

April 18, 2018

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Rating	BUY
Price	Rs492
Target Price	Rs518
Implied Upside	5.3%
Sensex	34,332
Nifty	10,526

(Prices as on April 18, 2018)

Trading data

Market Cap. (Rs bn)	991.6
Shares o/s (m)	2,011.7
3M Avg. Daily value (Rs m)	964.7

Major shareholders

Promoters	80.97%
Foreign	8.92%
Azim Premji Trust	2.41%
Public & Other	7.70%

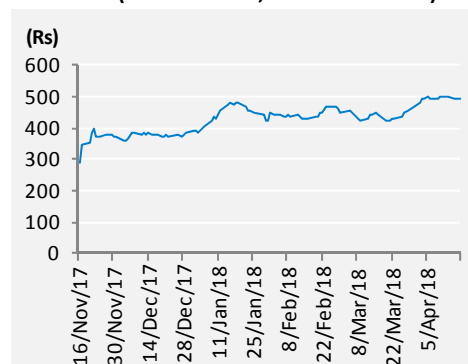
Stock Performance

(%)	1M	6M	12M
Absolute	10.8	NA	NA
Relative	7.4	NA	NA

How we differ from Consensus

EPS (Rs)	PL	Cons.	% Diff.
2019	5.6	NA	NA
2019	6.5	NA	NA

Price Perf. (RIC: HDFC.BO, BB: HDFCLIFE IN)



Source: Bloomberg

HDFC SL showed strong performance in APE growth at 32% YoY for FY18 slightly below our expectations (Pl: 35% YoY) mainly led by ULIPs. However, margins improved significantly by 120bps at 23.2% mainly on increase in share of protection segment (25.9% share of total new business premium) as it benefits from innovation and digitisation despite price competition. We have revised the APE growth estimates slightly and increased VNB margins. We maintain our recommendation of a BUY, and revise our TP to Rs518 (from Rs500) and value it at Rs1,040 bn (from Rs996 bn) translating to 4.3x FY20E EV.

- APE growth was quite robust compared to peers:** HDFC SL's total APE growth was strong at 32% YoY for FY18 while individual APE growth stood at ~31% YoY led by ULIPs (43.3% YoY growth). Participating segment has been slowing down for the company with ~5% growth YoY for FY18. Thus there was change in mix skewed towards ULIP at 57% (52% in FY17) and PAR at 28% (35% in FY17). However, management is comfortable with ULIP share at 55-60% of individual APE mix.
- Protection business has been driving profitability:** HDFC SL has grown its protection business with the help of 149 banca partnerships (117 in FY17) and currently stands at 11.3% on APE basis FY18. It continues to enjoy the market leader position in group credit life business growing at 63% YoY whereas it has been doing fairly well in individual and health protection segment as well. The company has seen continuous uptick in margins in protection segment despite price competition as it has benefitted largely on innovation (*Click2series products*) and digitisation.
- Operating metrics seen good improvement:** HDFC SL's persistency has improved in all the buckets except 61st on account of particular cohort which didn't so well in FY13 and the lag effect is continuing. Once this effect comes off, persistency will look good for 61st month as well as company has been making efforts and started with revival programs and other cohorts have been doing well. Margins for the company have shown significant improvement of 120bps YoY at 23.2% for FY18. This expansion has largely been contributed by growth in protection segment. We believe margins to improve further as share of protection increases and ULIP mix remains in the same range.

Key financials (Y/e March)	2017	2018E	2019E	2020E
Net Premiums (Rs m)	1,92,749	2,36,922	2,97,220	3,75,361
Growth (%)	19.1	22.9	25.5	26.3
Total Income (Rs m)	3,05,544	3,56,819	4,34,004	5,27,769
Surplus / Deficit (Rs m)	9,477	10,652	12,301	14,760
PAT (Rs m)	8,921	9,863	11,209	13,110
Growth (%)	9.0	10.6	13.7	17.0
EPS (Rs)	4.5	4.9	5.6	6.5
Embedded Value (Rs bn)	124.7	152.1	191.0	240.9

