Sharekhan by BNP PARIBAS

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ICICI Lombard General Insurance

A Steady quarter

Banks & Finance	Sharekhan code: ICICIGI	Result Update

Stock 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. 1,417**	
Price Target: **Rs. 1,750**	↔

↑ Upgrade ↔ Maintain ↓ Downgrade

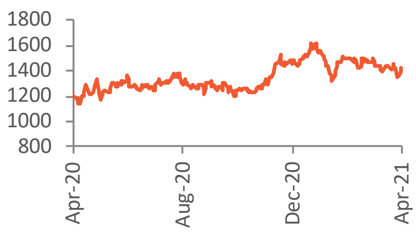
Company details

Market cap:	Rs. 64,414 cr
52-week high/low:	Rs. 1,625/1,125
NSE volume: (No of shares)	5.7 lakh
BSE code:	540716
NSE code:	ICICIGI
Free float: (No of shares)	20.1 cr

Shareholding (%)

Promoters	51.9
FII	28.4
DII	10.2
Others	9.5

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-3.9	-8.4	13.7	18.5
Relative to Sensex	-2.0	-7.0	-6.0	-36.1

Sharekhan Research, Bloomberg

Summary

- We retain Buy with unchanged price target of Rs 1750 with reasonable valuations at 38.6x / 31x FY2022E / FY2023E EPS.
- ICICI Lombard General Insurance (ILGI) reported steady numbers for Q4FY2021. Operational performance was largely in-line, helped by lower combined ratios.
- The combined ratio has been normalizing and stood at 101.8% for Q4, but on FY2021 basis, it stood at 99.8%, lower than 100.4% in FY2020.
- We expect the focus on diversifying into tier 3 & 4 cities is positive, and will help the company ride on growth drivers of diversifying product mix, multi-channel distribution network, backed by robust risk selection and strong investment return.

ICICI Lombard General Insurance (ILGI) reported steady numbers for Q4FY2021. Operational performance was largely in-line, helped by lower combined ratios. For the quarter, the GDPI came marginally below expectations, but on the basis of PBT and PAT the same were in-line and above expectations. Premium incomes normalised in FY2021 (GDPI growth stood at 5.2% y-o-y for the period). Performance was strong on the cost aspect, with a lower combined ratio of 99.8% (was 100.4% in FY2020) for FY2021. For Q4FY21, ROAE also improved sequentially to 18.8% (was 17.6% in Q3 FY2021) and stood at 21.7% for FY2021 (improved from 20.8% in FY2020). The solvency ratio has improved further to 2.90x (from 2.76x in Q3FY2021). Overall loss ratios continued to decline to 68.6% (from 72.9% for FY2020), which is a positive indicator. During the quarter, motor OD, Fire, engineering and others segment saw a y-o-y improvement in loss ratios. We expect the focus on diversifying into tier 3 & 4 cities to be a positive, and will help the company ride on growth drivers of diversifying product mix, multi-channel distribution network, backed by robust risk selection and strong investment return. The management indicated that low claim ratios may revert to normalised levels in the medium term. For the medium term, ICICI Bank has chosen to focus on the banking business, and hence while the management were hopeful to regain traction from that segment, but for the medium term that channel may be sub-par. With the merger with Bharti AXA they may also have additional Bancassurance partners, which will aid business traction. Despite challenges, the insurance industry and players have responded with agility and speed with greater adoption of digital tools and operational tweaks, which is encouraging. We find the general insurance space attractive with strong growth potential. A positive regulatory environment, focus on higher-margin business, scale-driven operating cost benefit potential, and increasing retail focus (better pricing) make ILGI an attractive franchise for the long term. We recommend a Buy on ILGI with an unchanged price target (PT) of Rs. 1,750.

Key positives

- As a testimony of strong underwriting and well-developing business streams, return on Average Equity (ROAE) was 21.5% in FY2021 as compared to 20.8% in FY2020.
- Healthy solvency ratio at 2.90 in Q4FY2021 was comfortably higher than the minimum regulatory requirement of 1.50x.

Key negatives

- Realised return on Investment portfolio declined a tad at 7.8% for FY2021 as against 7.9% in FY2020. Also, total investment leverage declines marginally to 4.09x for FY2021 end, partly due to the higher base.

