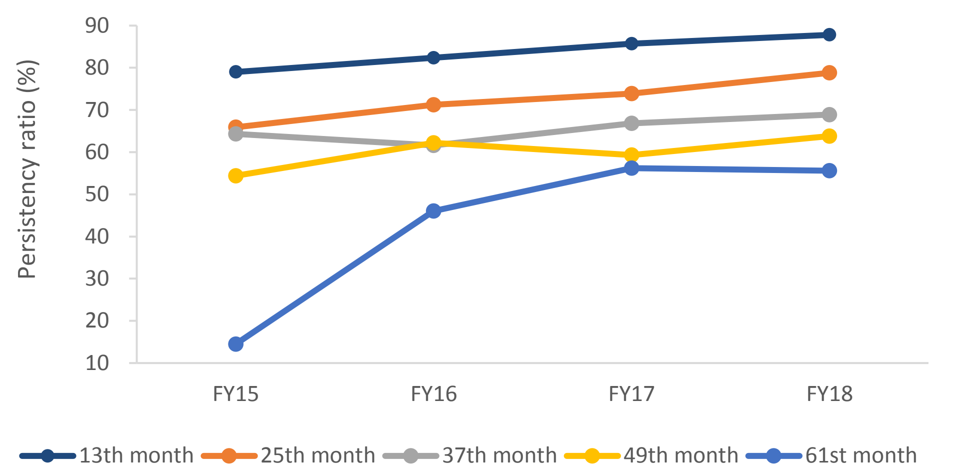
- Launch of new products under protection (higher margin). We expect protection to contribute to future pool of profits.
- Likely improvement in persistency level to aid margin expansion.
- Enhancement in cost-to-income ratio.

Exhibit 3: Protection business is gaining momentum



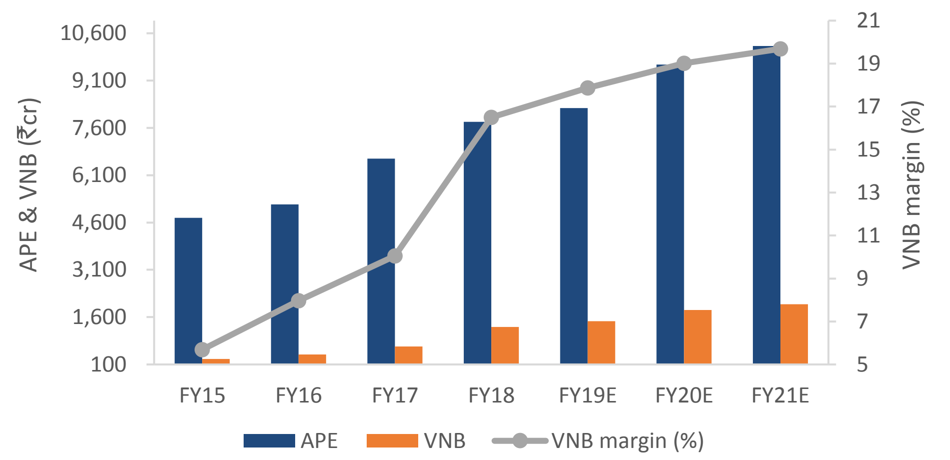
Source: Company, IIFL Research

Exhibit 4: Rising trend in persistency level for IPru Life



Source: Company, IIFL Research

Exhibit 5: Further room for improvement in VNB margin



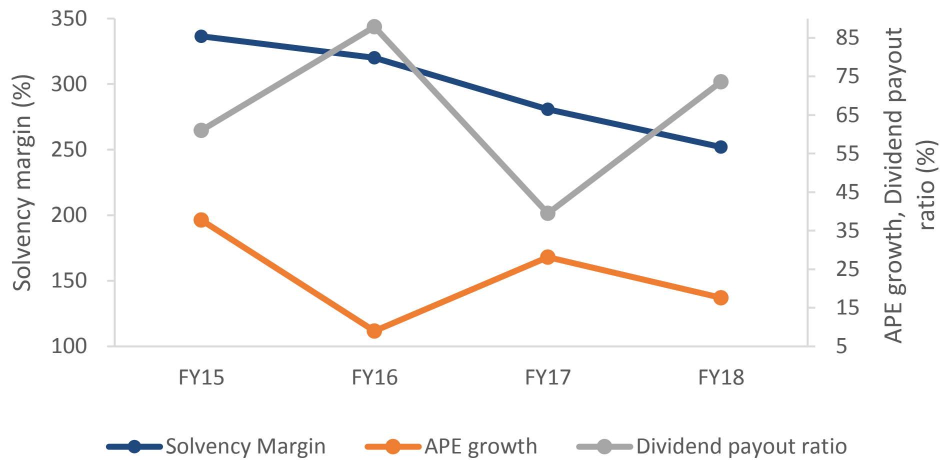
Source: Company, IIFL Research

Better solvency margin than the listed peers

New business and dividend payouts has reduced solvency margin from 336.5% in FY15 to 252% in FY18

Solvency margin reveals the capability of the insurance company to pay claims to its policyholders (regulatory requirement of 150%). The company has consistently been able to maintain higher solvency margin vs. listed peers. However, IPru Life's solvency margin has reduced to 252% in FY18 (234% in H1FY19) vs. 336.5% in FY15 owing to new business underwriting (~18% APE CAGR over FY15-18) and high dividend payouts. The company's solvency margin at 234% (H1FY19) is still better compared to listed peers (SBI Life - 221%, HDFC Life - 193%).

Exhibit 6: Solvency margin trend for IPru Life



Source: Company, IIFL Research

Embedded value and return on embedded value (RoEV) details

IPru Life's embedded value is likely to be driven by insurance profits, which would form a large share of operating variances. We expect moderation of operating RoEV in the range of 18-19%, backed by VNB margin expansion and higher unwinding of discount on opening embedded value.