Profitability & Valuation	2017	2018E	2019E	2020E
NBP Margin Post overrun (%)	22.0	23.2	24.0	25.1
RoE (%)	25.5	23.6	23.0	23.1
Operating RoEV (%)	21.7	21.5	23.6	24.5
RoEV (%)	24.2	23.6	26.9	27.2
Dividend Yield (%)	0.2	0.3	0.3	0.4
Price / EV (x)	8.0	6.5	5.2	4.1

Source: Company Data; PL Research

Exhibit 1: Profitability has increased as share of protection widens

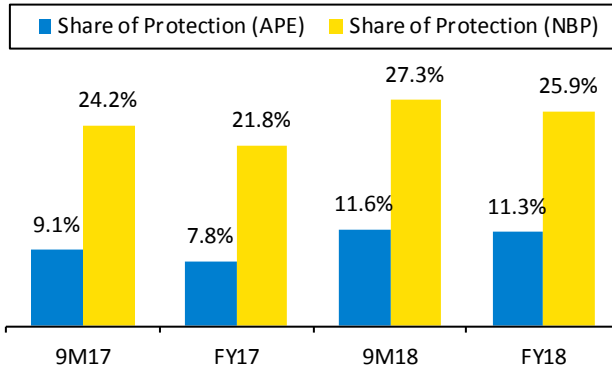
(Rs m)	Q4FY18	Q4FY17	YoY gr. (%)	Q3FY18	QoQ gr. (%)
Policyholders' Account					
Gross Premium Income	89,564	72,241	24.0	54,677	63.8
Net Premium Income	89,000	71,784	24.0	54,200	64.2
Income from Investments (Net)	(9,368)	48,662	(119.3)	42,531	(122.0)
Total (A)	81,346	1,20,870	(32.7)	96,845	(16.0)
Net Commission	4,087	3,401	20.2	2,625	55.7
Opex related to Insurance	10,998	8,076	36.2	7,769	41.6
Benefits Paid (Net)	44,111	28,637	54.0	31,200	41.4
Change in actuarial liability	15,725	76,082	(79.3)	52,673	(70.1)
Total (B)	77,379	1,18,038	(34.4)	95,047	(18.6)
Surplus / (Deficit)	3,968	2,832	40.1	1,797	120.8
Shareholders' Account					
Trf from Policyholders A/c	3,965	2,104	88.4	1,499	164.6
Investment Income	974	830	17.3	618	57.6
Total	4,939	2,934	68.3	2,117	133.3
Expenses other than related to insurance	6	174	(96.4)	7	(12.5)
Profit/(Loss) before Tax	3,390	2,576	31.6	2,162	56.8
Provision for Taxation	(79)	106	(174.5)	89	(189.1)
Profit/(Loss) after Tax	3,468	2,470	40.4	2,073	67.3

Source: Company Data, PL Research

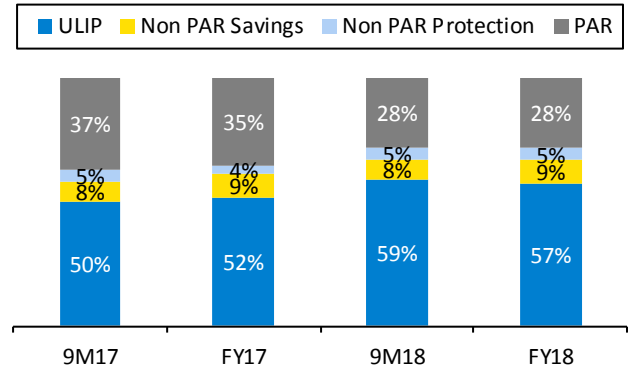
Exhibit 2: Key Data Points

	4Q18	4Q17	YoY Chg.	FY18	FY17	YoY Chg.
Individual APE	18.1	16.3	11.0	48.9	37.4	30.7
Group Premium	19.1	15.7	21.7	54.9	45.0	22.0
EV	NA	NA		152.2	124.7	22.1
Op RoEV (%)	NA	NA		21.5%	21.7%	(0.2)
VNB	5.0	3.9	28.2	12.8	9.2	39.1
NBAP Margins (%)	25.1	22.3	2.8	23.2	22.0	1.2

