Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

HDFC Life Insurance

Well placed to ride the tailwinds

Banks & Finance | Sharekhan code: HDFCLIFE | Company Update

3R MATRIX	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)	✓		
Right Valuation (RV)	✓		

+ Positive = Neutral - Negative

What has changed in 3R MATRIX

	Old		New
RS		↔	
RQ		↔	
RV		↑	

Reco/View	Change
Reco: **Buy**	↔
CMP: **Rs. 707**	
Price Target: **Rs. 850**	↑

↑ Upgrade ↔ Maintain ↓ Downgrade

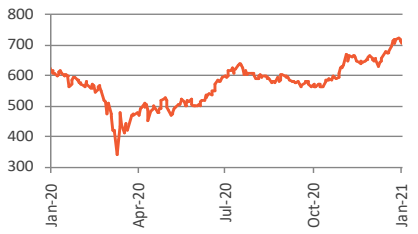
Company details

Market cap:	Rs. 142,826.04 cr
52-week high/low:	Rs. 731/339
NSE volume: (No of shares)	40.6 lakh
BSE code:	540777
NSE code:	HDFCLIFE
Free float: (No of shares)	79.9 cr

Shareholding (%)

Promoters	60.4
FII	23.8
DII	7.3
Others	8.5

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	7.8	23.5	18.2	13.1
Relative to Sensex	0.6	2.0	-19.4	-5.4

Sharekhan Research, Bloomberg

Summary

- We expect the Union Budget to provide favourable policy steps for the insurance industry; Possible steps may include providing a separate limit over and above the already available 80C limits and providing tax benefits to pension schemes (a la NPS) etc, HDFC Life being largest player is likely to benefit from tailwinds
- Latest figures for HDFC Life indicates strong traction; NBP up 18.8% YoY / 11% y-o-y for Q3FY2021 / 9MFY2021
- HDFC Life is attractive due to its strong business franchise, backed by favourable product/ distribution mix, high bancassurance share, and robust margins.
- The stock trades at 5.0x/4.2x its FY2022E/FY2023E EVPS; well-diversified product bouquet is a positive; we maintain Buy with a revised PT of Rs. 850.

We continue to prefer HDFC Life Insurance (HDFC Life) for its strong business franchise, backed by favourable product/distribution mix and a higher bancassurance channel sourcing, which helps the company report the industry's best (higher and sustainable) margins. We expect the government to provide favourable policy steps for the insurance industry (including life as well as non-life segments) in the Union Budget because of COVID-19 crisis . Insurance is an important social security tool, which helps safeguard against risks, which are a threat to life and livelihood. Measures such as providing a separate limit over and above the 80C limit and providing tax benefits to pension schemes (a la NPS) etc. are some possibilities. As per the provisional figures for Q3FY2021, NBP figures indicate healthy 18.8% growth y-o-y for HDFC Life, which is a smart recovery from the pandemic-induced challenges and indicates an encouraging Q3 performance. For December 2020 as well, HDFC Life posted good performance, with NBP increasing by 27% for December 2020, but on 9MFY2021 basis, NBP posted growth of 11% y-o-y (was 8.81% till year-to-date in November), indicating traction. Total APE (calculated) was also up by 7.4% for December 2020.

We believe while traction in the protection and annuity segments is still strong, segments such as credit protect and ULIPs would be seeing lower traction (understandably due to lower customer appetite and slower bank credit growth). However, the business mix of HDFC Life is favourable, with only 23% individual APE from ULIPs in H1FY2021 (has scaled down from 57% in FY2018 and 28% in FY2020). We believe the current COVID-19 health crisis has helped increase customer awareness and appetite for protection, which is likely to be helpful for protection products, which would be positive for HDFC Life from a growth standpoint. HDFC Life, being the largest private life player, is well placed to benefit from tailwinds of growth as well as supportive regulatory measures. Management has guided for high single-digit growth in annualised premium equivalent (APE) and value of new business (VNB) as a realistic possibility in FY2021. We expect growth to pick up from FY2022E. Protection and annuity business are gaining traction, backed by strong structural demand. Among products, Sanchay Par is expected to now improve, as banking channels see improved pickup of business. With increased credit offtake in housing and other segments, we expect credit protect business to pick up in FY2022E. We see life insurance as an attractive long-term bet with a long runway for growth, supported by India's demographics and underpenetrated/ underinsured Indian market. We believe players with a strong balance sheet and business metrics would be able to tide over the crisis. Going forward, we believe demand for protection policies and savings products would be likely growth drivers in FY2022E. We have fine-tuned our estimates for FY2022E and FY2023E. We maintain our Buy rating on the stock with a revised price target (PT) of Rs. 850.

