24 July 2018

1QFY19 Results Update | Sector: Insurance

ICICI Prudential Life Insurance

BSE SENSEX	S&P CNX
36,825	11,134

CMP: INR385 **TP: INR450 (+17%)** **Buy**

Bloomberg	IPRU IN
Equity Shares (m)	1,435
M.Cap.(INRb)/(USDb)	553.1 / 8.0
52-Week Range (INR)	471 / 347
1, 6, 12 Rel. Per (%)	-4/-13/-32
12M Avg Val (INR M)	614
Free float (%)	21.3

Financials & Valuations (INR b)

Y/E MARCH	2018	2019E	2020E
Net Premiums	268.1	310.0	366.1
Surplus / Deficit	13.6	13.7	16.1
Sh.holder's PAT	16.2	16.6	18.0
New bus.gr-unwtd (%)	16.2	13.0	18.0
New bus gr- APE (%)	16.0	12.5	16.2
Total prem gr - unwtd (%)	20.3	16.9	18.2
Solvency ratio (%)	252.5	224.7	205.6
NBP margin (%)	16.5	18.0	18.7
RoEV (%)	16.1	16.8	16.0
Total AUMs (INRb)	1,395	1,603	1,825
VNB (INRb)	12.9	15.3	18.4
EV (INRb)	187.8	219.3	254.4
Valuations			
P/EV (x)	2.9	2.5	2.2
P/EPS (x)	34.2	33.4	30.8

Mixed quarter; higher opex remains a drag on earnings

- IPRU reported a muted 1QFY19 performance, with shareholder net profits declining 31% YoY (25% miss) even as policyholder surplus stood in line at INR3b (est. of INR3b). Key highlights of 1QFY19: (a) 13% YoY growth in net premium income due to a 13% decline in new business premium. (b) Total commission expenses grew 29.3% YoY due to a change in product mix, while opex increased 44.5% due to higher advertisement/employee cost. (c) New business margin improved to 17.5% from 16.5% in FY18. (d) Share of protection business in total APE increased to 8.2%. (e) 49th month persistency improved by 450bp to 63.7%.
- **Premium growth muted; protection business now forms 8.2% of total APE:** IPRU reported an 18% YoY decline in total APE. Savings APE declined 21% YoY to INR12.8b, while protection APE grew strongly by 48% YoY to INR1.1b. Share of ULIPs in total new business APE stood at 79.8%, while that of protection business improved further to 8.2% (4.5% in 1QFY18). IPRU continues witnessing strong growth opportunity in the protection business, and we expect the business to account for ~10% of total premiums by FY20.
- **Operating metrics continue improving; new business margin expands to 17.5%:** IPRU reported a continued improvement in the persistency rate across various tenures. The 49th month persistency, thus, improved to 63.7% from 62.3% in FY18. New business margin has also expanded to 17.5% v/s 16.5% in FY18, helping drive 34% VNB growth. Product mix improvement remains the single-biggest driver of margin expansion.
- **Sharp rise in commission and operating expenses drags earnings:** New business commission increased to INR2.1b (from INR1.5b in 1QFY18) due to a change in product mix and growth in protection premium, while operating expenses rose 41% YoY mainly due to increased advertisement/employee cost. Total cost ratio was up 330bp YoY to 17.5%, though management indicated it to improve further as premium growth recovers. The share of agency channel/direct channel in the distribution mix dropped to 21.8%/11.7% from 30.5%/14.2% in 1QFY18.
- **Other highlights:** (a) Solvency ratio was down to 234.6% from 252% in FY18, primarily due to dividend payment and higher strain on account of an increase in the protection business. Management decided to moderate dividend payout, and thus, discontinue with special dividend. (b) Mortgage remains the dominant segment in the credit protect business.
- **Valuations to be driven by operating performance:** We have cut our PAT estimates by ~14%/17% for FY19/FY20 to factor in lower premium income and higher strain from new business due to an increase in share of protection business. We expect IPRU to deliver a 14.4% CAGR in new business APE over FY18-20, while margins are likely to improve from the current levels of ~17.5%. We, thus, estimate 20% CAGR in VNB over FY18-20, while RoEV is expected to sustain at ~16.5%. We value IPRU at INR450 per share, which corresponds to 2.5x FY20E EV. Maintain **Buy**.