Particulars (₹ in cr)	FY17	FY18	FY19E	FY20E	FY21E
Opening EV	**13,939**	**16,184**	**18,789**	**21,220**	**24,686**
EVOP (operating variances)	2,295	3,680	3,447	4,007	4,335
Economic assumption change & investment variance	582	113	(400)	200	200
Net capital injection	(632)	(1,188)	(616)	(741)	(800)
Closing EV	**16,184**	**18,789**	**21,220**	**24,686**	**28,421**
Value of in-force (VIF)	9,428	11,764	13,504	15,972	18,630
Adjusted net worth	6,756	7,024	7,716	8,714	9,791
Embedded value	**16,184**	**18,788**	**21,220**	**24,646**	**28,421**
Operating RoEV (%)	16.5	22.7	18.3	18.9	17.6
RoE (%)	28.7	24.4	21.1	22.6	21.6

Source: Company, IIFL Research

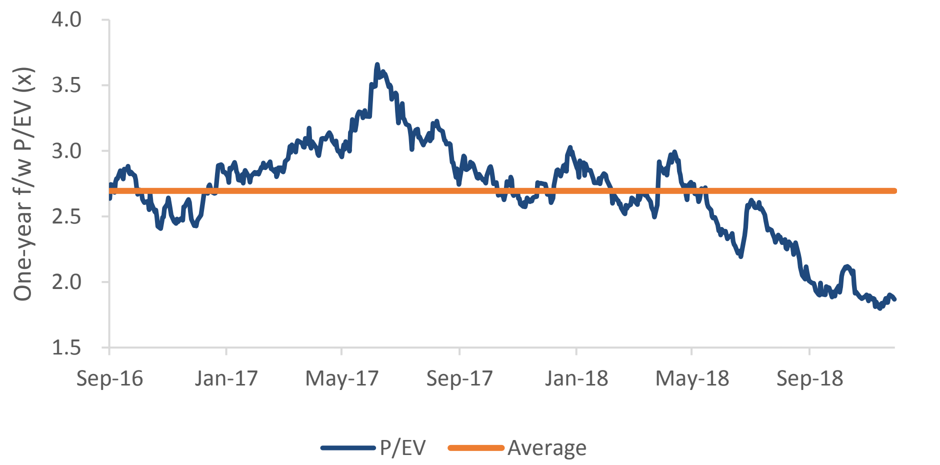
Valuation rationale and matrix

We value IPru Life using embedded value methodology as profitability based multiple would provide ambiguous valuation as the new business profit is front-loaded by high opex with premium inflow in subsequent period.

IPru Life is trading at ~33% discount to one-year forward P/EV

IPru Life is currently trading at attractive valuations (~1.8x FY20E P/EV) vs. peers. Based on embedded value methodology, we value IPru Life at 2.3x FY20E price/embedded value (providing 15% discount to average one-year forward P/EV for a period of 24 months). The valuation multiple is justified considering its retail leadership position and scope of improvement in VNB margin.

Exhibit 7: One-year forward price/embedded value



Source: ACE Equity, IIFL Research

Exhibit 8: Balance sheet summary and key ratios

Particulars ~₹cr	FY17	FY18	FY19E	FY20E	FY21E
Investments – Shareholders	6,640	7,749	8,366	9,108	9,906
Investments - Policyholders	1,14,946	1,30,791	1,49,676	1,70,657	1,93,480
Fixed Assets	214	422	435	456	478
Net current assets	26	(734)	52	(1,082)	(3,183)
Other assets	81	146	145	145	145
Total net assets	**1,21,906**	**1,38,374**	**1,58,674**	**1,79,284**	**2,00,826**
Shareholder's fund	6,408	6,884	7,716	8,714	9,791
Policyholder's fund	1,15,498	1,31,490	1,50,958	1,70,570	1,91,035
Total liabilities	**1,21,906**	**1,38,374**	**1,58,674**	**1,79,284**	**2,00,826**
Key Ratios					
Investment yield – Shareholder (%)	10.4	10.3	10.2	10.4	10.2
Investment yield - Policyholder (%)	14.1	9.2	8.8	9.0	8.9
Cost to net earned premium ratio (%)	14.1	12.8	13.1	13.6	13.1

Source: Company, IIFL Research

Key Risks

- Volatility in the capital markets may impact the company's business as IPru Life has large portion of business under linked segment (~82% FY18 APE). This has led to decline in individual APE for IPru Life by ~12% (FY19 YTD, November 30, 2018).
- Pricing pressure due to competition intensity may affect new business of the company.

SBI Life Insurance

CMP: ₹599; 1-year target: ₹712

Sector	Life Insurance
Recommendation	BUY
Upside	19%

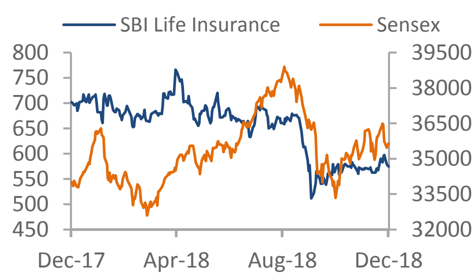
Stock Data	
Sensex	35,514
52 Week h/l (₹)	775/487
Market cap (₹ Cr)	59,900
BSE code	540719
NSE code	SBILIFE
FV (₹)	10
Div yield (%)	0.36

Shareholding Pattern (%)

	Mar-18	Jun-18	Sept-18
Promoters	84.1	84.1	84.1
DII+FII	8.8	9.2	9.2
Individuals	7.1	6.7	6.7

Source: ACE Equity, IIFL Research

Share Price Trend



Prices as on 03/01/2019

SBI Life Insurance Company Limited (SBI Life) is one of the leading private life insurer with market share of 21.9% (H1FY19), based on individual rated premium. It is well placed to capture new business through its distribution network coupled with higher productivity in issuance of policies. We expect new business premium (APE) CAGR of ~14% over FY18-21E backed by vast banca network. VNB margin is likely to improve by ~138bps over FY18-21E to 17.6% in FY21E driven by higher operating leverage. We recommend BUY on the stock.

Strong distribution network with rising productivity: SBI Life has strong customer reach due to the access to over ~22,000 branches of SBI. Further, the banca and agency channel productivity has seen an improvement over FY15-18, which will drive traction in new business.

Maintaining cost efficiency provides operating leverage: SBI Life enjoys industry leadership in terms of lower cost ratio (commission and operating expenses, ~11.3% in FY18). New business underwritten at lower cost is value accretive and will improve operating leverage resulting into VNB margin expansion of ~138bps over FY18-21E.

Outlook & Valuation: SBI Life has strong growth levers, sustained product mix and traction in individual business through its robust distribution network. Volume driven business coupled with low cost augurs well for the company. We value SBI Life using embedded valuation with a target multiple of ~2.6x FY20E P/EV (providing 10% discount to average one-year forward P/EV).

Financial Summary

Particulars (₹cr)	FY17	FY18	FY19E	FY20E	FY21E
Total Premium Income	21,015	25,354	32,509	40,282	49,168
APE	6,730	8,540	9,777	11,075	12,557
VNB*	1,036	1,570	1,839	2,178	2,482
VNB margin* (%)	15.4	18.4	18.8	19.7	19.8
PAT	955	1,150	1,390	1,851	2,311
PAT growth (%)	13.4	20.5	20.9	33.1	24.8
Adj Operating RoEV (%)	23.0	17.8	17.5	18.1	18.1
Price/Embedded Value	3.4	3.0	2.6	2.2	1.9

*Source: Company, IIFL Research; *FY17 VNB & VNB margin excludes tax benefit available by way of dividend income from equity*

Company Overview

SBI Life is a joint venture between State Bank of India (62.1% stake as on September 30, 2018) and BNP Paribas Cardif (22% stake). The company has ~2.4cr lives covered as on September 30, 2018.

