

CMP: ₹ 742

Target: ₹ 855 (15%)

Target Period: 12 months

BUY

October 20, 2024

## Volume growth to remain in focus over margins ...

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 ~25%

Q2FY25 performance: HDFC Life delivered healthy growth in new business premium accretion at 12% YoY to ₹ 14497 crore, in 1HFY25, driven by unit linked product and non-par business. APE (Annualised Premium Equivalent) growth came at 25% YoY, gaining market share. However, higher expense (~140 bps increase in opex ratio at 21.1%) led earnings growth at 15% YoY to ₹ 911 crore. Value of new business (VNB) grew by 17% YoY to ₹ 1656 crore, although VNB margin contracted by ~160 basis points to 24.6%, due to change in product mix. AUM expanded to ₹ 324942 crore, while embedded value stood at ₹52114 crore, up 21%.

### Investment Rationale

- Linked business remains robust; focus on volume to aid performance: APE growth remained healthy at 25% YoY, led by unit linked business. As anticipated, linked business witnessed higher growth, amid buoyancy in capital market, keeping share of linked broadly stable at 36% in 1HFY25. Focus on chasing growth with balanced product mix (continued focus on protection & annuity business) aiming 18-20% growth in business. Strategy focussing on customer accretion and improvement in penetration in tier 2 & 3 markets could aid growth. While ramping of agency channel is underway, traction in business should take a while to be evident.
- Declining trend in VNB margin continued; more volatility in near term: VNB margin declined 170 bps at 24.6%, amid higher traction in linked business and deferment in re-pricing of non-par products. While new surrender norms are expected to impact VNB margins (~100 bps), impact is expected to be toned down through alteration in product mix, better pricing and re-alignment of payout structure. Growth in VNB (15-17% in FY25E) remains priority with VNB margin remaining as an outcome. Thus, we lower estimates for VNB margins at 25.5% in FY26E.

### Rating and Target Price

- Growth in linked business, impacting margins, seems to be more of industry phenomenon. Strategy to focus on business growth by way of customer acquisition and improve penetration in tier 2 & 3 markets is seen to aid business growth. While new surrender norms have an impact of 100 bps, discussion on tweaking distribution payout holds the key.
- Valuing the stock at 2.8x FY26E EV, we revise target at ₹ 855 and maintain Buy recommendation.



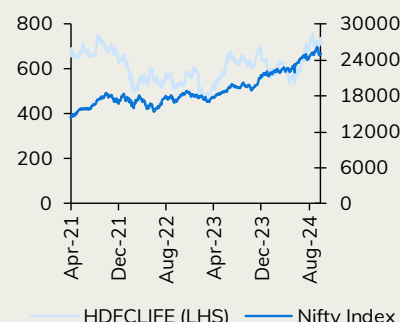
#### Particulars

Particulars	Amount
Market Capitalisation	₹1,59,792 crore
EV	52114 crores
AUM	₹324942 crore
52 week H/L	761/ 511
Net worth	₹14750 crore
Face value	₹ 10

#### Shareholding pattern

	Sep-23	Dec-23	Mar-24	Jun-24	Sep2024
Promoters	50.4	50.4	50.4	50.4	50.4
FII	30.5	31.3	30.0	26.6	25.6
DII	6.9	6.6	7.9	11.2	13.3
Public	12.2	11.8	11.6	11.8	10.8

#### Price Chart



#### Key risks

- Higher than expected erosion in margins
- Competitive intensity impacting business growth & IRR

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### Key Financial Summary

(₹ Crore)	FY21	FY22	FY23	FY24	3 year CAGR	FY25E	FY26E	2 year CAGR
New business premium	20107	24155	29085	29631	14%	36173	42296	19%
APE	8183	9664	13100	12963	17%	16171	19294	22%
Total premium	38583	45962	57533	63076	18%	74046	86344	17%
PAT	1360	1208	1360	1569		1794	2118	
EV	26625	30048	39526	47468		55803	65857	
P/E (x)	110.3	129.8	117.3	101.7		89.0	75.3	
P/BV (x)	17.4	10.1	12.3	10.9		10.1	9.3	
P/IEV (x)	5.6	5.2	4.0	3.4		2.9	2.4	
RoEV (%)	18.5	19.0	19.7	17.5		17.6	14.5	