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Exhibit 1: Quarterly performance (INRm)

Policyholder's account (INRm)	FY18				FY19				1Q19E	A v/s E
	1Q	2Q	3Q	4Q	1Q	2QE	3QE	4QE		
Net premium income	48,202	65,395	67,951	86,558	54,378	74,406	80,607	1,05,409	50,749	7%
Income from investments	35,177	28,130	65,442	(16,134)	23,212	39,467	42,755	55,911	26,323	-12%
Total income	**83,545**	**93,693**	**1,33,568**	**71,369**	**78,712**	**1,14,122**	**1,23,632**	**1,61,673**	**77,239**	**2%**
Commission paid	2,162	3,632	3,773	4,466	2,795	3,788	4,103	5,366	2,506	12%
Operating expenses	4,120	4,921	5,211	6,048	5,952	6,280	6,803	8,896	4,277	39%
Benefits paid	39,690	40,711	46,852	45,555	29,395	56,437	61,140	79,952	38,554	-24%
Change in actuarial liability	32,220	39,172	72,602	10,481	35,801	44,078	47,751	62,444	28,691	25%
Tax	262	228	237	475	306	224	242	317	122	151%
Surplus/(Deficit)	**3,965**	**3,554**	**3,372**	**2,740**	**3,009**	**3,294**	**3,569**	**4,667**	**3,073**	**-2%**
Shareholders' Account										
Amt trf frm P/H account	3,334	2,850	2,742	1,967	2,464	2,635	2,962	3,796	3,012	-18%
Income from investments	1,038	1,725	2,160	2,473	1,396	1,798	1,948	2,547	1,199	16%
Total income	**4,373**	**4,578**	**4,904**	**4,482**	**3,864**	**4,447**	**4,925**	**6,363**	**4,220**	**-8%**
Total expenses	**93**	**87**	**93**	**868**	**1,024**	**332**	**359**	**470**	**221**	**363%**
PBT	**4,281**	**4,491**	**4,810**	**3,614**	**2,840**	**4,115**	**4,565**	**5,893**	**3,999**	**-29%**
Tax	221	279	289	208	24	346	375	490	267	-91%
PAT	**4,059**	**4,212**	**4,521**	**3,406**	**2,816**	**3,769**	**4,190**	**5,403**	**3,731**	**-25%**
Key metrics (INRb)										
AUM	1,265.9	1,305.9	1,383.0	1,395.3	1,426.6	1,485.7	1,544.7	1,603.7		
EV	0.0	172.1	0.0	187.9	0.0	73.1	146.2	219.3		