Source: Company Data, PL Research

Exhibit 3: Share of protection has been increasing led by credit biz


Source: Company Data, PL Research

Exhibit 4: Share of ULIPs has increased on YoY basis to large extent


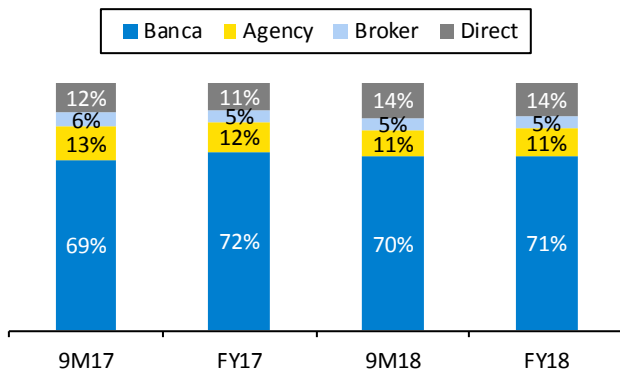
Source: Company Data, PL Research

Exhibit 5: Individual APE premium breakup on product basis

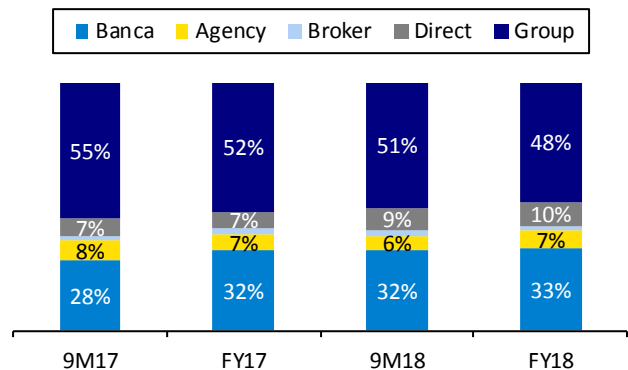
Growth in ULIP was cautiously lower as management is comfortable ULIP to be at 55-60% of the individual new business mix

	4Q18	4Q17	YoY Chg.	FY18	FY17	YoY Chg.
ULIP	55%	55%	0.5	57%	52%	5.0
Non PAR Savings	11%	10%	0.7	9%	9%	-
Non PAR Protection	5%	3%	2.4	5%	4%	1.0
PAR	29%	32%	(3.6)	28%	35%	(7.0)
<hr/>						
ULIP	9.70	8.90	9.0	27.87	19.45	43.3
Non PAR Savings	1.94	1.68	15.4	4.40	3.37	30.7
Non PAR Protection	0.91	0.44	105.2	2.45	1.50	63.4
PAR	5.07	5.28	(4.1)	13.69	13.09	4.6

Source: Company Data, PL Research

Exhibit 6: Individual sourcing mix: Banca remains dominant source


Source: Company Data, PL Research

Exhibit 7: Total sourcing mix: Direct share is gradually increasing


Source: Company Data, PL Research

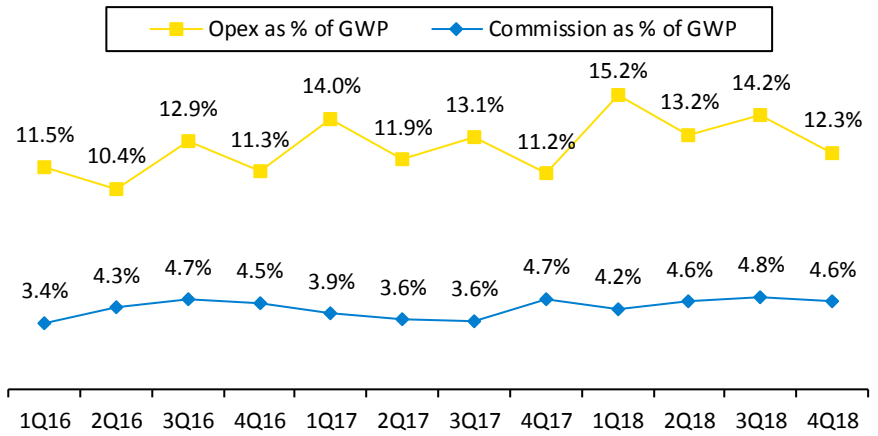
Direct channel has shown good traction in growth and the momentum continues