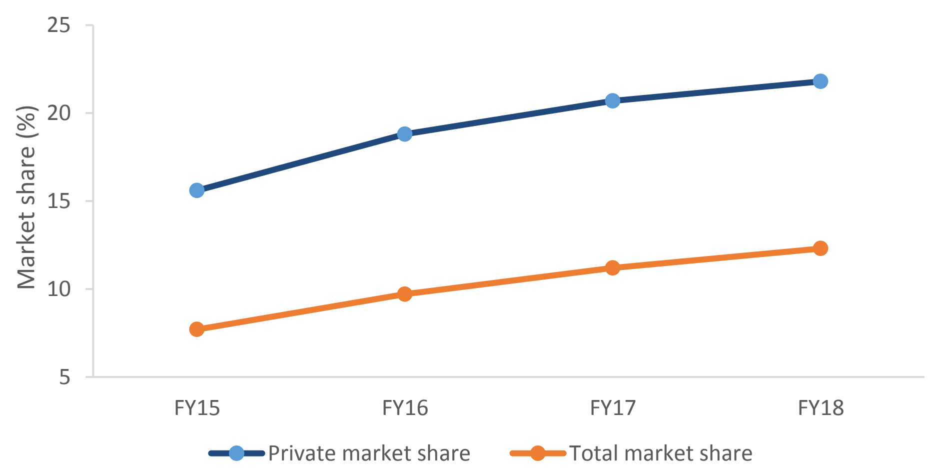
SBI Life has 15 products under protection and 25 products under savings segment (including ULIPs), across individual and group businesses.

Rising market share across individual business products

The total market share of SBI Life has increased to 12.3% in H1FY19 from 7.7% in FY15 (in terms of IRP)

SBI Life has gained traction in new business through individual product offerings. The total market share of SBI Life under individual rated premium (IRP) has increased to 12.3% in H1FY19 from 7.7% in FY15. The private market share has also increased to 21.9% in H1FY19 from 15.6% in FY15. We expect SBI Life to increase its focus on individual business backed by strong distribution network and prominent brand.

Exhibit 1: Traction in SBI Life's IRP market share



Source: Company, IIFL Research

High productivity across distribution channels

Productivity per agent has improved to Rs2.58lakh in FY18 from Rs1.77lakh in FY15

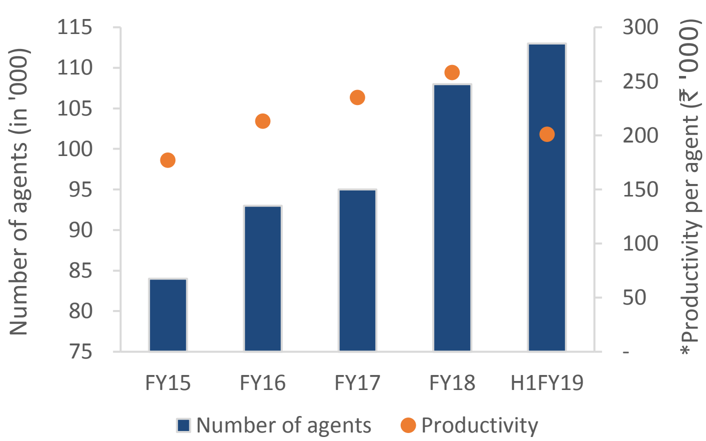
SBI Life is poised to witness traction in new business (especially under individual segment) through vast bancassurance (~61% H1FY19 NBP) and agency network (~21%). Total number of policies written by SBI Life has witnessed ~8% CAGR over FY15-18 with ~14.28 lakh policies written in FY18. The agency productivity has improved substantially to ₹2.58 lakh individual new business in FY18 from ₹1.77 lakh in FY15.

Exhibit 2: Number of policies written by SBI Life across channels

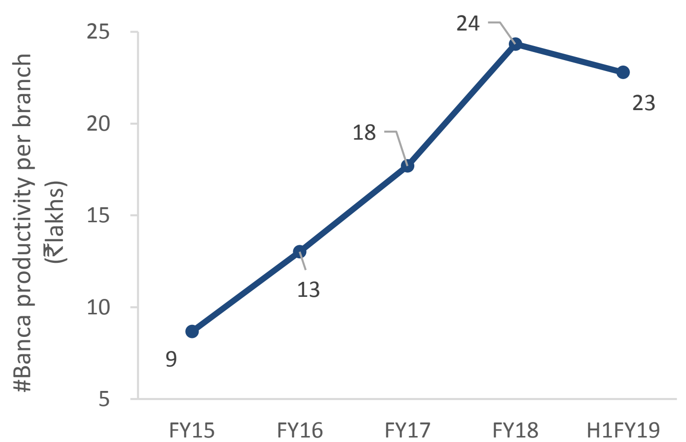
Source: Company, IIFL Research

Exhibit 3: Productivity across agency and bancassurance channels

Agency



Bancassurance



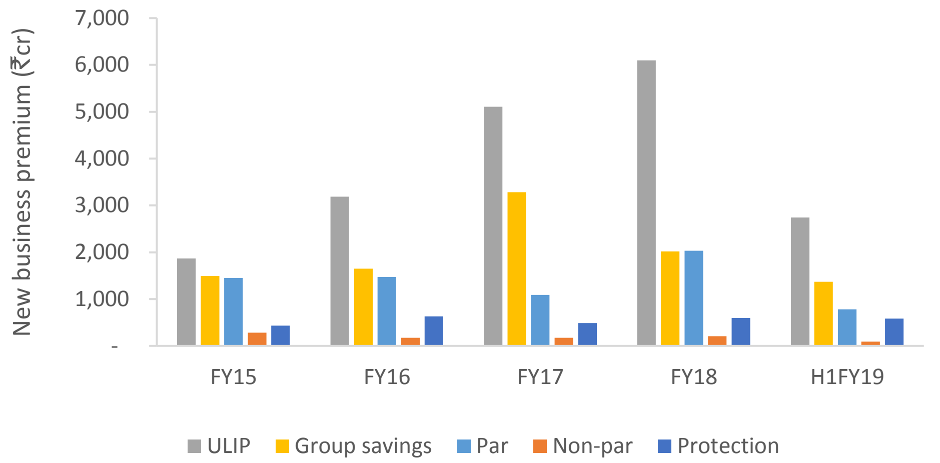
*Source: Company, IIFL Research; *Agency channel individual NBP divided by no. of agents; #Banca channel individual NBP divided by banca branches; First half of the financial year is seasonally a slower period for life insurance companies*

Traction in new business premium with focus towards retail

SBI Life is focused on individual retail business due to the strong distribution footprint of its parent SBI. The individual new business mix has increased from ~70% in FY16 to ~77% in FY18. With further improvement in productivity and strong distribution strength, we estimate new business premium (APE) CAGR of ~14% over FY18-21E.