Source: Company, MOSL

Exhibit 2: Quarterly snapshot

INRm	FY17				FY18				FY19	Change	
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q	1Q	YoY (%)	QoQ (%)
Net premium income	35,088	54,225	56,975	75,264	48,202	65,395	67,951	86,558	54,378	13	-37
Income from investments	53,564	37,094	-6,652	65,763	35,177	28,130	65,442	-16,134	23,212	-34	-244
Other income	139	153	153	144	164	170	175	192	197	20	3
Total income	88,844	91,441	50,474	1,41,171	83,545	93,693	1,33,568	71,369	78,712	-6	10
Commission paid	1,257	1,829	1,995	2,508	2,162	3,632	3,773	4,466	2,795	29	-37
Operating expenses	5,520	5,433	5,551	7,068	4,120	4,921	5,211	6,048	5,952	44	-2
Total commission & opex	6,777	7,262	7,546	9,576	6,282	8,553	8,984	10,513	8,747	39	-17
Total expenses	85,628	86,860	46,234	1,37,395	78,192	88,435	1,28,438	66,550	73,943	-5	11
Tax	4	356	234	194	262	228	237	475	306	17	-36
Surplus/(Deficit)	2,270	3,158	2,926	2,384	3,965	3,554	3,372	2,740	3,009	-24	10
Shareholders' Account	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q	1Q	YoY (%)	QoQ (%)
Amt trf from P/H acc	2,497	3,139	3,288	2,391	3,334	2,850	2,742	1,967	2,464	-26	25
Inc from Investments	1,961	1,278	1,667	1,753	1,038	1,725	2,160	2,473	1,396	34	-44
Total	4,459	4,418	4,958	4,424	4,373	4,578	4,904	4,482	3,864	-12	-14
Other expenses	80	96	89	129	91	88	93	115	99	9	-14
Amt trf to P/H acc	53	-32	-2	-1	2	-2	-	753	925	NA	23
PBT	4,326	4,354	4,871	4,296	4,281	4,491	4,810	3,614	2,840	-34	-21
Tax	278	166	370	214	221	279	289	208	24	-89	-89
PAT	4,049	4,188	4,500	4,082	4,059	4,212	4,521	3,406	2,816	-31	-17
Reported Ratios (%) : (on un-weighted premium)	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q	1Q	YoY (bps)	QoQ (bps)
Commission expense	3.5	3.3	3.5	3.3	4.8	5.5	5.5	5.4	5.5	70	10
Opex ratio	15.51	9.93	9.66	9.33	8.93	7.46	7.6	6.93	10.79	186	385
Calc Ratios (%)											
Commission expense	3.86	3.59	3.65	3.49	5.1	5.9	5.79	5.43	5.53	43	9
Opex ratio	16.95	10.67	10.16	9.85	9.72	7.99	8	7.35	11.77	205	441
Reported APE data:	FY17				FY18				FY19	YoY	QoQ
Savings APE (%)	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q	1Q	(bps)	(bps)
Total (INRm)				21,670	17,050	18,690	20,050	22,120	13,960		
ULIP	-	-	-	86.1	85.7	81.8	84.8	79.4	79.8	-589	41
Participating	-	-	-	8.4	8.3	12.3	10.2	9.2	9.7	141	56
Other savings	-	-	-	1.6	1.5	1.7	0.9	1.7	2.3	83	62
Protection	-	-	-	4	4.5	4.2	4	9.8	8.2	365	-160
Other ratios (%)	1QFY17	1HFY17	9MFY17	12MFY17	1QFY18	1HFY18	9MFY18	12MFY18	1QFY19	YoY (bps)	QoQ (bps)
Solvency Ratio	320.5	305.9	294.3	280.7	288.6	275.7	251.5	252	234.6	-5400	-1740
VNB margins			9.4	10.1	10.7	11.7	13.7	16.5	17.5	680	100
Persistency ratios (%) : excluding single premium	1QFY17	1HFY17	9MFY17	12MFY17	1QFY18	1HFY18	9MFY18	12MFY18	1QFY19	YoY (%)	QoQ (%)
13th Month	77.3	82.1	83.4	84.7	86.7	87	86.7	86.9	86.9	20	0
25th Month	68.9	72.5	72.9	73	74.6	74.3	75.8	77.6	79.2	460	160
37th Month	60	62.9	64.3	65.5	68.1	68.2	67.8	67.7	69.3	120	160
49th Month	56	61.1	60.6	58.3	60.1	60.6	61.8	62.3	65.1	500	280
61st Month	55.5	65.6	65.1	53.8	55.9	55.6	55	54	54.8	-110	80
Key metrics (INRb)	1QFY17	1HFY17	9MFY17	12MFY17	1QFY18	1HFY18	9MFY18	12MFY18	1QFY19	YoY (%)	QoQ (%)
VNB	-	-	4.2	6.7	1.8	4.2	7.7	12.9	2.4	34	-81
EV	-	-	0	161.8	-	172.1	0	187.9	0	NA	-100
AUM	-	-	1,136	1,229	1,266	1,306	1,383	1,395	1426.6	13	2

Source: Company, MOSL

(a) 73% of new business policies issued within 2 days in 1QFY19

Other highlights for the quarter

- Market share within the total industry stood at 11.3% (v/s 15.3% in 1QFY18). Within private sector, the market share was 21% (v/s 28% in 1QFY18)
- Retail renewal premium grew 57% YoY to INR36.2b, whereas group premium grew 57% YoY to INR4.0b.

