

CMP: ₹ 536

Target: ₹ 635 (18%)

Target Period: 12 months

BUY

October 23, 2022

Steady performance; better surplus aids earnings...

About the stock: HDFC Life is among the most dominant players in the Indian life insurance industry with a strong distribution network, parentage, operating metrics.

- Balanced product mix with focus on non-par, protection & annuity business
- Industry leading VNB margins of ~26-27%

Q2FY23 Results: Premium accretion slower; better surplus aid PAT

- NBP (pre-merger) grew at slower pace of 5% YoY at ₹ 10923 crore in H1FY23
- VNB margins (pre-merger) healthy at 27.6%, led by balanced product mix
- Persistency improved for 13th, 61st month to 88%, 54%, respectively
- PAT at ₹ 26.2 crore, up 19% YoY, aided by better surplus

What should investors do? HDFC Life's share price has given modest return of just over 6% in the past three years. Focus on diversified business growth, confidence on Exide acquisition provides comfort on fundamental strength.

- We retain our **BUY** rating on the stock

Target Price and Valuation: Insurance under penetration coupled with focus on product mix to aid healthy business growth and VNB margin. However, integration of Exide Life and uncertainty on stake of parent acts as near term deterrents. We continue to value HDFC Life at 2.9x FY24E EV with target price maintained at ₹ 635.

Key triggers for future price performance:

- Diversified product mix, product innovation and distribution strength to drive growth momentum
- Gradual improvement in VNB margin owing to selective product approach
- Management confident of achieving margin neutrality in next four to six quarters
- Uncertainty on parent merger remains a near term overhang

Alternate Stock Idea: Apart from HDFC Life, in our coverage we also like SBI Life.

- SBI Life also comes with a strong parentage with strong distribution network and superior cost efficiencies
- BUY with a target price of ₹ 1,500



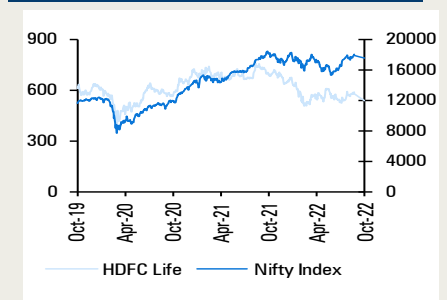
Particulars

Market Capitalisation	₹ 116427 crore
EV	₹ 33020 crore
AUM	₹ 204400 crore
52 week H/L	725/ 497
Net worth	₹15427 crore
Face value	₹ 10
DII holding (%)	6.26
FII holding (%)	28.8

Shareholding pattern

	Jun-21	Sep-21	Dec-21	Mar-22	Sept-22
Promoter	53.8	53.8	53.8	51.5	50.3
FII	26.1	30.1	30.5	26.3	28.8
DII	5.9	6.7	6.1	7.8	6.3
Others	14.2	9.4	9.7	14.4	14.6

Price Chart



Risk to our call

- VNB margin (post-merger) at 26.2%, while IEV at ₹ 36016
- Key risk:** 1) Delay in achieving margin neutrality post Exide merger, 2) Parent merger related clarity awaited

Research Analyst

Kajal Gandhi
kajal.gandhi@icicisecurities.com

Vishal Narnolia
vishal.narnolia@icicisecurities.com

Pravin Mule
pravin.mule@icicisecurities.com

Key Financial Summary

(₹ Crore)	FY19	FY20	FY21	FY22	3 year CAGR (FY19- FY22)	FY23E	FY24E	2 year CAGR (FY22-24E)
New business premium	14971	17238	20107	24155	17%	29783	35455	21%
APE	6049	7164	8183	9664	17%	12949	15488	27%
Total premium	29186	32707	38583	45962	16%	54418	65812	20%
PAT	1177	1371	1360	1208	1%	1445	1728	20%
EV	18296	20655	26625	30048	18%	37546	46074	24%
P/E (x)	92.7	79.7	80.4	94.6		79.1	66.1	
P/BV (x)	19.6	16.1	12.7	7.4		6.5	6.0	
P/IEV (x)	6.0	5.3	4.1	3.8		3.0	2.5	
RoEV (%)	20.1	18.1	18.5	19.0		17.6	17.1	