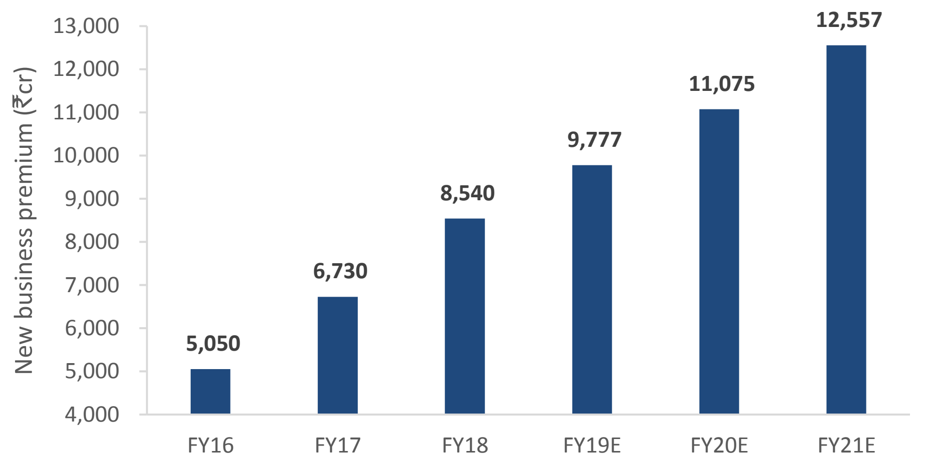
The share of individual business has increased from ~70% in FY16 to ~77% in FY18 (in terms of NBP)

Exhibit 4: Focus on individual business



Source: Company, IIFL Research

Exhibit 5: New business to continue gaining traction



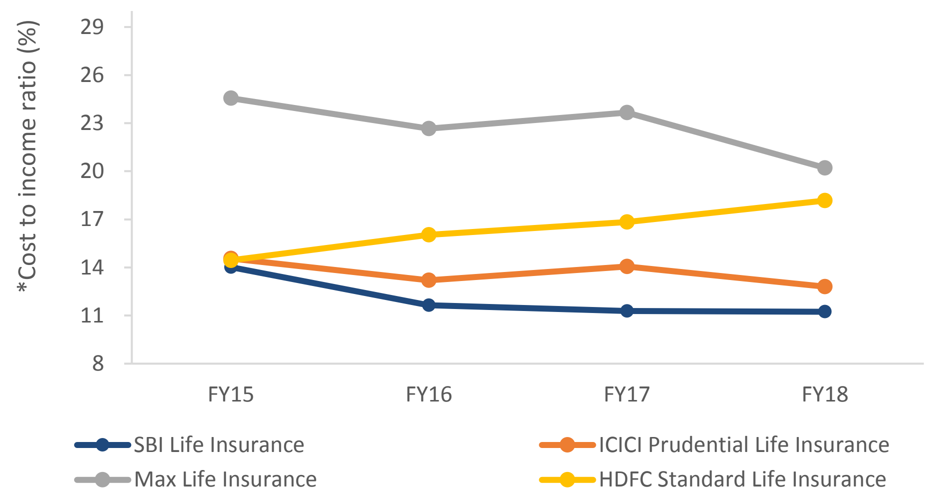
Source: Company, IIFL Research

Leadership in lower cost ratio across listed peers

SBI Life has been able to maintain lower cost ratio owing to strong bancassurance channel which provides (a) in-house cross selling advantage, (b) operational efficiency, and (c) scaled economies through vast distribution presence. We estimate cost ratio to remain stable at 11.5% by FY21E (11.3% in FY18).

Exhibit 6: Maintenance of cost leadership by SBI Life

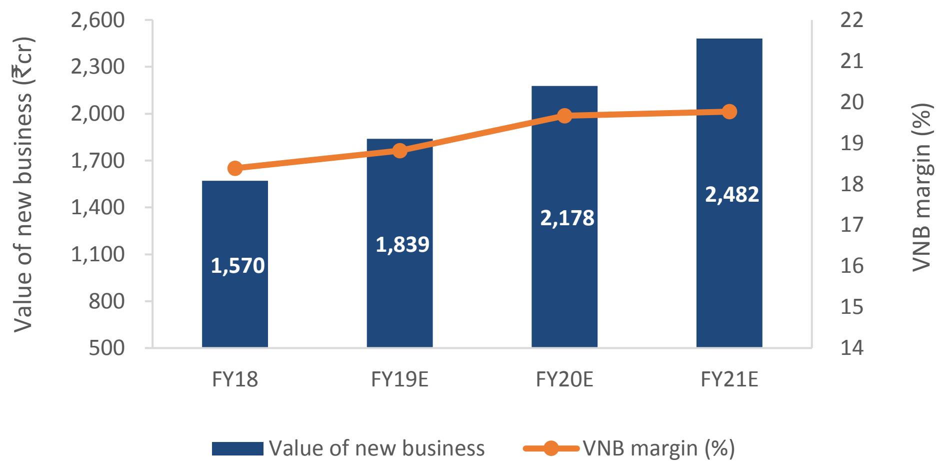
SBI Life operates at lower cost ratios within the private players



*Source: Company, IIFL Research, *Commission and Opex divided by net earned premium*

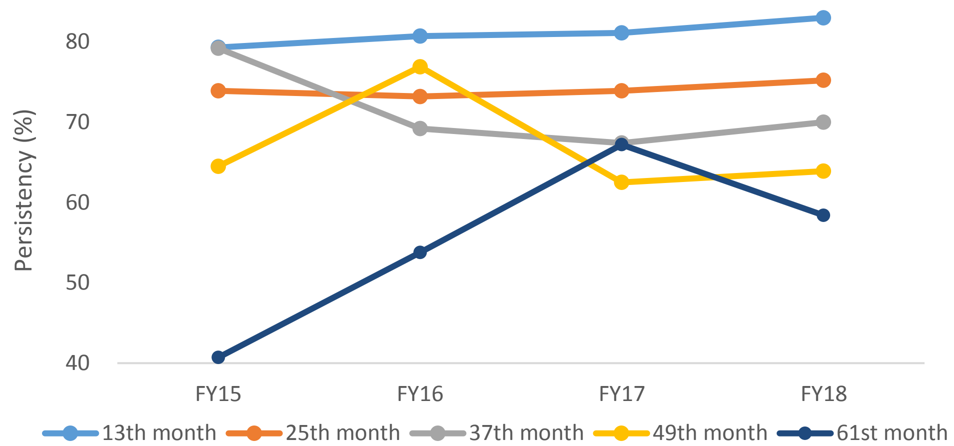
Moreover, VNB is likely to witness ~16% CAGR over FY18-21E, in-line with increase in APE backed by (a) higher new business volumes with lowering of acquisition expense, and (b) improvement in persistency ratio. The 13th month persistency has inched up to 83% in FY18 from 79.3% in FY15.