Our Call

Valuation - The stock trades at 5.0x/4.2x its FY2022E/FY2023E EVPS. Premium valuation to sustain as HDFC Life has a better diversified product bouquet (no segment contributing to more than 30% of the APE), best-in-class branding, strong metrics. We believe that the company is well-placed to deliver strong and sustainable long-term APE growth. Aided by strong fundamentals (robust balance sheet and consistent profitability) and high long-term growth potential for the Indian insurance industry in general and HDFC Life, in particular, we find HDFC Life an attractive long-term bet. We expect premium growth to normalise from Q4FY2021E and, going forward, a low base of March 20 (due to the COVID-19 lockdown) to help. We have fine-tuned our estimates for FY2022E and FY2023E. We maintain a Buy rating with a revised PT of Rs. 850.

Key Risks

A slowdown in business operations and higher slippages/bond downgrades due to economic weakness may impact earnings outlook.

Valuation — Rs cr

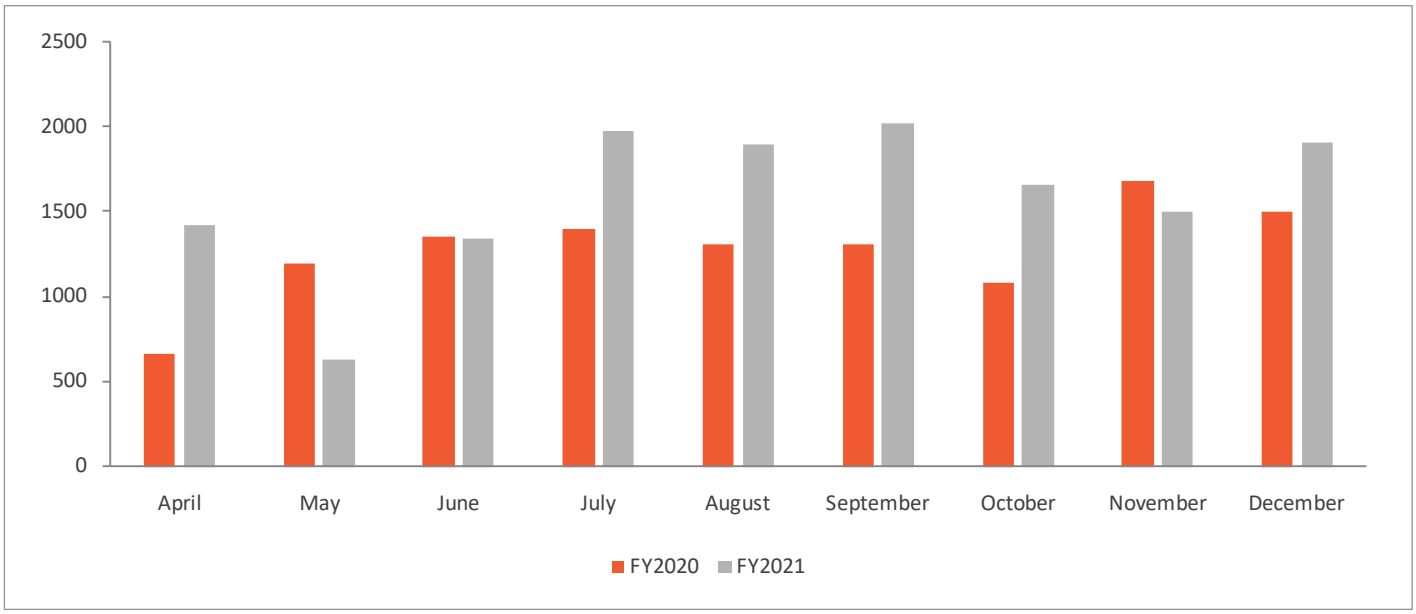
Particulars	FY19	FY20	FY21E	FY22E	FY23E
EV (Rs Cr)	18,301	20,650	23,954	28,505	34,064
New Business Margins (%)	24.6	25.9	23.0	24.0	24.0
Networth (Rs Cr.)	5,660	6,992	7,981	9,129	9,523
PAT (Rs Cr)	1,278	1,295	1,374	1,594	1,676
P/BV (x)	25.2	20.4	17.9	15.6	13.8
P/EPS (x)	111.6	110.2	103.9	89.5	85.1
P/EV (x)	7.8	6.9	6.0	5.0	4.2
ROE (%)	22.6	18.5	17.2	17.5	17.6
ROA (%)	1.02	1.00	0.91	0.92	0.93

