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Stock Update

Result Update

HDFC Life Insurance

VNB margin expansion led by non-par savings, weak Retail protection

Insurance		Sharekhan code: HDFCLIFE		
Reco/View: Buy	↔	CMP: Rs. 534	Price Target: Rs. 670	↔

↑ Upgrade ↔ Maintain ↓ Downgrade

Summary

- HDFC Life (standalone) reported a 10% growth in VNB. VNB margin expanded to 28.3% in Q2FY2023 (up 174 bps y-o-y/150 bps q-o-q).
- This was driven by strong growth in non-PAR savings segment (27% y-o-y). Share of non-par savings increased to 32.5% of overall APE in Q2FY2023 from 26.5% in Q2FY2022. Share of ULIPs fell to ~18.3% in Q2FY2023 versus 21.5% in Q2FY2022. Increase in group protection (53% y-o-y) also contributed to margin expansion.
- APE growth was muted at 4% y-o-y as strong growth in group protection and non-par savings was offset by weak performance in ULIPs, group savings and individual protection segments.
- The stock currently trades at 3.1x/2.6x its FY2023E/FY2024E EVPS. We maintain a Buy with an unchanged PT of Rs. 670.

HDFC Life Insurance (HDFCLIFE) reported ~15% q-o-q and 41% y-o-y growth in net premium income. VNB margins improved by 174 bps y-o-y to 28.3% on standalone basis, primarily driven by a more optimal business mix. Including Exide Life, VNB margin stood at 26.2% in H1FY23 vs standalone margin at 27.6% in H1FY23. The company aims to maintain FY22 VNB margin of 27.4% in FY23E. VNB increased by 10% y-o-y on standalone basis. Company has guided to improve this momentum as it looks to grow consolidated VNB at 15%+ in FY23E. APE growth was muted at 4% y-o-y as strong growth in group protection and non-par savings was offset by weak performance in ULIPs, group savings and Individual Protection. On the distribution front, Agency channel APE grew 28% yoy with contribution increasing to 14% from 12% in Q2FY22. APE growth through the bancassurance channel was muted at 9% y-o-y in Q2FY23; ex-HDFC Bank, the growth was strong at 18.5% y-o-y. Market volatility lowered ULIP sales and weakness in retail protection led to a decline of 28% y-o-y in the direct channel.

Key positives

- Standalone VNB margins (standalone) expanded to 28.3% (up 174 bps y-o-y/150 bps q-o-q), driven by optimum product mix.
- Solvency ratio at 210% versus 178% in Q1FY2023 due to equity infusion of Rs. 2,000 crore from HDFC Ltd, partially offset by dividend payment.

Key negatives

- Slowdown in individual protection APE (down 39% y-o-y/ 4% q-o-q)

Management Commentary

- Management has guided to achieve VNB margin neutrality for the consolidated entity in the next four quarters.
- Company continues to look at newer segments to generate growth as competition in retail protection segment remains intense and hence it may have let go some business. Non-PAR/annuity is likely to witness healthy growth while retail protection should see a gradual recovery over H2FY23.

Our Call

Valuation – We maintain Buy on the stock with an unchanged PT of Rs. 670: HDFCLIFE currently trades at 3.1x/2.6x its FY2023E/FY2024E EVPS. In the near term, Non-PAR/ Annuity is likely to witness healthy growth while retail protection should see a gradual recovery over H2FY23. Company remains focused on maintaining a balanced product mix across businesses, with an emphasis on product innovation and superior customer service. We believe the structural story for the insurance sector continues to be attractive with a long runway for growth and strong players are likely to be well placed. We expect HDFCLIFE to deliver ~20% VNB CAGR over FY22-24 and estimate margin to remain ~28% by FY24.We have fine-tuned our estimates and our target multiple. We maintain a Buy with an unchanged price target (PT) of Rs. 670.

Key Risks

Muted demand. Any adverse regulatory policies/guidelines may affect its profitability.