Exhibit 7: VNB trend for SBI Life



Source: Company, IIFL Research

Exhibit 8: Persistency ratio for SBI Life across periods



Source: Company, IIFL Research

Embedded value and return on embedded value (RoEV) details

SBI Life's embedded value is likely to be driven by increasing value of new business. We expect RoEV in the range of 17-18% over FY19-FY21E backed by higher APE, sustained VNB margin (~138bps over FY18-21E) and higher unwinding of discount on opening embedded value.

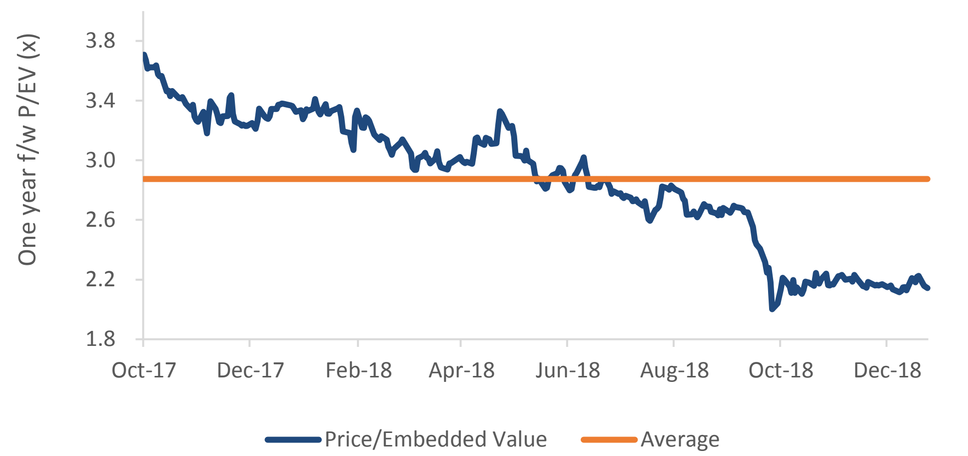
Particulars (₹cr)	FY18	FY19E	FY20E	FY21E
Opening EV	**17,420**	**20,170**	**23,213**	**27,281**
EVOP (operating variances)	3,170	3,493	4,201	4,934
Economic assumption change & investment variance	(180)	(200)	200	100
Net capital injection	(240)	(250)	(333)	(415)
Closing EV	**20,170**	**23,213**	**27,281**	**31,900**
Value of in-force (VIF)	12,700	15,580	18,180	20,968
Adjusted net worth	7,470	7,633	9,101	10,932
Embedded value	**20,170**	**23,213**	**27,281**	**31,900**
Operating RoEV (%)	17.8	17.5	18.1	18.1
RoE (%)	19.0	19.6	22.1	23.1

Source: Company, IIFL Research

Valuation rationale and matrix

SBI Life is currently trading at comfortable valuation (~2.2x FY20E P/EV) as compared to its peers. Based on embedded value methodology, we value SBI Life at 2.6x FY20E price/embedded value (providing 10% discount to average one-year forward P/EV for a period of 14 months). The valuation multiple is justified considering its strong brand, diversified distribution channels and traction in new business.

Exhibit 9: One-year forward price/EV



Source: ACE Equity, IIFL Research

Exhibit 10: Balance sheet summary and key ratios

Particulars ~₹cr	FY17	FY18	FY19E	FY20E	FY21E
Investments – Shareholders	4,296	5,014	6,006	7,191	8,521
Investments – Policyholders	91,535	1,09,422	1,29,821	1,55,101	1,85,961
Fixed Assets	538	581	620	651	683
Net current assets	2,678	2,968	6,294	6,960	8,718
Other assets	178	171	171	171	171
Total net assets	**99,225**	**1,18,156**	**1,42,912**	**1,70,074**	**2,04,054**
Shareholder's funds	5,552	6,528	7,633	9,101	10,932
Policyholder's funds	93,673	1,11,628	1,35,279	1,60,973	1,93,122
Total liabilities	**99,225**	**1,18,156**	**1,42,912**	**1,70,074**	**2,04,054**
Key Ratios					
Investment yield - Shareholder's fund (%)	9.4	9.0	8.6	8.8	9.0
Investment yield - Policyholder's fund (%)	9.9	7.6	7.6	8.1	8.3
Cost to net earned premium ratio (%)	11.7	11.3	11.6	11.5	11.5

Source: Company, IIFL Research

Key Risks

- Subdued capital markets may lead to lower new business.
- Reduction in stake by one of the promoters (mainly BNP Paribas Cardif) to comply the minimum public shareholding may lead to underperformance of stock. However, we believe the existing stock price has already factored in the above scenario.

HDFC Standard Life Insurance

CMP: ₹391; 1-year target: ₹458

Sector	Life Insurance
Recommendation	BUY
Upside	17%

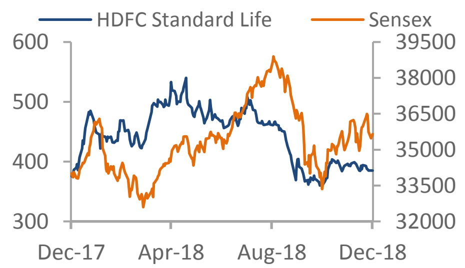
Stock Data	
Sensex	35,514
52 Week h/l (₹)	547/354
Market cap (₹ Cr)	78,689
BSE code	540777
NSE code	HDFCLIFE
FV (₹)	10
Div yield (%)	0.35

Shareholding Pattern (%)

	Mar-18	Jun-18	Sept-18
Promoters	81.0	80.9	80.8
DII+FII	11.3	11.0	10.7
Individuals	7.7	8.1	8.5

Source: ACE Equity, IIFL Research

Share Price Trend



Prices as on 03/01/2019

HDFC Standard Life Insurance Company (HDFC Life) is the largest private life insurance player in India, based on total new business premium (H1FY19). HDFC Life has best-in-class VNB margin (higher than listed peers) backed by product innovation with focus towards credit protect and annuity based products. We expect new business premium (APE) CAGR of 18% over FY18-21E driven by traction in protection business. We estimate VNB margin expansion by ~192bps over FY18-21E. We recommend BUY on the stock.

Strong market positioning backed by brand 'HDFC': HDFC Life has a leading position with market share of 21.2% (H1FY19; private life insurance) based on total new business premium. We expect HDFC Life to gain further market share due to product innovation like low-cost protection, credit protect, etc.

Focus on protection to enhance VNB margin: The share of protection business based on new business premium has increased from 17.2% in FY16 to 28.7% in H1FY19. We expect the share of protection business to increase going ahead backed by strong digital foothold.