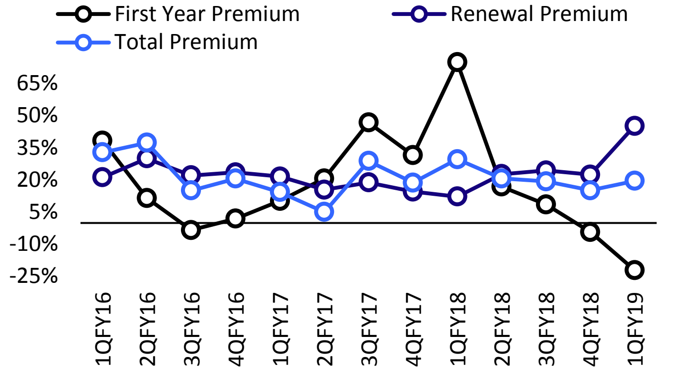
(b) 91% of new business applications initiated via digital platform
(c) Claims TAT decreased from 6 days in FY14 to 3 days in 1QFY19

1QFY19 Concall highlights

- Protection mix: 8% of the APE as of 1QFY19
- Expense ratio were elevated due to muted premium income
- June monthly numbers were sequentially better
- Non-bank channels have contributed 45% of the APE
- Surrenders have reduced by 35% YoY due to specific efforts of the management.
- Cost ratios for protection segment are higher
- In Q2FY18 company had introduced certain products which has different commission structure
- Drop in PAT is due to decline in Non-PAR life and Annuity segment
- Drop in solvency is due to dividend payout and due to increase in the protection business. Dividend declaration to come down
- Opex ratio is based on the forecast of the business numbers (not on the last year's numbers)
- Advertisement and promotion expenses for protection segment. Increase in employee count to ~15,000ee as of FY18; the flow of the manpower cost in 1QFY19
- Annuity business : Going forward company will focus on deferred annuity whereas currently company is focusing on immediate annuity
- Capital raising: Levers of capital management is dividend policy (special dividend will come down). Can raise tier II capital up to 25% of the equity capital
- INDAS is going to change the entire measurement of Revenue, profit. Smoothening of product
- Policyholder surplus : Discount rate used for the liability is function of yield on portfolio (not entirely dependent on the interest rates)
- Lot of new business was written in annuity in Q4 last year
- Group business has 3 comp: Group fund, group credit life , group term business: Most of the growth has come in protection side and credit life
- More clarity on expenses as the quarter passes by
- In a single premium policy strain should be lower as the compared to other policies
- Mortgage is still the largest part of credit protect segment
- Group protection has grown faster than individual protection
- Deferred annuity in the current Indian environment will be high risk on the balance sheet
- Surrender in ULIP before 5 years is not captured in the persistency ratios

