

# Star Health

Refer to important disclosures at the end of this report

## Roadshow feedback: Well poised for profitable growth

We hosted management of Star Health and Allied Insurance Company in Mumbai on 23rd Mar'22 for meetings with a large number of DIIIs to discuss the company's business performance and growth trajectory and address investor concerns. The key highlights: 1) the company is well on track to return to profitable growth; 2) its capital position is comfortable to support growth in coming years.

- Investors positive on retail health insurance:** Most of the investors were confident about the strong growth potential of retail health insurance business in India and acknowledged Star Health's MOAT in this business segment. At the time of the IPO, the hesitation of DIIIs was mainly on valuation grounds, and worse-than-expected results of Q3FY22 further dented confidence. However, after the recent correction in the stock price and increasing prospects of a quicker turnaround in profitability in the wake of blunting Covid-19 severity, investors are looking at Star Health closely.
- Profitability turnaround to start from Q4FY22:** Management appeared confident about a profitability turnaround in Q4FY22. Management believes that in the absence of any further Covid-19 wave, Star Health's performance in FY23 will reflect normalcy in business, with the loss ratio at ~65% and CoR at 94-95%. Benign hospitalization needs during the Omicron wave led to an improvement in claim frequency, while the gradual withdrawal of Covid-19 compliance-led overheads on non-Covid procedures eased claims severity. Easing claims frequency and severity should drive a quicker improvement in the claims ratio.
- Growth has a long runway:** On growth, the company sees a long runway and has reiterated its focus on the retail segment. Management is confident of delivering above-industry growth at ~23-25% in retail health. On the group side, the company will focus on the profitable SME segment but will reduce its already small exposure in large corporate group health. On retail health, Star Health has reiterated its focus on volume (new policy)-led growth and sees a large demand base in rural and younger population. In the post-pandemic world, the company is seeing increasing demand for health insurance from youngsters and increasing demand for higher sum assured.
- Capital position comfortable:** On capital, management does not see the need for any capital raise in the next two years, as once the profitability normalizes, the required solvency margin will move to premium from claim, and the available solvency margin will benefit from net income accrual. Beyond this, a risk transfer based reinsurance treaty may be considered as another alternative to manage capital. If at all needed, Star Health can resort to raising sub-debt as well.
- Agency remains core of distribution:** On the distribution front, the agency channel remains the core of its distribution strategy and the company will continue to add ~100,000 individual agents a year for the next 3-4 years. The company is working to strengthen its bancassurance channel. However, management clarified that its approach is driven by profitable growth and not just topline growth, and hence it will not go for any large bank distribution channel if terms make business unprofitable. In the web aggregator and direct online segment, the company is doing well and growth in these channels will be faster than overall company growth.
- Hospital network expansion in selective manner, new addition with pre-agreed rates only:** With ~12,000 hospitals under its network, Star Health has a reasonably expansive hospital network. This means that the company is expanding its hospital network selectively in some geographies, mostly semi-urban and smaller towns. The company maintains its focus on increasing the network of hospitals with pre-agreed rates (hospitals with which the company has pre-agreed rates for a list of standard medical procedures), and the addition of hospitals is done on this basis only. The existing network hospitals that currently do not have pre-agreed rates are also being transitioned to pre-agreed rates. This helps the company manage the claims costs better.

<b>CMP</b>	<b>Target Price</b>
<b>Rs 660</b> as of (March 24, 2022)	<b>Rs 1,040 (■)</b> 12 months
<b>Rating</b>	<b>Upside</b>
<b>BUY (■)</b>	<b>57.5 %</b>

### Change in Estimates

EPS Chg FY22E/FY23E (%)	-/
Target Price change (%)	NA
Target Period (Months)	12
Previous Reco	BUY

### Emkay vs Consensus

	EPS Estimates	
	FY22E	FY23E
Emkay	(21.8)	12.0
Consensus	(19.5)	12.7
Mean Consensus TP (12M)	Rs 846	

### Stock Details

Bloomberg Code	STARHEAL IN
Face Value (Rs)	10
Shares outstanding (mn)	576
52 Week H/L	940 / 584
M Cap (Rs bn/USD bn)	380 / 4.98
Daily Avg Volume (nos.)	340,067
Daily Avg Turnover (US\$ mn)	3.3