Source: Company; Sharekhan estimates

HDFC Life sees continued growth traction, indicates business strength

As per the provisional figures till December 2020, HDFC Life reported reasonable 4% y-o-y growth in individual APE (Calculated) mainly because of high base of the previous year.

Total NBP monthly trajector



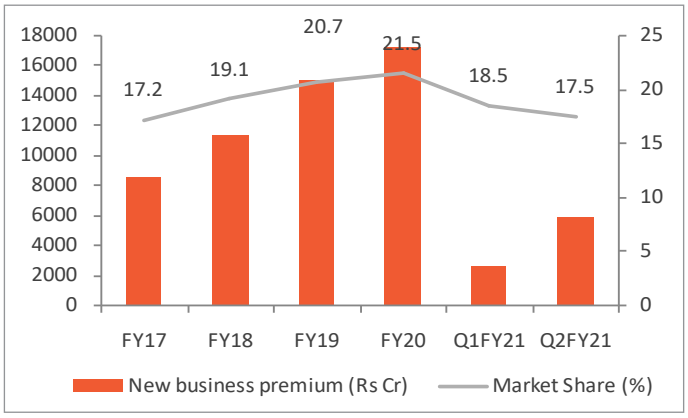
Source: IRDAI, Sharekhan Research

NBP jumped up sharply by 27% y-o-y and 9MFY2021 growth is now at 11%. While traction in protection and annuity segments is still strong, segments such as credit protect and ULIPs are seeing lower traction (understandably due to lower customer appetite and slower bank credit growth). For the first nine months of FY2021, NBP stood at Rs. 13,631.7 crore, up 11% y-o-y, despite the high base effect (due to launch of a new product in FY2020), which is positive.

Total APE (calculated) too is up by 7.4% for December 2020. We believe the current COVID-19 health crisis has helped increase customer awareness and appetite for protection, which is likely to be helpful for protection products, which would be positive for HDFC Life from a growth standpoint. Management had earlier indicated that the high growth has been a function of strong traction in its protection and par portfolio. Moreover, spurred by COVID-19 crisis, improvement in digital capabilities, and higher share of direct business compared to peers also helped. The life insurance industry has also continued to see good traction, especially the private life insurance sector, which indicates an encouraging revert to normalcy.