Exhibit 8: Individual APE premium breakup on sourcing basis

	4Q18	4Q17	YoY Chg.	FY18	FY17	YoY Chg.
Corp Agents	71%	76%	(5.1)	71%	72%	(1.0)
Agency	11%	11%	0.0	11%	12%	(1.0)
Broker	5%	4%	1.2	5%	5%	-
Direct	14%	10%	3.9	14%	11%	3.0
Corp Agents	13.16	12.37	6.4	34.72	26.93	28.9
Agency	1.99	1.75	14.1	5.38	4.49	19.9
Broker	0.91	0.60	49.8	2.45	1.87	30.7
Direct	2.53	1.58	60.2	6.85	4.11	66.4

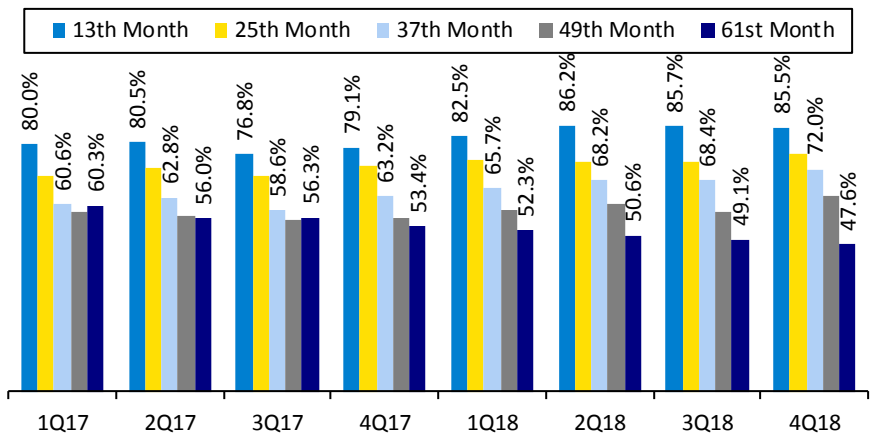
Source: Company Data, PL Research

Exhibit 9: Opex Ratios have increased slightly as company continues to do investments

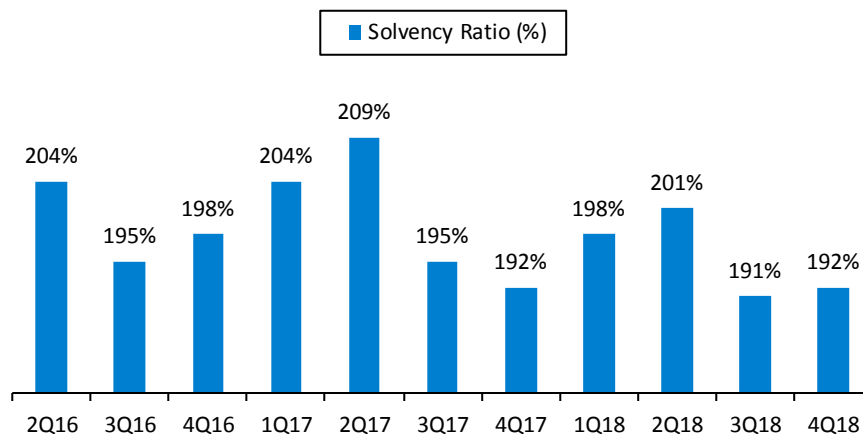


Source: Company Data, PL Research

Exhibit 10: Persistency Ratio has improved and trickled down to lower buckets



Source: Company Data, PL Research

Exhibit 11: Solvency Ratio decreased slightly yet at healthy level


Source: Company Data, PL Research

Exhibit 12: Estimates change table – We tweak our estimates on APE growth

Rs Bn	Old		Revised		% Change	
	FY19E	FY20E	FY19E	FY20E	FY19E	FY20E
APE	75.2	97.7	74.0	97.5	(1.6)	(0.2)
VNB	17.4	23.0	17.8	24.5	2.2	6.5
VNB Margin (%)	23.1	23.6	24.0	25.1	0.9	1.6
EV	192.6	238.6	191.0	240.9	(0.8)	1.0
Price target (Rs)	500		518		3.6	
Recommendation	BUY		BUY			