Our Call

Valuations - ILGI trades at 38.6x/31x its FY2022E/FY2023E EPS and valuations indicate its long-term business resilience even during challenging times. The stock has corrected by ~13% from its highs and considering the strong fundamentals, ILGI's strong execution capabilities, conservative underwriting, and healthy solvency, we believe that the risk reward is favourable for long term investors. We believe the general insurance industry is an attractive space, which has a long runway for long-term growth. ILGI has demonstrated its strong underwriting, healthy solvency, and improving loss ratios, which should help it ride over medium-term challenges due to COVID-19 disruptions. We retain a Buy on ILGI with an unchanged PT of Rs. 1,750.

Key Risks

Business disruptions and impact on GDPI growth due to COVID-19, adverse regulatory policies / guidelines, and aggressive risk pricing by peers may impact ILGI's profitability and growth.

Valuations Rs cr

Financial Summary	FY19	FY20	FY21	FY22E	FY23E
Gross Direct Premium Income (GDPI)	**14,488**	**13,313**	**14,003**	**16,103**	**17,875**
Profit After tax	1049	1194	1473	1683	2085
ROE (%)	21.3	19.5	21.2	19.7	20.6
EPS (Rs)	23.1	26.3	32.4	37.0	45.9
BVPS (Rs)	117.1	135.0	160.4	188.1	222.4
P/E (x)	61.4	53.9	43.7	38.2	30.9
P/BV (x)	12.1	10.5	8.8	7.5	6.4

Source: Company; Sharekhan estimates

ICICI Lombard Concall – Q4 FY2021

On Economy: Before the second COVID wave, Indian economy was displaying improvement trends, which was reflected in strong GST collections, strong manufacturing PMI, uptake in Auto sales and growth in imports. However, the second COVID wave is a concern.

Industry growth: General insurance Industry has seen growth of 5.2% in FY2021

FDI Limit increase: Budget announcement of increase in FDI limit from 49% to 74% will be a long term positive.

Strategy: The management is focusing on expanding distribution network to increase presence in Tier 3 / 4 cities and the agents including POS as on Mar 2021 stood at 59545 against 55615 as on Dec-2020. The management has guided its strategy to revolve around the 5 pillars of consistent market leadership, diverisified product mix, with multi-channel distribution network, excellence in claim settlement and technology, robust risk selection and strong investment return in a diversified portfolio.

Growth of company vs industry: The GDPI for FY2021 grew by 5.2% to 14003 crores, largely in line with industry growth of 5.2%. The Q4 FY2021 GDPI grew by 9.4% y-o-y compared to industry growth of 14%. The growth was mainly driven by a focus on preferred segments.

Claim Ratio: Average claim size of motor TP is expected to increase after some of the recent judgements. The management has accordingly re-assessed the motor TP outstanding book and decided to strengthen the reserves appropriately.

Tax rate: PAT for FY2021 stood at Rs 1473 crores against Rs 1194 crores in FY2020 on account of lower effective tax rate

Claims: Total number of claims for FY2021 stood at around 50,000 and amount was Rs 375 crores. Claims are expected to normalize over the long term.

Digital is positive growth driver: Digital initiatives by the management has proven beneficial to the company.

Strong outlook for FY2022: The management guided that the company has entered the FY22 with strong capital and strengthened reserves and is also looking forward to the acquisition of Bharti AXA which awaits its final approval from IRDA and NCLT. The management guided that in coming year, industry is expected to grow between 12-15%.

Claims ratio: The motor claims and non-Covid claims are expected to drop, but not to the extent of Q1 FY2021.

Guidance: Management guided that ROE would be around 20%.

Results Rs cr

Particulars	Q4FY21	Q4FY20	YoY (%)	Q3FY21	QoQ (%)
Gross Direct Premium Income (GDPI)	**3478.0**	**3181.0**	**9.3**	**4034.0**	**-13.8**
Gross premium written	3559.9	3231.5	10.2	4111.7	-13.4
Premium earned (Net)	**2764.8**	**2431.5**	**13.7**	**2611.4**	**5.9**
Income in shareholders account	920.7	452.0	103.7	452.1	103.7
Total Expenses	470.6	222.9	111.1	33.8	1291.5
PBT	**450.1**	**370.6**	**21.4**	**418.2**	**7.6**
Taxes	104.4	88.7	17.7	104.7	-0.3
PAT	**345.7**	**281.9**	**22.6**	**313.5**	**10.3**
Solvency ratio (x)	2.96	2.17	79 BPS	2.76	20 BPS
Combined ratio (%)	101.8	100.1	170 BPS	97.9	390 BPS