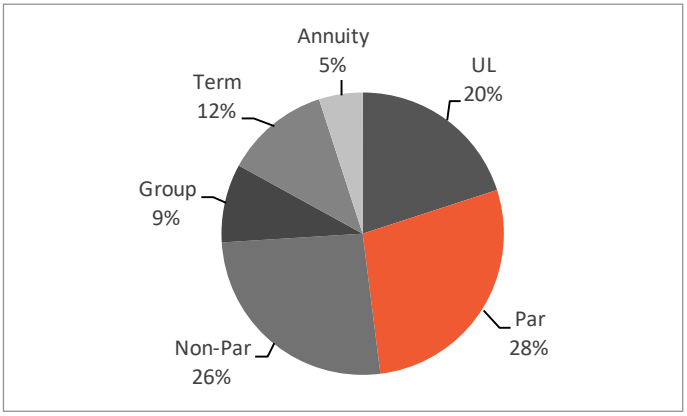
Financials in charts

Leadership in new business premium



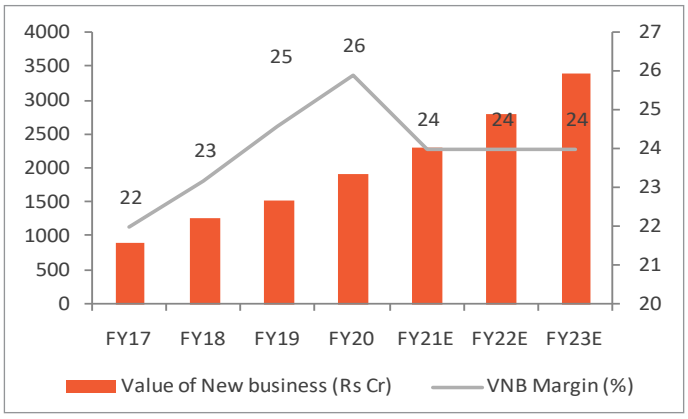
Source: Company, Sharekhan Research

Maintaining a balanced product mix (%) across cycles



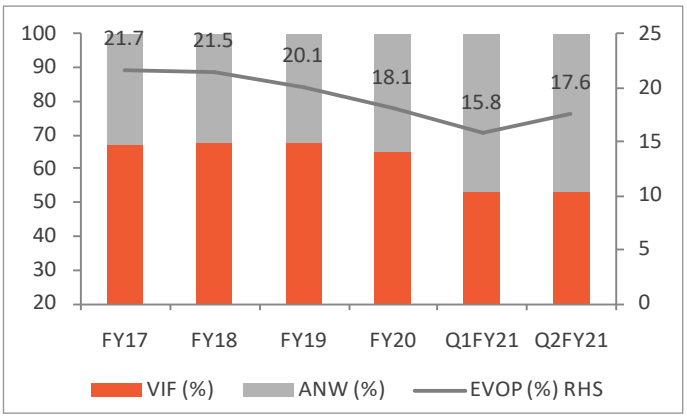
Source: Company, Sharekhan Research

Strong growth in VNB, industry-leading VNB margins



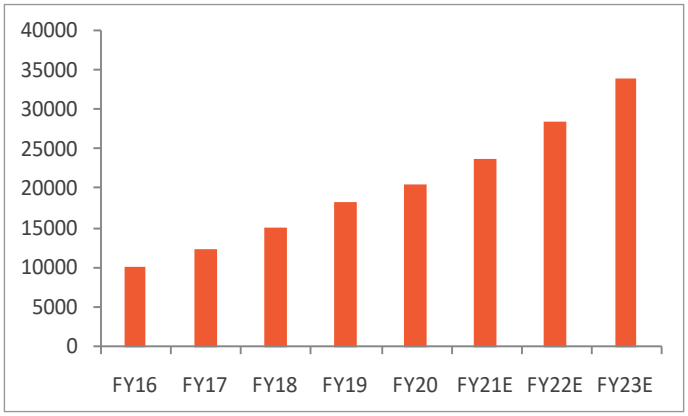
Source: Company, Sharekhan Research

Embedded Value Components



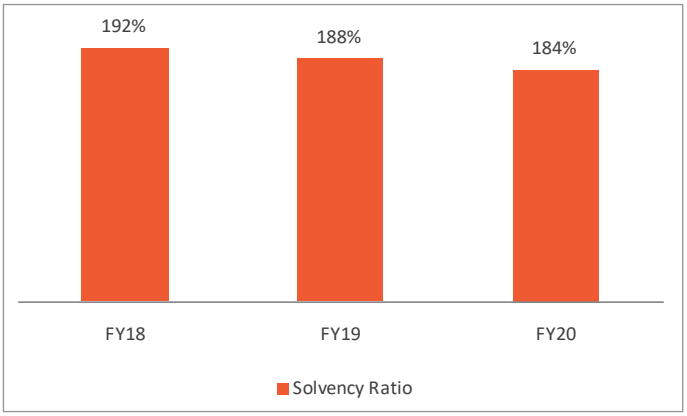
Source: Company, Sharekhan Research

Embedded Value



Source: Company, Sharekhan Research

Healthy Solvency Ratio



Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector view - Fast revert to normalcy, long runway for growth for life insurance players

For the latest quarter, the overall premium/APE growth for the insurance industry continued to be encouraging even as weak demand for market-linked ULIPs etc. continues. However, strong demand for protection and non-PAR segments continues. Even for December, performance continued to improve as compared to the past nine months of FY2020, which indicates that the insurance sector is steadily but surely reverting to normalcy. Factors such as a large protection gap and expanding per capita income are key long-term growth drivers for the sector. According to industry reports, India has a high protection gap; and credit protection product is still at an early stage and has the potential to grow multi-fold as the penetration of retail loans improves in the country. Hence, we believe the insurance sector has a huge growth potential in India. In this backdrop, we believe strong players such as HDFC Life, armed with the right mix of products, services, and distribution, are likely to gain disproportionally from the opportunity.