Key takeaways of recent quarter & conference call highlights

Q2FY23 Results: Premium growth slower; surplus boosts PAT

- Exide Life merger completed on October 14, 2022 and Q1FY23 numbers are restated. Hence, YoY and QoQ numbers are not comparable
- On a pre-merger basis, new business premium grew at a slower pace at 5% YoY at ₹ 10923 crore in H1FY23 and new business margin was at 27.6% vs. 26.4% in H1FY22. Including Exide, H1FY23 new business premium was reported at ₹ 11325 crore. Individual WRP market share declined 140 bps YoY to 14.8%
- Total APE (pre-merger) registered a growth of 11% YoY at ₹ 4549 crore for H1FY23, in line with industry growth. Merged total APE at ₹ 4914 crore
- Non-par saving products now form 37% vs 32% in H1FY22, while annuity business contributes 7% vs. 5% a year ago
- Opex ratio increased ~230 bps YoY from 12% to 14.3%. On a merged basis, opex ratio was at 14.7%
- AUM was at ₹ 204392 crore, up 7% YoY. Debt to equity mix in AUM was at 68:32 with ~99% of debt investments in G-secs and AAA bonds. Including Exide, AUM was at ₹ 224901 crore
- Persistency ratio improved with 13th month persistency at 88% and 61st month persistency at 54% vs. 86% and 52% in H1FY22, respectively
- Indian embedded value was at ₹ 33020 crore as of September 2022, up 15% YoY. Solvency ratio was at 2.1x. Merged IEV at ₹ 36016 crore

Q2FY23 earnings conference call highlights

- Also, 46-48% of individual business is contributed by HDFC Bank, while 30% of group business is contributed by entities in HDFC group together
- A ₹ 1000 crore of MTM on debt and steady equity return impacted unwind rate
- Aim for 15-17% growth in premium in FY23E.
- With merger of Exide Life, aims for VNB neutrality in next four quarters
- Growth in group protect remains healthy due to growth in disbursement of partners, deepening of relationship through new verticals and engaging in new partnership
- Have increased rates on non-par and annuity offering amid rise in interest rates. Do not see substantial competition from relatively short term debt based investments offerings in the market
- Launched various standalone products and offerings in combination with partners

Peer comparison

Exhibit 1: ICICI Direct coverage universe (Insurance)

Sector / Company	CMP		M Cap	EPS (₹)				P/E (x)				P/EV (x)				RoE (%)				
	(₹)	TP(₹)		Rating	(₹ bn)	FY21	FY22	FY23E	FY24E	FY21	FY22	FY23E	FY24E	FY21	FY22	FY23E	FY24E	FY21	FY22	FY23E
SBI Life Insurance	1245	1500	Buy	1246	14.6	15.1	16.3	20.0	85.5	82.7	76.3	62.1	3.7	3.1	2.8	2.4	15.2	8.5	10.9	13.0
HDFC Life	536	635	Buy	1164	6.7	5.7	7.4	8.9	79.6	93.7	71.2	59.2	4.1	3.8	3.0	2.4	17.6	18.0	18.1	18.2