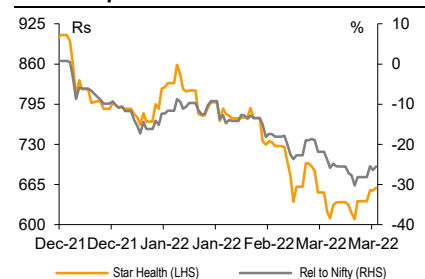
### Shareholding Pattern [Quarter]

Promoters	58.9 %
FIIIs	10.2 %
DIIIs	27.4 %
Public and Others	3.5 %

### Price Performance

(%)	1M	3M	6M	12M
<b>Absolute</b>	(3)	(17)	-	-
<b>Rel. to Nifty</b>	(4)	(18)	-	-

### Relative price chart



Source: Bloomberg

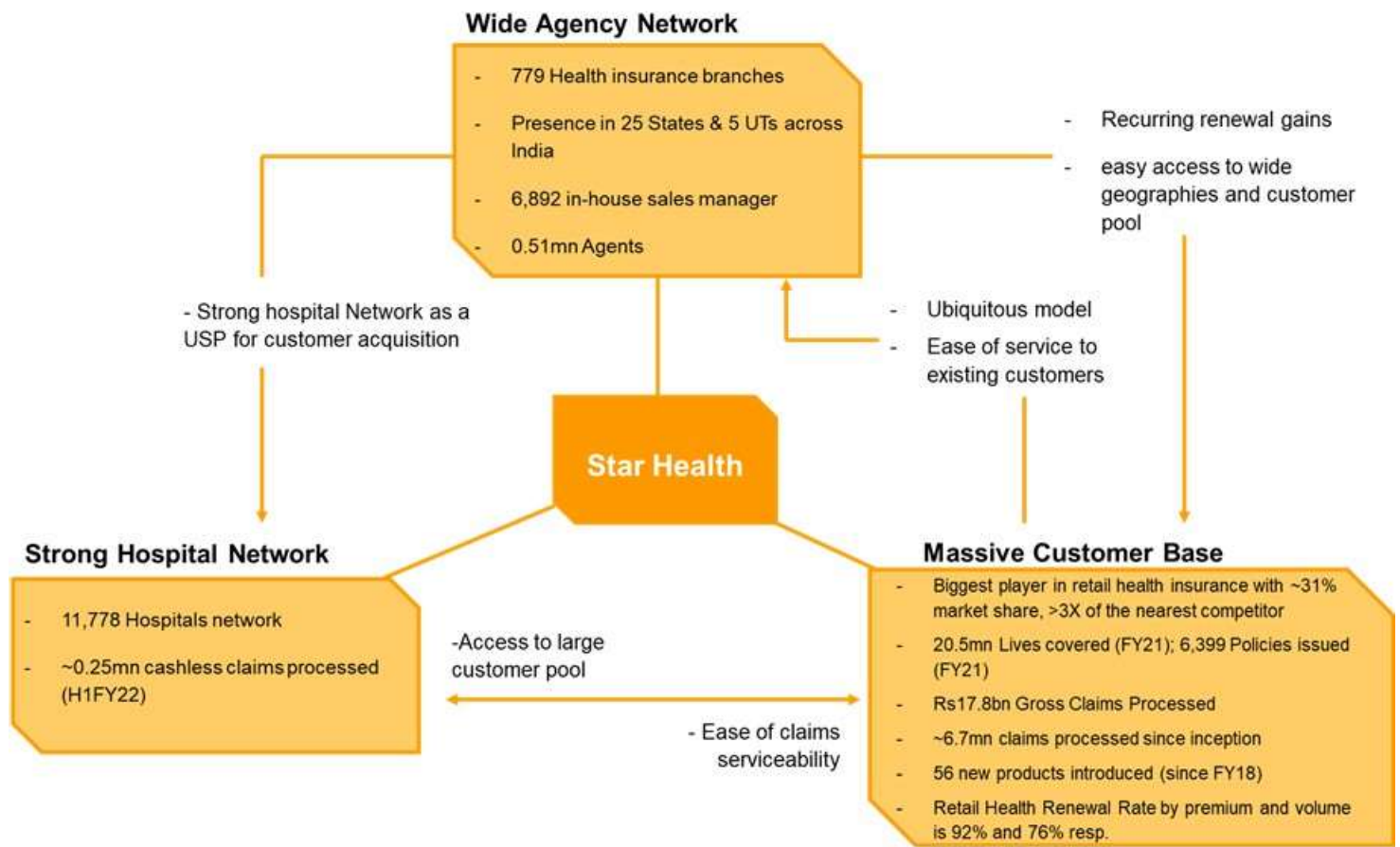
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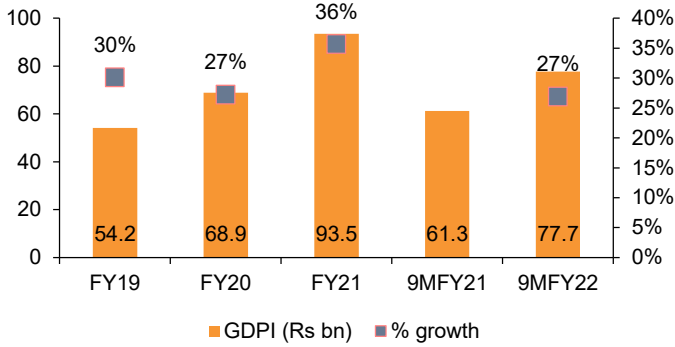
- **Product innovation and shift to Wellness from Illness to be key growth drivers:** Star Health has been a pioneer in product innovation. It was the first company to offer products focused on senior citizens, people with pre-existing conditions, etc. It continues to innovate in product offerings. It has launched a women-centric product on the International Women's Day in 2022. In the initial weeks of the launch, the product has seen good traction. Star Health is also actively looking to expand the product horizon by offering Wellness products vs. the current Illness-focused mix.
  - **Price hike taken in flagship product:** The company has taken a ~15% price hike in its flagship Family Health Optima plan. For other products, a price hike will be taken only if required. The company maintained that increasing the price of a product is the last option to be exercised only after other options to maintain product profitability are exhausted. The company highlighted that it has never increased the prices of its senior citizen plan in the last 14 years, as it remains profitable. On the reserve front, the company is comfortable with its IBNR of Rs3.38bn as of Q3FY22.
  - **Star Health remains an attractive profitable growth story:** Overall, Star Health remains an attractive story in a sunrise sector. 1-2 quarters of profitable growth delivery will likely lead to a material outperformance of Star Health's shares, in our view. We reiterate Buy with our Mar'23 TP of Rs1, 040, implying an FY25E P/E of ~46x and P/GWP of 2.8x.
- Please see our sector model portfolio (Emkay Alpha Portfolio): [BFSI-Insurance \(Page 6\)](#)