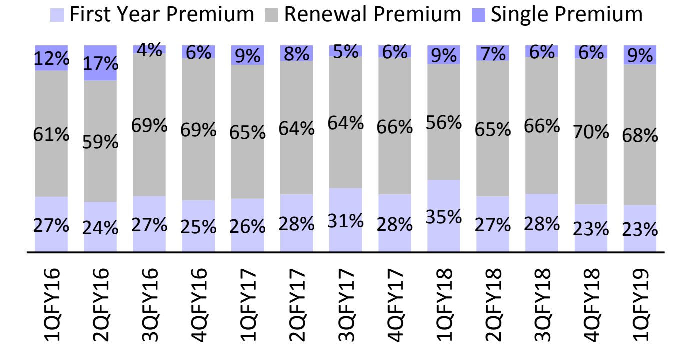
Story in charts

Exhibit 3: Total/renewal premium grew ~20%/45% YoY



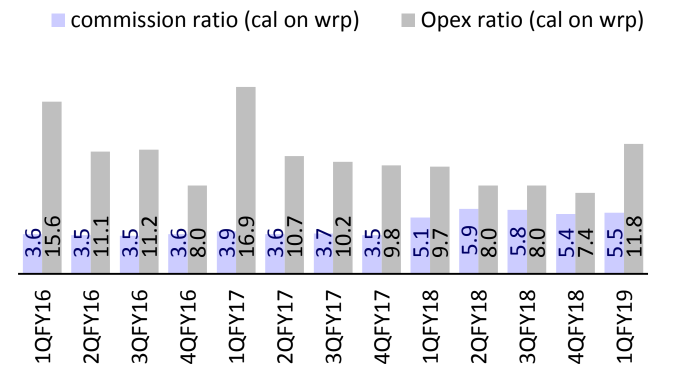
Source: Company, MOSL

Exhibit 4: Share of renewal premium increased to 68% from 56% a year ago



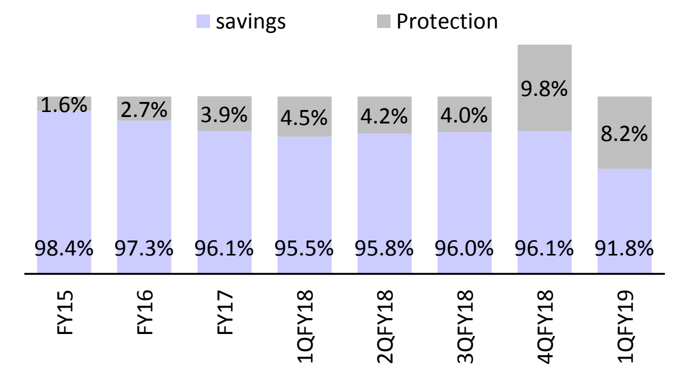
Source: Company, MOSL

Exhibit 5: Total expense ratio stood at 17.5% (v/s 14.2% in 1QFY18)



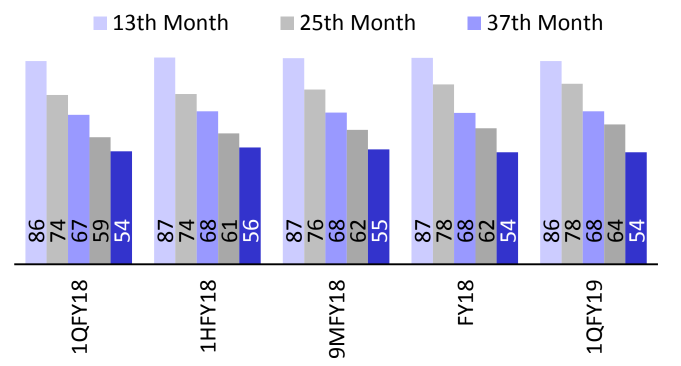
Source: Company, MOSL

Exhibit 6: Share of protection business increased to 8.2%



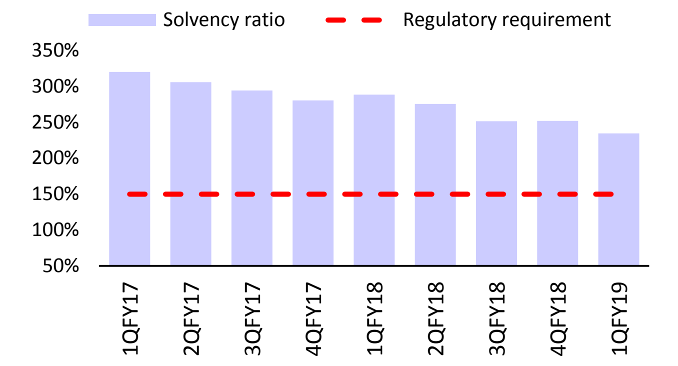
Source: Company, MOSL

Exhibit 7: Persistency ratio has improved across the curve



Source: Company, MOSL

Exhibit 8: Fall in the solvency ratio due to dividend payout and higher strain due to protection business



Source: Company, MOSL

Exhibit 9: Change in estimates

INR b	Old Est.		Revised Est.		Estimates Chg	
Technical Account	**FY19E**	**FY20E**	**FY19E**	**FY20E**	**FY19E**	**FY20E**
Net Premiums	317.2	384.0	310.0	366.1	-2.3	-4.7
Income from Invt	164.5	185.9	164.4	186.1	0.0	0.1
Total income	**482.7**	**571.0**	**475.5**	**553.4**	**-1.5**	**-3.1**
Commission	15.7	18.6	15.8	19.8	0.7	6.3
Operating expenses	26.7	32.1	26.2	31.0	-2.1	-3.3
Surplus / Deficit	**14.7**	**16.1**	**13.7**	**16.1**	**-6.5**	**0.1**
Shareholder's Account						
Total Income	22.3	25.4	19.4	21.4	-12.9	-15.6
Total Expenses	1.4	1.7	1.4	1.7	0.0	0.0
PBT	20.9	23.7	18.0	19.8	-13.7	-16.7
PAT	**19.2**	**21.6**	16.6	18.0	-13.7	-16.7