## Concall highlights and outlook

- Product mix includes - ULIP at 36%, Non-par savings at 38%, Participating products at 15%, Protection at 6% and Annuity at 5%.
- Company recorded 22% growth in number of policies and 7% rise in ticket size during the quarter.
- APE growth guidance to 18-20%, while the VNB is expected to grow in the 15-17% range. VNB Margins will be an outcome and the company will balance its product mix to protect the margins.
- ULIP segment saw moderate dip during the quarter. However, new product launches in the non-par category aided premium growth. ULIPs will remain in range of ~30% levels. Buoyancy in the equity markets has resulted in strong customer demand for ULIPs. Management will focus on cross selling other products to newly-acquired customers.
- Change in the product mix (higher demand in unit linked product) and deferment in re-pricing of certain non-par products (impact of 30-40 bps on VNB margin) resulted in pressure on margins during 1HFY25.
- Strong growth in non-par savings products, achieving a 76% YoY increase, aided by new product launched this year.
- HDFC pension crossed ₹1 lakh crore of AUM with a market share of 43.6%.
- Company has successfully relaunched more than 40 products contributing to about ~95% of the business as on 1 October 2024.
- Under the new surrender regulations, pricing in protection and annuity products is expected to improve which will aid improvement in VNB margins in 2HFY25.
- Counter share at HDFC Bank continued to be stable at ~65%. Nearly ~70% of business in agency has been coming from Tier2/3 cities. Agent addition is helping the company to penetrate into deeper areas.
- As on 30th Sep 2024, solvency ratio stood at 181%. Management raised subordinated debt of ₹1000 crores in Oct'24 thereby improving solvency to 192% post the sub-debt issue.
- In order to mitigate the impact of new surrender regulations, the company has adopted tailored solutions including claw back & deferment of commissions.
- Credit Protection growth has been slow due to moderation in disbursements among the credit partners. Further, there is some competitive pressure building up and management will continue to moderate pace of business with the partners wherein pricing is unsustainable. Given limited reinsurance in credit protect business, management is not willing to participate in aggressive pricing.

**Exhibit 1: Variance Analysis**

	Q2FY25	Q2FY24E	Q2FY24	YoY (%)	Q1FY25	QoQ (%)	Comments
First Year Premium	3,253.4	3,090.0	2,565.6	26.8	2,357.9	38.0	
Renewal Premium	8,831.0	9,122.8	7,838.9	12.7	6,410.6	37.8	Graudal improvement in persistency
Single Premium	4,843.0	5,168.0	4,535.8	6.8	4,042.4	19.8	
Net Premium income	16,569.7	17,207.9	14,756.0	12.3	12,509.6	32.5	
Income from Investments	11,870.8	4,041.2	8,218.3	44.4	14,197.5	-16.4	Gains from ULIP segment aids income from investment
Total revenue	28,440.5	21,249.1	22,974.3	23.8	26,707.2	6.5	
Commission	1,851.2	808.8	1,186.9	56.0	1,470.3	25.9	
Operating expenses	1,681.4	2,323.1	1,740.1	-3.4	1,267.2	32.7	Total expense ratio higher at 21.1%
Management Expenses	3,532.5	3,131.8	2,927.0	20.7	2,737.5	29.0	
Benefits paid	10,298.6	12,045.5	9,337.1	10.3	8,827.8	16.7	
Change in Actuarial Liability	14,453.5	5,276.1	11,016.1	31.2	14,565.7	-0.8	
Total Expenses	24,752.1	17,321.6	20,353.2	21.6	23,393.5	5.8	
<b>Surplus/ (deficit)</b>	<b>39.6</b>	<b>753.7</b>	<b>229.2</b>	<b>-82.7</b>	<b>464.3</b>	<b>-91.5</b>	<b>VNB margins declined at 24.6% owing to change in</b>
Transfer to SH's A/c	286.6	286.6	286.6	0.0	286.6	0.0	
Transfer to SH's A/c	385.4	250.0	135.4	184.6	266.5	44.6	
Investment income	268.8	226.3	246.8	8.9	257.2	4.5	
Profit/ (loss) before tax	437.6	381.3	330.7	32.3	497.5	-12.0	
PAT	433.0	377.3	376.8	14.9	477.7	-9.3	Lower VNB margin impacted earnings momentum
<b>Key Metrics</b>							
NBP	8,096.4	8,258.0	7,101.3	14.0	6,400.3	26.5	
AUM	3,24,941.9	1,31,267.4	2,64,869.5	22.7	3,10,244.0	4.7	Healthy AUM growth at 23%
IEV	52,114.0		42,908.0	21.5	49,611.0	5.0	