Source: Company; Sharekhan Research

Outlook and Valuation

Sector view - Long runway for growth, opportunity for strong players to gain

We believe that the insurance sector has huge growth potential in India. Significant under-penetration, formalisation of the economy, rising awareness for financial protection (accelerated by the pandemic), large protection gap, and expanding per capita income, among others, are key long-term growth drivers for the sector. In this backdrop, we believe strong players such as ILGI, armed with the right mix of products, services, and distribution network, are likely to gain disproportionally from the opportunity. The Rajya Sabha has passed the Bill to hike the foreign direct investment (FDI) limit in the insurance sector to 74% which we believe is long term positive for the industry, and could open doors for faster growth and deeper penetration.

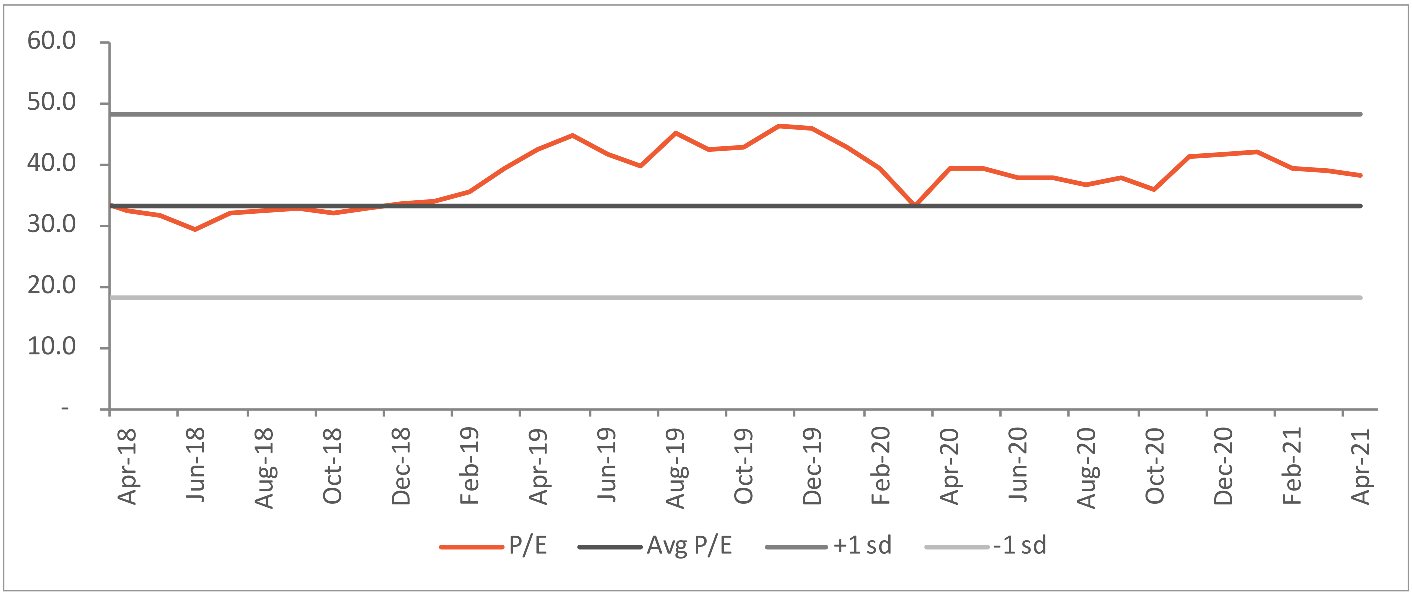
Company outlook - Strong fundamentals, attractive for the long term