Source: Company, MOSL

Valuations and view

- We believe the life insurance sector in India is in a sweet spot, where strong structural potential is now overlapping with buoyant equity markets, rising share of financial savings and higher disposable income. We expect Indian insurers to trade at a premium to global insurers.
- Private sector life insurance companies have 51% market share in total new business APE, and IPRU is amongst the market leader. Favorable demographics, increasing customer awareness about financial products, strong distribution network and superior brand image should help IPRU sustain WRP CAGR at 22% over FY18-20.
- **Valuations to be driven by operating performance:** We have cut our PAT estimates by ~14%/17% for FY19/FY20 to factor in lower premium income and higher strain from new business due to an increase in share of protection business. We expect IPRU to deliver a 14.4% CAGR in new business APE over FY18-20, while margins are likely to improve from the current levels of ~17.5%. We, thus, estimate 20% CAGR in VNB over FY18-20, while RoEV is expected to sustain at ~16.5%. We value IPRU at INR450 per share, which corresponds to 2.5x FY20E EV. Maintain **Buy**.

Financials and valuations: ICICI Prudential Life Insurance Company

Technical account (INR m)	FY17	FY18	FY19E	FY20E
Gross Premiums	2,23,540	2,68,036	3,12,799	3,69,846
Reinsurance Ceded	(1,988)	(2,581)	(2,774)	(3,722)
Net Premiums	2,21,553	2,68,107	3,10,025	3,66,123
Income from Investments	1,49,769	1,12,615	1,64,444	1,86,089
Other Income	188	936	1,040	1,155
Total income	**3,71,927**	**3,82,172**	**4,75,509**	**5,53,368**
Commission	7,589	14,033	15,781	19,821
Operating expenses	23,572	20,299	26,165	31,030
Total commission and opex	**31,161**	**34,332**	**41,946**	**50,851**
Benefits Paid (Net)	1,49,979	1,72,808	2,35,152	2,86,915
Chg in reserves	1,74,976	1,54,475	1,83,659	1,98,112
Total expenses	**3,56,115**	**3,61,615**	**4,60,758**	**5,35,878**
Provisions for debt, tax, misc.	4,288	5,727	4,502	5,061
Surplus / deficit before tax	**11,523**	**14,830**	**14,657**	**17,384**
Prov for Tax	788	1,201	932	1289
Surplus / Deficit	**10,735**	**13,630**	**13,725**	**16,095**
Shareholder's a/c (INR m)	**FY17**	**FY18**	**FY19E**	**FY20E**
Transfer from technical a/c	11,315	10,892	11,858	13,514
Income From Investments	6,669	7,419	7,493	7,850
Total Income	**18,270**	**18,362**	**19,406**	**21,425**
Other expenses	409	420	546	737
Contribution to technical a/c	18	753	836	929
Total Expenses	**427**	**1,173**	**1,382**	**1,666**
PBT	**17,843**	**17,189**	**18,024**	**19,760**
Prov for Tax	1,028	997	1,442	1,778
PAT	**16,815**	**16,192**	**16,583**	**17,981**
Growth	***2%***	***-4%***	***2%***	***8%***
Premium (INR m) & growth (%)	**FY17**	**FY18**	**FY19E**	**FY20E**
New business prem - unwtd	77,604	90,210	1,01,937	1,20,286
New business prem - wrp	64,862	75,227	84,658	98,377
Renewal premium	1,44,907	1,77,465	2,10,862	2,49,560
Total premium - unwtd	2,22,511	2,67,674	3,12,799	3,69,846
New bus. growth - unwtd	14.7%	16.2%	13.0%	18.0%
New business growth - wrp	27.0%	16.0%	12.5%	16.2%
Renewal premium growth	16.9%	22.5%	18.8%	18.4%
Total prem growth - unwtd	16.1%	20.3%	16.9%	18.2%
Premium mix (%)	**FY17**	**FY18**	**FY19E**	**FY20E**
New business - unwtd				
- Individual mix	89.9%	93.1%	93.0%	94.0%
- Group mix	11.4%	9.8%	7.0%	6.0%
New business mix - APE				
- Participating	9.5%	10.6%	10.9%	11.6%
- Non-participating	4.8%	5.0%	8.5%	10.8%
- ULIPs	85.7%	84.4%	80.6%	77.6%
Total premium mix - unwtd				
- Participating	11.7%	12.0%	11.8%	13.0%
- Non-participating	13.6%	12.8%	17.7%	20.0%
- ULIPs	74.8%	75.2%	70.5%	67.0%
Individual prem sourcing mix (%)	**FY17**	**FY18**	**FY19E**	**FY20E**
Individual agents	23.5%	25.6%	26.6%	27.6%
Corporate agents-Banks	57.1%	52.6%	51.6%	51.4%
Direct business	12.8%	16.0%	16.6%	16.4%
Others	6.6%	5.8%	5.2%	4.6%