## Financial Summary

### Exhibit 2: Profit and loss statement

₹ crore

(₹ Crore)	FY23	FY24	FY25E	FY26E
Premiums earned - Net	56764.0	61959.2	73049.8	85187.2
Interest, Dividends & Rent	12844.7	15811.5	16072.9	18358.0
Others income (incl. MTM)	1096.8	460.8	3385.5	3792.7
Total Revenue	70,705	78,231	92,508	1,07,338
Commission	2910.8	5256.3	7588.1	8858.9
Operating expenses	8437.4	6901.1	7550.8	8796.9
Benefits paid (Net)	38872.3	39696.5	45723.7	52354.4
Change in valuation of policy liabilities	18586.2	48419.4	27013.9	30629.6
Provision for tax	159.1	-592.4	127.5	-3.7
Surplus/(deficit) after tax	1335.0	-21767.6	1624.6	2143.6
Transfer to Shareholders' account	1,469	799	1,369	1,821
<b>(₹ Crore)</b>	<b>FY23</b>	<b>FY24</b>	<b>FY25E</b>	<b>FY26E</b>
Amounts transferred from Policyholders	1468.9	799.1	1369.3	1821.1
Income from investments	719.7	1002.2	1117.3	1080.4
Total	2,252	1,814	2,487	2,901
Total expenses	979.4	250.5	745.0	845.0
Profit before Tax	1272.4	1563.8	1741.5	2056.5
Provision for tax	-87.7	-5.0	-52.2	-61.7
PAT	1,360	1,569	1,794	2,118

Source: Company, ICICI Direct Research

### Exhibit 4: Balance sheet

₹ crore

(₹ Crore)	FY23	FY24	FY25E	FY26E
<b>Sources of Funds</b>				
Share capital	2149	2151	2151	2151
Reserve and surplus	10815	12050	13255	14581
Credit/[debit] fair value change account	20	451	466	483
Networth	12987	14652	15872	17215
Policyholders' funds	224447	276916	329319	389574
Funds for Future Appropriations	2185	2161	2417	2739
<b>Total Liabilities</b>	<b>239619</b>	<b>293729</b>	<b>347608</b>	<b>409529</b>
<b>Applications of Funds</b>				
Shareholders' investments	13132	14882	16370	18007
Policyholders' investments	146449	181797	203612	228046
Asset held to cover linked liabilities	79201	95542	105096	115605
Loans	1585	1897	2430	2963
Fixed assets - net block	380	416	424	433
Deferred tax asset				
Net current assets	-1326	-804	19676	44475
<b>Total Assets</b>	<b>239422</b>	<b>293729</b>	<b>347608</b>	<b>409529</b>

Source: Company, ICICI Direct Research

### Exhibit 3: Key ratios

(Year-end March)	FY23	FY24	FY25E	FY26E
<b>Valuation</b>				
Diluted EPS (₹)	6.3	7.3	8.3	9.8
BV (₹)	60.4	68.1	73.8	80.0
EV per share	183.9	220.7	259.4	306.2
P/E	117.3	101.7	89.0	75.3
P/BV	12.3	10.9	10.1	9.3
P/IEV	4.0	3.4	2.9	2.4
<b>Efficiency Ratios (%)</b>				
Commission expenses as a % of Gross Premium	5.1	8.3	10.2	10.3
Management expenses as a % of Gross Premium	19.7	19.3	20.4	20.4
<b>Return Ratios and capital (%)</b>				
Return on Net worth	18.1	18.2	18.2	18.2
Operating RoEV	18.2	17.5	17.5	17.8
<b>Key Ratios (%)</b>				
VNB Margin	27.6	26.3	25.5	25.8

Source: Company, ICICI Direct Research

### Exhibit 5: Growth ratios

(Year-end March)	FY23	FY24	FY25E	FY26E
NBP	29085	29631	36173	42296
Growth (%)	20	2	22	17
Linked	12400	14733	18350	22448
Growth (%)	3	19	25	22
Non Linked	45134	48344	55695	63896
Growth (%)	33	7	15	15
APE	13336	12963	16171	19294
Growth (%)	38	-3	25	19
VNB	3674	3501	4377	5302
Growth (%)	37	-5	25	21
EV	39527	47468	55803	65857
Growth (%)	32	20	18	18
AUM	238782	292220	325078	361658
Growth (%)	17	22	11	11
PH Funds	146449	181797	203612	228046
Growth (%)	35	24	12	12
SH Funds	13132	14882	16370	18007

Source: Company, ICICI Direct Research

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Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



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