HDFC Life's premium valuation likely to persist: HDFC Life continues to enjoy premium valuation vs. peers due to its superior margin profile, balanced product mix, blended distribution channels and strong brand recognition. We expect the valuation premium to persist going ahead and thus value it at 4.3x FY20E P/EV (providing 10% discount to average one-year forward P/EV).

Financial Summary

Particulars (₹cr)	FY17	FY18	FY19E	FY20E	FY21E
Total Premium Income	19,445	23,564	28,831	34,678	41,420
APE	4,190	5,530	6,579	7,751	9,074
VNB	923	1,282	1,575	1,913	2,278
VNB margin (%)	22.0	23.2	23.9	24.7	25.1
PAT	892	1,109	1,304	1,476	1,686
PAT growth (%)	9.2	24.4	17.6	13.2	14.2
Operating RoEV (%)	21.7	21.5	20.2	21.2	20.5
Price/Embedded Value	6.3	5.2	4.4	3.7	3.1

Source: Company, IIFL Research

Company Overview

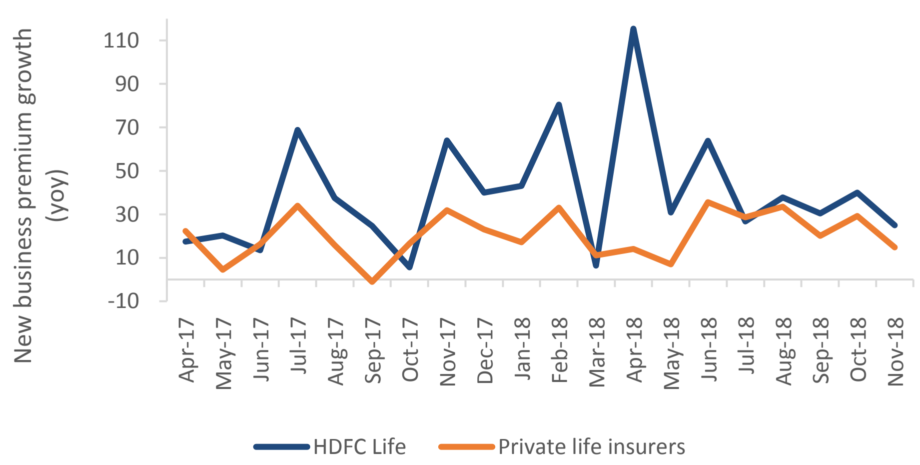
HDFC Life is a joint venture between HDFC Limited (~51.6% stake) and Standard Life Aberdeen (~29.3%). It is a leading long-term life insurance solutions provider in India, offering a range of individual and group insurance solutions. It has two wholly owned subsidiaries i.e. HDFC Pension (pension fund manager under NPS) and HDFC International Life and Re Company (reinsurance business in UAE).

Robust track record for new business vis-à-vis industry

HDFC Life has a strong track record in terms of new business premium with growth significantly higher than listed peers and overall private life insurance space. The new business premium for HDFC Life has risen by ~30% yoy in FY18 and ~40% in FY19 yoy YTD (upto November, 2018), whereas the entire private segment has registered growth of ~17% yoy in FY18 and ~23% yoy in FY19 YTD.

New business premium for HDFC Life has risen by ~30% in FY18 and ~40% in FY19 YTD yoy

Exhibit 1: HDFC Life vs. Private life insurers



Source: IRDAI, IIFL Research

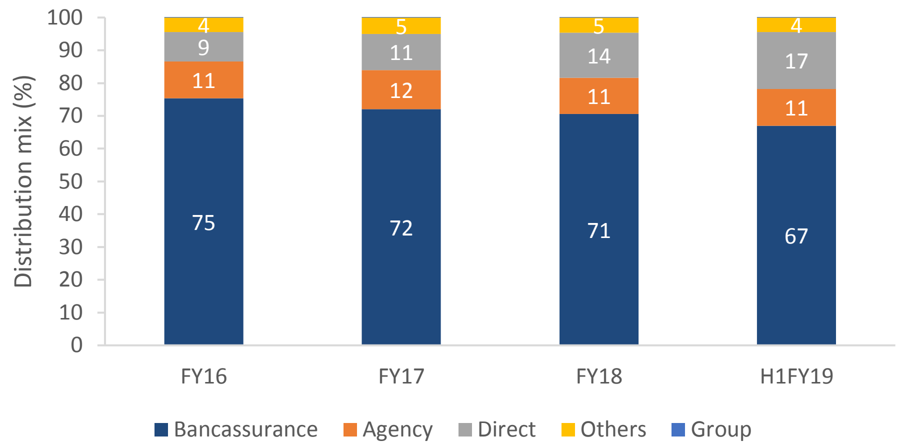
Distribution channels backed by investment in digital

Bancassurance channel continues to source maximum proportion of total individual APE for HDFC Life (~67% in H1FY19). The company has tie-ups with 170 partners under bancassurance and cross-selling.

The share of business from bancassurance channel has, however, declined on a relative basis from ~75% of total individual APE in FY16 to ~71% in FY18 due to traction under direct channel owing to online sourcing of policies. We expect HDFC Life's investment towards digital platform and mobility to reap benefits for sourcing new business on an absolute basis.

Banca channel sources ~67% (H1FY19) of the total individual APE

Exhibit 2: Distribution channels mix



Source: Company, IIFL Research

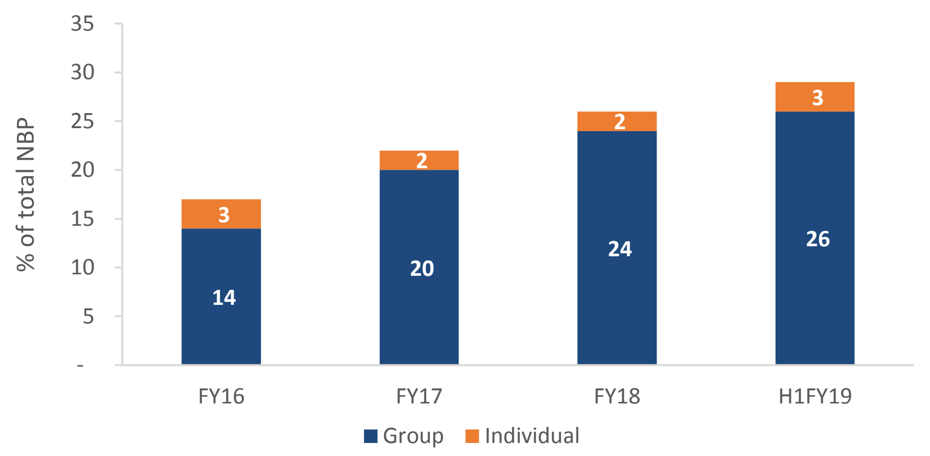
Higher salience towards protection segment

The contribution from protection products in total new business premium (especially group business) has increased from ~17% in FY16 to ~26% in FY18 (~29% in H1FY19). HDFC Life's long term strategy is to continue to bank upon the opportunity under protection segment including retail credit.