Financials and valuations: ICICI Prudential Life Insurance Company

Balance sheet (INR m)	FY17	FY18	FY19E	FY20E
Sources of Fund				
Share Capital	14,354	14,355	14,355	14,355
Reserves And Surplus	46,976	51,382	61,918	72,989
Shareholders' Fund	64,060	68,818	79,570	90,970
Policy Liabilities	2,51,695	3,09,934	3,67,839	4,69,022
Prov. for Linked Liab.	8,39,365	9,23,124	11,17,943	12,18,557
Funds For Future App.	6,042	8,780	10,096	11,609
Current liabilities & prov.	28,365	34,479	41,363	49,623
Total	**12,47,408**	**14,18,187**	**16,38,791**	**18,62,826**
Application of Funds				
Shareholders' inv	66,349	77,466	83,663	90,775
Policyholders' inv	2,70,674	3,32,889	4,02,105	5,15,937
Assets to cover linked liab.	8,78,783	9,75,020	11,17,943	12,18,557
Loans	806	1,451	1,712	1,934
Fixed Assets	2,138	4,221	4,727	5,389
Current assets	28,657	27,142	28,642	30,234
Total	**12,47,408**	**14,18,187**	**16,38,791**	**18,62,826**
Operating ratios (%)	**FY17**	**FY18**	**FY19E**	**FY20E**
Investment yield (%)	13.0%	8.6%	10.8%	10.7%
Commissions / GWP	**3.4%**	**5.2%**	**5.0%**	**5.4%**
- first year premiums	7.3%	13.9%	14.0%	15.7%
- renewal premiums	2.0%	1.9%	1.9%	1.8%
- single premiums	0.6%	1.9%	1.2%	1.1%
Operating expenses / GWP	10.5%	7.6%	8.4%	8.4%
Total expense ratio	**13.9%**	**12.8%**	**13.4%**	**13.7%**
Claims / NWP	67.7%	64.5%	75.8%	78.4%
Solvency margin	289%	252%	225%	206%
Persistency ratios (%)	**FY17**	**FY18**	**FY19E**	**FY20E**
13th Month	85.7%	87.8%	88.2%	88.3%
25th Month	73.9%	78.8%	80.5%	80.8%
37th Month	66.8%	68.9%	71.8%	72.8%
49th Month	59.3%	63.6%	65.1%	67.1%
61st Month	56.2%	54.8%	58.2%	59.4%
Profitability ratios (%)	**FY17**	**FY18**	**FY19E**	**FY20E**
New business margin (%)	10.1%	16.5%	18.0%	18.7%
RoE (%)	28.7%	24.4%	22.4%	21.1%
RoIC (%)	34.8%	33.4%	34.2%	37.0%
EVOP as % of IEV	16.4%	22.8%	19.5%	18.8%
RoEV (%)	16.0%	16.1%	16.8%	16.0%
Valuation ratios	**FY17**	**FY18**	**FY19E**	**FY20E**
Total AUMs, Rs bn	1,229	1,395	1,604	1,825
- of which equity AUMs (%)	47%	48%	48%	49%
Dividend (%)	74%	66%	35%	40%
Dividend payout ratio (%)	40%	74%	36%	38%
EPS, Rs	11.7	11.3	11.6	12.5
VNB (INRb)	6.6	12.9	15.3	18.4
EV (INRb)	161.7	187.8	219.3	254.4
EV/Per share	112.7	130.8	152.8	177.2
VIF as % of EV	58%	63%	63%	64%
P/VIF	5.9	4.7	4.0	3.4
P/AUM (%)	45%	40%	34%	30%
P/EV (x)	3.4	2.9	2.5	2.2
P/EPS (x)	32.8		33.4	30.8

NOTES

Explanation of Investment Rating	
Investment Rating	Expected return (over 12-month)
BUY	>=15%
SELL	< - 10%
NEUTRAL	> - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

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