**Exhibit 1: Star Health's MOAT - Widespread distribution network (agents & branches), strong hospital network and a large pool of retail customers create a virtuous cycle for Star and strengthen its position sustainably**



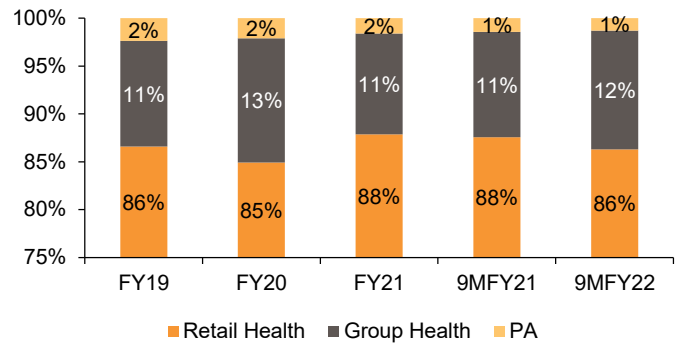
Source: Emkay Research

**Exhibit 2: GDP witnesses consistent growth above ~20% levels**



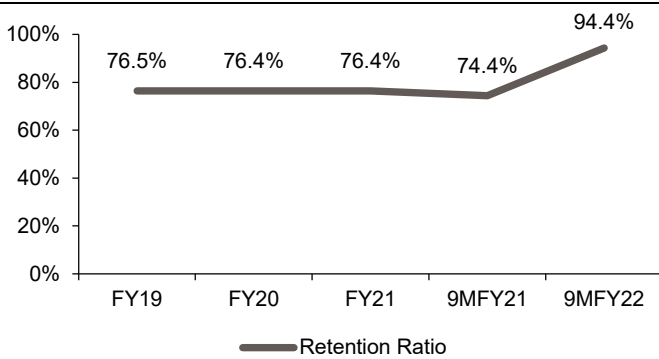
Source: Company, Emkay Research

**Exhibit 3: Retail health remains at the core**



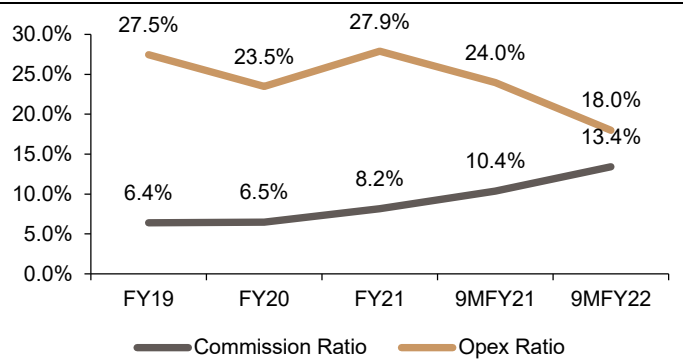
Source: Company, Emkay Research

**Exhibit 4: Retention ratio change reflects the changed reinsurance strategy post regulatory intervention**



Source: Company, Emkay Research

**Exhibit 5: Increase in net commission ratio shows higher retention**



Source: Company, Emkay Research

**Exhibit 6: Key Financials**

<b>Policyholder Account (Y/E Mar, Rs mn)</b>	<b>FY19</b>	<b>FY20</b>	<b>FY21</b>	<b>FY22E</b>	<b>FY23E</b>	<b>FY24E</b>	<b>FY25E</b>
Gross Direct Premium (GDPI)	54,154	68,907	93,490	1,15,793	1,43,600	1,76,671	2,17,359
Gross Written Premium (GWP)	54,154	68,907	93,490	1,15,793	1,43,600	1,76,671	2,17,359
Net Written Premium (NWP)	41,415	52,614	71,448	1,08,606	1,34,685	1,65,696	2,01,709
Net Earned Premium (NEP)	35,795	46,930	50,228	95,168	1,21,731	1,49,367	1,83,199
Net incurred claims	22,976	30,874	43,695	85,171	81,297	1,00,116	1,22,872
Net commission expense	2,638	3,409	5,838	14,055	16,711	19,675	22,788
Operating expense	9,827	11,020	14,014	18,566	22,351	27,083	32,465
Other expense	48	-58	0	0	0	0	0
Total Expense	35,488	45,246	63,546	1,17,791	1,20,359	1,46,874	1,78,125
Underwriting result	307	1684	(13318)	(22624)	1372	2493	5074
Investment income	1,340	1,924	2,606	4,438	5,814	7,412	9,294
Operating profit	1,647	3,608	-10,712	-18,186	7,187	9,905	14,368

<b>Shareholder Account (Y/E Mar, Rs mn)</b>	<b>FY19</b>	<b>FY20</b>	<b>FY21</b>	<b>FY22E</b>	<b>FY23E</b>	<b>FY24E</b>	<b>FY25E</b>
Operating profit	1,647	3,608	-10,712	-18,186	7,187	9,905	14,368
Investment income	614	1,011	1,631	2,823	2,891	3,320	3,914
Other income	1	0	3	75	0	0	0
Expenses and provisions	440	485	1,382	1,045	884	884	884
Profit before tax	1,822	4,134	-10,460	-16,333	9,193	12,341	17,397
Tax expense	540	1,415	-2,204	-4,083	2,298	3,085	4,349
Profit after Tax	1,282	2,720	-8,256	-12,250	6,895	9,255	13,048