HDFC Life has gained traction under group protection (~26% of total NBP in H1FY19) majorly through group credit products. According to the company, the average rate charged on group credit protection business is 30% higher than that on individual protection product. This provides higher value in terms of margin for HDFC Life.

Protection mix has increased from 17% in FY16 to 26% in FY18

Exhibit 3: Increasing share of protection business



Source: Company, IIFL Research

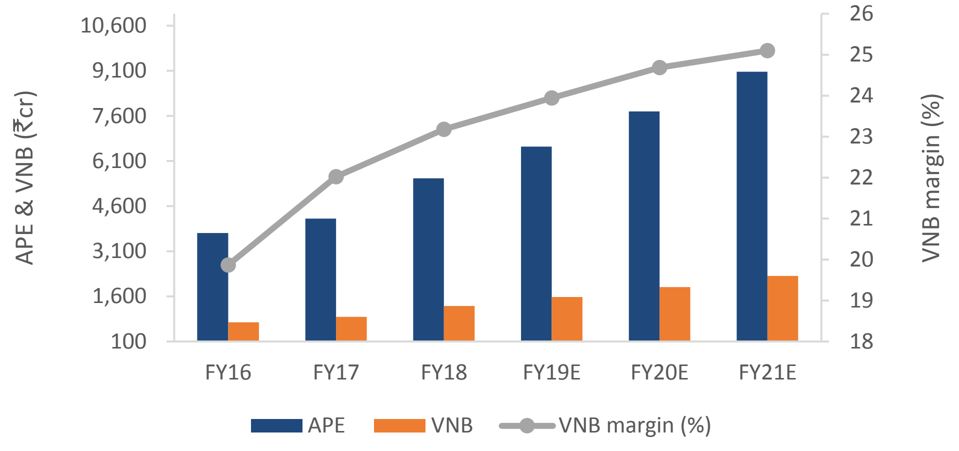
Overall, we expect HDFC Life to remain a strong proxy play under protection segment. However, we expect the company's margin to moderate going ahead on account of increasing competitiveness in the similar category by other private insurance players.

Room for improvement in new business (VNB) margin

HDFC Life's VNB margin has increased significantly by ~331bps over FY16-18 on the back of rising share of new business from high margin protection business. Traction in protection segment coupled with new product launches and improvement in persistency across periods would further aid margin. However, this would be neutralized by incremental operating costs towards protection segment and investments towards digital technology. Overall, we expect VNB margin to expand by ~192bps to ~25% over FY18-21E.

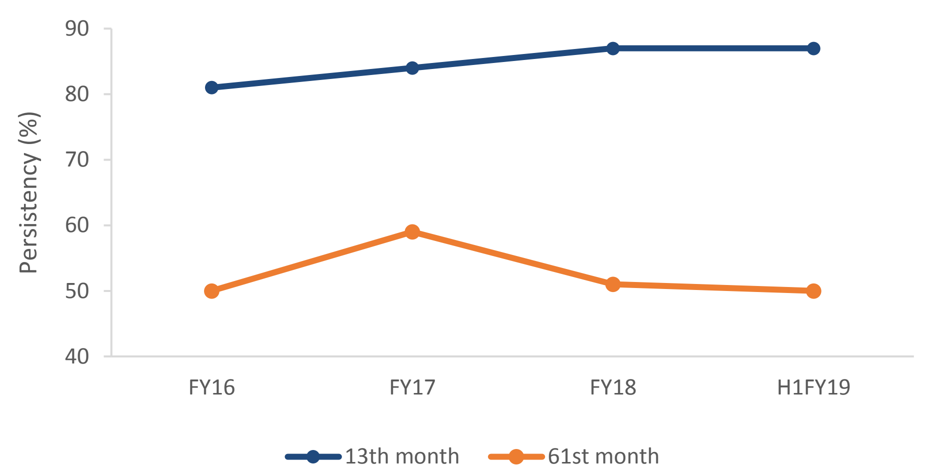
VNB margin has increased significantly by ~331bps over FY16-18 on the back of rising share of new business from Protection

Exhibit 4: APE and VNB margin trend for HDFC Life



Source: Company, IIFL Research

Exhibit 5: Persistency trend for HDFC Life



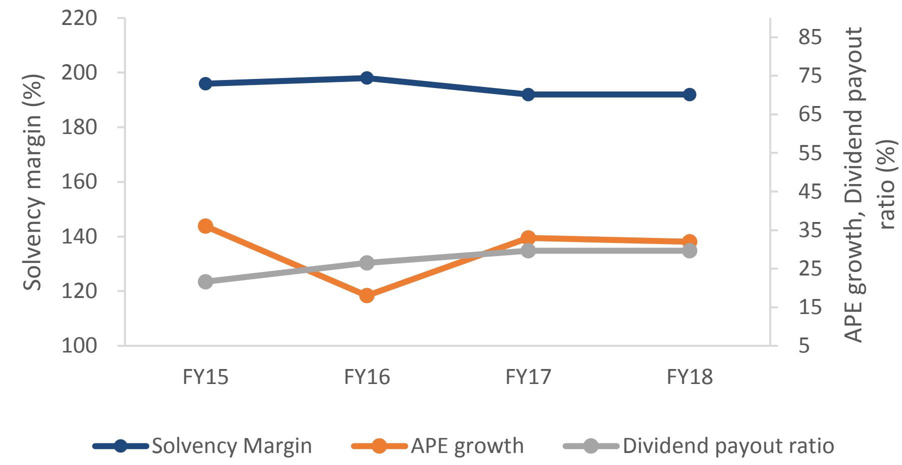
Source: Company, IIFL Research

Stable solvency despite growth in the underlying business

Internal accruals from in-force policies to keep the solvency position stable

HDFC Life's solvency ratio stood at 193% as on September 30, 2018. The company, despite not raising capital over last seven years (except in form of ESOPs), has maintained healthy dividend payout ratio. The new business growth and dividend payout have been funded through the internal accruals of the surplus from the in-force policies. The management has stated that capital infusion would not be required in the scenario of 50% CAGR in new business APE over FY18-21E due to strong internal accruals.