ILGI's long-term business fundamentals have remained steady even during times of a crisis. We believe the company is seeing the benefits of improved traction with the auto segment's OEMs (improved volumes) as well as higher demand for health products (due to increased fear factor because of the pandemic) resulted in better recovery traction for the company. Lower-than-normal claims in motor, with lower incidence of surgeries etc., are expected to normalise in the medium-term, but operational improvements/business traction are positive for core profitability. ILGI has also been able to maintain an attractive loss ratio with attractive metrics, which indicates its strong fundamentals. ILGI's strategy to forego the crop business and instead focus on strong growth in preferred segments (fire, retail health, motor OD, etc.) indicate its emphasis on a profitable growth strategy (crop business had less visibility and low profitability). ILGI's business reach (by virtue of a multichannel distribution network, including branches of promoter bank) adds to its competitive advantage. Moreover, the company's conservative underwriting (a key differentiator in the insurance business) is displayed from its referencing triangle, which has been showing lesser incurred losses consistently since the last several years and its loss ratio has been consistently trending downwards, which is also a significant positive. Positive regulatory environment, focus on higher-margin business, scale-driven operating cost benefit potential, and increasing retail focus (better pricing) make ILGI an attractive franchise for the long term.

Valuation - Maintain Buy with unchanged Price Target of Rs 1750

ILGI trades at 38.6x/31x its FY2022E/FY2023E EPS and valuations indicate its long-term business resilience even during challenging times. The stock has corrected by ~13% since highs and considering the strong fundamentals, ILGI's strong execution capabilities, conservative underwriting, and healthy solvency we believe that the risk reward is favourable for long term investors. We believe that the general insurance industry is an attractive space, which has a long runway for long-term growth. ILGI has demonstrated its strong underwriting, healthy solvency, and improving loss ratios, which should help it ride over medium-term challenges due to COVID-19 disruptions. We retain a Buy on ILGI with an unchanged PT of Rs. 1,750.

One-year forward P/E (x) band



Source: Bloomberg, Sharekhan Research

Peer valuation

Particulars	CMP	P/BV (x)		P/E (x)		RoA (%)		RoE (%)	
		FY22E	FY23E	FY22E	FY23E	FY22E	FY23E	FY22E	FY23E
ICICI Lombard GI	1,417	7.6	6.4	38.6	31.1	3.1	3.8	19.7	20.6
New India Assurance Company Ltd	149	1.6	1.8	18.2	15.2	2.2	2.1	8.9	8.7

Source: Company, Sharekhan Research, Bloomberg

About company

ILGI is the fourth largest non-life insurer and the largest private-sector non-life insurer in India. The company offers customers a comprehensive and well-diversified range of products, including motor, crop, health, fire, personal accident, marine, engineering, and liability insurance. ILGI has 250+ offices and 35,000+ individual agents (including POS) and ~840 virtual offices. The company's key distribution channels are direct sales, individual agents, corporate agents - banks, other corporate agents, brokers, MISPs and digital, through which it serves individual, corporate, and government customers.

Investment theme

ILGI had maintained around 7% market share based on GDPI from FY2020 till now. The company has been able to maintain a strong growth trajectory, but it has also been successful in keeping costs under control, along with building reach via both physical and virtual channels. The Insurance business's profitability and returns are strongly dependent on underwriting skills of the insurer, which is, hence, the key. ILGI's long term business fundamentals remained unchanged even in times of a crisis. We believe that the general insurance industry is an attractive space, which has a long runway for long-term growth. ILGI has demonstrated its strong underwriting, healthy solvency, and improving loss ratios, which should help it tide over medium-term challenges.

Key Risks

- Business disruptions and impact on GDPI growth due to COVID-19, adverse regulatory policies / guidelines, and aggressive risk pricing by peers may impact ILGI's profitability and growth.

Additional Data

Key management personnel

Mr Bhargav Dasgupta	Managing Director & CEO
Mr Gopal Balachandran	Chief Financial Officer & Chief Risk Officer
Mr Lokanath Kar	Principal Compliance Officer
Mr Vinod Mahajan	Chief Investment Officer
Mr Girish Nayak	Chief Customer Service, Technology & Operations
Mr Sanjay Datta	Chief Underwriting, Reinsurance & Claim

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	SBI Funds Management Pvt Ltd	2.2
2	FIL Ltd	2.0
3	Aditya Birla Sun Life Asset Manage	1.6
4	Vanguard Group Inc/The	1.6
5	Kotak Mahindra Asset Management Co	1.4
6	Kotak	1.4
7	BlackRock Inc	1.3
8	Governmnet Pension Fund	1.1
9	Nomura Holdings Inc	1.1
10	St James Place PLC	0.7

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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