Source: Company, ICICI Direct Research

Exhibit 2: Variance Analysis

	Q2FY23	Q2FY23E	Q2FY22	YoY (%)	Q1FY23	QoQ (%)	Comments
First Year Premium	2,423.1	2,115.0	2,078.0	16.6	1,708.7	41.8	Exide merger completed. Non-par witnessed traction
Renewal Premium	6,906.6	6,259.0	5,034.5	37.2	5,100.5	35.4	Steady persistency led to healthy renewal
Single Premium	3,952.8	4,073.0	4,518.4	-12.5	3,240.5	22.0	
Net Premium income	13,110.9	12,323.4	11,444.0	14.6	9,847.2	33.1	
Income from Investments	9,862.6	1,775.9	9,032.9	9.2	-3,234.8	-	Surge in int income led by steady yields and uptick in equities
Total revenue	22,973.5	14,099.2	20,476.9	12.2	6,612.3	247.4	
Commission	690.7	517.6	509.9	35.5	663.5	4.1	
Operating expenses	1,839.4	1,478.8	1,349.9	36.3	1,557.7	18.1	Opex ratio increased ~230 bps YoY from 12% to 14.3%
Management Expenses	2,530.0	1,996.4	1,859.8	36.0	2,221.2	13.9	
Benefits paid	11,730.8	8,379.9	8,337.6	40.7	7,274.1	61.3	
Change in Actuarial Liability	8,350.7	3,402.2	10,049.9	-16.9	-2,955.5	-	
Total Expenses	20,081.5	11,782.1	18,387.4	9.2	4,318.6	365.0	
Surplus/ (deficit)	262.9	278.8	177.8	47.8	-38.2	-	Healthy premium growth led to better surplus
Transfer to SH's A/c	218.2	200.0	201.9	8.0	250.8	-13.0	
Investment income	159.9	157.1	203.4	-21.4	120.2	33.0	
Profit/ (loss) before tax	327.3	292.1	276.0	18.6	361.1	-9.4	
PAT	326.2	288.1	274.2	19.0	360.0	-9.4	Higher surplus and appropriation boosted earnings

Key Metrics

NBP	6,376.0	6,188.0	6,596.4	-3.3	4,949.2	28.8	
AUM	2,24,901	1,52,398	1,91,212	17.6	2,00,123	12.4	Decent growth in AUM witnessed
IEV	33,015		28,703	15.0	29,709	11.1	

Source: Company, ICICI Direct Research

Exhibit 3: Change in estimates

(₹ Crore)	FY23E			FY24E		
	Old	New	% Change	Old	New	% Change
Premiums earned - Net	54,164	53,669	-0.9	65,697	64,690	-1.5
Transfer to Shareholders' account	1,271	1,149	-6.3	1,400	1,244	-9.1
PAT	1,563	1,445	-22.9	1,879	1,728	-13.7
EV/Share	178	178	-4.4	219	218	-4.7

Source: Company, ICICI Direct Research

Exhibit 4: Assumption

	Current		Earlier	
	FY23E	FY24E	FY23E	FY24E
NBP growth	23.3	19.0	25.5	19.0
AUM growth	14.3	15.0	14.2	15.0
EV Growth	25.0	22.7	25.3	23.0
Commission ratio	4.5	4.5	4.1	4.6
VNB Margin	26.0	26.0	26.0	26.0
Operating RoEV	18.2	18.2	18.2	18.2

Source: Company, ICICI Direct Research

Financial summary

Exhibit 5: Policyholders Account

(₹ Crore)	FY20	FY21	FY22	FY23E	FY24E
Premiums earned - Net	32223.6	38122.3	45396.2	53669.1	64690.2
Interest, Dividends & Rent	6845.3	7861.2	9459.3	11409.0	13139.3
Others income (incl. MTM)	-9807.5	24816.4	9756.7	10492.0	12130.3
Total Revenue	29,261	70799.9	64,612	75,570	89,960
Commission	1491.18	1676.22	1940.3	2445.8	2979.0
Operating expenses	4266.9	4586.0	5612.3	6516.4	8081.9
Benefits paid (Net)	19021.5	22574.8	31863.6	32217.4	37122.0
Change in valuation of policy liabilities	2440.8	40829.6	24681.5	30627.2	35550.4
Provision for tax	149.0	274.4	184.4	999.5	1320.0
Surplus/(deficit) after tax	971.4	690.7	215.4	1436.5	1699.2
Transfer to Shareholders' account	1,191	991	1,009	1,149	1,244