<b>Balance Sheet (Y/E Mar, Rs mn)</b>	<b>FY19</b>	<b>FY20</b>	<b>FY21</b>	<b>FY22E</b>	<b>FY23E</b>	<b>FY24E</b>	<b>FY25E</b>
<b>Source of Funds</b>							
Net worth	13,926	16,437	42,242	63,135	63,135	63,135	72,838
Fair value gains	0	31	-76	0	0	0	0
Net worth including fair value gains	13,926	16,468	42,166	63,135	63,135	63,135	72,838
Borrowings	2,500	2,500	2,500	7,250	7,250	7,250	7,250
<b>Total</b>	<b>16,426</b>	<b>18,968</b>	<b>44,666</b>	<b>70,385</b>	<b>70,385</b>	<b>70,385</b>	<b>80,088</b>

<b>Application of Funds</b>							
Investments	30,301	42,900	68,367	1,06,032	1,31,549	1,61,715	1,99,449
Shareholders	9,523	14,782	26,321	35,623	40,449	46,928	56,061
Policyholders	20,778	28,117	42,046	70,409	91,100	1,14,787	1,43,388
Other Assets	2,401	2,486	5,203	9,336	7,089	4,059	1,203
Cash & Bank Balances	8,930	6,114	18,790	8,517	8,130	10,012	12,287
Other current assets	7,093	9,767	12,650	10,000	10,000	10,000	10,000
Current liabilities	9,003	11,794	15,643	17,832	20,867	24,299	29,895
Provisions	24,939	30,506	51,946	65,163	78,117	94,447	1,12,957
Net Current Assets	-17,920	-26,418	-36,149	-64,478	-80,854	-98,734	-1,20,565
Accumulated losses	1,644	0	7,245	19,495	12,601	3,345	0
<b>Total</b>	<b>16,426</b>	<b>18,968</b>	<b>44,666</b>	<b>70,385</b>	<b>70,385</b>	<b>70,385</b>	<b>80,088</b>

<b>Key ratios (Y/E Mar, %)</b>	<b>FY19</b>	<b>FY20</b>	<b>FY21</b>	<b>FY22E</b>	<b>FY23E</b>	<b>FY24E</b>	<b>FY25E</b>
Retention ratio	76.5	76.4	76.4	93.8	93.8	93.8	92.8
Incurred claims ratio	64.2	65.8	87.0	89.5	66.8	67.0	67.1
Net commission ratio	6.4	6.5	8.2	12.9	12.4	11.9	11.3
Expense ratio	23.7	20.9	19.6	17.1	16.6	16.3	16.1
Combined ratio	94.3	93.2	114.8	119.5	95.8	95.2	94.5
NWP/Net worth	3.0	3.2	1.7	1.7	2.1	2.6	2.8
Return on Equity	10.6	17.9	-28.2	-25.8	10.9	14.7	19.2
Solvency ratio	153.0	150.0	223.0	175.1	187.8	177.0	173.0

Source: Company, Emkay Research

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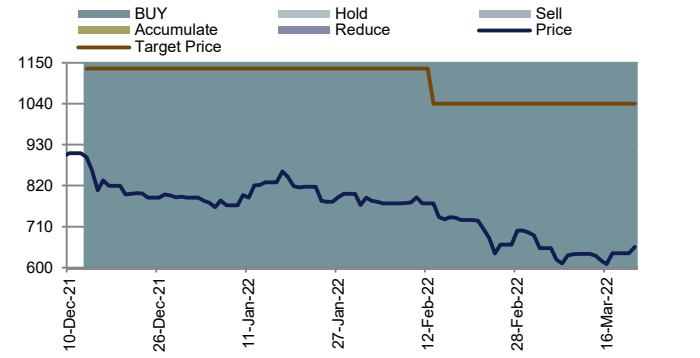
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**RECOMMENDATION HISTORY TABLE**

Date	Closing Price	TP	Period (months)	Rating	Analyst
13-Feb-22	772	1,040	12m	Buy	Avinash Singh
13-Dec-21	897	1,135	12m	Buy	Avinash Singh

Source: Company, Emkay Research

**RECOMMENDATION HISTORY CHART**



Source: Bloomberg, Company, Emkay Research

## Emkay Alpha Portfolio – BFSI-Insurance



### Analyst: Avinash Singh

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#### Sector

Insurance and Non-lending Financials

#### Analyst bio

Avinash Singh holds a PGDM and CFA. He has over 13 years of experience, including 10 years of research experience on the sell side. His team currently covers four insurance and one asset management stocks.