Source: Company Data, PL Research

Exhibit 13: We increase our TP to Rs518 (from Rs500) on 4.3x (from 4.2x) FY20E P/EV

PT calculation and upside	
Op RoEV	24.5%
CoE	11.8%
g	5.0%
Embedded value	240.9
Price / Embedded value	4.3
Appraisal Value	1,040
Number of shares, mn	2,012
Valuation per share	518
CMP	492
<i>Upside (%)</i>	5.3%

Source: Company Data, PL Research

Exhibit 14: Key metrics and EV movement

Rs bn	FY13	FY14	FY15	FY16	FY17	FY18	FY19E	FY20E
APE	32.5	25.2	31.8	36.2	40.9	55.4	74.0	97.5
YoY growth (%)		-22.2	26.2	13.5	13.0	35.7	33.5	31.6
NBV	6.0	6.6	7.4	7.2	9.2	12.8	17.8	24.5
YoY growth (%)		10.0%	12.1%	-2.8%	28.2%	38.9%	38.5%	38.1%
EV Movement								
Opening IEV	48.2	58.7	69.9	88.0	102.3	124.7	152.1	191.0
New Business Value	6.0	6.6	7.4	7.2	9.2	12.8	17.8	24.5
EVOP	9.6	11.1	15.2	14.3	22.2	26.8	35.9	46.9
Dividend payout	-	1.2	1.7	2.2	2.4	2.0	2.1	2.0
Closing EV	58.7	69.9	88.0	102.3	124.7	152.1	191.0	240.9
<i>Adjusted Net worth</i>	<i>16.9</i>	<i>20.1</i>	<i>27.9</i>	<i>32.9</i>	<i>41.4</i>	<i>48.1</i>	<i>55.6</i>	<i>64.2</i>
<i>Value in force (VIF)</i>	<i>41.8</i>	<i>49.8</i>	<i>60.1</i>	<i>69.4</i>	<i>83.3</i>	<i>104.0</i>	<i>135.5</i>	<i>176.7</i>
Ratios (%)								
NBAP margins	12.7	15.2	18.5	19.9	22.0	23.2	24.0	25.1
RoEV	21.8	21.1	28.3	18.8	24.2	23.6	26.9	27.2
Operating RoEV	19.9	18.9	21.8	16.3	21.7	21.5	23.6	24.5

Source: Company Data, PL Research

Appendix

Exhibit 15: Policyholders' Account (Technical Account)

Technical account (Rs m)	FY12	FY13	FY14	FY15	FY16	FY17	FY18E	FY19E	FY20E
Net earned premium	1,01,561	1,12,648	1,19,764	1,47,625	1,61,788	1,92,749	2,36,922	2,97,220	3,75,361
Investment income	2,407	25,424	50,733	1,22,495	17,906	1,11,406	1,18,343	1,35,043	1,50,435
Other income	367	276	2,412	789	971	1,389	1,554	1,741	1,972
Total Revenue	1,04,335	1,38,348	1,72,910	2,70,908	1,80,665	3,05,544	3,56,819	4,34,004	5,27,769
Commission expense	5,776	6,394	5,141	6,235	7,018	7,920	9,333	11,350	13,367
Operating expense	12,695	13,438	12,807	14,890	18,718	23,853	28,232	34,932	41,835
Benefit Cost	82,072	1,11,517	1,47,532	2,38,864	1,41,700	2,60,551	3,02,713	3,68,679	4,49,995
Total expense	1,00,544	1,31,865	1,68,611	2,62,688	1,71,068	2,96,067	3,46,167	4,21,703	5,13,008
Surplus / Deficit	3,792	6,483	4,299	8,220	9,597	9,477	10,652	12,301	14,760

Source: Company Data, PL Research

Exhibit 16: Shareholders' Account (Revenue Account)

Shareholder's a/c (Rs m)	FY12	FY13	FY14	FY15	FY16	FY17	FY18E	FY19E	FY20E
Transfer from policyholders account	2,505	3,937	7,654	6,709	7,182	7,863	8,503	9,884	12,574
Investment income	466	712	1,141	2,009	1,688	2,269	2,775	2,805	2,248
Expenses	261	92	2,370	672	626	991	897	890	1,022
Profit before tax	2,710	4,557	6,425	8,046	8,350	9,141	10,382	11,799	13,800
Tax expenses	0	42	-828	191	166	220	519	590	690
Profit after tax	2,710	4,515	7,253	7,855	8,184	8,921	9,863	11,209	13,110