Exhibit 6: Stable solvency position - HDFC Life



Source: Company, IIFL Research

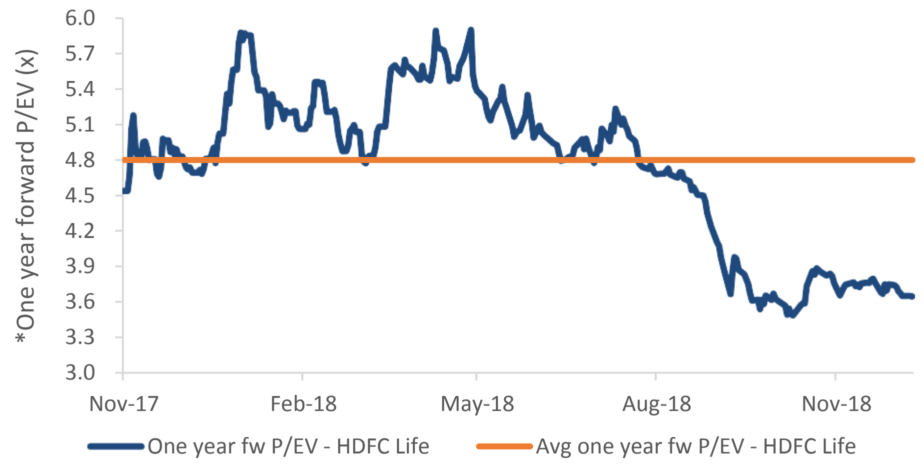
HDFC group always commands rich valuations

HDFC Life has expensive stock valuation since its listing on the stock exchanges in November, 2017. The average one year forward price to embedded value of the stock is 4.8x for the period of over 13 months since listing. This is on account of following reasons:

- Leadership in VNB margin vs. listed peers
- Consistent ROEV of more than 20% over FY16-18
- Traction in high value protection segment
- Experienced management and brand pedigree

HDFC group trades at a premium valuation on account of consistent financial performance of the group. HDFC Limited has traded at an average premium of ~30% since April, 2017 as compared to Nifty Bank index. We value HDFC Life at ~4.3x FY20E price to embedded value (providing 10% discount to average one-year forward P/EV).

Exhibit 7: One year forward valuation - HDFC Life



*Source: Company, IIFL Research; *HDFC Standard Life listed on November 17, 2017*

HDFC Ltd has traded at an average premium of more than 30% since April, 2017 as compared to Nifty Bank index

Exhibit 8: HDFC Ltd vs. Bank Nifty - Forward valuation

Source: Company, IIFL Research

Exhibit 9: Embedded value and return on embedded value (RoEV)

Particulars (₹ in cr)	FY17	FY18	FY19E	FY20E	FY21E
Opening EV	**10,230**	**12,470**	**15,216**	**17,796**	**21,322**
EVOP (Operating variances)	2,220	2,682	3,071	3,769	4,373
Economic assumption change & investment variance	255	260	(100)	200	100
Net capital injection	(235)	(196)	(391)	(443)	(506)
Closing EV	**12,470**	**15,216**	**17,796**	**21,322**	**25,289**
Value of In-force (VIF)	8,327	10,362	12,210	14,788	17,672
Adjusted Net Worth	4,143	4,854	5,586	6,534	7,617
Embedded Value	**12,470**	**15,216**	**17,796**	**21,322**	**25,289**
Operating RoEV (%)	21.7	21.5	20.2	21.2	20.5
RoE (%)	25.5	25.8	25.2	24.4	23.8

Source: Company, IIFL Research

Exhibit 10: Balance sheet summary

Particulars ~₹cr	FY17	FY18	FY19E	FY20E	FY21E
Investments - Shareholders	3,246	4,070	4,881	5,828	6,960
Investments - Policyholders	88,492	1,02,533	1,16,516	1,34,149	1,55,329
Fixed Assets	353	341	363	381	399
Net current assets	(853)	(1,128)	(852)	(623)	(1,817)
Other assets	48	19	19	19	19
Total net assets	**91,286**	**1,05,835**	**1,20,927**	**1,39,754**	**1,60,890**
Shareholder's funds	3,839	4,749	5,586	6,534	7,617
Policyholder's funds	87,447	1,01,086	1,15,341	1,33,220	1,53,273
Total liabilities	**91,286**	**1,05,835**	**1,20,927**	**1,39,754**	**1,60,890**
Key Ratios					
Investment yield - Shareholder's (%)	7.7	7.7	7.4	7.7	7.8
Investment yield - Policyholder's (%)	13.9	9.0	7.0	8.0	8.0
Cost to net earned premium ratio(%)	16.5	18.1	18.2	17.8	17.9

Source: Company, IIFL Research

Key Risks

- New product launches by competitors under protection segment could result into mean reversion of the VNB margin.
- Regulatory clampdown on premium rates under credit protect business could lead to business moderation.

Annexure - Life insurance metrics

	Key terminologies	Abbreviation	Explanation
Income	Gross Written Premium	GWP	Total premium collected during the period. It comprises premium from new customers (new business premium) and existing customers (renewal premium).
	Annualised Premium Equivalent	APE	Sum of annualised first year premiums on regular premium policies plus 10% of single premium policies.
	Retail Weighted Received Premium	RWRP	100% of first year premiums on retail regular premium policies plus 10% of single premiums received from customers during the year.
Profitability	Value of New Business	VNB	VNB is a measure of future profit streams of the new business written during the year. It is the present value of future profits to shareholders as measured in the year in which the business is written.
	Value of New Business margin	VNB margin	VNB margin is the ratio of VNB for the period to APE for the period. It is similar to the profit margin for any other business.
	New Business Strain	-	The accounting loss associated with the initial years of a life insurance policy is referred to as strain.
Embedded Value	Embedded Value	EV	It is similar to the Book Value of companies in other sectors. It is sum of the Company's net worth and the present value of all future profits to shareholders from the existing book of the company (including new business written in the year).
	Embedded Value Operating Profit	EVOP	The key components of EVOP are expected investment income on opening EV (unwind), value of new business added during the year and EV variances. EV variance is a measure of the performance as compared to what was assumed in arriving at the EV at the beginning of the year.
Quality of Business	Persistency	-	It measures the proportion of policyholders who have continued with their policies. It indicates ability of the company to retain customers. Maintaining high level of persistency is critical as it provides scope of regular revenues through renewals. The 13th month persistency ratio typically reflects the quality of sales performance. The 49th month persistency ratio enables to assess the proportion of customers paying all premiums as majority of regular premium contracts have a minimum premium payment period of five years.
Financial Position	Solvency Ratio	-	Solvency is a regulatory measure of capital adequacy. It is expressed as a ratio of available capital and required capital. It is critical in determining the ability to meet future contingencies and fund growth plans. A high solvency ratio instills confidence in customers and investors in the ability of the company to pay claims. The control level of solvency ratio is 150%.

Recommendation Parameters for Fundamental/Technical Reports:

Buy – Absolute return of over +10%
Accumulate – Absolute return between 0% to +10%
Reduce – Absolute return between 0% to -10%
Sell – Absolute return below -10%

Please refer to http://www.indiainfoline.com/research/disclaimer for recommendation parameter, analyst disclaimer and other disclosures.

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