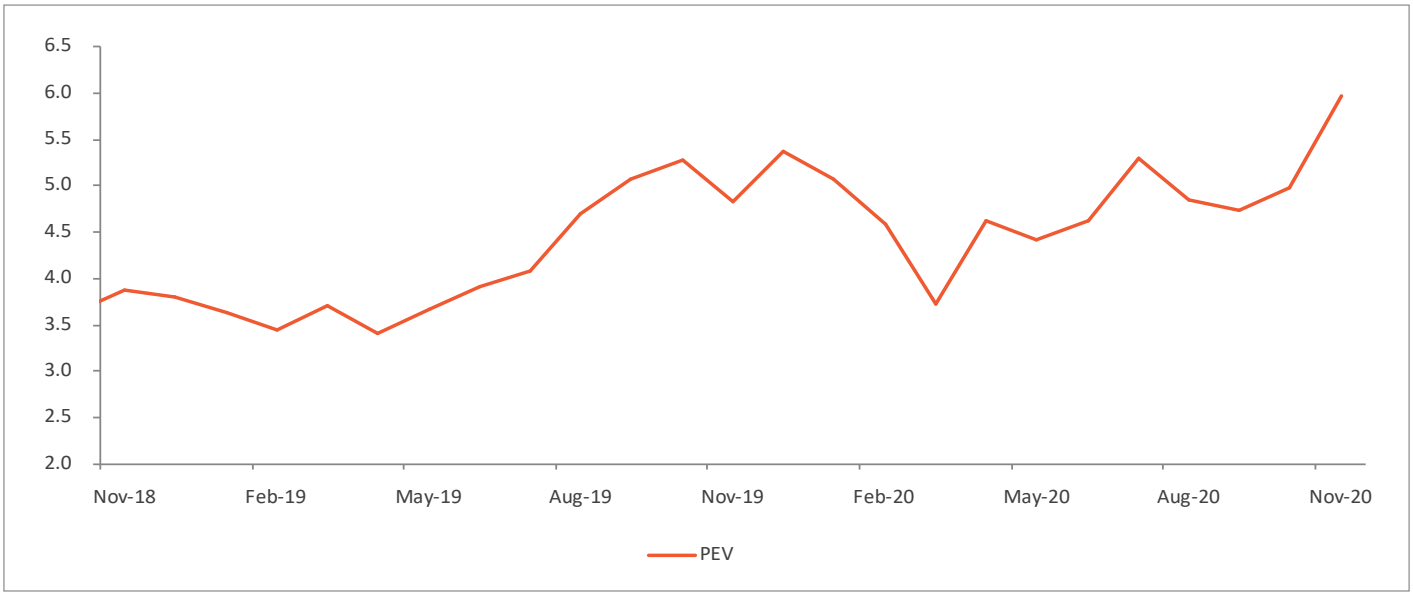
■ Company outlook - Superior product mix, healthy metrics make HDFC Life attractive

HDFC Life is well placed with healthy capitalisation and a favourable business mix. With a high proportion of protection and savings-related products, we believe HDFC Life is better placed in the present environment. We expect the government may provide favourable policy steps for the insurance industry (including life and non-life) in the Union Budget because of the pandemic. Possible steps may include providing a separate limit over and above the already available 80C limits and providing tax benefits to pension schemes (a la NPS), among others. Being the largest player, HDFC Life is likely to benefit from favourable tailwinds. Latest figures for HDFC Life indicate 18.8% NBP growth for Q3FY2021, and 11% y-o-y for 9MFY2021 basis, indicating strong traction. The company's sustained high persistency ratio indicates client service and quality of products offered, which are critical for long-term sustainability. Improving 13-month/49-month persistency for HDFC Life is also a healthy indicator. HDFC Life is a strong and attractive business franchise and the Indian insurance space is an attractive sector for the long term. Structurally, we expect HDFC Life to deliver VNB margins of ~24% over the next 2-3 years (on a normalised basis) and its calibrated risk management has resulted in low EV and VNB sensitivity in the non-par segment, which is a positive support for valuations.