Valuation (Consolidated) Rs cr

Particulars	FY22	FY23E	FY24E	FY25E
APE (Rs. cr)	9,760	11,580	13,900	16,100
VNB (Rs. cr)	2,680	3,200	3,830	4,520
VNB Margin (%)	27.5	27.6	27.6	28.1
EV (Rs. cr)	30,050	37,500	44,100	53,200
PAT (Rs. cr)	1,327	1,480	1,780	2,030
EPS (Rs.)	6.3	6.9	8.3	9.4
ROE (%)	10.0	9.3	10.8	11.4
P/EV (x)	3.8	3.1	2.6	2.2
P/VNB (x)	42.1	35.9	30.0	25.5

Source: Company; Sharekhan estimates

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		↔	

ESG Disclosure Score NEW

ESG RISK RATING 20.01

Updated Oct 08, 2022

Medium Risk

NEGL	LOW	MED	HIGH	SEVERE
0-10	10-20	20-30	30-40	40+

Source: Morningstar

Company details

Market cap:	Rs. 114,762 cr
52-week high/low:	Rs. 725 / 497
NSE volume: (No of shares)	36.2 lakh
BSE code:	540777
NSE code:	HDFCLIFE
Free float: (No of shares)	94.6 cr

Shareholding (%)

Promoters	50.3
FII	28.8
DII	6.9
Others	14.0

Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	-5.8	-0.2	-3.6	-21.8
Relative to Sensex	-6.9	-9.3	-9.4	-18.6

Sharekhan Research, Bloomberg

Key result highlights

- **Balanced product mix:** Company expects its product mix to remain balanced post-merger also. Product innovation has been a key differentiator and has played a critical role in driving business growth. Several of the company's savings products – such as Sanchay Plus and Sanchay-PAR Advantage – have seen strong traction. Within Non-PAR segment, shorter tenure – Sanchay FMP product is seeing a healthy growth and contributed 20% to the total Non-PAR APE. Higher interest rate continues to offer healthy growth opportunities in traditional savings business. Credit protection segment grew 66% y-o-y in 1HFY23. The company continues to look at newer segment to generate growth as competition in retail protection remains intense and hence it may have to let go some business. The company has further launched a new product – "Click to Protect" which will further aid the growth in protection business. Management also guided to achieve VNB margin neutrality for the consolidated entity in the next four quarters.
- **Completion of merger:** Exide Life got merged with the company post the final approval by the IRDAI in Oct 2022 with effect from April 1, 2022. The transaction got completed within 14 months. The merger is likely to improve the geographical presence for the company in South India, in Tier-II and -III regions.
- **Improvement in persistency ratio:** Persistency ratio improved across most buckets. The change in product mix toward higher share of non-par savings aided persistency.
- **Distribution mix:** On the distribution front, Agency channel APE grew 28% y-o-y with contribution increasing to 14% from 12% in Q2FY22. APE growth through the bancassurance channel was muted at 9% y-o-y in 2QFY23; ex-HDFC bank growth was strong at 18.5% y-o-y. Market volatility has resulted in lower ULIP sales and the weakness in retail protection led to decline of 28% y-o-y in the direct channel. Strong growth being witnessed in new relation - Bandhan, Yes and IDFC First Bank. Further, the bank added India Post Payments Bank that will further aid the growth. Around 46-48% of the business comes from HDFC Bank channel and the company is likely to keep this at ~50%. In agency channel, the company added ~24,000 agents in H1FY23.
- **Others:** Mr. Suresh Badami has been elevated as the Deputy MD of the company currently from Executive Director & Chief Distribution Officer.