Source: Company Data, PL Research

Exhibit 17: Balance Sheet

Balance sheet (Rs m)	FY12	FY13	FY14	FY15	FY16	FY17	FY18E	FY19E	FY20E
Sources of Fund									
Shareholders' Fund	22,098	22,042	22,131	25,919	31,586	38,387	45,089	52,546	61,176
Borrowings	-	-	-	-	-	-	-	-	-
Policyholders' Funds:									
Insurance reserves and provisions	3,09,622	3,82,315	4,85,781	6,42,608	7,01,812	8,65,806	10,53,887	12,85,463	15,70,051
Others	4,603	6,486	3,130	4,641	7,055	8,668	13,002	19,503	29,254
Total	3,36,323	4,10,843	5,11,041	6,73,168	7,40,454	9,12,860	11,11,978	13,57,511	16,60,481
Application of Funds									
Shareholders' inv	5,894	8,338	16,156	21,962	26,402	32,456	29,215	26,876	26,022
Policyholders' inv	79,903	1,07,273	1,47,062	1,99,085	2,58,629	3,46,915	4,76,425	6,41,463	8,51,090
Assets to cover linked liabilities	2,36,098	2,83,331	3,42,074	4,49,203	4,57,270	5,38,005	6,13,325	6,99,191	7,97,078
Net Current Assets	-2,230	-392	-459	-2,358	-6,741	-8,523	-11,668	-15,493	-20,127
Other Assets	16,058	12,293	6,209	5,276	4,894	4,007	4,680	5,475	6,418
Total	3,35,723	4,10,843	5,11,042	6,73,168	7,40,454	9,12,860	11,11,978	13,57,511	16,60,481

Source: Company Data, PL Research

Exhibit 18: Embedded Value

Embedded Value (Rs m)	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19E	FY20E
Embedded Value	48,160	58,660	69,860	87,960	1,02,300	1,24,681	1,52,137	1,91,022	2,40,927
Annualised Premium Equivalent (APE)	30,851	32,454	25,240	31,843	36,156	40,852	55,444	74,037	97,467
New Business Value		6,000	6,600	7,400	7,195	9,225	12,816	17,752	24,510
New Business Margin (%)		18.5%	26.1%	23.2%	19.9%	22.6%	23.2	24.0	25.1
EV Operating Profit		9,600	11,100	15,200	16,632	22,193	26,825	35,938	46,884
Operating RoEV (%)		19.9	18.9	21.8	18.3	21.7	21.5	23.6	24.5

Source: Company Data, PL Research

Exhibit 19: Key Ratios

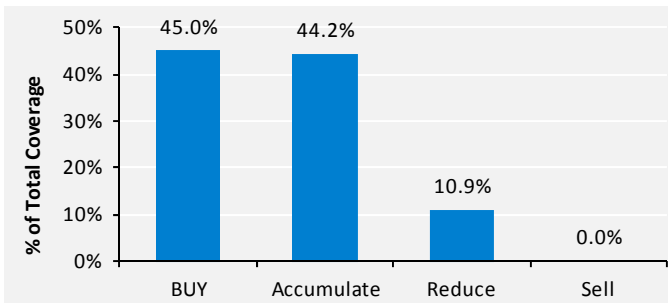
Key ratios	FY12	FY13	FY14	FY15	FY16	FY17	FY18E	FY19E	FY20E
Commission expense/GWP (%)	5.7	5.6	4.3	4.2	4.3	4.1	3.9	3.8	3.5
Operating expense/GWP (%)	12.4	11.9	10.6	10.0	11.5	12.3	11.8	11.7	11.0
Total expense/GWP (%)	18.1	18.0	14.9	14.2	15.8	16.3	15.7	15.4	14.6

Source: Company Data, PL Research

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Sell	:	Over 15% underperformance to Sensex over 12-months
Trading Buy	:	Over 10% absolute upside in 1-month
Trading Sell	:	Over 10% absolute decline in 1-month
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