■ Valuation - Premium valuations to sustain; maintain Buy with PT of Rs. 850

The stock trades at 5.0x/4.2x its FY2022E/FY2023E EVPS. Premium valuation to sustain as HDFC Life has a better diversified product bouquet (no segment contributing to more than 30% of the APE), best-in-class branding, strong metrics. We believe that the company is well-placed to deliver strong and sustainable long-term APE growth. Aided by strong fundamentals (robust balance sheet and consistent profitability) and high long-term growth potential for the Indian insurance industry in general and HDFC Life, in particular, we find HDFC Life an attractive long-term bet. We expect premium growth to normalise from Q4FY2021E and, going forward, a low base of March 20 (due to the COVID-19 lockdown) to help. We have fine-tuned our estimates for FY2022E and FY2023E. We maintain a Buy rating with a revised PT of Rs. 850.

One-year forward P/EV (x) band



Source: Bloomberg, Sharekhan Research

Peer valuation

Particulars	CMP (Rs / Share)	P/BV (x)		P/E (x)		RoA (%)		RoE (%)	
		FY21E	FY22E	FY21E	FY22E	FY21E	FY22E	FY21E	FY22E
HDFC Life	707	17.9	15.6	103.9	89.5	0.91	0.92	17.2	17.5
ICICI Pru Life	510	8.6	6.5	62.1	52.2	0.84	0.84	14.8	16.1

Source: Bloomberg, Sharekhan Research

About company

Established in 2000, HDFC Life is a leading long-term life insurance solutions provider. The company offers a range of individual and group insurance solutions that meet various customer needs such as protection, pension, savings, investment, and health. HDFC Life continues to benefit from its increased presence across the country. The company has a wide reach with 400+ branches and additional distribution touch points through several new tie-ups and partnerships, including own sister concern bank. The company also has 270+ partnerships, comprising traditional partners such as NBFCs, MFIs, and SFBs, and includes more than 40 new ecosystem partners. The company has a strong base of financial consultants.

Investment theme

HDFC Life stands out among its peers with its strong parentage, robust brand recall, along with advantages that come with an industry leader sister concern bank, which has an attractive retail business and gives deep client penetration and arguably the best means to channelise growth for the insurance business. HDFC Life is among the top private insurers in India and enjoys 21.5% (was 20.7% in FY2019) market share (in total new business) as of FY2020. We believe HDFC Life's sustained product leadership will help it maintain superior VNB margins and operating RoEV, relative to peers, which provide support to its valuations. We believe the insurance market has significant growth opportunities and HDFC Life is well placed to capture them. By virtue of its bancassurance partnerships, digital strength, and industry-leader status, HDFC Life should be able to deliver steady VNB and EVOP CAGR over the long term (aided by high margins in the protection business and improving persistency) in a normalised state of business, which will support valuations.

Key Risks

A slowdown in business operations and higher slippages/bond downgrades due to economic weakness may impact earnings outlook.

Additional Data

Key management personnel

Ms. Vibha Padalkar	Managing Director & Chief Executive Officer
Mr. Niraj Shah	Chief Financial Officer
Mr. Parvez Mulla	Chief Operating Officer
Mr. Srinivasan Parthasarathy	Senior Executive Vice President, Chief Actuary & Appointed Actuary
Mr. Prasun Gajri	Chief Investment Officer

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Capital Group Cos Inc/The	7.0
2	JPMorgan Chase & Co	2.8
3	FIL Ltd	1.3
4	Vanguard Group Inc/The	1.2
5	SBI Funds Management Pvt Ltd	1.2
6	BlackRock Inc	1.1
7	Motilal Oswal Asset Management Co	0.9
8	Axis Asset Management Co Ltd/India	0.9
9	Nomura Holdings Inc	0.7
10	Mirae Asset Global Investments Co	0.6

Source: Bloomberg

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

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