Results (Consolidated) **Rs cr**

Particulars	Q2FY23	Q2FY22	Q1FY23	y-o-y (%)	q-o-q (%)
New Business Premium	6,376	6,596	4,949	(3.3)	28.8
Net Premium	13,138	11,468	9,870	14.6	33.1
Income from investments	9,784	8,875	(3,301)	10.2	NM
Other income	65	45	60	44.7	9.3
Total Income	23,002	20,502	6,637	12.2	246.6
Net Commission	683	511	401	33.6	70.5
Operating Expenses	1,842	1,352	1,560	36.2	18.1
Provision for taxes	24	14	15	74.7	64.2
Surplus/(Deficit)	248	164	210	51.3	18.5
PBT	331	278	363	18.9	(8.9)
PAT	329	276	361	19.3	(9.0)

Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector view - Strong growth outlook

Life insurance business in India is poised for double-digit growth in terms of premium value, led by higher Individual protection volumes and group insurance going ahead. A large protection gap and expanding per capita income are key long-term growth drivers for the sector. Credit protection product is still at an early stage and has the potential to grow multifold as the penetration of retail loans improves. Hence, we believe the insurance sector has a huge growth potential in India. In this backdrop, we believe strong players armed with the right mix of products, services, and distribution are likely to gain disproportionally from the opportunity.

■ Company outlook - Superior product mix & sector tailwinds to drive sustainable business growth

HDFC Life is well placed with healthy capitalisation and superior product mix. With high proportion of protection and savings-related products, we believe HDFC Life is better placed in the present environment. Being the largest player, HDFC Life is likely to benefit from favourable tailwinds. The company's sustained persistency ratio indicates client service and quality of products offered, which are critical for long term sustainability. The company is a strong business franchise and there is a runway for growth led by strong sector tailwinds despite higher competition.

■ Valuation - We maintain Buy on the stock with an unchanged PT of Rs. 670

HDFCLIFE currently trades at 3.1x/2.6x its FY2023E/FY2024E EVPS. In the near term, Non-PAR/Annuity is likely to witness healthy growth while retail protection should see a gradual recovery over H2FY23. The company remains focused on maintaining a balanced product mix across businesses, with an emphasis on product innovation and superior customer service. We believe the structural story for the insurance sector continues to be attractive with a long runway for growth and strong players are likely to be well placed. We expect HDFCLIFE to deliver ~20% VNB CAGR over FY22-24 and estimate margin to remain ~28% by FY24.We have fine-tuned our estimates and our target multiple. We maintain Buy with an unchanged price target (PT) of Rs. 670.

Peer Comparison

Companies	CMP (Rs/Share)	MCAP (Rs Cr)	P/VNB (x)		P/EV (x)		RoE (%)	
			FY23E	FY24E	FY23E	FY24E	FY23E	FY24E
HDFC Life Insurance Company	534	1,14,762	35.9	30.0	3.1	2.6	9.3	10.8
ICICI Prudential Life Insurance	500	71,985	27.9	24.5	2.1	1.8	9.0	9.8

Source: Company; Sharekhan Research

About company

Established in 2000, HDFC Life is a leading 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 250+ partnerships, comprising traditional partners such as NBFCs, MFIs, and SFBs, and includes more than 40 new ecosystem partners.

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 channelize growth for the insurance business. We believe HDFC Life's sustained product leadership will help it maintain superior VNB margins and operating RoEV, relative to peers, which would provide support to its valuations. We believe the insurance business 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 EV CAGR over the long term (aided by high margins in the protection business and improving persistency) which will support valuations.

Key Risks

Muted demand. Any adverse regulatory policies/guidelines may affect its profitability.

Additional Data

Key management personnel

Ms. Vibha Padalkar	MD & CEO
Mr. Suresh Badami	Deputy MD
Mr. Niraj Shah	CFO
Mr. S. Parthasarathy	Chief Actuary
Mr. Prasun Gajri	Chief Investment Officer

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	HOUSING DEVELOPMENT FINANCE CORP LTD	47.00
2	CAPITAL GROUP COS INC	6.11
3	JP MORGAN CHASE AND CO	4.32
4	EXIDE INDUSTRIES	4.05
5	FMR LLC	1.95
6	EUROPACIFIC GROWTH FUND	1.84
7	VANGUARD GROUP INC	1.74
8	ABRDN 2006 LIMITED	1.66
9	BLACKROCK LTD	1.29
10	SBI FUNDS MANAGEMENT LTD	1.29

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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