### EAP sector portfolio

Company Name	BSE200 Weight	EAP Weight	OW/UW (%)	OW/UW (bps)	EAP Weight based on Current NAV	Change vs last published EAP (bps)
<b>BFSI-Insurance</b>	<b>1.34</b>	<b>1.34</b>	<b>0%</b>	<b>0</b>	<b>100.00</b>	
HDFC Life Insurance	0.51	0.44	-13%	-7	32.98	0
ICICI Pru Life	0.18	0.17	-11%	-2	12.34	0
Max Financial	0.17	0.17	1%	0	12.54	0
SBI Life	0.48	0.57	18%	9	42.14	0
<b>Cash</b>	<b>0.00</b>	<b>0.00</b>	<b>NA</b>	<b>0</b>	<b>0.00</b>	<b>0</b>

Source: Emkay Research

\* Not under coverage: Equal Weight

■ High Conviction/Strong Over Weight ■ High Conviction/Strong Under Weight

### Sector portfolio NAV

	Base					Latest
	1-Apr-19	23-Mar-21	23-Sep-21	23-Dec-21	23-Feb-22	23-Mar-22
EAP - BFSI-Insurance	100.0	154.9	190.8	170.1	156.5	149.3
BSE200 Neutral Weighted Portfolio (ETF)	100.0	155.3	191.9	171.1	156.6	148.9

\*Performance measurement base date 1<sup>st</sup> April 2019

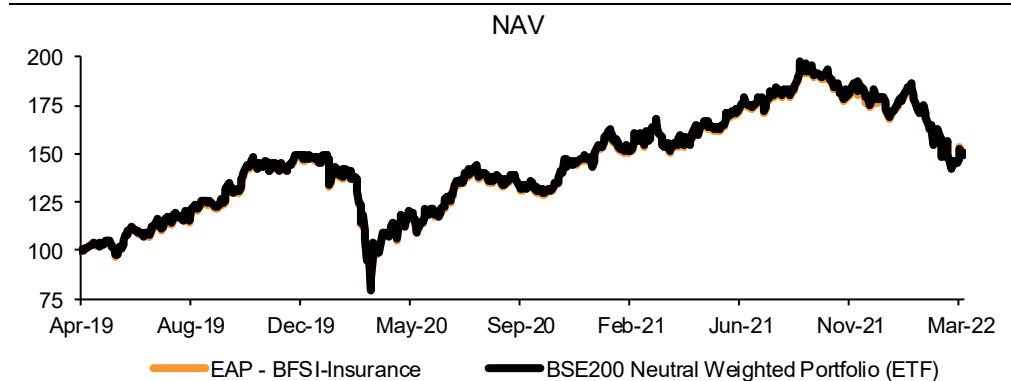
Source: Emkay Research

### Price Performance (%)

	1m	3m	6m	12m
EAP - BFSI-Insurance	-4.6%	-12.2%	-21.7%	-3.6%
BSE200 Neutral Weighted Portfolio (ETF)	-4.9%	-13.0%	-22.4%	-4.1%

Source: Emkay Research

### NAV chart



Source: Emkay Research

Please see our model portfolio (Emkay Alpha Portfolio): [Nifty](#)

Please see our model portfolio (Emkay Alpha Portfolio): [SMID](#)

“Emkay Alpha Portfolio – SMID and Nifty are a supporting document to the Emkay Alpha Portfolios Report and is updated on regular intervals”



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Ratings	Expected Return within the next 12-18 months.
BUY	Over 15%
HOLD	Between -5% to 15%
SELL	Below -5%

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