Source: Company, ICICI Direct Research

Exhibit 6: Shareholders Account

(₹ Crore)	FY20	FY21	FY22	FY23E	FY24E
Amounts transferred from Policyholders' account	1191.4	990.9	1009.2	1149.2	1243.9
Income from investments	437.8	647.6	789.4	1180.5	1482.5
Total	1,648	1,638	1,799	2,330	2,726
Total expenses	260.4	285.0	618.5	840.0	945.0
Profit before Tax	1387.4	1353.5	1180.0	1489.7	1781.3
Provision for tax	16.5	-6.6	-27.5	44.7	53.4
PAT	1,371	1,360	1,208	1,445	1,728

Source: Company, ICICI Direct Research

Exhibit 7: Balance Sheet

(₹ Crore)	FY20	FY21	FY22	FY23E	FY24E
Sources of Funds					
Share capital	2019	2021	2113	2112	2112
Reserve and surplus	4968	6407	13285	15278	16958
Credit/[debit] fair value change account	-192	207	85	103	126
Networth	6800	8638	15486	17492	19197
Policyholders' funds	119502	162818	187116	236488	297909
Funds for Future Appropriations	883	991	941	1228	1684
Total Liabilities	127185	173066	204163	255208	318789
Applications of Funds					
Shareholders' investments	5855	8542	15238	20266	26954
Policyholders' investments	67189	90538	108311	120225	134652
Asset held to cover linked liabilities	54182	74760	80622	92795	106715
Loans	299	424	643	1176	1709
Fixed assets - net block	330	340	343	350	357
Net current assets	-670	-1538	-993	20396	48403
Total Assets	127185	173066	204163	255208	318789

Source: Company, ICICI Direct Research

Exhibit 8: Key Ratios

(Year-end March)	FY20	FY21	FY22	FY23E	FY24E
Valuation					
No. of Equity Shares (Crore)	201.9	202.1	211.2	211.2	211.2
Diluted EPS (₹)	6.8	6.7	5.7	6.8	8.2
BV (₹)	33.7	42.7	73.3	82.8	90.9
EV per share	102.3	131.7	142.3	177.8	218.2
P/E	79.7	80.4	94.6	79.1	66.1
P/BV	16.1	12.7	7.4	6.5	6.0
P/IEV	5.3	4.1	3.8	3.0	2.5
Efficiency Ratios (%)					
Commission expenses as a % of Gross Premium	4.6	4.3	4.1	4.5	4.5
Management expenses as a % of Gross Premium	17.6	16.2	16.4	16.5	16.8
Return Ratios and capital (%)					
Return on Net worth	22.2	17.6	18.0	18.1	18.2
Operating RoEV	18.1	18.5	18.4	18.2	18.2
Key Ratios (%)					
VNB Margin	25.9	26.1	27.4	26.0	26.0

Source: Company, ICICI Direct Research

Exhibit 9: Key parameters

(Year-end March)	FY20	FY21	FY22	FY23E	FY24E
NBP	17238	20107	24155	29783	35455
Growth (%)	15	17	20	23	19
Linked	11192	11242	12028	13316	15590
Growth (%)	-1	0	7	11	17
Non Linked	21514	27341	33935	41102	50222
Growth (%)	20	27	24	21	22
APE	7164	8183	9664	12949	15488
Growth (%)	18	14	18	34	20
VNB	1919	2190	2675	3399	4066
Growth (%)	25	14	22	27	20
EV	20655	26625	30048	37546	46074
Growth (%)	13	29	13	25	23
AUM	127226	173839	204170	233287	268321
Growth (%)	1	37	17	14	15
PH Funds	67189	90538	108311	120225	134652
Growth (%)	18	35	20	11	12
SH Funds	5855	8542	15238	20266	26954

Source: Company, ICICI Direct Research

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Pankaj Pandey

Head – Research

pankaj.pandey@icicisecurities.com

**ICICI Direct Research Desk,
ICICI Securities Limited,
1st Floor, Akruiti Trade Centre,
Road No 7, MIDC,
Andheri (East)
Mumbai – 400 093
research@icicidirect.com**

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